



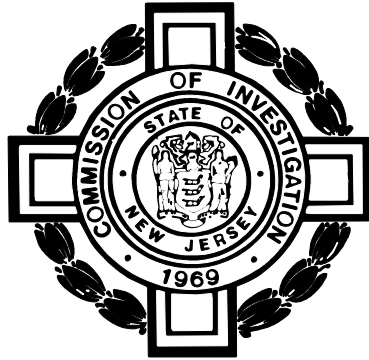
*State of New Jersey*  
*Commission of Investigation*

# **E-ZPass**

## **The Making of a Procurement Disaster**

*June 2004*

*State of New Jersey*  
*Commission of Investigation*



**E-ZPass**

**The Making of a  
Procurement  
Disaster**

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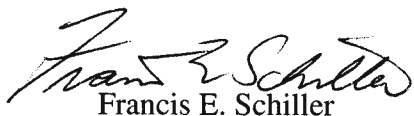
**Francis E. Schiller**  
*Chair*  
**W. Cary Edwards**  
**Joseph R. Mariniello, Jr.**  
**Kathy Flicker**  
*Commissioners*

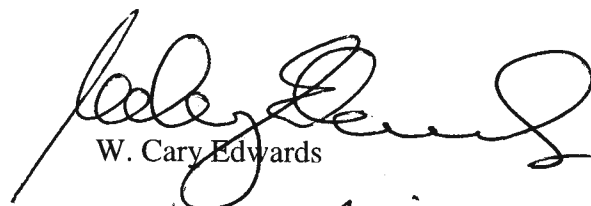
June 2004

Governor James E. McGreevey  
The President and Members of the Senate  
The Speaker and Members of the General Assembly

The State Commission of Investigation herewith formally submits, pursuant to N.J.S.A.  
52:9M, a final report of its investigation of the E-ZPass electronic toll collection system  
procurement and financing.

Respectfully,

  
Francis E. Schiller

  
W. Cary Edwards

  
Joseph R. Mariniello, Jr.

  
Kathy Flicker

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# *Executive Summary*

## **Introduction**

On March 10, 1998, a consortium of public transportation agencies formally executed a contract for the design, installation, operation and maintenance of an electronic toll collection (ETC) system that would link New Jersey to the regional network known as E-ZPass.<sup>1</sup> The contract was unique in a number of aspects, not the least of which was that it formed the basis for the largest, most complex ETC system ever proposed. Toll collectors and coin machines on some of the nation's busiest highways, bridges and tunnels, north to New York and south through Delaware, would be replaced by high-tech transponders, sensors, fiber optics, cameras and computers to handle millions of transactions daily. Further, the plan called for the system to pay for itself – no money down and no payments by the Consortium – with revenue to be generated by two primary sources: fines against E-ZPass scofflaws and the commercial leasing of fiber-optic telecommunication cable. Though the contract expressly called for the Consortium members to cover any losses incurred at the end of the ten-year contract term, no such deficit was projected.<sup>2</sup> Indeed, the system was promoted as one that actually would yield a hefty surplus, notwithstanding substantial up-front indebtedness in the form of \$300 million in taxable, interest-bearing bonds issued via the New Jersey Economic Development Authority for capital construction and operation.

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<sup>1</sup> Established in 1995, the Consortium initially consisted of the New Jersey Turnpike Authority, the former New Jersey Highway Authority (operator of the Garden State Parkway) the Port Authority of New York and New Jersey, the South Jersey Transportation Authority (operator of the Atlantic City Expressway). The State of Delaware Department of Transportation joined in 1996. The New Jersey-based entities jointly accounted for 83 percent of the project.

<sup>2</sup> During the initial phases of the procurement, prior to the selection of a vendor, the Consortium considered an eight-year contract term but later established a 10-year term.

Once the contract was executed, however, the project immediately began to unravel, and the fallacies of the self-funding plan became publicly apparent.

The contractor team led by MFS Network Technologies (MFS) of Omaha, Nebraska, fell behind on construction and installation. As technicians struggled to make the new system operational after many delays, machinery and software malfunctioned or failed altogether. In many instances, the equipment simply could not distinguish legitimate customers from violators. Both the Customer Service Center and the Violations Processing Center – “back-office” administrative components critical to the program’s operational and financial viability – became hopelessly mired in a data swamp. Amid a cascade of consumer complaints and burgeoning deficit projections, questions arose over the system’s fundamental integrity. In early 2002, the New Jersey Assembly Transportation Committee held public hearings on a range of matters related to the E-ZPass controversy. On July 10, 2002, the panel issued a report recommending, among other things, that the Legislature formally ask the State Commission of Investigation to conduct an independent probe. The Commission, acting on its own statutory volition, adopted a resolution on October 9, 2002, authorizing an investigation as follows:

*Whether the laws of New Jersey have been faithfully executed and effectively enforced in connection with the process leading to and resulting in the financing of the E-ZPass regional electronic toll collection system; whether public officers and employees and officers and employees of public corporations and authorities faithfully and properly discharged their duties in connection therewith, and whether the laws of New Jersey pertaining to the award of public contracts are adequate to protect the interests of the State.*

Through this report, the Commission makes public its findings and recommendations.<sup>3</sup>

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<sup>3</sup> As with all of its investigations, the Commission utilized its statutory subpoena power to obtain thousands of pages of documentary materials and summoned 29 witnesses for sworn executive session testimony.

## **Summary of Key Findings**

The E-ZPass contract was the product of an ill-advised, inappropriate procurement process that lacked proper safeguards to ensure accountability and to protect the public's interest. In essence, a major capital project of unprecedented scope and technical complexity was removed from the sphere of normal competitive bidding and treated for procurement purposes as a contract for professional service. Professional-service contracting, however – typically employed by government to negotiate and retain private engineering, legal or other expertise – was not designed, and was never intended, for use in procurements as unique and massive as E-ZPass. Its injudicious use in this instance constituted the foundation of an administrative and financial debacle of immense proportions, a debacle that laid bare serious gaps in the laws governing public-project contracting in this state.

The Commission also found that once the professional-service approach was chosen, the process of carrying the procurement to completion fell prey to human error, and to obvious mismanagement and manipulation by senior personnel at the New Jersey Department of Transportation (NJDOT) and the New Jersey Turnpike Authority.

Procurement documents were vaguely written, and the solicitation and evaluation of vendor proposals were rushed, in some instances unreasonably so. Members of the vendor evaluation team complained that they were given insufficient time to review the proposals prior to making a contract-award recommendation and that their requests for additional time and information were rejected. Further, every member of the evaluation team testified under oath that, as a group, they were instructed by a ranking NJDOT official to score the vendor proposals at least twice. Team members testified that this

occurred during a confidential, late-night session. This unusual exercise boosted the final numerical ranking of MFS's proposal vis-à-vis that of competing bidder Lockheed Martin IMS Corp. (Lockheed).

Further, the Commission found that the procurement unfolded against the backdrop of events and circumstances that evidence the taint of multiple conflicts of interest. On one level, then-NJDOT Commissioner Frank J. Wilson engaged in private-sector employment discussions with companies doing business with the state, including two with corporate links to the procurement, one of which hired Wilson. Though he signed a letter purportedly recusing himself from the procurement process at the time, an examination of the full record suggests he violated the terms of that recusal at a critical stage in the vendor-selection process. The Commission also examined the activities of a private consultant hired initially by NJDOT, and later by a Consortium contractor, to provide advice on fiber-optic technology and other matters. This consultant, Kingston Cole, had a pre-existing professional relationship with Wilson, who sought no-bid state contracts for Cole and who served on an evaluation committee that chose Cole's firm for NJDOT work. Cole and Wilson conferred regularly prior to the award of the E-ZPass contract. Cole also met privately with representatives of the vendors competing for the contract, including MFS, and played an active role in final negotiations leading to the preparation and submission by the vendors of their best and final offers. During this process, Cole authored a confidential strategy memorandum suggesting that MFS's chief competitor, Lockheed, be misled as to how prospective vendors were to address the issue of fiber optics in their project proposals.



Also at issue behind the scenes were questions regarding MFS's true agenda in the E-ZPass procurement. The firm had limited experience in electronic-toll projects; rather, it was a specialist in a narrower array of systems integration services, primarily the installation and marketing of fiber-optic telecommunications networks for commercial gain. In the months immediately following the award of the E-ZPass contract, a top Consortium official expressed concern that MFS's goal was to structure the deal in such a way as to maximize its potential profit from a fiber-optic network that, as an adjunct to the primary E-ZPass initiative, was to be of greater significance to the MFS team. This official pointed out that the fiber array here would complete a larger regional fiber network already installed by the firm.

On another level, the Commission found that when it came to the conduct of public-sector due diligence in this matter, thoroughness was sacrificed for expediency. No comprehensive independent study was ever undertaken by or on behalf of the Consortium or the toll-paying public to determine whether the E-ZPass revenue projections, and the assumptions which lay beneath them, were reasonable, realistic and attainable – particularly in the context of possible vendor performance failures. No serious or extensive consideration was given, prior to the award of the contract, to possible alternatives to the self-funding approach – even though both prospective vendors advocated such alternatives. Ultimately, while the prevailing vendor, MFS, undertook appropriate private-sector due diligence to protect its own financial position and fashion a contract proposal to avoid risk, the Consortium's public toll authorities did not. They agreed to assume full liability for an untested and uncertain funding strategy, despite the scope and imminence of the associated risk.

In essence, the Consortium agreed to participate in a thoroughly lopsided public/private partnership in which the vendor was authorized to share in the profits if the project yielded a surplus but would bear none of the loss in the event of a deficit.

It is especially noteworthy, and quite revealing, that during this investigation, no one stepped forward to claim credit and/or responsibility for the primary revenue component underlying the purported self-funding approach – the self-defeating idea that hundreds of millions of dollars could be collected from E-ZPass toll cheats.

According to evidence and sworn testimony, the lack of concern for fiduciary duty during this procurement approached the status of deliberateness. Internal and external warnings of possible financial problems were actively and repeatedly minimized, or ignored altogether, and efforts by skeptical mid-level officials to paint an accurate picture of cost and revenue projections were actively and repeatedly frustrated. Indeed, it is striking that throughout the key phases of this procurement, over the course of more than a year, the purported merits of the project's funding strategy repeatedly were touted, without qualification, in the Consortium's public press releases and pronouncements despite what can only be characterized as a relentless tide of internal skepticism, highlighted by these milestones:

- Although the Turnpike Authority officially was designated the Consortium's lead agency, the Authority's own finance personnel were cut out of the evaluation process in the months leading to the award of the contract. Nonetheless, the Authority's Chief Financial Officer was pressured, virtually at the last minute, to sign off on the purported accuracy of cost and revenue projections underlying the MFS proposal as

presented to the Authority's governing board for approval. She refused to do so because the numbers were not verified.

- When personnel at another Consortium entity, the New Jersey Highway Authority, raised serious questions in a confidential memorandum prior to the contract award about the viability of fundamental violation-revenue estimates, their concerns were set aside, as was their recommendation that a major accounting firm be retained to conduct an impartial analysis.
- Several months before the contract was finalized and executed in March 1998, persistent concern prompted John J. Haley, Wilson's successor as NJDOT Commissioner, to empanel a task force to examine the project's financial structure. This group's work, however, was limited in scope and amounted to little more than an academic exercise in the face of bureaucratic and political momentum to get the deal done.

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The Commission's investigation shows that the E-ZPass project was plagued from the start by a financial shortfall that has only mushroomed with time. As of the end of 2003, nearly \$575 million had been spent on E-ZPass while total revenues from the two primary projected sources – administrative fees collected from E-ZPass violators and commercial leasing of fiber-optic cable – barely topped \$100 million. Further, the bulk of this \$100 million – \$84.5 million – was derived from commercial leasing of the fiber-optic network installed along the toll-road rights-of-way. While it is true that fiber-optic revenue initially tracked original projections, this component was never anticipated to

account for more than one-fourth of the E-ZPass system's overall revenue requirements under the contract.<sup>4</sup> The lion's share of revenue was to have been drawn from violation fees. Through the end of 2003, the violation-fee revenue was projected to total more than \$311 million. In reality, it came in at less than \$20 million – approximately 6 percent of the target. Meanwhile, the system's overall cost continues to mount and is expected to exceed \$1.2 billion when the current contract expires in 2012.<sup>5</sup>

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If some of the essential issues in this report carry an air of familiarity, it is because they mirror those which arose previously in the Commission's inquiry into the state's enhanced motor vehicle inspection contract.<sup>6</sup> Both procurements embodied assiduous efforts to privatize portions of key public services; both, for their type, were unprecedented in scope and cost; and both, once executed, provided a framework for operational failure and profound financial exposure for similar reasons – lack of due diligence, flawed contract documents, manipulation of the bid evaluation process and failure to heed reasonable warnings.

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<sup>4</sup> The total fiber-optic revenue projected through 2008, the original contract expiration date, was approximately \$118.5 million based upon long-term commercial leases that produced the bulk of their yield at lease inception. Thus, even if fiber-optic revenues were to be fully realized as projected, only \$20 million remain to be realized through 2008. This represents an insignificant offset to the burgeoning costs of the toll collection system.

<sup>5</sup> This overall cost projection is conservative and was derived from the sum of the following key elements: \$574.6 million in E-ZPass construction and operating costs through December 15, 2003; \$450 million in projected contractual payments to ACS State and Local Solutions, the current E-ZPass system operator, going forward until the year 2012 at an annual rate of \$45 million; \$205 million in estimated additional interest expense, through 2019; and \$33.3 million in estimated costs associated with various debt refinancings. Additionally, a new contract will have to be negotiated with a vendor to operate the system after the present contract expires in 2012. Further, these estimates do not take into consideration the need for physical improvements, application of new technologies, replacement equipment or further potential refinancing.

<sup>6</sup> See Commission report, *N.J. Enhanced Motor Vehicle Inspection Contract*, March 2002.

Given the enormous amounts of time, money and resources wasted as a consequence of these misbegotten procurements, it is imperative for those in authority to undertake the corrective legislative and regulatory reforms necessary to prevent similar momentous blunders from occurring in the future, starting with an overhaul of the public-project contracting system.

In order to prevent problematic and inappropriate use of the negotiated, professional-service procurement structure, as occurred with E-ZPass, the definition of what constitutes a professional service under the law must be clarified and made explicit.

Further, the combined history of the emissions-inspection and E-ZPass contracts makes plain the inadequacy and ineffectiveness of the existing system for fairly and rationally promulgating and administering public project procurements on that scale. The state, therefore, needs to develop a new system to deal with those unique procurements that, owing to their enormity, their technical complexity, their extreme cost and a host of imponderable issues they present at the outset, require custom treatment and careful oversight. The Governor and the Legislature should establish a special task force to develop such a system and to recommend a practical methodology for implementing it.

Finally, the citizens of New Jersey will have little reason to place full confidence in the integrity of the state's public-project procurement system unless and until the state establishes a central mechanism for applying proper financial and programmatic oversight of the essential contracting process. Under the current configuration of state government, oversight responsibilities for public-project procurements are fragmented among several agencies. The Governor and Legislature should review this structure and either reorganize it or create an independent auditor/comptroller with authority to

establish a centralized system for auditing, monitoring and certifying such complex procurements. The level of mismanagement and manipulation that occurred during the course of both the emissions-inspection and E-ZPass procurements is the best evidence that New Jersey must establish this type of due-diligence watchdog to act in the public's interest.

## ***Mismanagement and Manipulation of the Procurement***

The regional Consortium's E-ZPass project was the largest, most complex initiative of its kind ever attempted in the United States. Many witnesses told the Commission that, as such, it would have presented its architects with daunting challenges even under the most ideal of circumstances. Five large toll-collection bureaucracies with different agendas and priorities spanning the boundaries of three states were thrust into an artificial alliance, some quite reluctantly.<sup>7</sup> Once there, they confronted a tangle of communication, coordination and technical issues that had to be overcome in order to achieve a collective, unprecedented goal. Given the political sensitivity of the toll-paying public to two perennial sore points – cost and convenience – the pressure was on to get the job done, swiftly and economically.

Thus, on the theory that it would bring flexibility and efficiency to a complex, highly technical undertaking, it was determined that the E-ZPass procurement would be treated uniquely, not as a run-of-the-mill capital project, but rather as an integrated set of professional services. This meant that the selection of a vendor could lawfully proceed beyond the normal bounds of competitive public bidding. Interested vendors were

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<sup>7</sup> Members of the New Jersey Turnpike Authority, the then-New Jersey Highway Authority and the South Jersey Transportation Authority, as well as the Commissioner of the New Jersey DOT are all appointed by and serve at the pleasure of the Governor of New Jersey. The appointment of members to the Port Authority of New York and New Jersey is split between the Governors of New York and New Jersey.

According to sworn testimony and documentary evidence, the Port Authority and the then-Highway Authority, operator of the Garden State Parkway, were hesitant to join the Consortium for a variety of reasons. At the time of the Consortium's formation, the Port Authority was already proceeding with its own E-ZPass procurement for bridge and tunnel crossings with Lockheed as the prime contractor. Highway Authority officials, meanwhile, feared their agency would suffer a financial penalty with installation of an electronic system because its toll collection already was heavily dependent upon efficiencies wrought by wide usage of automated toll collection machinery. The South Jersey Transportation Agency, operator of the Atlantic City Expressway, also had unilaterally engaged a vendor (MFS) to install electronic tolls, but SJTA officials nonetheless viewed membership in the Consortium as an opportunity to take advantage of economies-of-scale associated with a larger, centralized back-office administrative operation.

required to fulfill certain benchmarks routine for public procurements, including pre-qualification and submission of responses to a formal Request for Proposals (RFP). But the actual contract award occurred through a hybridized process built around certain practices typical of the private sector, a process in which vendors formulated “best and final offers” (BAFOs) through confidential negotiations with public officials. In the end, the lowest responsible bid was not the principle determinant.

This approach was designed to foster a creative, streamlined contracting process, presumably to the Consortium’s advantage. Instead, driven by an unrealistic schedule and by a single-minded commitment to the notion that E-ZPass could be achieved at no cost – and turn a profit – the negotiated procurement method utilized in this instance became the framework for mismanagement and manipulation. It served to concentrate undue power and discretion over every major activity – from enforcing the schedule to briefing the decision-makers to hammering out the final contract terms – into the hands of a few individuals with little accountability. On another level, it virtually guaranteed that the conduct and substance of meetings, discussions, correspondence and other contacts between public officials, consultants and vendor representatives were veiled from public view. Further, the actual procurement documents were loosely worded on the key issue of funding, the lines of governmental authority over the process lacked clarity, and vendor evaluations were rushed and manipulated.

Ultimately, this procurement was approached in such a way that the combined absence of oversight and transparency produced a contract award recommendation under circumstances that strongly suggest malfeasance.



## **Who Was in Charge?**

As the E-ZPass procurement got under way in late 1995, it was agreed that the New Jersey Turnpike Authority would serve as lead entity on behalf of the regional Consortium. Each member agency would maintain statutory autonomy, devote staff to various advisory committees and participate in an Executive Council established to ensure shared policy-making, but the Turnpike Authority was to be in charge of designing, awarding, implementing and administering the actual contract.<sup>8</sup>

In reality, however, the lines of control over the process were substantially bifurcated and fraught with bureaucratic friction. For significant periods of time – including a critical juncture that produced the contract-award recommendation – the procurement was directed, not by the Turnpike Authority, but by senior officials at the New Jersey Department of Transportation.

The key figure at the outset was then-NJDOT Commissioner Frank J. Wilson. An aggressive manager with extensive experience in public transportation, Wilson joined Governor Christine Todd Whitman's Cabinet in April 1994 from San Francisco's Bay Area Rapid Transit (BART) system, where he had served as General Manager since 1989. When Wilson arrived in Trenton, the subject of upgrading and modernizing toll-collection operations already had been a topic of discussion and study in New Jersey for a number of years. By mid-1994, however, the issue had acquired new urgency. Other states in the northeast corridor, including New York and Massachusetts, already had taken steps to deploy electronic-toll networks, and individual toll authorities closer to

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<sup>8</sup> See Appendix at p. A-5 for letter and formal resolution referencing formation of the Consortium and the Turnpike's participation. The ETC Executive Council consisted of the executive directors of all participating agencies, or his/her designee. Further, the Turnpike Authority Chairman designated one

home, including the Port Authority of New York and New Jersey and the South Jersey Transportation Authority, had embarked on unilateral procurements. Wilson concluded that a broad-based electronic toll project was ripe for development and implementation, and he took the lead in organizing a regional, multi-agency approach to the task.<sup>9</sup> In sworn testimony before the Commission, Wilson validated the accuracy of statements he made before the Assembly Transportation Committee, to wit:

*. . . [T]his project appeared to have all the signs of a project that was ready to go. So we looked at what would be required to take it from the development stage and the demonstration stage to the actual implementation stage. . . . I had a hand in making that decision. . . [and] I took the lead in the outreach to these other entities.*

Wilson's involvement, however, was more extensive than merely lining up members of a regional consortium. Prior to public release of the Consortium's RFP in April 1996, the Commissioner met privately and separately with prospective vendors. He told the Assembly Committee and the Commission:

*I think I spoke with a number of those bidders who came by and wanted to talk to me about their interest in the project, the program, who they were, what they were doing, and to let me know that they were going to be participating in this pre-qualification process . . . which was pretty typical of people who wanted to do business with the state. Letting the Commissioner know that they are interested in the program and wanted to participate.*

Wilson also acknowledged a direct role in shaping the RFP. He advocated the negotiated procurement approach and provided advice and direction on the issue of how

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Turnpike Board member, other than the N.J. Commissioner of Transportation, to serve on the Council in a policy oversight role. The N.J. Commissioner of Transportation served as Chairman of the Council.

<sup>9</sup> Wilson's efforts in this regard were facilitated by the fact that in his position as New Jersey's DOT Commissioner, he was not only Chairman of the ETC Executive Council but also a member of the governing boards of all regional and in-state toll authorities that were to make up the Regional Electronic Toll Collection Consortium, with the exception of the Delaware Department of Transportation.

the document should be structured and presented with regard to cost and funding. He told the Assembly Transportation Committee:

*What I asked was that we make sure the RFP included an opportunity for the bidders to be **as creative as they could be and innovative in terms of how they would price the project.** (emphasis added)*

Wilson said he did so because early in his tenure, he came to believe that the E-ZPass procurement embodied a unique and potentially lucrative money-making opportunity for both the private and public sectors. At the core of this view was recognition that the Regional Consortium, taken as a whole, accounted for more than 40 percent of all tolls paid nationally. Wilson told the committee:

*Because the market was never faced with an opportunity to do a program that would embrace 40 percent of all tolls taken in the nation . . . the general feeling was that that should present some opportunity for vendors to reap rewards that weren't typical from other projects. And the notion was that if those vendors were willing to share that with the state, then we would be able to discover that as part of this procurement. So rather than using the low bid procurement, this was a negotiated procurement, so that conversation could happen around that notion . . . [T]he message would have been is there any way to share the benefits of doing that with the state or with the consortium?*

The objective, Wilson stated,

*. . . was to allow the bidding community to be able to openly present to us options that were available to us. Rather than be prescriptive and tell the vendors how to bid the job, it was done in reverse . . . Here is the technology we want. You tell us what it is going to cost and any other creative, innovative approaches that you have that would either lower the cost or raise the revenue.*

Wilson told the Commission in this regard:

*It was a conscious decision not to dictate terms to the marketplace . . . I made that decision.*

Top officials of Consortium member agencies who participated in the early phases of the procurement confirmed Wilson's direct involvement from the start. Lewis B. Thurston III, Executive Director of the New Jersey Highway Authority, told the Commission that the notion that the system could pay for itself "was the brainchild of Commissioner Wilson."<sup>10</sup> Wilson made it plain, Thurston testified, that the Whitman administration's goal was to undertake E-ZPass without a toll or tax increase:

*I recall him using the phrase 'Trust me' they would find a way to fully fund the project without a need for an increase in tolls. I believe he said, 'I will find a way.'*

James A. Crawford, Executive Director of the South Jersey Transportation Authority, echoed Thurston, telling the Commission in sworn testimony that "self-funding was Frank Wilson's idea." Wilson denied making such a statement to Crawford but conceded that he did make a "commitment" to Thurston to achieve the project without cost to the Consortium agencies, collectively or individually. Wilson testified:

*Yes, that was my commitment to him.*

Wilson also participated at various junctures in the hiring and assignment of certain individuals who assumed key roles in the E-ZPass procurement. A former colleague of Wilson's at BART, Thomas E. Margro, was hired as Chief Engineer of the New Jersey Turnpike Authority in 1995 – at the strong urging of Wilson, according to former Turnpike Authority Commission Chairman Frank X. McDermott. Wilson

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<sup>10</sup> The Commission reviewed contemporaneous notes made of discussion during a December 8, 1995, meeting conducted by Thomas E. Margro, then the Turnpike Authority official in charge of the procurement. The notes were made by Francis K. O'Connor, a Turnpike employee assigned to the project. In those notes, O'Connor recorded, "Wilson feels no [A]uthority pays."

acknowledged putting forth Margro's name for consideration for the job, and as Chief Engineer, Margro's domain was widened to included the task of managing the nascent electronic-toll procurement.<sup>11</sup>

The BART connection surfaced again when NJDOT early in Wilson's tenure retained the services of a California-based consulting firm, Kingston Cole & Associates, to provide advice on transportation issues and initiatives, particularly in the area of advanced technology related to telecommunications and fiber optics. During Wilson's employment at BART, Cole had been hired as a paid consultant to that transit system, and, in one notable project there, helped to broker a deal in which fiber-optic cable was deployed along BART's right-of-way. The private sector partner in that transaction was MFS Network Technologies, which installed the fiber under terms of a capitalized lease program at no upfront cost to BART. MFS ultimately became the successful vendor in the Consortium's E-ZPass procurement based upon a similar \$0-down financing structure funded, in part, by the commercial leasing of fiber-optic cable installed along toll-road rights-of-way. In sworn testimony before the Commission, Cole stated that he was brought to New Jersey at Frank Wilson's behest "to look for ways to make money for the state," particularly in the realm of telecommunications and fiber optics. He stated that Wilson was particularly interested in testing the feasibility of applying the BART model in New Jersey and that he, Cole, traveled the state touting the merits of the public/private partnership approach. As Cole put it in his testimony:

*. . . I was . . . trying to give these guys advice, saying here's what's going on in the country. Here's what the technologies are. Here's how you can do these kinds of deals. . . . Now, when they sat down, whoever they were in the room, certainly enough of them that had*

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<sup>11</sup> Margro served as the Turnpike's Chief Engineer until September 1996, when, in the midst of the E-ZPass procurement, he resigned to become General Manager of BART, the same post previously held by Wilson.

*talked with me at length realized that there is some gold in them there hills. That there's a way to make this thing work and get our system built and pay for part of it. So I was the preacher. So I preached and they listened.*

\* \* \*

**Q.** *How did you become associated with the [New Jersey] Department of Transportation?*

**A.** *He (Wilson) brought a team of people out to BART to look at things. And part of that was BART was so proud of their new public right-of-way partnership deal, that they decided to brief their old leader. And I sat down with staff, and we took them through it. And when it was all said and done, he said, "You know, you ought to think about coming back to New Jersey."*

Cole's business relationship with the NJDOT began with the receipt by his firm of small, non-competitive, sole source contracts. As time went on, however, Cole was positioned for much larger contracts awarded ostensibly through competitive bidding. As the E-ZPass procurement unfolded, his role evolved from conceptual advocate to hands-on mechanic, as he was assigned to assist in the final negotiations leading to a contract-award recommendation.<sup>12</sup>

The hiring of Margro and the retention of Cole were among a chain of events that defined bureaucratic ownership by NJDOT of substantive elements of the electronic-toll procurement. Indeed, Edward Gross, the then-Acting Executive Director of the Turnpike Authority, testified he had no hand in bringing Cole or Margro into the project, or in the hiring of Margro to be Chief Engineer of Gross' own agency. Further, in terms of the line of authority with regard to matters involving E-ZPass, Margro reported, not to Gross or to the Turnpike Authority's governing board, but directly to Wilson. The Turnpike's

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<sup>12</sup> For a more detailed examination of the links between Wilson, Cole and MFS, see the section of this report entitled *A Web of Connections* at p. 70.

existing staff was bypassed again when Margro hired Paul A. Carris, a Port Authority transportation engineer and planner, as his top lieutenant in the procurement. Cole testified that he brought Carris' availability to Margro's attention through Wilson.

In September 1996, Margro announced his intention to resign from the Turnpike to accept an offer to return to BART as General Manager, the post formerly held there by Wilson. Margro was replaced by a career toll-road employee, but with that appointment, the Chief Engineer's job description no longer encompassed the E-ZPass procurement. That responsibility instead was transferred directly inside NJDOT and assigned to David M. Mortimer, one of Wilson's top aides.

A former businessman and Sussex County Republican Party leader, Mortimer had no professional expertise in engineering or accounting, no higher education degree, no experience in toll-road operations and had never administered a large organization. Indeed, when he joined NJDOT as a policy liaison in early 1994, Mortimer's prior government experience consisted of a stint as supervisor of the New Jersey General Assembly's legislative bill room. Several months after Wilson arrived as Commissioner, however, he elevated Mortimer into one of the agency's most senior positions – Chief of Staff – with direct responsibility over the day-to-day operations of one of New Jersey's largest state-agency bureaucracies.

In September 1996, the scope of Mortimer's duties was expanded still further when Wilson assigned him to replace the departing Margro as chairman of the E-ZPass project's core procurement mechanism – the Multi-Agency Evaluation Team (MET), a unit established by the regional Consortium to assess and score vendor proposals and to

make a contract-award recommendation. Wilson testified that he selected Mortimer, in part

*[b]ecause he had the same qualities and abilities to administer – he had the same capabilities that Tom Margro did in terms of administrative capabilities to keep a project like this intact and moving. . . . I wanted to be sure that now that we [were] in the middle of this program with Tom leaving that I had someone whose ability I could rely on and I knew would carry it out.*

With Mortimer's transition into the role of MET Chairman, the procurement entered a critical phase on a fast track. The two Turnpike Authority staffers who had been assigned primary roles in the project to date – Carris and Francis K. O'Connor, a Turnpike Authority employee assigned to the ETC project under the title of Special Project Control Administrator – were abruptly transferred to NJDOT's Ewing Township headquarters outside Trenton. Written guidelines were issued establishing the Consortium's clear preference for contract proposals that would enable E-ZPass to pay for itself. With Mortimer presiding, Consortium officials met privately and separately with representatives of the vendor teams led by MFS and Lockheed to formulate and revise best and final offers. Then, just hours after their receipt by the MET team, the vendors' final offers were evaluated under Mortimer's supervision at a scoring session held in a conference room adjoining the Commissioner's suite of offices at NJDOT. MFS emerged as the winner.<sup>13</sup> The date was October 10, 1996. Thus, within barely three weeks of Mortimer's first official day as the MET chairman – September 20 – the evaluation team delivered a contract-award recommendation. Subsequent to the MET recommendation, Mortimer also served as the lead figure in a series of presentations to

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<sup>13</sup> For a detailed examination of the circumstances surrounding the vendor evaluation and scoring process, see the section of this report, *A Questionable Evaluation*, at p. 55.



the Consortium's Executive Council and to various governing boards of the Consortium's member authorities. These presentations, highlighted by a PowerPoint computer slide show, delineated the purported merits of the MFS offer versus that submitted by Lockheed and served as a basis for the ultimate contract award.

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It is noteworthy that although the Commission confirmed through documentary evidence and sworn testimony from multiple witnesses that NJDOT eclipsed the Turnpike Authority in this critical phase of the E-ZPass procurement, several of the key players – Mortimer and Wilson on one hand and Gross on the other – provided thoroughly contradictory sworn testimony.

Mortimer told the Commission at various junctures that during the period in question, September-October 1996, he and Gross

*. . . had frequent contact, and it was of substantive matters.*

\* \* \*

*. . . I would talk to Ed about time lines. I would talk to him about issues that were being . . . raised among the Consortium members and how they were being disposed of.*

\* \* \*

*. . . Ed was the guy I would go to and talk to and strategize with about how do we address this issue, what do you recommend, what other issues; so it would have been about equipment, about structure, about schedule, about budgets . . .*

Wilson testified:

*. . . Ed Gross had a little more responsibility for the day-to-day business of the transaction that was going forward principally because his organization, agency, was going to lead the Consortium.*

Gross, meanwhile, swore that he played no “substantive” role in the procurement until after November 15, 1996. On that date, Gross issued a written opinion setting aside an administrative protest that had been filed by Lockheed challenging the MFS contract-award recommendation. Until then, Gross testified,

*I did not play a role whatsoever in the terms and conditions of the procurement, in the process of review, and in the scoring. The only thing I did was I was supportive. You know, as the staff was needed to support the process . . . the Turnpike staff was always available to perform whatever was needed for the review committee, but I did not do anything of a substantive nature.*

\* \* \*

*I don't even recall having a conversation with Dave Mortimer in connection with the procurement process other than I think he was the one that called me and told me that in 24 hours he wanted Paul Carris and Fran O'Connor to leave the Turnpike offices and temporarily go to the DOT facility and work out of there.*

\* \* \*

**Q.** . . . [B]etween . . . August of '96 . . . and October or November 1, '96 . . . do you remember having any conversations with Dave Mortimer other than the one you testified to about moving Carris and O'Connor; conversations related to soliciting your opinion or input on any decisions that he made or that were made during that time period in relation to the procurement?

**A.** Absolutely not. It didn't happen.

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Gross further testified it was his belief that Mortimer's assignment as MET Chairman, along with the transfer of Carris and O'Conner to NJDOT, was part of a concerted strategy to "make sure that I didn't get involved in the procurement process . . . ." Gross stated that he and Wilson "didn't have a very good professional relationship" at the time due, in part, to a dispute over privatization. According to Gross, the Commissioner had proposed expanding the procurement to include turning over the entire toll-collection operation to one or more private vendors, something Gross opposed. Gross stated he took the matter to the Governor's Office where Governor Whitman, after listening to both sides, vetoed the plan. With that, Gross testified, Wilson "hardly talked to me from that day on."

In his testimony, Wilson recalled "discussion" surrounding this issue of toll-collection privatization but could not remember if he attended a meeting on the issue with Gross and Governor Whitman. As to Gross' claim that he had little to do with the E-ZPass procurement process leading to the contract-award recommendation in the fall of 1996, Wilson testified:

*Q. Would it surprise you to learn that Ed Gross informed the Commission that he had no active role in the procurement of E-ZPass until the Lockheed protest of November of 1996?*

*A. The question is would it surprise me?*

*Q. Yes.*

*A. I'd be surprised.*

## **Wilson’s “Recusal”**

One extraordinary and untoward event that occurred during Wilson’s watch as NJDOT Commissioner was his acceptance of a job offer from an engineering company that not only had done considerable business with the State of New Jersey in its own right, but was also a corporate relative of a firm that was part of the original MFS contracting team. The firm that hired Wilson – Daniel, Mann, Johnson and Mendenhall (DMJM) – was one of several private-sector concerns with which Wilson engaged in employment discussions during the E-ZPass procurement.<sup>14</sup> The circumstances surrounding these discussions, particularly with regard to Wilson’s purported recusal from the procurement process at a critical juncture, raise serious questions about the integrity of that process and the manner in which it was administered.

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On August 19, 1996, Wilson told staff of the Executive Commission on Ethical Standards (ECES) that he had been approached by several firms inquiring about his availability for possible employment. He was instructed by ECES to notify his supervisor, Governor Whitman, of the identity of the companies and to specify that henceforth he would recuse himself from any involvement with them. In a letter dated August 20, 1996, Wilson identified the firms in his letter as “AECOMM”, Booz, Allen & Hamilton and Dames & Moore and advised Whitman that, effective immediately, he intended to avoid any business dealings with them, “including but not limited to actions,

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<sup>14</sup> In April 1996, DMJM was awarded a primary engineering consulting contract from NJ Transit for the Southern Jersey Light Rail Transit System. This contract, including additional work orders subsequently approved by NJ Transit, eventually was worth more than \$90 million. At the time of the award, Wilson, as NJDOT Commissioner, was a member of the NJ Transit Board.

decisions, considerations, discussions etc.”<sup>15</sup> At the same time, he designated Deputy Transportation Commissioner Sharon L. Landers to handle any matters that might arise concerning the firms. Because Wilson, as NJDOT Commissioner, also served on the governing boards of NJ Transit, the Port Authority of New York and New Jersey, the New Jersey Turnpike Authority, the New Jersey Highway Authority and the South Jersey Transportation Authority, he sent identical notices to those agencies.

In his letter of recusal, however, Wilson did not mention any subsidiaries of the listed companies. Besides Booz, Allen & Hamilton the firms that had approached him about possible employment were DMJM, part of the AECOM corporate group, and the firm of O’Brien-Kreitzberg and Associates (OBK), a subsidiary of Dames & Moore. At the time, all had active contracts either with NJDOT or with other agencies of government with which Wilson was affiliated as Commissioner. Further, DMJM was a corporate sibling of Frederic R. Harris Inc., another AECOM subsidiary that was, at the time, a subcontractor on the team assembled by MFS to seek the regional Consortium’s E-ZPass contract.<sup>16</sup> Meanwhile, Booz, Allen & Hamilton was associated with the Lockheed team in the E-ZPass procurement.

When he appeared before the Commission under oath during this investigation, Wilson testified that he used the names of holding companies rather than subsidiaries in his letter of recusal on the theory that it would provide the broadest notice of his intent to

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<sup>15</sup> See Appendix at p. A-8 to review a copy of Wilson’s recusal letter. In it, he erroneously identified as “AE Comm” the firm with which he intended to avoid business dealings. The correct firm was AECOM, whose full corporate name was AECOM Technologies Corp. AECOM and AE Comm are separate and unrelated business entities.

<sup>16</sup> On November 26, 1996 – after a formal recommendation had been made to award the E-ZPass contract to MFS – MFS advised the Consortium that its engineering subcontractor, Frederick R. Harris, Inc., voluntarily withdrew from participation in the procurement. Frederick R. Harris, Inc. and Daniel, Mann, Johnson and Mendenhall (DMJM) have since merged as a single entity within the AECOM corporate group.

avoid even the appearance of any conflicts of interest. Wilson stated that persons familiar with the transportation and infrastructure engineering industries would know the component companies associated with AECOM and Dames & Moore. He testified:

*Q. . . . [W]hat caused you to [cite] the parent company as opposed to writing the parent company and all the subsidiaries that are part of that parent company in your recusal letter?*

*A. . . . I was talking to one company, DMJM. If I had written DMJM down, that meant I could have dealt with any issues dealing with the other subsidiary companies because I didn't recuse myself from them. So I felt the broader recusal was to list the parent company which would embrace all the companies that are under them. I mean, I never gave it a thought to list 10 operating companies here, nine of which I wasn't talking to at the time.*

*Q. But those nine operating companies could be having contact with the DOT during this time period. . . . [W]hat caused you to write . . . AECOM . . . instead of AECOM subsidiaries . . . [and] put people more on notice of what companies you are recusing yourself from?*

*A. It just – you know, I felt I was doing that by listing the parent company.*

*Q. But . . . [do] you think Governor Whitman, use her as an example, Governor Whitman knew that Daniel, Mann was a subsidiary of AECOM?*

*A. I don't know what Governor Whitman knew or didn't know.*

*Q. . . . Do you think anyone reading this letter would know that Daniel, Mann was a subsidiary of AECOM?*

*A. Yes.*

*Q. They would?*

*A. Yes.*

*Q. How would they know that?*

*A. People in the business know who owned companies. I mean, it may not be common knowledge to a layperson, but people in the industry certainly know who owns whom.*

Wilson testified that he did not become aware of links between any of the firms listed in his recusal letter and the E-ZPass procurement until September 3, 1996 – two

weeks after circulating the document. On that date, he attended a meeting with the three officials then engaged in central roles in the procurement: Margro, Carris and Mortimer.<sup>17</sup> According to the participants, the session opened with a discussion of the schedule and timeline for the procurement and then turned to the fact that two vendor proposals had been received by the Consortium. Although these proposals had been submitted more than one month prior to this meeting, Wilson testified that he, as NJDOT Commissioner – with his own agency orchestrating the procurement and Margro reporting directly to him – was not aware at the time of the vendors’ identities or any terms of their proposals. Wilson stated that only when the names were mentioned during this meeting did he realize that the E-ZPass procurement fell within the scope of his recusal. With that, he testified, he abruptly terminated his involvement in the meeting, told the others that henceforth he was not to be involved in the process and left the room. Mortimer testified that, despite his role as a top aide to Wilson, this was the first time he learned of his boss’ recusal. According to Carris, the meeting unfolded as follows:

*. . . We were going to be updating Mr. Wilson on the status of the procurement, on the – where we were schedule-wise. I had prepared a document which was a comparison of the proposals which had been done to date that was by no means complete, with the intention of going through that. We got to the meeting and after discussing the process issues, schedule issues, when I got to the point of going into that presentation I was – Commissioner said, I can’t look at this, and basically the meeting was concluded so I never got to share the material.*

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<sup>17</sup> Wilson could not recall whether the venue for this encounter was a meeting or a telephone conference call. Mortimer, Carris and Margro each recalled a meeting held at NJDOT headquarters.

The Commission's investigation shows that subsequent to the September 3 meeting, Wilson continued to engage in contacts and discussions with individuals directly involved in the E-ZPass project on matters that bore directly upon the procurement.

One such contact occurred during the week of September 16, 1996, when Wilson participated in a conference call with Mortimer, Margro and Carris. It is not clear who initiated the call. Mortimer told the Commission that during this conversation, Wilson was briefed on the status of the procurement schedule and on the preparation of guidelines that were to be issued by the Consortium for use by the vendors in preparing best and final offers (BAFOs). The participants testified that the discussion also dealt with the prospect that the project could generate revenue and the possibility that it could pay for itself. As it turned out, the BAFO guidelines – issued just four days after this conference call – informed the vendors that the Consortium's preference was for contract proposals that would enable the E-ZPass project to be self-funding.

When Mortimer appeared at the November 1996 Lockheed protest hearing, he testified that on September 16, 1996, he, Margro and Carris spoke to Wilson in a telephone conference. During the call, they briefed Wilson on the time-line schedule and the BAFO guidelines that were being prepared for distribution to both Lockheed and MFS. They advised Wilson that they believed the procurement could be self-funding and might even generate revenue to the Consortium. According to Mortimer, Wilson responded to the effect – go for whatever you can get.

Carris testified:

*. . . I remember Wilson using words very carefully that could easily allow someone to say, Oh, he wants zero down, zero payment, and no cost. But he did not use words that explicitly said that.*



- Q.** *What do you mean when you said he used his words very carefully?*  
**A.** *That's that – I was listening very carefully and what came out of that was is, he never actually said or directed us to make it zero cost.*

\* \* \*

- Q.** *Do you remember Wilson making a statement, “Go for whatever you think you could get,” during this telephone call?*  
**A.** *Yeah, okay. Yes.*

In his testimony, Wilson stated the call was initiated by Mortimer, Margro and Carris. He stated he was under the impression at the time that the purpose of it was to update him on the procurement schedule and to discuss process issues related to the MET chairmanship transition from Margro to Mortimer. Wilson testified he did not know that the issue of self-funding would arise. Indeed, he testified that, despite his then-longstanding belief that the project should not cause the Consortium agencies to incur any direct upfront costs – this was “the first time I heard the notion that this thing could be self-financed . . .” :

*That I wanted it, that I demanded it, well, then, that's the message that they took from it; but I was advised that based on the work of this procurement, not vendor specific, not time specific, not terms and conditions here; but it appears as if under this option approach . . . that this could be self-funding. That's the first time I heard of the concept of we can get it all paid for. I said if you are able to that, well, then, fine, you know, get the best deal you can for the consortium.*

Carris interpreted Wilson's comment to be of a discretionary, not mandatory, nature. Carris, using his own interpretation, drafted the September 20, 1996 BAFO language as follows:

*Based upon discussions and interaction with the MFS/Chase Team over the last several weeks, it is the opinion of the Consortium that this program will be self-funding by the proposer. The Consortium believes that the system and services it seeks to acquire will be provided at no*

*cost to the Consortium and may, in fact, generate revenue in excess of costs based on the composition and structuring of your BAFO.”*<sup>18</sup>

Carris’ interpretation, however, was not shared by his colleagues. Mortimer and, to a lesser extent, Margro, criticized the language. Carris testified that Margro and Mortimer both believed the proposal had to be self-funded. Further, Carris categorized Mortimer as a “hard-liner” when it came to the \$0 down, \$0 payment approach. Carris opined that Mortimer based his opinion on his interpretation of the Wilson conversation. Prior to releasing the guidelines, Carris also sought the opinion of Ed Gross, who agreed with the language.

Wilson testified that his participation in this discussion was proper because it dealt with the overall programmatic aspects of electronic toll collection – something that, despite his recusal, he had a continuing obligation to monitor as NJDOT Commissioner – and not with the specifics of the procurement *per se*. Wilson testified:

*. . . [M]y recusal, in my view, and hopefully the view of everyone involved in the process [was] that I’m not to be involved in the selection, ranking, scoring and award of the contract to any of these vendors, but it did not include [abrogation] of responsibilities for schedule policy issues, I retained that. And I thought I did an adequate job in telling people what I was involved in and why, and what I was not involved in and why.*<sup>19</sup>

The record reflects that Wilson again participated in discussions relative to the procurement schedule in early October, just days before the vendor proposals were to be scored. In this instance, a portion of the discussion was initiated by Wilson himself,

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<sup>18</sup> Lockheed Martin received identical September 20, 1996 BAFO language. See Appendix at p. A-12.

<sup>19</sup> In his appearance before the Assembly Transportation Committee on June 10, 2002, Wilson testified that he understood that his recusal meant, “... I at that point could not have any further conversations with anybody directly involved with that, including people on my staff.”

although in sworn testimony before the Commission, he sought to leave the opposite impression:

**Q.** . . . *[W]ould it have been appropriate for you actually to actively participate in making calls yourself asking about procurement schedules and deadlines?*

**A.** *No.*

\* \* \*

*I don't recall ever making any calls, because I thought I adequately described to everyone involved that I simply needed to know, as a default mechanism, when you're off track, let me know. If we're on track, fine, then I'm working with the schedule that we have and I'll operate against that. So there is no reason for me to be calling in and asking, you know, these questions routinely . . . .*

On October 8, 1996, Wilson placed a telephone call to Mortimer at the behest of a Lockheed executive, Amy Rosen, who at the time was serving as a member and Vice Chair of the NJ Transit Board of Directors. The call coincided with a meeting scheduled the same day between Lockheed representatives and Consortium officials to set the stage for submission of a final E-ZPass proposal. A similar meeting was to be held the following day, October 9, 1996, with MFS executives. On October 10, both vendor proposals then were subjected to final evaluation and scoring by the MET team. Wilson testified that he reached out to Mortimer

*. . . because it was a very pointed question that I was asked about the schedule and whether or not it was being delayed. And I had no knowledge or any awareness that there was a delay, but I couldn't be sure, and maybe there [were] things happening that I was not aware of. So it was just a call, I asked my [office] to find Mr. Mortimer . . . and simply asked him whether the program was going ahead according to schedule that I had. And he indicated that it was.*

\* \* \*

Q. . . . Who raised the question of the schedule with you that caused you to make the phone call?

A. It was an executive from Lockheed.

Q. Why is the executive from Lockheed contacting you?

A. I have no idea.

\* \* \*

Q. Amy Rosen is the vice chairman, New Jersey Transit board of directors?

A. That's correct.

Q. She's also an executive from Lockheed?

A. Correct. I thought it was strange.

Q. Okay, so what happened in this conversation?

A. [She] simply said we are meeting today and is the schedule – some material change in the schedule, is my recollection. And I thought she asked are we meeting today, like the Transit Board. And I said, no, we don't have a meeting today. Can you please check, I'm missing this point. I think the procurement group is meeting today. And I had heard that we've got a problem with the schedule. I said, I'm not aware of it, I have no knowledge of it. I assume the schedule is okay, but I'll check on the schedule. That was the reason for the call to Mr. Mortimer.

Q. Well, certainly, Ms. Rosen knows she is the executive of Lockheed, correct?

A. I think so.

Q. And she, certainly, knows that Lockheed is involved in the E-ZPass procurement, correct?

A. I think so.

Q. And you already said she had a copy of this August 20 [recusal] letter?

A. I think so.

\* \* \*

Q. . . . [D]id you think [it] inappropriate that she's contacting you directly inquiring about anything about E-ZPass after receiving this letter from you?

A. My initial reaction was once I understood the meeting she was referring to was not us meeting at the Transit Board, you know, this

*happens in an instance when she's asking about a meeting of the group was to be a little concerned; but then as soon as she said why she was calling, I didn't have any issues. She was just asking is the schedule being materially [a]ffected. And I didn't ask her why she wanted to know or what the purpose was. It was a schedule issue, fine, I'm dealing with it. I told her I didn't know about any schedule problem, of any delay or acceleration, but I'll check. And then she said, fine, thank you, good bye. And hung up.*

**Q.** *Did she attempt to call Ms. Landers prior to calling you?*

**A.** *I don't know.*

**Q.** *Did you at any time during that conversation indicate to her that she should be contacting Sharon Landers on these issues?*

**A.** *On the issue of scheduling, no, I did not.*

**Q.** *Your testimony is that any conversation relating to scheduling or deadline is not part and parcel of your recus[al]?*

**A.** *I didn't believe so.*

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During the period in which these contacts occurred, Wilson engaged in out-of-state employment interviews with the firms whose recruitment efforts had prompted his purported recusal. Following an initial meeting in Los Angeles on August 26, 1996, with the president of DMJM and the chief executive officer of its parent company, AECOM, Wilson traveled again to Los Angeles for a September 18 meeting that focused on prospective job responsibilities and compensation. Subsequently, in a letter dated October 24, 1996, DMJM sent Wilson a letter formally extending a job offer. During the same period, Wilson traveled to Virginia to meet with executives of Booz, Allen & Hamilton and to Los Angeles for discussions with representatives of OBK/Dames & Moore. Wilson turned down subsequent employment offers from those firms. On November 21, 1996, he accepted the DMJM offer. Wilson officially resigned his post as NJDOT Commissioner on December 27, 1996.

Wilson's August 20, 1996 recusal letter clearly designated Deputy Commissioner Landers to act in his stead with regard to the companies linked to his job search. Landers, however, told the Commission that she did not participate in matters related to the E-ZPass procurement, including the vendor evaluation process. Moreover, Landers stated that between the critical period of late September and October 10, 1996 – when a contract-award recommendation was made – Mortimer would have been on his own reporting directly to the Consortium. Landers stated that she had general supervisory responsibility for

*some of the things Dave might have done, but I don't, I never got involved in the procurement. So, I basically, I would say he was, he was in charge of that aspect of it reporting directly to the Consortium at that point.*

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Wilson's selective treatment of his own recusal is troubling in its own right, but it is part of a broader area of concern with regard to real and potential or perceived conflicts of interest involving top officials of state government. In this instance, New Jersey's chief transportation official placed himself in a position that ultimately required him to resign and walk away, in midstream, from the largest and most complex transportation project in the state's history – following closely on the heels of the project's senior manager, Thomas E. Margro. As a vivid illustration of how his own abrupt departure may have affected the course of the E-ZPass procurement, the Commission noted Wilson's own testimony before the Assembly Transportation Committee on June 10, 2002. During that appearance, Wilson expressed an opinion about the importance of risk

assessment and of securing a proper public/private balance in the assignment of risk in procurements. He stated:

*We heard a lot of testimony this morning about a private sector vendor coming to the state and saying it needed to accept risk. Well, you can just as easily turn that around. The bidders that bid to us were considerable bidders with considerable resources. And the state could easily have said to them, you accept the risk. It's your balance sheet exposed.*

*And so if you are uncertain about – if you really are uncertain about what you've just been offered, then you simply say to the vendor, if you are that secure in what you've offered, then you step up and take the revenue risk or the cost risk.*

*And those things are done routinely in many agencies that I have been in. And currently, clients will do that to us. Because whether they have questions or have doubts or not, they will put the risk on the private sector.*

\* \* \*

*I personally would never have taken that kind of risk, give me a guaranty.*

Wilson then responded specifically that he would not have approved the shift of the vendor risk to the state:

**Q.** . . . *[I]f you were approached or if you were asked to approve something that required a guaranty, you would have said no. Is that correct?*

**A.** *Absolutely correct.*

In this instance, however, the Commission's investigation shows that the financial risk associated with the E-ZPass project was specifically shifted by MFS to the Consortium in late September and early October 1996, while Wilson was Commissioner of Transportation.<sup>20</sup> Accordingly, had he not "recused" himself during a critical juncture

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<sup>20</sup> See Appendix at p. A-9 to review a copy of October 10, 1996 letter faxed from MFS in which the firm stated that the Consortium would need ". . . to provide assurance that it will underwrite its financial performance over the project life."

in the procurement, this shifting of the full risk to the Consortium may, based upon his own words, never have come to pass.

The fact that this occurred at all – let alone amid circumstances suggesting a conflict of interest on Wilson’s part – demonstrates the need for statutory and/or regulatory mechanisms to ensure proper oversight and accountability by government agencies whose top officials, through their own actions, place personal ambition potentially at odds with the public interest.

### **Flawed RFP/Flawed Methodology**

The E-ZPass procurement was built around a formal Request for Proposals (RFP) issued by the Consortium on April 12, 1996. The intent behind this voluminous document was to give the vendor community a clear picture of the nature and scope of the electronic toll project and to set forth guidelines and specifications for the development and submission of contract proposals. At its root, the E-ZPass RFP was framed as a “performance-based” or “functional” procurement document, meaning that rather than delineating with great specificity how the actual job should be done, vendors were given flexibility to devise strategies for accomplishing key goals according to a fixed procurement schedule.

According to the official who supervised production of the RFP – Paul A. Carris, the ETC Program Manager for the New Jersey Turnpike Authority – the ambitiousness of that schedule was exemplified by a stringent deadline imposed for issuance of procurement materials by his office. Carris testified that when he took the assignment in early January 1996, he received unusually blunt instructions to issue a Request for



Information/Request for Qualifications (RFI/RFQ) within four weeks for consideration by prospective vendors. In his testimony, Carris could not recall why there was such a rush, but he did manage to issue the RFI/RFQ on January 29, 1996. These documents preceded the RFP, and were used to help draft it. The Commission found that even before the RFP hit the street, however, questions arose about its structure and clarity. Also, subsequent to its release, the document was altered in a number of substantive ways by a series of amendments adopted by the Consortium even as prospective vendors worked to finalize their proposals in response to it. Further, as ultimately written, the RFP afforded little protection against, and indeed may actually have provided a basis for, mismanagement and manipulation of the procurement process.

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During group meetings prior to the issuance of the RFP, some vendors and Consortium personnel expressed concern that the project appeared, at least in outline form, to be so large as to make a single procurement both untenable and unmanageable. It was suggested during these discussions that the procurement be broken into pieces so that vendors with particular expertise in discrete areas – construction, systems management, administrative operations and others – could bid separately and selectively on contracts governing each component. As ultimately structured, however, the RFP – calling as it did for a singular “DBOM,” or design, build, operate and maintain package – effectively required vendors to form teams because none had the capability or wherewithal to submit a credible response unilaterally. Charles D. McManus, then-Chief Engineer of the New Jersey Highway Authority and a member of the vendor

evaluation team, was among those who worried that this approach would squelch vendor participation, particularly in light of the ambitious schedule laid out – vendor responses were to be due within 90 days. McManus testified:

*My suspicions were aroused by the minimal competition caused by the size of the bid request. I thought that was crazy.*

Of approximately one dozen pre-qualified vendors who attended the initial pre-RFP meeting in January, only three actually submitted bids: Chase Manhattan Bank N.A., Lockheed Martin IMS Corp. (Lockheed) and MFS Network Technologies (MFS). Ultimately, Chase Manhattan joined the MFS team, which, along with a separate group put together by Lockheed, were the only vendor teams to prepare and submit proposals.<sup>21</sup>

• • •

Just weeks prior to the proposal submission deadline for vendors, the RFP was altered in a number of crucial areas, including the criteria to be used by the Consortium in the vendor evaluation process.

In its initial rendering, the RFP ranked technical skill as the foremost evaluation criterion, followed by experience, cost, management, personnel and facilities, in that order. On July 5, 1996 – three weeks before the July 26<sup>th</sup> submission deadline for vendor proposals – the order of importance of these evaluation criteria was abruptly reshuffled. An addendum elevated “cost” from third to first, followed by technical skill and so on.

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<sup>21</sup> Lockheed’s team consisted of Syntonic Inc.; Parsons Brinckerhoff; Booz, Allen & Hamilton; Daidone Electric; RBT/Strum; First Union Bank; Bell Atlantic ; Alphatech; AAA (NJ Clubs); and NJMTA. The MSF team consisted of Fredrick R. Harris Inc., Chase Manhattan Bank, Vollmer & Associates, U.S. Public Technologies Inc., and TMCS Inc.

According to Carris, this change was imposed from the top down under the direction of Wilson and Margro and had a significant impact on the procurement because the central focus was now shifted from nuts and bolts to money. Carris testified:

*Q. As a participant in the process, did you have an issue or a problem with elevating cost at this point?*

*A. I did. I had an issue with just changing the criteria midstream, because I wasn't clear how we were going to make this happen without problems.*

*Q. How do you think it affected the procurement?*

*A. Significant way.*

*Q. How significant?*

*A. It shifted the emphasis from the technical solution, which the engineers were more concerned about, to the creativity of the options. And it also then put us in a position of having less apples to apples comparison.*

*Q. So obviously then it became more subjective when you're saying less apples to apples.*

*A. Yes.*

Even as cost emerged as the chief criterion upon which vendor proposals were to be evaluated and scored, the RFP remained vague as to how the issue should actually be approached and framed. Consistent with the fundamental notion advanced early on by Wilson that the E-ZPass procurement be exploited, if possible, for revenue to the benefit of both the public and private sectors, vendors merely were instructed to be creative on financing and to be open to the prospect of negotiating the final terms of their proposals. A key section of the RFP, entitled "Proposal Procedures, 1.0 – Requirements and Conditions for Proposals," stated, in part:

*The procurement of the new toll collection systems and customer service center operations will be a multi-step, negotiated procurement*

*process where technical experience and competence will be evaluated in conjunction with the price for the work under this Contract. Furthermore, the procurement process will include evaluation and negotiation of proposed financial and work scope options and innovations or other business opportunities presented by the Proposers that make their Proposal more attractive to the Consortium. These options can take the form of added value, revenue that offsets capital and operations costs associated with the services and materials provided under this Contract, or other initiatives that could produce revenue opportunities for the Consortium.*

At Section 9.07, prospective vendors were urged to develop “options” that would bring “creative financial innovations” to the performance of the contract:

*Proposal options shall be prepared and submitted to reflect any financial alternatives that may be proposed to provide ‘added value’ to the [Consortium]. Such financial alternatives can include, but are not limited to, financing options, public/private partnership, surcharges and other creative financial innovations.*

This section further stated, again in general terms:

*The Proposer may offer technical options that, in general, provide ‘added value’ to the [Consortium] for this project. ‘Added value’ can include offsets to the project capital and/or operational costs, cost savings for materials or services, revenue generation, and similar financial returns while maintaining the core project elements and specified functionality and performance criteria.*

Beyond this language, the RFP specified only one mandatory option that prospective vendors would be required to submit as part of their proposals – a so-called “Smart Card” component. Various witnesses told the Commission that this requirement was inserted at Wilson’s insistence on the theory that Smart Card technology, designed to provide consumers with a single credit-card-type transaction device to handle everything

from electronic tolls to banking and shopping, eventually would become a substantial revenue generator for the state.<sup>22</sup>

Beyond Smart Card, however, the RFP spelled out no explicit standards against which individual vendor proposals could be measured on cost and financing, no objective means to gauge the reasonableness and suitability of funding options and no methodology to ensure that the proposals could be accurately and meaningfully compared to one another. Carris told the Commission the RFP was drafted in such a way as to make it “very challenging” because it contained no mechanism to ensure that competing vendor responses could be subjected to a clear “apples to apples” comparison. Carris stated “there was a lot of judgment trying to decipher what we were getting and then balancing that against the other proposals.” Further, the RFP was silent as to how risk and liability would be apportioned between the Consortium and the vendors if a given funding strategy collapsed. All of these matters were left to be defined through negotiations, an exercise marked by extensive behind-the-scenes revision and recalculation that continued, literally, until just hours before the vendor proposals were scored and a contract-award recommendation was made.

After submitting initial proposals, representatives of the MFS and Lockheed vendor teams made oral presentations and then met separately and privately with Consortium officials during the first two weeks of September 1996. No official record of these discussions exists because no minutes were kept, but participants told the Commission that the Consortium, through the person of its lead negotiator, David M. Mortimer, was increasingly insistent that the proposals be structured in such a way as to

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<sup>22</sup> At the time, Smart Card technology was still in its infancy.

minimize up-front costs and maximize long-term revenues. Pursuant to those goals, the sessions focused heavily on two options that had already been topics of informal discussion within the Consortium for months: the possibility of drawing substantial revenue from toll violators and from the sale or lease of fiber-optic cable installed along the toll-road rights-of-way.

In sworn testimony before the Commission, Donald E. Mauer, then-Chief Engineer of the South Jersey Transportation Authority and a member of the Consortium's vendor evaluation team, summarized the evolution of this unique process:

*The original offerings from MFS and Lockheed said here's the cost to build this. And then discussions and negotiations ensued, and then we called it a best and final offer and then a revision to that best and final offer. Each time those revisions occurred, the concept was to go from the [Consortium] paying the cost of the job to this new theme of some type of creative financing that would allow the [Consortium] not to pay the cost of the job, and ultimately never to pay the cost of the job because it was self-funded.*

*So the first offering that came from the vendors was conventional. Build this, give me this much money for it. The second offering came in with an additive of fiber optic revenue and the additive theme of violation enforcement, administrative penalty collection. Fiber optics was an add-on. There was no fiber optic [leasing] in the core bid. There was a communication link [to] all the toll plazas . . . but never a fiber optic communication backbone for revenue resale.*

*. . . So they were brand-new concepts. They showed up during the period of time after the original proposal was received but during the course of the evaluation by the MET team that these were revenue enhancers.*

On September 20, 1996, MFS and Lockheed were formally advised that self-funding was to be considered the favored approach as each prepared a best and final offer (BAFO).<sup>23</sup> According to the text of a letter bearing that date to both vendors from Carris,

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<sup>23</sup> See Appendix at p A-12.

*The Consortium believes that the system and services it seeks to acquire will be provided at no cost to the Consortium and may, in fact, generate revenue in excess of the costs based on the composition and structuring of your BAFO.*

This document, which set forth official “BAFO guidelines” to be followed, triggered a flurry of facsimile exchanges, telephone calls and meetings as the vendors amended and re-amended their proposals amid consultations with the small group of Consortium officials led by Mortimer. At one point in this frenetic process, according to witnesses, the thickening alphabet soup of acronyms became a source of some amusement as BAFOs, upon revision, came to be referred to by the participants as BARFOs, or “Best and Really Final Offers.”

It is noteworthy that even after the Consortium, through Carris’ September 20, 1996 letter, had put in writing its clear preference for a project framed in such a way as to pay for itself at no cost to the toll authorities, neither of the two prospective vendors advocated a self-funding approach. Indeed, Lockheed never submitted a proposal built completely around self-funding; the firm, even in its BARFO, adhered to the notion that the Consortium would have to invest at least some money at the outset in order to make the project viable. As to MFS, although the firm ultimately did propose a financing structure designed to meet the \$0 down, \$0 payments goal – and won the contract largely as a result – its representatives repeatedly advised the Consortium that they preferred an alternative that would provide “budget certainty” via some level of expenditure by the toll authorities in the early years of the project.<sup>24</sup>

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<sup>24</sup> See Appendix at p. A-14.

Early in October 1996, after it became apparent that neither vendor's BAFO satisfied the Consortium's zero-cost mandate, their representatives were summoned to separate private meetings and told to re-visit their drawing boards to crunch the numbers one more time. On October 8, 1996, with Mortimer presiding, Lockheed executives were instructed to submit final revisions no later than midnight. The following day, again with Mortimer in charge, representative of MFS received similar instructions. The following morning, MFS faxed a final offer that incorporated a new series of "expanded service options" dramatically boosting the revenue projections associated with the firm's initial contract proposals. Virtually overnight, the MFS net revenue projections for violation fees, fiber optics and other options for the proposed contract grew from approximately \$59 million to \$297 million, an increase of \$238 million, or more than 400 percent. This revision was significant in the procurement because MFS was now positioned more positively than Lockheed. Only days earlier, as of the October 2, 1996 BAFOs, Lockheed had projected combined net revenues of approximately \$150 million compared to \$59 million from MFS. By October 10, Lockheed's revenue projection had only increased to approximately \$196 million.<sup>25</sup>

The dramatic increase in MFS's revenue projection was subjected to no meaningful scrutiny by the Consortium. Carris testified that "outside of just a general discussion, I don't believe there was any extra effort made to vet these numbers." Moreover, although the MFS proposal included \$148 million in additional revenue projected via an expanded fiber-optics option, the proposal was not forwarded to the Consortium's fiber-optics consultant for comment. MFS's revised final offer also

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<sup>25</sup> See Appendix at p. A-3 for chart depicting the dramatic shift in vendor revenue projections.



substantially boosted proposed revenue from the “Smart Card” option. In its October 2, 1996 submission, MFS had included no potential revenue for this option. However, within the firm’s revised final offer, the value of this component was abruptly inflated to \$67 million – half of which (\$33.5 million) was to be destined for the Consortium’s coffers. Not only was this presumed revenue source not vetted or evaluated prior to the selection of MFS as the E-ZPass contractor, it was arbitrarily reduced to an \$8 million item by the MET team – but only after the selection of the vendor. For its part, MFS was careful to qualify the presumed significance of the Smart Card option. At one point late in the process, for example, MFS stated:

*We have included a Smartcard options statement in this clarification document. At this time, we are proposing that the Consortium and the MFS team develop a Smartcard strategu (sic) by the first quarter of 1998. At this time, there is no financial impact of the Smartcard option on this project.* (emphasis added)

Louis A. Fuertes, the then-Business Development Manager of the Corporate Strategy and Development Group of Chase Manhattan Bank, testified as to his recollection of the purpose of the October 9, 1996, meeting between MFS representatives and Consortium staff:

**Q.** *[D]uring that meeting were you asked to submit additional revenues and which turned out to be this out-of-system revenue during that meeting?*

**A.** *Yes.*

**Q.** *Who asked you to submit that?*

**A.** *I remember Dave Mortimer playing a prominent role in this meeting. I don’t know if he was the individual who requested this, but we left that meeting with this as a deliverable. I don’t recall exactly whether he was the first person or the last person to request it, but I know he requested it at some point.*

- Q. Again, exactly what was requested of Chase or Chase/MFS at that 10-8, 10-9 meeting, in relation to the out-of-system revenues?*
- A. To develop an estimate for what those might mean for the consortium.*

\* \* \*

- Q. All the documents submitted to the consortium at that point indicated, with designated parameters, that there would have been a projected shortfall at the end of the eight years to the consortium, is that correct?*
- A. That's correct.*
- Q. And then, at the 10-8 or 10-9 meeting, Chase Manhattan/MFS was instructed by the consortium to provide estimates on what eventually gets culled out of system revenues, is that correct?*
- A. Right. If I could just expand on that, fiber had been involved in the prior estimates. Fiber is involved again in the out-of-system estimates, but on a more expanded basis, so fiber is a little bit of a funny one because it was in the numbers before and it's in these expanded ones, it continued forward, but on a broader basis.*

Significantly, MFS' revised final offer also set forth a twist to the cost picture: the concept that a self-funded E-ZPass program could only be achieved if the Consortium would agree to underwrite the financial performance over the life of the project. This language eventually became the basis for what was later termed the "True-Up" agreement under which the Consortium members ultimately assumed full responsibility for any shortfall associated with E-ZPass revenue projections and which set forth a formula in which each member would be assessed a share of the cost. It is noteworthy that this lopsided risk formula ran completely counter to the thinking that had prevailed within the ranks of the Consortium early on in the procurement. According to Thomas E. Margro, the former Turnpike Authority Chief Engineer who was first in charge of the E-ZPass procurement, the early expectation was that the overall project risk ultimately would be

shared with whatever vendor was selected. Further, when the MET team accepted MFS's revised final offer, and thus gave an official imprimatur to the shifting of the risk entirely to the Consortium, it was done in an *ad hoc* manner and not pursuant to any specifications, process or technical language drawn from the RFP or any other procurement documents.

### **Vendor Performance Problems: Known but Minimized**

During the course of the E-ZPass procurement, Consortium officials were informed that MFS had experienced technical problems in connection with the deployment of two smaller but concurrent electronic-toll ventures in this region. In the wake of one of these instances, the Consortium was urged to include in its RFP a requirement that all prospective vendors demonstrate technical proficiency through on-site testing as part of the evaluation process prior to the award of the contract. That suggestion, however, was set aside.

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In 1995, before joining the Consortium's regional effort, the Port Authority of New York and New Jersey pursued a separate procurement, competitively bid, to install electronic tolls at its Hudson River bridge and tunnel crossings. In addition to preparing detailed written proposals, qualified vendors were required by the RFP – at their expense – to demonstrate technical proficiency in test lanes as part of the evaluation process. Walter A. Kristlibas, then-Manager of the Port Authority's electronic-toll unit and an overseer of the demonstration tests, described the agency's motivation:

*We thought, for purposes of the Port Authority being able to select the technology, that [a pre-proposal test] was something that would give us an opportunity to really get beyond the fuzzy edges of the glossy pieces of paper that typically come in a proposal and really see if the rubber hits the road, and that's the way we ran the procurement.*

Two vendors ultimately submitted proposals – MFS and Lockheed. MFS utilized a test lane at a toll plaza in Mays Landing, Atlantic County, that was operated and maintained by the South Jersey Transportation Authority. Lockheed carried out its test on the George Washington Bridge between New York and New Jersey. In each instance, the test called for a fully operational toll-collection regime in which actual vehicles would pass through the toll gates in a real-time exercise observed and evaluated by Port Authority personnel.

Two Port Authority officials who participated in the evaluation told the Commission that MFS performed poorly in these lane tests. Walter A. Kristlibas testified that the firm demonstrated a “lack of coordination” in carrying out the test requirements and failed in a number of instances to accurately record toll transactions. Further, Kristlibas stated that MFS provided the test monitors with no guidance as to its test sequence. He described it as “*ad hoc*.” “We had been told by MFS that this was a mature test site. In fact, they had worked on it for two years . . . .” Kristlibas testified. “. . . [B]ut it was obvious to myself and our people that were with me from the Port Authority that [MFS] wasn’t quite ready for prime time . . . .”

Commission staff also interviewed Andrew Fogel, who at the time of these tests was Kristlibas’ deputy on the project. Fogel stated that MFS conducted the test in a way that was “difficult to follow” and the lane “didn’t do what it was supposed to do.” He

stated, “Overall, they (MFS) didn’t show us much.” Fogel stated that the firm and its technicians were “ill-prepared for the test and the results were indicative of that.” By contrast, according to Kristlibas and Fogel, Lockheed satisfied most of the test requirements and, in large part as a result of that, ultimately was awarded the agency’s electronic-toll contract.<sup>26</sup>

The Port Authority lane tests were conducted and completed in May 1996, approximately one month after the Consortium’s own electronic-toll RFP had been issued. Kristlibas, who also participated in that procurement as the Port Authority’s representative on the Consortium’s vendor evaluation team, told the Commission that he related his concerns about MFS’s test-lane performance to Consortium officials, including his colleagues on the evaluation team.<sup>27</sup> MET team members Mauer, Carris and McManus confirmed that they were aware of the lane-performance testing, and were kept informed of the results by Kristlibas. Kristlibas further testified that he also urged the Consortium to revise or amend its RFP to include a similar pre-proposal test requirement for prospective vendors, but that his suggestion was rejected:

*Q. At what point in the [Consortium] evaluation process did this [test] proposal come up?*

*A. Well, at the very beginning while we were putting the RFP together. The Port Authority [said] we think that for us it worked and we think that it would probably be something that would benefit New Jersey, also.*

*Q. So you wanted to actually incorporate that [test] requirement into the RFP?*

*A. Yes, sir.*

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<sup>26</sup> A written record of these tests no longer exists. As far as the Commission was able to determine, it was among the multitude of documents destroyed in the September 11, 2001 terrorist attack on the World Trade Center, the Port Authority’s headquarters.

<sup>27</sup> Kristlibas was appointed chief of E-ZPass operations at the New Jersey Turnpike Authority in June 2002 and currently holds that position.

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*[T]here was a discussion initiated by the Port Authority, and that was rejected.*

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In another electronic-toll procurement that overlapped the Consortium's regional initiative, the South Jersey Transportation Authority (SJTA) in late 1994 hired MFS to upgrade toll machinery along the Atlantic City Expressway. The SJTA project, initially targeted for completion in 1997, did not become operational until some three years later due to problems encountered by the firm during construction and installation. According to Donald E. Mauer, then the Authority's Chief Engineer, MFS "struggled to put the proper resources on the job so they could execute the daily work in a daily fashion. . . . Construction went off very slowly and then it continued to get slower." Once installation of the system was finally completed in early 1997, Mauer testified, the firm had difficulty achieving a satisfactory level of performance during pre-operational testing. "They struggled with it," Mauer stated. "When they said it was ready to go out there and tested it . . . their ability to pass the test was difficult. There were many interruptions to the test. There were many or numerous errors that were found that during beta testing you can find, identify and try to correct. . . . It did progress over a long period of time." The SJTA testing occurred at approximately the same time that the Consortium awarded its own ETC contract to the firm in March 1997. Crawford sent material to the Consortium related to these problems but with no change in the ultimate result.

In the end, the contract award to MFS was reduced by \$323,413.78 for work on the project that was to be completed by another vendor.

Crawford stated the reaction from Gross was to the effect that the SJTA as a small agency had not applied the proper level of oversight to ride herd on the vendor and that he planned to take action that would prevent similar problems with the Consortium's procurement. He stated that Mortimer's reaction was that there were no problems. Kathleen M. Sharman, SJTA's Director of Finance, told the Commission that ". . . [M]y impression was that they (Consortium staff) thought it was because we didn't know what we were doing. And the contractor was . . . right and it must be something we were doing wrong."

## **Vendor/Agency Complaints**

After the release of the RFP on April 12, 1996, at least one team of prospective vendors and one Consortium toll-road authority separately expressed concerns that, given the complexity of the project, the procurement was proceeding along an overly ambitious schedule. Requests for additional time in which to prepare responses to the RFP, however, were denied, even amid the abrupt change in evaluation criteria.

In a letter dated June 4, 1996, to ETC Program Manager Paul A. Carris at the Turnpike Authority, an executive of Valley National Bank complained that the RFP was replete with "many gray areas . . . which prevent us from providing a response."<sup>28</sup> Peter J. Southway, the bank's First Senior Vice President, told Carris – in language which, in

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<sup>28</sup> Valley National Bank of Wayne, N.J., was one of the four pre-qualified vendors in the E-ZPass procurement. Its team consisted, among others, of International Business Machines, EDS, ISYS, MasterCard, Waring LaRosa, O'Brien-Kreitzburg and Louis Berger & Associates.

retrospect, seems prophetic – that his firm “will not participate in a program that is not clearly developed” and warned that unless vendors were given more time to complete proposals, the Consortium was risking long-term operational problems. Indeed, Southway cited “the current debacle” involving difficulties associated with installation of an E-ZPass system on New York’s Metropolitan Transportation Agency (MTA) network.<sup>29</sup> He added, “As the old adage of haste makes waste seems to remarkably carry true in history, we are asking that the [C]onsortium carefully review our correspondence and commence discussions in order to develop a positive resolution.” Southway explicitly requested that the deadline for submission of vendor responses to the RFP be extended by approximately 2 1/2 months, from July 12, 1996, until October 1, 1996. Valley National Bank later amended its request for an extension to September 15.

In addition to his letter, Southway took the unusual step of attaching for Carris’ review a copy of an internal corporate memo, marked HIGHLY CONFIDENTIAL, to Southway from Valley National Senior Vice President Edward L. Lawrence. The memo states, in part:

*Peter, following some very technical and business oriented discussions between our current, prospective and possibly former team members it had become evident that the size and scope of the Consortium proposal does not allow enough time to respond in the manner in which we feel would be a) accurate b) credible. Although team members realize that this particular proposal will be one of negotiated procurement none can really assess their full costs and/or risks and are not willing to rely on the fact that all will be taken care of within the process. We have been building a team based upon our own VNB values and I believe it is a winning one, however, after reviewing the O’Brien-Kreitzberg oversight report` relative to the MTA project it is clearly evident that if we follow down the current*

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<sup>29</sup> Southway was referring to traffic chaos, highly publicized at the time, that attended the introduction of E-ZPass on the Throgs Neck Bridge linking the boroughs of Queens and The Bronx in New York City.



*path we and our team members could be part of a similar carnage in the future. None of the team members including VNB wish to have that type of recognition.*

*Let me be as clear as I can in my next remark, IT IS MY RECOMMENDATION THAT IF AN EXTENSION IS NOT GRANTED THAT VNB NOT PROCEED IN THE BIDDING PROCESS. This is a disappointing conclusion however our reputation and those of our team members are an overriding facet of this process.*

Lawrence's concerns were echoed in the text of a June 5, 1996 letter to him from an official at IBM, one of Valley National's putative E-ZPass partners. Kathy Daw, IBM's Northeastern Area Government Practice Leader, wrote that it is "not unusual" in such procurements for vendors to be given as much as five months to prepare responses once the RFP has been issued and vendor teams have been established. In this instance, Daw observed the proposal submission deadline was approximately two months away. "Our primary concern is one of time," she told Lawrence. "There is simply not enough time to put together a thorough and comprehensive proposal for a project of this magnitude and complexity requiring the skills of numerous team member firms."

Approximately three weeks later, similar time-related concerns were expressed by Lewis B. Thurston III, Executive Director of the New Jersey Highway Authority. In a June 27, 1996 letter to NJDOT Commissioner Wilson, Thurston observed that the original RFP had been amended twice to date and that a third addendum was in preparation. He also cautioned against taking steps that might diminish the already-small pool of interested, pre-qualified vendors, thus stifling competition. Thurston wrote, in part:

*It is my understanding that several of the lead vendors have requested further extensions of 45-60 days to submit their proposals, and that one vendor indicated that without the extension they would not be able*

*to submit a proposal. From the outset of the RFP process we have felt that the schedule was unduly tight in a number of respects, including the time for vendors to respond to the RFP. Additionally, we are not aware of non-changeable deadlines in the schedule which necessarily would require rejection of extension requests. Accordingly, we are not opposed to extensions of time up to 45-60 days for vendors to submit their proposals, particularly if the effect of rejection of the request is to eliminate a vendor proposal, thus reducing competition.*

Ultimately, either no extension, or one of only a matter of a few weeks, was granted, and the Valley National team withdrew. In a letter to then-ETC Project Manager Margro dated July 1, 1996, Lawrence stated that “based upon the advise (sic) that an extension is only available through 4:00 p.m., July 26, 1996, Valley National Bank will not be submitting a proposal as a pre-qualified proposer for this contract.”

Thurston testified that he and others at the Highway Authority continued to voice concern that the procurement schedule was unreasonably ambitious even after vendor proposals were received and evaluated leading to a contract award recommendation in October 1996:

- Q.** . . . [D]id you experience any kind of time pressure that would have a detrimental effect on the procurement?
- A.** Yes, we did. . . . [W]hen the proposals came in and when particularly the best and final offer and revised best and final offers came in, there was a schedule set for that that was basically dictated by the Department of Transportation. And our feeling at the Highway Authority was that that schedule was too tight, there wasn't sufficient time for full evaluation, and we requested additional time to do that, which was not granted.

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Looking back on these events, particularly the unsuccessful requests for additional preparation time, the Commission is constrained to point out that, as it happened, nearly 11 months transpired between issuance of the E-ZPass RFP and the

actual award of the contract. Further delays caused yet another year to pass before the contract was actually executed on March 10, 1998. In total, approximately 23 months went by between the release of the RFP and the actual launch of the E-ZPass program.

## **A Questionable Evaluation**

The task of assessing and scoring the substantive merits of the competing MFS and Lockheed proposals fell to a “Multi-Agency Evaluation Team” (MET) established for that purpose pursuant to the RFP. The team consisted of five members, one each from the participating Consortium entities: Paul A. Carris, the Electronic Toll Collection Program Manager employed by the Turnpike Authority; Charles D. McManus, Chief Engineer of the New Jersey Highway Authority; Donald E. Mauer, Chief Engineer of the South Jersey Transportation Authority; Walter A. Kristlibas, Chief of ETC Operations for the Port Authority of New York and New Jersey; and Howard R. Giddens Jr., Assistant Deputy Director for the State of Delaware Department of Transportation.

Aside from Giddens, none of MET members was experienced in public- or private-sector finance, despite the fact that cost had been elevated by the Consortium to be the criterion of foremost importance in the evaluation process.<sup>30</sup> Thus, as a team, they were heavily dependent upon the purported accuracy of financial information and data provided by others, primarily the vendors and the various Consortium agencies. Further, the team was not administered from among its own, but from without, first by Turnpike Authority Chief Engineer Thomas E. Margro and later, beginning in September 1996 – as

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<sup>30</sup> Giddens testified that he previously worked for E.I. DuPont de Nemours Co. for approximately 15 years in various financial management positions, two or three years in business management capacities and seven years with DELDOT.

the procurement entered the crucial phase in which vendor offers were negotiated, evaluated and scored – by NJDOT Chief of Staff David M. Mortimer. The Commission determined that under Mortimer’s direction, the vendor evaluation process was thoroughly manipulated.

In sworn testimony before the Commission, Mortimer, individually, and the MET members, as a group, were completely at odds in recounting core aspects of the evaluation process and the nature of their relationship. Mortimer described his role as chairman *ex officio* as one in which he served merely as a “conduit” and a “moderator,” stating, “I didn’t wield omnipotent power there.” According to MET members, however, Mortimer actively lobbied for the self-funding approach to the exclusion of any other. Under his direction, they testified, the evaluation process devolved into a rush-job in which artificial deadlines prevented adequate analysis of key documents, including those dealing with financial risk to the Consortium. They testified that questions were discouraged and that Mortimer denied requests for additional time in which to conduct the review. They testified that they were instructed by Mortimer to score the vendors’ final proposals within hours of the receipt of those documents by the group and that when the numerical difference between the point totals turned out to be quite narrow, Mortimer ordered a second round of scoring in which MFS emerged as the clear winner. One MET member whose individual score favored Lockheed told the Commission that he received a veiled threat from Mortimer. Ultimately, notwithstanding these issues and concerns, the vendor evaluation unfolded as it did in this instance because the MET members were compliant in the face of Mortimer’s purported authority over them and over the process.

There is no evidence to suggest that, at the time of these events, they brought any such complaints to a higher level of government authority.

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On October 10, 1996, Mortimer, the MET members and assorted staff from the various Consortium entities gathered in a conference room in the Commissioner's suite of offices at NJDOT. Earlier that day, a revised final offer had been received from MFS incorporating a detailed series of new cost and revenue estimates. A similar "BARFO" had been received less than 24 hours earlier from Lockheed. As the day unfolded, the team members were told by Mortimer that the time had come to score the vendor proposals. Aides and other Consortium agency officials were told to leave the room, and the scoring session proceeded late into the night. According to the New Jersey Highway Authority's Charles D. McManus, the events of that evening were the culmination of "an intensive, ugly process" that was rushed to a premature conclusion:

*Q. Prior to the scoring . . . did you believe that the MET team had adequate time to review all the proposals and ask all the questions?*

*A. No, we were pushed. No.*

*Q. Who was pushing you?*

*A. David Mortimer was pushing.*

\* \* \*

*Q. . . . [I]s it fair . . . to say that you went to the MET team scoring . . . a lot of questions remained unanswered, but at the same time you were asked to score the vendor proposals?*

*A. Yes . . . [T]he whole process was an expedited process. From beginning to end, it was a push.*

McManus and other MET members testified that they were particularly troubled to find that they would be required to score the vendor proposals on the same day that MFS's final offer had been received. This document, which had been faxed to Carris at approximately 8 a.m. the morning of October 10, contained a host of new revenue estimates, none of which had been subjected to careful scrutiny. Carris testified that outside of a "general discussion," there was no extra effort made to vet the proposed additional revenue. The MFS final offer also contained a major caveat: the company's firm position that the self-funding approach would be viable only if the toll authorities comprising the Consortium assumed the full burden of risk. McManus testified:

*Q. Is this the first document [you saw] at least in written form that indicates the shifting of risk from MFS to the Consortium?*

*A. The first one I saw.*

\* \* \*

*. . . This is very, very detailed and, you know, to properly [review] it, it should probably have been circulated to a number of staff people to really go through it carefully. So, I mean, obviously this document is much more detailed than one day would permit you to digest . . .*

*Q. So you're saying you didn't have adequate time, preparation to review that document prior to the second MET vote?*

*A. That's probably fair.*

*Q. Again, you believed there was a topic of discussion by the MET team members after seeing that document that they wanted more time to digest what was presented [by] MFS instead of voting that same day?*

*A. I'm sure I felt uncomfortable voting at that time. . . .*

The Port Authority's Kristlibas testified that the MET team collectively was startled by the terms of MFS's final offer because for the first time "it became crystal

clear” to the group that the vendor was not willing to share any portion of the risk for a funding approach that the vendor itself believed was problematic. Kristlibas testified:

*Q. . . . Isn't it a fact that MFS was telling the Consortium at this point, "We want a zero down, zero payment scheme, but we really don't think it's going to be attainable?"*

*A. Yes, sir.*

*Q. Is this the first time that was formally put in writing to the Consortium, do you know?*

*A. Yes.*

*Q. Did that cause any discussion by the MET team members after reading that?*

*A. Yes, sir.*

*Q. Did that cause the MET team members to – well, how did the MET team members react to that after reading that?*

*A. It was almost as if they were struck blind by lightning, because all along we were led to believe that MFS would syndicate some of the risks going forward, and this was the first time that I recall seeing in writing that they would assume none of the risks and, in fact, are saying to us that, based on what David Mortimer had laid out to them as the going-forward plan, they didn't think that this project would – can be – can go forward with it.*

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*Q. Do you recall if, during any of these discussions that occurred that evening, whether any member of the MET team asked Mr. Mortimer or the group as a whole for more time to conduct the evaluation, that they were concerned it was being too abrupt?*

*A. Yes, sir.*

*Q. And what do you recall about that?*

*A. [We were told] No, you are not leaving this room until the final vote is taken.*

*Q. Who raised those concerns?*

*A. Several members, including myself.*

*Q. And what did you say?*

*A. That the members here are very tired, that we've gone without sleep for a very long time . . . [t]hat we've been here for a very long time,*

*that we've gone through two straw polls and that this is way too important a process for us to undertake at this point without getting some rest.*

- Q.** *Did anybody ask for a specific amount of time extension?*  
**A.** *A couple of days.*

\* \* \*

- Q.** *What reason did he give you not to grant the extension?*  
**A.** *That we've received all of the information that we're going to receive, that each member had the opportunity to ask all the questions that they wanted to ask and, if you hadn't already asked it, there is no other opportunity now to ask it. That essentially we've exhausted our time in which to query either one of the vendors. It was put in those terms.*

Donald E. Mauer, then-Chief Engineer of the South Jersey Transportation Authority was one of several MET members who testified that the team was rebuffed when it sought more time to review and evaluate an alternative financing approach proposed by MFS – a so-called “budget certainty” approach that would have required the Consortium to put some money down in the early years of the project:

- Q.** *So the MET team thought the second approach of MFS in their September 27<sup>th</sup> letter warranted further consideration?*  
**A.** *Yes.*

- Q.** *Who didn't believe it warranted further consideration?*  
**A.** *Mr. Mortimer.*

- Q.** *And what did he base that on?*  
**A.** *I recall a statement . . . something to the effect that it's his belief, if you look at what's coming from the vendor community, that this job can be self-funded and we need to pursue that line.*

Carris testified that Mortimer discouraged the group from any focus or analysis on the second approach:

- Q.** *How much consideration did the MET team give to Approach No. 2?*



*A. I don't remember a lot of discussion on it. I do remember Dave Mortimer focusing on one and wanting to go in that direction.*

*Q. Do you remember Mr. Mortimer stating words to the effect, "We've got what we want in Approach No. 1. We're not going to consider Approach No. 2?"*

*A. Yeah, I think I do remember – I do remember something to that effect.*

*Q. So is it fair [for] us to rely upon that at this time Mortimer decided or at least voiced his decision to the MET team that you're not going to consider Approach No. 2?*

*A. Yes.*

\* \* \*

*Q. . . . What statement do you remember now that he made?*

*A. That the zero down, zero payment gives us what we need and there's no reason to consider the other one.*

According to Kristlibas, Mortimer expressed anger with MFS for submitting the second approach they way they did:

*Q. How do you know he was angry?*

*A. He expressed more than disappointment in having received and read this, in the manner in which MFS had articulated it, and I recall general statements being made on his part that, "No way could New Jersey possibly pursue this kind of an option, and [MFS executive] Bill Thompson knows better than that."*

Mauer testified that he and his MET colleagues also were restricted throughout the evaluation as to whom they could consult about the procurement, particularly when it came to contacting NJDOT personnel and expressing skepticism over the viability of the self-funding approach. Mauer testified:

*Q. Did you ever express your skepticism to Mr. Mortimer or others on the MET team?*

*A. Yeah. In writing no. In a conversation, yes.*

*Q. All the way up through the process that the MET team scored the proposals?*

*A. Yeah, uh-huh.*

*Q. What was Mr. Mortimer's reaction when you voiced your skepticism to him?*

*A. I didn't say I got brushed off, but I got a very cursory, you know, don't worry about it. You know South Jersey's [SJTA] a small deal. There's a bigger picture out there. You know, it will work. Don't worry about it.*

*Q. How about other members of the Department of Transportation, did you ever voice your skepticism to them?*

*A. Never really had an opportunity to speak to anybody else at the DOT. Dave was the face of the department. . . .There were very few people brought to the table from the department during the MET [process]. . . .*

MET members described the actual scoring of the vendor proposals as a laborious process that dragged well past midnight on October 10, 1996. Thick packets of detailed scoring sheets were distributed separately for the MFS and Lockheed packages. Divided according to the core evaluation criteria, these forms contained dozens of discrete categories to which each evaluator had to attach a numerical score. MET members told the Commission that they were under the impression going in that this would be the only scoring exercise of the evening. Once they finished, however, Mortimer collected sheets, left the room for a period of time and then returned to instruct the group that the proposals would have to be scored again. Although their recollections differ as to the timeframe in which this occurred, each of the MET members testified that a second round of scoring did indeed occur and that Mortimer stated it was necessary because the margin of difference between the point totals tallied for each proposal was narrow.

Mauer testified:

*Q. Who tells you you're going to [score] it again?*

A. *Mr. Mortimer. He says that the – he had reviewed the results and it was necessary for us to score again.*

Q. *Did he tell you why it was necessary for you to score again?*

A. *I believe the phrase he used was the spread wasn't big enough, the margin of – you know, the difference between the two vendors.*

Q. *Did he tell you which vendor received the most amount of points the first time?*

A. *No, he did not. He did not say that. He just said the spread wasn't big enough.*

Q. *What relevance was the fact that the spread wasn't big enough?*

A. *To me, none. . . . [I]n the world that I practice, competitions are based upon the merits. If you are the number one score-getter, then you're the number one score-getter. The size of the spread after the process you follow doesn't make much difference. . . .*

Q. *So after Mr. Mortimer made this comment to you, what discussion did the MET team have with Mr. Mortimer about the reasons why they had to re-score . . . ?*

A. *I don't remember a whole lot of specifics about the conversation. I do remember a lot of grumbling, a lot of concern that we've already scored once, what's the purpose in the second score if there is a clear winner and a clear loser? The magnitude of the spread, again, is not germane to the discussion because there is a winner and a loser. It's not a tie. After a couple of hours it was all fruitless. We were going to do it again and that was it.*

\* \* \*

*Dave's mind was made up and he wasn't going to change it. We were going to re-score again. We were going to submit a second set of score sheets.*

Carris testified that after the initial round, he confronted Mortimer, complained that the group had not had enough time for an adequate review and asked that they be given additional time. He stated that Mortimer was non-responsive and left the room to have the scores tallied. Upon returning, Mortimer informed the team that it would have to rescore. Carris testified:

*Q. What's the significance of [the call for a re-score] in your mind?*  
*A. That was information I didn't need to hear.*

*Q. Why not?*  
*A. Because it could sway people.*

*Q. Did [Mortimer] tell you who received the higher point total?*  
*A. That I don't remember.*

According to the sworn testimony of various participants, the point differential between the two vendors increased as a result of the re-scoring. However, since no agency was able to locate and produce to the Commission the first set of scoring sheets, the exact point totals and the results of the first scoring are unknown.<sup>31</sup> Giddens testified that he scored the proposals differently the second time. He stated, "I believe that – I don't remember it being significant, but I do have an impression . . . that my MFS score went up slightly, but I'm not sure. I think my differential changed, that was what I remember, and I don't remember if it was MFS went up a little bit or Lockheed went down a little bit, and I certainly don't remember why." McManus also testified that he changed his score the second time, "Yes, but I chose not to change anything except for the one area which was on the revenue side." Carris testified that he also changed his scores in the second round. He said he did so not because anyone explicitly asked or ordered him to but because during the interval between the two scorings, he briefly reviewed the documents and concluded that, on the merits, MFS deserved a higher score in several categories:

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<sup>31</sup> The final evaluation scores for the proposals were 4538.75 points for MFS/Chase and 4004.75 for Lockheed Martin IMS. The Final Average Weighted Score was 907.75 for MFS/Chase and 800.95 for Lockheed.

*Q. . . . [H]ow did you change your score from the first time you did the evaluation to the second time you did the evaluation?*

*A. I went back and reviewed the documents, and if I felt that I had a better understanding of where – what we were getting, I adjusted the score and I adjusted it – it did not change my initial selection, but it did, in effect, give a broader range between a winner and a loser.*

*Q. And your initial selection was whom?*

*A. MFS.*

*Q. So . . . you didn't change the final result of your scoring, you still remained consistent with MFS –*

*A. Yes.*

*Q. – but you increased the point total so MFS would have a higher point differential looking at your evaluation sheet.*

*A. . . . [Y]es.*

*Q. What transpired between your first scoring session and your second that would justify increasing the point differential between the MFS proposal and the Lockheed proposal?*

*A. Being able to go back and review the documents where I had questions in my mind, and meet the deadline that was imposed on us.*

*Q. And the deadline was imposed by Mortimer?*

*A. Yes.*

*Q. Other than yourself, did any other MET team members ask for additional time to review the documents prior to scoring?*

*A. I might have been the only one to actually go to Dave and say that I felt we collectively needed more time.*

*Q. Were you acting as a spokesman for the group?*

*A. Yes.*

*Q. And until he saw the scoring himself, he didn't think that was a good idea; is that correct?*

*A. That's correct.*

\* \* \*

*Q. Did Mortimer ever attempt to have you change your point total?*

*A. Outside of making the statement to the group, no.*

*Q. . . . Did he ever [imply] in one way or another that your point total should be greater between the two proposals?*

A. *To me directly, no.*

Q. *How about indirectly?*

A. *Outside of his statement to the group, no.*

\* \* \*

Q. . . . *[D]id you think you had enough time to review the proposals prior to your scoring on that evening?*

A. *No.*

\* \* \*

*I just know that as a group we were pretty burned out and resented the fact that we were still sitting there at that hour of the morning.*

Q. *Did he give you any reason why he needed that scoring done that particular night as opposed to coming back the next day?*

A. *No.*

Kristlibas told the Commission that when it became apparent that he, on behalf of the Port Authority, had given higher scores overall to Lockheed, Mortimer called him aside for a private meeting punctuated by pressure and by what Kristlibas interpreted as a thinly veiled threat:

*Before the final scoring . . . the Port Authority was really a minority vote, and that was pretty obvious to all of the evaluators before the final scoring was done, so Mr. Mortimer asked to speak with me privately, and I remember going into an office outside of the commissioner's area, and his [Mortimer's] approach with me was more along the lines of why was I being so stubborn. [Mortimer said] it was very clear that MFS is the better choice for New Jersey, offering greater revenue benefits, and it's very clear that I was opinionated and that, for reasons unknown to him, I was voting for Lockheed Martin, and he wanted to know if [the] reason could possibly have been that, during the Port Authority procurement we had selected Lockheed Martin as opposed to MFS, and I recall responding to him that it has nothing to do with the prior selection by the Port Authority. I'm going simply by this RFP, I'm going by the proposal and I'm going by the revenue projections that each vendor was presenting, and added to that evaluation is some knowledge of the capability and performance of each, and that I cannot, in all good conscience, vote for MFS.*

*At that point he – he asked me whether I had considered the effects of my vote on my career, and I remember responding to him, by body language, surprise. I asked him, “What did you mean by – what do you mean?” he says, “Well, you know, you’ll be the minority vote, you are obviously going to ask questions, you know, why didn’t you see it the same way. It certainly would be better for all of us if we had a unanimous vote, unanimous approach on this.” I said, “I wish I could see it your way, but I can’t. I’m not going to change my vote.”*

*He then said something like, “I think you are being very stubborn about this. I like you, but you are really being very stubborn about this.” And there might have been another exchange between he and I, I don’t remember the exact words, but I then left the room.*

\* \* \*

**Q.** *My question is, how did you interpret his statement to you?*

**A.** *He was attempting to speak to me in a Dutch uncle fashion, that he was more experienced, I was kind of rough around the edges, not quite as politically attuned as, perhaps, I should have been. My interpretation was not that it was any kind of physical threat in any way or that I would be summarily fired upon my return, but images of Commissioner Wilson, being a very powerful commissioner with the Port Authority, certainly were dancing in my head, and I think, whether he intended it or not, that’s the image that I got.*

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Mortimer testified that he had no recollection of such an encounter and strenuously denied making any threatening statements related to Kristlibas’ career:

**Q.** *Kristlibas has told us that during the scoring that night you asked him into a private room to have a private discussion with him about his opinion on the procurement. Do you remember a private conversation with Kristlibas in a private office at DOT?*

**A.** *I don’t.*

**Q.** *How about a statement that you told him, you ought to think about your career going forward?*

**A.** *I wouldn’t say that to anybody under any circumstance.*

\* \* \*

*I have no recollection of any of those statements at all. The one I would flatly deny is ever saying to somebody you got to think of your career.*

Mortimer acknowledged that as the non-voting chairman of the MET team, he never reviewed the substance of the vendor offers and proposals. As to statements by Carris, Mauer, McManus and Kristlibas that they asked for more time to examine the vendor, Mortimer testified that he had no recollection of such requests. Indeed, it was Mortimer's testimony that the time allotted for the evaluation was more than sufficient:

*Q. Do you believe that there was an adequate time frame between receipt of the best and really final offers and the evaluation for the MET team to digest all the material?*

*A. Yes, because it was an incremental process. It wasn't like you were getting all of it at once. They had digested huge amounts of information over an extended period of time, so . . . what they needed to focus on between the BAFO and the BARFO was finite, in terms of information.*

Mortimer denied having been the force behind the self-funding approach and testified that he could not recall what attention was given to an alternative suggested by MFS that would have required the Consortium to invest funds in the project during its early years:

*Q. Did you ever say words to the effect that you wanted a no-cost deal from either vendor?*

*A. I don't believe I ever used the words "I want." I'm not trying to be literal. I'm trying to understand the intent of your question.*

*Q. How about the intent of the –*

*A. I believe that . . . at discussions subsequent to a lot of input that was taken that the statement was made that the consortium believed that this – there was an opportunity for it to be a no-cost proposal for the state – for the consortium.*



\* \* \*

*Q. [What,] if any, consideration did the consortium give to the second approach?*

*A. I don't have a specific recollection of what consideration was given it.*

*Q. . . . [O]ther people told us that Approach 2 really was not considered. . . . Can you tell us . . . how did it happen or why did it happen?*

*A. I don't have a recollection of that happening, and I don't know . . . what consideration it was or wasn't given. I just don't recall.*

\* \* \*

*Q. Do you remember if Mr. Carris brought Approach Number 2 to your attention . . . ?*

*A. I don't remember that he did or he didn't. He may have and he may have brought it up amongst a group. I just don't recall that.*

*Q. . . . Do you remember a discussion within the MET team about Approach Number 2?*

*A. I don't remember whether there was or there wasn't.*

\* \* \*

*Q. The MET team has universally told us that it was your decision to reject Approach number 2; do you have any comment on that?*

*A. I wasn't in a position to reject it.*

*Q. Why weren't you in a position to reject it?*

*A. I had no vote.*

*Q. . . . [T]hey were told not to consider Approach number 2 by you and that's why it wasn't considered?*

*A. I don't have any recollection of making that statement, nor do I have any reason to believe I would.*

As to the contention by every member of the MET that he instructed them to score the vendor proposals twice because the initial margin between them was too narrow, Mortimer testified:

*Q. How many scorings were there?*

*A. How many scorings?*

Q. Yes.

A. Oh, one, I would guess. I can't think of another one.

\* \* \*

A. As I said, I'm unaware of more than one scoring of the proposals.

\* \* \*

A. I only have one recollection – I only have a recollection of one scoring being done.

\* \* \*

Q. . . . Every MET team member has indicated to us that they scored the proposals more than once?

A. I don't have a recollection of that.

Q. As a matter of fact, they also said they're universal in why they re-scored because a statement was attributed to you that the point differential between the two vendors was not substantial enough, and that's why they were asked to re-score. Do you have a comment on that.

A. I find it difficult to believe.

\* \* \*

. . . I have no reason to think that I would do that, because it doesn't matter whether it's one point or a thousand points, so I have no reason to understand why that would be said.

Q. Well, doesn't it matter if you are concerned about a [vendor] protest?

A. No. As I said to you before, I operated from the premise that this was going to be protested, because procurements can be protested no matter what it is.

## A Web of Connections

The E-ZPass procurement, in addition to unfolding amid then-NJDOT Commissioner Wilson's private-sector employment discussions, occurred against the backdrop of a broad web of connections involving Wilson; NJDOT; a California-based

fiber-optic consultant, Kingston Cole; and the prevailing vendor, MFS Network Technologies. In summary, the Commission found:

- During Wilson's 30-month stint as head of NJDOT, the agency paid Cole more than \$257,000 for consulting services on a range of matters related to fiber-optic technology, including the electronic-toll procurement.
- Wilson and Cole had a pre-existing professional relationship. During Wilson's earlier tenure as head of San Francisco's Bay Area Rapid Transit (BART) system, Cole was retained as a BART consultant on at least three separate occasions.
- While working for BART, Cole brokered a public/private partnership between the transit system and MFS for installation of a fiber-optic network along BART's right-of-way. This type of partnership later served as a model for the Consortium's E-ZPass procurement as awarded to MFS.
- In seeking NJDOT contracts, Cole submitted a resume that identified Wilson as a reference.
- Wilson sought to have Cole retained as an NJDOT consultant without competitive bidding. Wilson also served on a vendor evaluation committee that recommended the award of a state contract to Cole's firm. Wilson's Chief of Staff, David M. Mortimer, also served on an NJDOT evaluation committee that awarded work to Cole's firm.

- Cole participated in private discussions and negotiations with representatives of the two finalists in the Consortium's E-ZPass procurement, MFS and Lockheed.
- Cole authored a confidential memorandum recommending a strategy to mislead Lockheed on the issue of whether the vendor proposals should include a fiber-optic component.
- In a written evaluation submitted immediately prior to the scoring of Lockheed and MFS proposals, Cole recommended that the Consortium accept the MFS proposal.
- Payments to Cole were made through NJDOT until September 1996, when his firm was abruptly retained as a subcontractor to the Consortium's "special services consultant," Phoenix Planning and Evaluation Ltd. During this period, which coincided with Wilson's purported recusal from matters related to the procurement, Cole's firm received approximately \$20,000 in payments from Phoenix.<sup>32</sup>

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<sup>32</sup> In examining the connections between MFS, Cole and Wilson, the Commission received sworn testimony from numerous individuals and conducted an exhaustive review of documentary materials. Those materials included records obtained from NJDOT, Kingston Cole & Associates, the Turnpike Authority and other governmental agencies, including the New Jersey Executive Commission on Ethical Standards (ECES), which conducted a confidential inquiry into alleged conflicts of interest related to personal employment discussions pursued by Wilson with firms identified as NJDOT vendors while serving in Governor Whitman's Cabinet. The ECES inquiry, which tangentially involved certain aspects relevant to the E-ZPass procurement, was closed in May 1997 based upon a settlement – "Administrative Disposition by Mutual Consent" – in which Wilson agreed to pay a \$1,200 penalty despite no finding by the ECES of an actual impropriety under the express terms of New Jersey's Conflict of Interest statute. Wilson resigned as NJDOT Commissioner effective December 1996 to take employment as Vice President of the firm Daniel, Mann, Johnson & Mendenhall (DMJM) of California, a NJDOT contractor and sister firm of a company, Frederick Harris Inc., that at the time of his employment discussions was slated to be an MFS subcontractor on the E-ZPass project. DMJM and Harris have since merged as one of a number of subsidiaries of AECOM. Wilson went on to become President of another subsidiary, AECOM Enterprises Inc., based in Los Angeles. In May 2004, he returned to the public sector as President and Chief Executive Officer of the Metropolitan Transit Authority of Houston, Texas.

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Wilson was sworn in as NJDOT Commissioner on April 6, 1994. Prior to that, he had served as General Manager of San Francisco’s BART system for approximately five years. In July 1992, BART hired Cole’s firm, Kingston Cole & Associates of San Raphael, Calif., to study how to generate revenue by exploiting the market value of BART’s right-of-way. A year later, BART retained Cole to work on renewal of its pay-telephone concession. In 1994, Cole again was hired by BART, this time as a consultant on a proposed revenue-sharing partnership between the transit system and MFS/NT.<sup>33</sup> The goal of this initiative was the design and installation of a multi-duct, fiber-optic telecommunications system along BART’s right-of-way. Under terms of the deal, MFS retained Pitney Bowes Corp. to arrange a capitalized leasing program to finance some \$40 million worth of hardware and construction. This approach enabled the transit agency – with no money down – to pay off the capital cost of the network over time with revenue from the leasing of the fiber cable to commercial interests.

Cole, an attorney, former California political operative and former Pacific Bell executive, founded his consulting firm as a sole proprietorship in 1987. According to a “Statement of Qualifications” submitted to NJDOT, Kingston Cole & Associates claims a clientele drawn exclusively from the public sector and boasts of “expertise in creating public/private partnerships.” The Statement advised that the firm uses “a dynamic process that recognizes and blends the needs of the private sector to make a profit and the public

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<sup>33</sup> MFS/NT, or Metropolitan Fiber Systems/Network Technologies, was formed in 1988, a subsidiary of Peter Kiewit Sons Inc., a telecommunications/construction/energy company in Omaha, Nebraska. In August 1996, MSF was acquired by WorldCom, which spun the firm off to Georgia-based Able Telecommunications 18 months later in July 1998 as New Jersey struggled to get its MFS-operated E-ZPass system up and running. In February 2000, MSF changed its name to Adesta Communications, which was acquired in December 2000 by Bracknell Corp. Adesta declared bankruptcy in September 2001.

sector to generate revenues” and further advised that the firm “advocates the use of flexible Requests for Proposals (RFPs) that include functional bidding requirements and innovative proposal evaluation processes.”

In October 1994, some six months after Wilson became NJDOT Commissioner, he met with Cole in New Jersey. In a follow-up letter to Wilson dated October 11, 1994, Cole wrote, “Thank you for the opportunity last week to discuss the revenue and telecommunications needs of the State of New Jersey. Per our conversation, a proposal is enclosed with terms and conditions necessary to begin working with you on the development of the Department of Transportation’s rights of way.” Cole further wrote that he had already begun to review vendor proposals and “. . . would like to begin negotiations with Cellular One (and other potential cellular firms) as soon as possible. I have enclosed a draft letter of authorization for my firm that will allow me to begin the process. Please execute the letter, subject to any corrections or amendments, and I will contact Cellular One immediately. I have reserved the week of October 24<sup>th</sup> through the 29<sup>th</sup> for another trip to New Jersey.”

The Commission’s investigation revealed that this was the beginning of a lucrative consulting relationship from which Cole’s firm netted \$257,800.53 in contract payments from NJDOT between October 1994 and January 1997.

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Records reflect that during that 27-month period, the state issued four separate purchase orders for Cole’s services. The first two were “DPAs,” or Direct Purchase Authorizations, awarded without competitive bidding in the amount of \$5,000 each. The

initial DPA, earmarked “CONSULTANT SERVICES FOR TELECOMMUNICATIONS SERVICES FOR EVALUATION OF ROW,” was paid based upon an invoice submitted by Cole dated October 16, 1994. The second \$5,000 DPA, for “CONSULTANT SERVICES – EVALUATE FIBER OPTIC DEVELOPMENT/ROW (PHASE 2),” was paid to Cole through his invoice dated December 10, 1994. Cole, in sworn testimony, characterized these initial contracts as of the same pattern used to develop his firm’s relationship with BART. Kingston Cole & Associates initially was awarded two sole source contracts with BART prior to winning three contracts that were competitively bid by the transit agency.

Over the next three months, Cole’s involvement with NJDOT grew appreciably. On March 15, 1995, the state issued a third purchase order – in the amount of \$190,000 – again retaining Cole’s firm, in this instance to assist the agency in planning for ways to draw revenue from the leasing of highway rights-of-way to telecommunications companies.<sup>34</sup> Although this consulting contract ultimately was awarded through competitive bidding, events and circumstances suggest the process was manipulated.

Records examined by the Commission show that Wilson initially attempted to secure a sole source waiver exempting the contract from competitive bidding. Wilson testified that he did so “because the belief was that we were going to take a quick and inexpensive look to see if there were any opportunities that existed in New Jersey state market to work in sort of a partnership with them.” The New Jersey Treasury Department’s Bureau of Purchase and Property refused to grant the waiver, however, and

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<sup>34</sup>Material submitted to NJDOT by Cole in pursuit of this consulting contract included a list of 11 professional references, all of whom were based in California – with one exception: “Mr. Frank Wilson, Commissioner, New Jersey Department of Transportation.”

the proposal was advertised for bids. Five firms, including Cole's, responded to an RFP designed to solicit proposals for a consultant to assist the NJDOT in a planning effort to maximize revenue from leasing Rights-of-Way spaces to telecommunications firms. The five-person vendor evaluation committee consisted of Wilson himself, Deputy NJDOT Commissioner Sharon L. Landers, NJDOT Director of Procurement John Naiman, Jr., Deputy State Treasurer James Archibald and Supervisor of Purchasing Enrico G. Savelli. The committee unanimously recommended the contract be awarded to Cole's firm, which offered a bid of \$164,000. The low bidder, Goodkind & O'Dea Services at \$119,985, was bypassed by the evaluation committee on technical points. Treasury awarded \$164,000 for a combination of fixed-fee and hourly tasks; ultimately, the total award was boosted to \$190,000 based upon a \$26,000 allowance for optional work under certain hourly tasks. Between March 29, 1995, and September 4, 1996, Cole submitted 14 invoices and was paid a total of \$187,457 on this contract.

Lana Sims, the then-Director of the Division of Purchase and Property, told an investigator for the Executive Commission on Ethical Standards that, "in general, the Purchase Bureau does not like to have a commissioner or a deputy commissioner sit on (vendor) evaluation committees. She (could) not recall any other instances where a commissioner, during Sims' tenure, sat on an evaluation committee." However, Sims told the ECES that Wilson and Landers "were on the committee because they wanted to be ... and there was nothing to prohibit it." Sims also told ECES that "Cole's practice of using Frank Wilson as a reference on Cole's proposal is exceptional and extraordinary." Wilson was also questioned by the SCI as to why he served on the evaluation committee



given the fact that initially he wanted to award the contract to Cole's firm using a no-bid sole source approach. Wilson testified that he saw nothing improper.

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The fourth purchase order, dated May, 23, 1996, was for work by Cole on a request for proposals pursuant to the development of NJDOT and toll authority rights-of-way for telecommunications purposes, including a fiber-optic cable network. Procurement documents examined by the Commission suggest another effort to manipulate the competitive bidding process in Cole's favor.

NJDOT initially sought to award this work via a change order for Cole's existing \$190,000 contract. At the agency's request, Cole submitted a "Change Order and Related Scopes of Work" document, estimating therein that the total dollar value of the change order was not to exceed \$396,000. Agency officials subsequently prepared a requisition, along with a "Request For Waiver of Advertising," for the work in the total amount of \$396,000. Treasury, however, rejected the waiver request and directed that the contract be advertised for bids. A subsequent RFP sought a "marketing and telecommunications consultant to take the lead in the development and preparation of a request for proposal for the use by the Department of Transportation (NJDOT) and various New Jersey toll road authorities to solicit innovative partnership proposals from the telecommunications systems industry which meet NJDOT's and the authorities' functional requirements while developing business arrangements to maximize revenue to NJDOT and the authorities for use of their respective rights of way for a fiber optic background system." Three prospective vendors responded: Kingston Cole & Associates, Edwards & Kelcey and

Universal Field Services, Inc. Following a preliminary evaluation, two of the bidders – Cole and Edwards & Kelcey – were scheduled to make oral presentations on March 14, 1996. However, citing “business reasons,” Edwards & Kelcey abruptly withdrew its bid, and the presentations were cancelled, leaving Cole and Universal in the running. On March 22, 1996, the evaluation committee unanimously recommended that the contract be awarded to Cole, which offered a total bid price of \$223,440. Universal, the low bidder at \$147,800, was bypassed due to low technical marks in scoring by a six-person evaluation committee, which included three senior NJDOT officials – Chief of Staff David M. Mortimer, Assistant Commissioner Stanley G. Rosenblum and Executive Director of Aeronautics, John S. Penn. The other members of the evaluation committee were Associate Deputy State Treasurer John Ekarius, Acting Administrator of OTIS Ron Maxson and State Supervisor of Purchasing Enrico G. Savelli. Mortimer, then the Chief of Staff, was specifically selected by Wilson as an evaluator. When questioned by the Commission if he had ever served as an evaluator of any kind of contract proposal submitted by Kingston Cole, Mortimer initially testified, “I was never an evaluator on any contract in my services to state government.” Under further questioning, however, Mortimer later acknowledged that he did serve as Cole’s evaluator on this occasion.<sup>35</sup>

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<sup>35</sup> The Commission reviewed documents that revealed Mortimer also served as an evaluator on at least two other occasions. One involved a \$563,603 contract awarded to O’Brien-Kreitzberg and Associates (OBK) on May 23, 1995, to examine NJDOT’s organizational structure, project-delivery capacity and management system. The second contract, also involving OBK, was awarded on November 22, 1995, totaling more than \$5.8 million to assist NJDOT in the implementation of a project management and control system that evolved from recommendations contained in a report prepared by OKB under the previous contract. In addition to Mortimer, Frank J. Wilson and Sharon L. Landers were members of the vendor evaluation committees for both of these contracts.

Ultimately, Treasury approved an award of \$270,000 to cover a combination of fixed-fee and per-hour tasks, and NJDOT issued a purchase order in the same amount. Cole submitted eight invoices between June 4, 1996, and January 3, 1997, and was paid a total of \$60,427.50.

On January 13, 1997, Cole was directed by NJDOT to suspend work because of a dispute over legislation authorizing NJDOT to proceed with commercial fiber-optic development of highway rights-of-way. In October 1997, the agency took action to cancel the contract because it still lacked statutory authority to proceed and because it had, by then, sufficient internal expertise to eliminate the need for an outside “fiber optics market specialist.”

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Records examined by Commission staff show that beginning at least as early as the first quarter of 1995, Kingston Cole was becoming a key behind-the-scenes player, not just in cell tower right-of-way issues, but in the Whitman administration’s emerging plans for an electronic toll-collection and telecommunications system along the regional interstate highway system. Indeed, in March 1995, Wilson relied on Cole for the preparation of a presentation to the Governor on this issue. Also, a NJDOT memorandum dated September 19, 1995, refers to Cole’s involvement in “developing requirements, soliciting proposals, evaluating responses, and negotiating resultant agreements or licenses for two RFP processes.”<sup>36</sup> The memorandum further states, “The timeliness . . . was brought to bear in the past week with the announcement by the Governor that she wants to move ahead with electronic toll collection implementation.

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<sup>36</sup> See Appendix at p. A-18.

Commissioner Wilson has announced that a consortium of New Jersey transportation agencies will be moving full speed ahead to install electronic toll collection.” According to this memo, one result of Cole’s work was a recommendation to Wilson that two RFPs be issued on parallel tracks. The first would package all rights-of-way in various transportation agencies’ domains and offer the full array through a bidding process to qualified vendors to construct, operate, maintain and market a fiber-optic system. The second RFP would solicit proposals to construct, maintain and operate an electronic toll collection system along the rights-of-way. The recommendation for this pair of RFPs called for them to be “functional in nature, inviting creative proposals to develop the business relationship between public and private sectors.” The memorandum further stated, “Based upon the feasibility research from the Kingston Cole & Associates contract, Commissioner Wilson has recommended that a public/private approach is the method to use, rather than just building everything entirely with state or federal funds.” Wilson testified that Cole’s recommendation that the ETC procurement proceed as a public/private partnership was not accepted, but he acknowledged that the RFP did allow for vendors to submit options to help finance all, or parts of, the system.

Invoices submitted by Cole show that throughout 1995 and into 1996, he met on numerous occasions with Wilson and other senior NJDOT officials, and with representatives of various vendors, including MFS and Lockheed. By mid-1996, with the electronic toll procurement well under way, Cole characterized himself in a June 6, 1996, memo to Sharon L. Landers and Stanley G. Rosenblum as “the Commissioner’s liaison to the Authorities for the ETC project on two basic different (sic) levels: As the person who can assist them in determining the value . . . for fiber optic components of the various

[vendor] proposals now due on July 12<sup>th</sup>,” [and] “As a facilitator to mitigate and assuage any potential problems, tensions, etc., that may develop among the various Authorities and the NJDOT during negotiations.”

A review of billing invoices submitted by Cole to the NJDOT for payment revealed he began formal work on the electronic-toll project as of May 29, 1996. From that date through June 12, 1996, he billed the agency for 6.75 hours of work. On June 18, 1996, however, Cole sent a letter to Thomas J. Calu, Project Manager of the NJDOT, notifying the agency of a professional relationship between himself and the engineering firm of Fredrick R. Harris, Inc. Cole indicated that Harris intended to be a subcontractor on the MFS electronic-toll vendor team. Subsequent to submission of this letter, all billing by Cole to NJDOT on ETC-related work ceased. Around this same period, Cole testified, Wilson informed him that he, Cole, would no longer be involved with the procurement but gave no reason other than stating, “I want you out of there.” Cole’s invoices, however, show that he resumed work related to the electronic-toll procurement on August 19, 1996, and billed NJDOT for 41.5 hours through August 31 of that year. Less than one week later, on September 5, 1996, Cole was instructed via NJDOT to submit his invoices under “other arrangements with the Turnpike.” The “other arrangements” were that Cole abruptly became a subcontractor to the Turnpike’s special services consultant, Phoenix Evaluation and Planning Ltd. Margaret Melhem, that firm’s Vice President, testified that she could not expressly recall how Cole came to be paid through Phoenix’s contract with the Turnpike Authority, but she acknowledged that the Turnpike asked Phoenix to “run him through our contract.” Melham testified:

*Q. Did you in any way vet Mr. Cole?*

A. *No.*

Q. *Did you know his quality of work?*

A. *No.*

Q. *So, essentially, you were asked by the client to put someone on under the contract and you, through your company – or your company said yes.*

A. *(Witness nods.)*

Q. *Without trying to be ridiculous, he could have been a guy off the street? You wouldn't have known, correct?*

A. *I do not know – it was not my – in the line of my responsibilities, so I really don't know what, if any, discussions were had about Mr. Cole.*

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Witnesses told the Commission that Cole was present at and participated in meetings between Consortium officials and vendor representatives leading to the preparation and submission of best and final offers for the electronic-toll contract. He was identified to the other participants as the “fiber expert.” Kristlibas testified that Cole was introduced at MET team meetings by Mortimer on behalf of Wilson as the person who would “lead us through the maze of fiber talk.”

In a document dated September 3, 1996, and prepared by Cole as a “Memorandum for File” re: “Initial Negotiating Positions for Fiber Optic Network/ETC,” he stated, “MFS has clearly presented a better proposal in this area.” Cole further wrote, “The Lockheed offer on the table is clearly unacceptable. In both sets of interviews, their personnel were told informally that the offer was not enough, i.e. just putting fiber on the Turnpike and ignoring the needs and revenue potential of the other Authorities is unacceptable.” Cole stated that his “recommended strategy” at this stage in the ETC

procurement would be to “see if” Lockheed and its partner, Symphony Management, have

*gotten the message to seriously amend their proposal. If not, we should consistently tell them that winning the ETC portion of the RFP does not include any type of fiber optic system. (Emphasis added) The Consortium, or its various members, reserve the right to seek an alternative approach to building a State-wide system exclusive of the ETC project.*<sup>37</sup>

Carris testified that he became angry and upset upon reading Cole’s recommendation. Carris stated that, “he (Cole) was drawing conclusions on things that none of us had gotten to that point yet, and he had a lot of other information he was putting into this to draw his own conclusions for his own reasons that did not seem to be in sync with where we were going with the process and investigation of getting information from the vendors.”

Kristlibas recalled reviewing the memorandum at the time and discussing what he felt were its potential implications with Carris:

**Q.** *And what opinion did you give Mr. Carris?*

**A.** *Something along the lines of, it looks like this is stacking the deck.*

**Q.** *In what way? What do you mean, “Stacking the deck?”*

**A.** *It was clear to me, before September 3<sup>rd</sup>, that Lockheed Martin was not going to up the ante on the fiber. That was made pretty clear in their presentations to the evaluation team, and I saw no opening in their position to suddenly begin, you know, . . . putting more chips on the table.*

*I got a message from the position that they were taking that they were not going to engage in . . . the type of increase in projected revenues from fiber. They stopped beyond a point and they refused to go any higher, and I certainly had the impression that MFS every day saw new and better opportunities for increasing fiber revenue and, so, their presentations just continued to show higher and higher net revenues . . .*

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<sup>37</sup> See Appendix at pp. A-24 through A-31.

*There were so many documents that went back and forth that Kingston Cole, I think, was quite aware that Lockheed simply didn't have the fiber strength, background, infrastructure that MFS did, and, therefore, it couldn't possibly compete in a fiber arena as opposed the purely systems integration and back office services for electronic tolls.*

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*My intuition told me that was the case, and that was based on the language that he used, which was relatively derogatory, relative to Lockheed not getting the message, they really are not into fiber, really don't have the background, their sub[contractor] is really not a player in the game.*

*I fairly quickly formed the opinion that, not only was Lockheed Martin not going to take a different position substantially than one they already had on the issue of fiber, but that Kingston Cole's opinion of Lockheed Martin, especially on the fiber side, was not going to change.*

Cole testified that the tone and tenor of his September 3, 1996 memorandum was to give his client “some hard edge, push the edge of the envelope, push back at these guys, see what best deal we can get.” Cole stated that the strategy was to “be tough with them.”

On October 9, 1996 – the day before the final MET team scoring of the vendor proposals – Cole submitted a memorandum to Carris analyzing the fiber-optic elements of the proposals submitted by both MFS and Lockheed. Cole concluded that the Lockheed offer was “fundamentally flawed” while the proposal from MFS was “fundamentally sound.” He stated, “We recommend that the Consortium seriously consider this [MFS] option, despite our reservations concerning construction and maintenance costs. Any final terms and conditions should be fully scrutinized and negotiated to the Consortium's maximum advantage.” This memorandum was submitted to Carris the day before the MET team convened to undertake a final scoring of the vendor proposals.



## **The Lockheed Protest**

On October 21, 1996, 11 days after MFS prevailed in the evaluation team's scoring of vendor proposals, Lockheed filed an administrative protest. The thrust of the firm's complaint was that the Consortium unfairly and improperly altered the RFP immediately prior to the due date for vendor proposals and misled Lockheed about revenue options during the phase in which best and final offers were formulated. The firm also charged that MFS was privy to inside information via Kingston Cole that fiber would be wrapped into the E-ZPass project and that Frank J. Wilson had participated in job-search discussions with companies that were members of both vendor teams. On October 25, 1996, the presiding officer in the protest – Acting Turnpike Authority Executive Director Edward Gross – served notice that a hearing would commence two-and-a-half days later. He rejected Lockheed's request seeking a one-week adjournment to "conduct discovery and prepare its presentation of the protest." In a written opinion issued November 15, 1996, after a six-day evidentiary hearing, Gross denied Lockheed's protest and determined that the procurement process should proceed.

On April 1, 1997, a week after the Turnpike Authority's governing board voted to award the contract to MFS, Lockheed filed a second protest. Gross recused himself, and the job of hearing officer fell to Diane Scaccetti, then the Turnpike's Deputy Executive Director. A limited hearing was held and in an opinion issued May 2, 1997, Scaccetti denied Lockheed's request to cancel the contract and re-issue the RFP. The findings and results of both proceedings were upheld on June 12, 1997, by the Appellate Division of State Superior Court.<sup>38</sup>

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<sup>38</sup> Nachtigall v. N.J. Turnpike Authority, 302 N.J. Super. 123 (App.Div. 1997)

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The Commission is constrained to question the legitimacy of the overall process utilized in the Lockheed protest because neither the hearing officers nor the court were aware at the time of their deliberations of the unusual circumstances under which the vendor proposals were evaluated and scored by the MET team; the full extent of the relationship between Frank J. Wilson, Kingston Cole, and MFS; the full scope of Wilson's contacts with procurement officials after his purported recusal; and the existence of Cole's memorandum in which he posited a strategy to mislead Lockheed at a critical juncture.

Sworn testimony by witnesses in this investigation also raises questions about whether the administrative proceedings were properly and thoroughly conducted. For example, a number of individuals privy to the vendor selection process did not testify in either of the protest proceedings. The absentees included the entire MET proposal evaluation team with the exception of Paul Carris, who did testify.

Further, Scaccetti told the Commission that she had little familiarity with key aspects of the E-ZPass procurement and no experience as a hearing officer in administrative proceedings. She testified that she reluctantly agreed to preside in the Lockheed matter at the behest of Gross and Turnpike Authority Chairman Frank X. McDermott. Scaccetti also testified that she received inadequate legal counsel and found herself relying on attorneys for the involved parties:

**Q.** *Did you have difficulty with that assignment?*

**A.** *Yes, I did.*

**Q.** *What was that?*

**A.** *. . . I didn't have, what I considered, to be adequate [legal] counsel. I'm not an attorney, and I knew that it would be . . . unfriendly. This was the second time that Lockheed was protesting. They had hired attorneys out of New York as well as attorneys out of Trenton. And, again, . . . Mr. Gross did not provide the counsel that I had asked for; so, yes, I was uncomfortable with the assignment.*

**Q.** *Did you voice these concerns to Mr. Gross?*

**A.** *Yes, I did.*

**Q.** *What was his response?*

**A.** *You get what you get.*

**Q.** *You get what you get?*

**A.** *That's it, I got in-house counsel from the Turnpike, one of our staff attorneys who did not have a lot of experience or any experience in the conduct of a protest hearing. I had no experience in the conduct of a protest hearing, so we were walking into what I considered to be a dark closet.*

One result, Scaccetti testified, was that she lost control of the proceedings:

*I had a hearing that was run like a zoo, because there was a lot of – obviously a lot of antics going on. They [participants] knew this was my first hearing. I had a lot of misbehaving in the room where I couldn't hear what was being presented to me. It was an experience I would prefer never to repeat.*

Scaccetti acknowledged that her lack of experience and knowledge of the procurement may have resulted in some issues being overlooked, such as information related to the peculiar way in which the MET scoring had been conducted:

*. . . [T]his was something that had gone on for 18 or 19 or 20 months by that point in time with RFIs and RFPs and proposals and BAFOs and second BAFOs and documents just too voluminous for me ever to go through in what was, for me, a very short period of time. . . . I had 30 days . . . to get their briefs, look at what they presented, conduct the hearing, analyze the results from the hearing, and issue a report . . . but in hindsight, it may very well have been relevant. At that moment*

*of time my lack of overall knowledge of that project probably wasn't to my benefit in terms of knowing what to ask for to make those evaluations . . . [G]oing in hindsight, it [the full record of the MET proceedings] may have been a very important thing to ask for.*

## ***Obstruction/Avoidance of Financial Due Diligence***

When the E-ZPass contract was signed and formally executed on March 10, 1998, it was advertised as a zero-cost express lane to the high-tech future of toll collection. Start-up costs were to be covered by substantial borrowing via a \$300 million bond issue under the imprimatur of the New Jersey Economic Development Authority. But the bonds and the interest on them would be repaid with revenue drawn primarily from fines against E-ZPass violators and the leasing of fiber-optic telecommunications cable installed along the toll-road rights-of-way. Indeed, it was announced that the project not only would break even but would actually make money: projections showed more than \$608 million in revenue over the eight-year contract period against some \$573 million in estimated overall costs, for a net profit of \$34.9 million. This unique financing structure was the centerpiece of an effusive outpouring of rhetoric for public consumption that accompanied the project's official launch. "It is a unique public-private partnership that advances our goal of a seamless, regional electronic toll system that will unify the northeast under one integrated system," Governor Whitman declared. "It also means that Garden State motorists will soon be able to reap the benefits of advanced technology at no cost to the taxpayers." In the same press release, Turnpike Executive Director Edward Gross characterized the financing plan as "21<sup>st</sup> century thinking for 21<sup>st</sup> century technology."

Amid the hubbub, however, a dark financial cloud already loomed.

In the months preceding the launch, unpublicized internal recalculations of the cost and revenue projections, primarily with regard to violation-fee revenues, along with

revisions of the proposed contract term, combined to reveal a decline of nearly 80 percent in the estimated profit – falling from \$159 million at the time the Turnpike Authority’s governing board had awarded the contract to \$34.9 million when the contract was executed, a drop of more than \$124 million.<sup>39</sup> As events soon showed, that trend would continue unabated. By early 2002, not only had the malfunctioning E-ZPass system failed to net a single dollar, it produced a deficit approaching \$500 million – missing its launch-date profit target by more than 1,400 percent.

The Commission examined a wide range of events and circumstances surrounding the E-ZPass procurement and found that the financial collapse should have come as a surprise to no one, least of all those in charge of orchestrating it. Normal and reasonable due diligence was obstructed or avoided altogether, known risks were minimized, warnings of potential fiscal peril were set aside and key personnel were ignored.

### **No Independent Financial Evaluation**

The Commission found that prior to the award of the E-ZPass contract, no comprehensive, independent study was undertaken by or on behalf of the Consortium to test the validity of key assumptions upon which the MFS revenue projections were based. The failure to exercise appropriate public-sector due diligence in this matter occurred despite deep skepticism that permeated the ranks of Consortium personnel, including those at a senior level. Executive Directors of two of the five participating toll authorities, members of the vendor evaluation (MET) team, finance department staffers in various agencies – including the Turnpike Authority itself, the lead entity – all testified

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<sup>39</sup> The \$159 million includes fiber-optic revenue projections over 20 years. The \$34.9 million contains a 10-year revenue projection for fiber.

under oath that, prior to the contract award, they expressed serious reservations, to those in charge, over whether E-ZPass could ever pay for itself or generate a profit. Indeed, this tide of doubt continued throughout the months leading up to the project's launch in March 1998.

Much of this internal, unpublicized skepticism centered on the self-funding strategy's primary underpinning – a plan to raise hundreds of millions of dollars through fines levied against motorists caught cheating. The system was to work like this: Vehicles passing through the new toll gates without proper E-ZPass registration would be identified by a photographic image of the license plate. The plate numbers then would be processed through a vast motor-vehicle database, and violators each would be assessed a \$25 “administrative fee.” Total proceeds from this component alone were projected in the range of \$400 million – fully two-thirds of the total E-ZPass gross revenue stream that was anticipated over the term of the contract.

But reliance on scofflaws as the main funding source for an initiative on the scale of a regional electronic-toll system had never been attempted in the United States, and some in the Consortium questioned whether the violation system could ever be effectively enforced. Others worried that as more and more motorists signed up for E-ZPass amid a concerted promotional effort planned by the Consortium, the pool of violation revenue would diminish more rapidly than anticipated. Further, at the time of the contract award to MFS in March 1997, legislation to authorize the monitoring, photographing and processing of license numbers had not been enacted.

Among those who vocalized doubts about the violation-funding approach was James A. Crawford, Executive Director of the South Jersey Transportation Authority.

Crawford told the Commission that he and his colleagues at the SJTA harbored serious reservations throughout the procurement and that he personally conveyed the agency's concerns on numerous occasions to Consortium officials, including Mortimer and Gross. Crawford said that even after summary presentations were made by Mortimer that the funding structure under the MFS proposal would yield a substantial surplus, he, Crawford, advised his agency's governing board that a deficit was just as probable. As a result, the SJTA determined at an early stage that it would be prudent to establish a reserve account that could be drawn upon to cover the agency's share in anticipation of a revenue shortfall.<sup>40</sup>

Kathleen M. Sharman, the SJTA's Director of Finance, told the Commission, "I was very skeptical that the projected revenue would be forthcoming." Speaking of her interaction on this issue with personnel at other member agencies of the Consortium during this period, Sharman testified, "We all thought it was a little bit crazy."

Separately, top personnel at the New Jersey Highway Authority, operator of the Garden State Parkway, developed similar concerns. Heavy reliance on violators for funding was a major issue for the Highway Authority because the Parkway was to account for approximately \$244 million in violation revenue over eight years – fully three-quarters of the total projected for the entire Consortium. Lewis B. Thurston III, the Highway Authority's Executive Director, testified:

*I was always skeptical. I tried to be optimistic as a member of the Consortium team and the administration team, but I was always skeptical that . . . sufficient revenue could be realized.*

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<sup>40</sup> Despite such concerns, the SJTA continued to participate in the Consortium effort because it still offered the agency an opportunity to take advantage of a centralized back-office administrative operation for customer service and toll violations processing.



*This was somewhat uncharted waters. No agency, no transportation agency had done something similar. So it was difficult for anybody to point to experience, either to say that it was going to work or not going to work and revenue would be sufficiently realized. So we were all somewhat speculating.*

Thurston and other Highway Authority officials told the Commission that they raised doubts verbally in various Consortium meetings throughout the summer and fall of 1996. By December, their core concerns crystallized in the form of a written memorandum produced by Budget Officer Thomas F. Butler and signed by him and two other Authority officials, Charles D. McManus and Stanley Ciszewski. The memorandum, dated December 27, 1996, suggested that based upon the Highway Authority's own calculations, no more than approximately \$20 million – less than one-tenth of the vendor's projection – would be derived from Parkway E-ZPass violations, even if the system functioned optimally. The analysis was based upon data showing that most Parkway toll violations were committed by a relatively small core of regular transgressors. Highway Authority officials concluded that in all likelihood, this pool – and the revenue generated by it – would only decline over time. They recommended the Consortium retain a major accounting firm to conduct an independent analysis. Thurston forwarded the document to Mortimer and Gross under a cover letter, stamped "CONFIDENTIAL," dated January 8, 1997:

*Throughout the procurement process our representatives have been concerned and have expressed these concerns about public acceptance of the massive enforcement effort necessary to attempt to deal with all violators and the reliability of revenue to be derived from the administrative fee associated with the violations. We continue to have these concerns.*

*Because of the tightness and intensity of the procurement schedule, it was not possible to do as much analysis of the revenue potential to*

*verify the vendors (sic) assumptions, as we might have liked. Because of the recent delays in the process, our staff has had an opportunity to do some further evaluation relative to this concern.*

*Enclosed is a copy of an evaluation report which our three principal project representatives have submitted to me which includes some analytical data and a recommendation to have an independent firm do further analysis. [Highway Authority] Chairman [Joseph] Buckelew and I have reviewed this and feel we should share this information with you at this time so that you, as the lead persons and agencies in the consortium, may have the benefit of it. We believe it would be beneficial to have further analysis done and I will be glad to discuss with you the appropriate manner in which that should be done both for the consortium and for the Highway Authority.*

*I look forward to discussing this matter with you after you have had a chance to review the enclosed information.<sup>41</sup>*

Although the issues raised in this document went to the very heart of the proposed self-funding approach, Gross and Mortimer both swore to the Commission that they could not recall seeing it.

Subsequent to this communication, Butler and McManus told the Commission they were summoned to a meeting at Turnpike Authority headquarters to discuss the Highway Authority's concerns. In sworn testimony, both expressed vivid recollection of this session and identified the other attendees as Paul A. Carris of the Turnpike, the ETC Program Manager; Francis K. O'Connor of the Turnpike, at the time ETC administrative manager; and Carol Ann Hollows, an aide to Mortimer at NJDOT. Carris, O'Connor and Hollows all testified that they could not recall this meeting. No representatives from the other Consortium agencies were invited or formally notified of the Highway Authority's memorandum.

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<sup>41</sup> See Appendix at pp. A-32 through A-41 to review confidential Highway Authority memoranda and the response of Turnpike Authority consultant Phoenix Planning and Evaluation Ltd..

On January 17, 1997, a firm that had been hired by the Turnpike Authority to serve as a “special services consultant” during the procurement – Phoenix Planning and Evaluation Ltd. of Maryland – submitted a memorandum critiquing the Highway Authority’s evaluation. In this same document, however, Phoenix conceded that “violation rates [projected for] post ETC implementation are difficult to predict.” In light of that, the firm seconded the Highway Authority’s suggestion that an independent review be conducted.

The Commission found no evidence to show that any such review, either in response to concerns expressed by the Highway Authority or by Phoenix, was carried out prior to the award and execution of the E-ZPass contract.

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A number of witnesses in this investigation referred to Phoenix as the Consortium’s “financial adviser.” But Margaret Melhem, who served at the time as the firm’s principal representative to the Consortium, told the Commission that that term was inaccurate and inappropriate.

Melhem testified that Phoenix had no prior experience in electronic-toll collection, had never worked in conjunction with toll authorities and performed no evaluations in fundamental areas related to the E-ZPass project’s financial assumptions and underpinnings. At the time, according to Melhem, the firm employed a staff of approximately 12 to 16 individuals serving government clients primarily in the area of “electronic benefit transfer” systems related to the administration of food stamp and cash-welfare benefit programs. Melhem testified that Phoenix was not hired by the

Consortium as an instrument of due diligence and was not asked to evaluate the feasibility of the self-funding approach. Further, she testified that the firm did not assess the reliability of the violation-revenue projections. Moreover, because Phoenix lacked expertise in fiber-optics, it deferred to another consultant – Kingston Cole & Associates – when it came to the issue of estimating revenue from the lease of fiber-optic cable along the toll road rights-of-way. Melhem stated that Phoenix engaged in no independent data-gathering, and did not evaluate the cost and revenue projections submitted by either Lockheed or MFS.

Phoenix was selected through competitive bidding by the New Jersey Turnpike Authority under terms of a \$150,000 contract in April 1996.<sup>42</sup> Other bidders included the major accounting firms of Deloitte & Touche, which withdrew its proposal prior to evaluation, and Coopers & Lybrand, L.L.P., which was disqualified based upon a determination that it had an existing auditing relationship with one of the pre-qualified vendors vying for the overall electronic toll collection contract. Prior to its disqualification, Coopers had finished a close second – 135 points behind Phoenix, based upon a possible total of 4,000 – in the evaluation scoring. Documents reviewed by the Commission show that officials of the Highway Authority expressed a preference for Coopers based on the view that the firm possessed greater experience in matters related to toll collection.

Melhem described Phoenix’s role as one that evolved over time, starting with an explicit focus on two areas: development of formulas for allocating costs among the

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<sup>42</sup> Phoenix was hired as the Consortium’s “special services consultant” based upon a \$150,000 contract executed on August 7, 1996. Through the fall of that year, Phoenix was paid a total of \$225,750, which included fees for additional services rendered.

Consortium members, and assessing the functionality of the ETC program’s back-office, or “clearing-house,” operations (i.e. the Customer Service Center and Violations Processing Center.) Melhem testified that upon reviewing the E-ZPass Request for Proposals (RFP), Phoenix found it unduly vague in specifying the operational requirements of these clearing-house functions. The firm requested a clarifying amendment. Melhem testified that the request was denied by Consortium officials on grounds that “there was a timeline.” Melhem addressed a number of key issues in her sworn testimony:

*Q. Was Phoenix ever asked to evaluate the feasibility of the self-financing approach?*

*A. No.*

\* \* \*

*Q. How about, were you ever asked by the consortium to evaluate the underlying premise that administrative fines assessed to toll violators could be or would be sufficient as a funding mechanism for the entire project?*

*A. No.*

\* \* \*

*Q. Would Phoenix be considered the financial consultant to the Consortium during the procurement? I should say, financial advisor to the Consortium.*

*A. No, No. We were primarily looking at the clearinghouse operations and then helping them run some models based on the data that we were given, but, I mean, again, toll roads are not our area of experience, so we, you know, never represented ourselves as such.*

As the procurement entered the best-and-final-offer stage in October 1996, Melhem testified, Phoenix undertook some limited modeling work to examine the potential effects of different E-ZPass violation rates and market penetration rates.

However, she stated that the firm relied solely on data provided by the Consortium entities and the bidders, and that Phoenix was never asked to assess the validity of the operational assumptions upon which these numbers were based.

Beyond Phoenix, in the months prior to the contract's execution in March 1998, the Turnpike Authority retained Public Financial Management Inc. (PFM) as a general financial advisor. However, at no time was PFM asked to provide any advice to the Consortium relative to the actual E-ZPass procurement. In a July 17, 1997, letter to Gross, the firm stated:

*While PFM currently serves, and has served in the past, as the general Financial Advisor to the New Jersey Turnpike Authority..., PFM has not been asked to provide advice to the Authority or any Consortium member for the ETC project up to this point. PFM has not been involved in structuring the Financing Plan. All information received by PFM regarding the Project has been obtained over the past eight days.*

*The scope of PFM's assignment has been limited to the tasks outlined above [i.e. the role of Newcourt Capital as financial advisor to MFS and the appropriateness of lender rates and fees]. Furthermore, given the accelerated deadline of nine days for PFM's review, we could not provide you with comfort, if asked, that a thorough evaluation of the financing structure of the Financing Plan could be completed. Any conveyance of PFM's opinions contained herein by the Authority to the consortium represents tacit agreement by the Authority, acting as the lead agency to the Consortium, as to the limited nature of PFM's scope of work.*

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During the summer and fall of 1997 – after the contract was awarded but before its formal execution – then-NJDOT Commissioner John J. Haley raised questions and concerns related to various aspects of the deal, including the revenue projections.<sup>43</sup> At

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<sup>43</sup> Haley succeeded Wilson as NJDOT Commissioner in early 1997.

the time, personnel at the Port Authority were questioning the projected rate of E-ZPass violators, contending that the Consortium estimates were overly optimistic. In late September, Haley empaneled a special “Working Group” to review key aspects of the procurement to that point. However, not all agencies were asked to participate; indeed, three of the Consortium’s five entities were left out, including the Consortium’s lead entity – the Turnpike Authority – and the two agencies that had consistently raised questions about the projected revenue streams, the New Jersey Highway Authority and the South Jersey Transportation Authority. Further, the work of this group was curtailed after about two weeks, sufficient time to produce a cursory report but not to conduct an in-depth review with independent data testing the revenue assumptions.<sup>44</sup>

Notably, Gross testified that he only became aware of the existence of Haley’s task force after the fact. Gross stated that Haley put the group together “behind my back.” Gross also testified that had he been aware of the plan, “I would have been opposed to it” on the grounds that it contributed to a delay in the completion of the procurement.

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Another opportunity for public-sector due diligence presented itself during the weeks immediately preceding the formal execution of the contract when the New Jersey

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<sup>44</sup> Members of the “Working Group” were Carol Ann Hollows of NJDOT; Steven Peyser of Public Resource Advisory Group Inc.; Karen A. Antion and Charles F. McClaffery of the Port Authority of New York and New Jersey; Howard R. Giddens, Jr. of DELDOT; and James Poole of the N.J. Department of Treasury.

Economic Development Authority (EDA) was asked to play a central role in raising start-up capital for the project.

In early February 1998, EDA Chief Executive Officer Caren Franzini received an unsolicited telephone call from the State Office of the Treasurer. On the other end of the line was James Poole, Director of the Division of Public Finance, who informed Franzini that an application for financing soon would be submitted to EDA in connection with the E-ZPass procurement. Franzini testified that the caller conveyed a clear sense of urgency and made it plain to her that “they wanted to get it done right away.” EDA records show that an application for the issuance of \$300 million in taxable EDA bonds was submitted by the Consortium’s chosen vendor, MFS Network Technologies, on February 23, 1998. The application received both preliminary and final approval 16 days later on March 10, 1998 – the same day of the contract’s formal execution. Between the date of its receipt and its unanimous approval by the EDA’s governing board, the MFS application – in accordance with the agency’s statutory obligations and its standard operating procedure in such matters – was subjected to minimal scrutiny.

According to Franzini, the proposed financing package was already structured when it reached EDA for consideration, and the agency played no role in designing it, evaluating its underlying assumptions or lining up prospective investors. The sole purpose of EDA’s involvement was to act as a “conduit” for the issuance of bonds on behalf of the Consortium, given the fact that no individual member of that regional group possessed unilateral legal standing to borrow for the whole. Although it is not unusual for EDA to serve as a lending conduit, this instance was unique in at least two respects, according to Franzini. It was the agency’s first involvement in issuing bonds for



multiple toll authorities grouped as a single unit, and the relative speed with which this particular financing was handled was “the exception rather than the norm” for typical EDA projects.

Franzini testified that the EDA’s overriding concern with the MFS application was two-fold: that buyers of the bonds be protected against potential loss and that EDA itself be indemnified. She said EDA officials were satisfied that an appropriate level of investor security would be provided by the financing proposal’s so-called “True Up” Agreement, which obligated the Consortium members to pay off the bonds with attendant interest if insufficient revenue were generated during E-ZPass operations. As to the issue of safeguarding EDA’s position, Franzini testified that she was assured by Gross that an indemnity clause would be written into the final bond documents prior to closing. EDA also secured a legal opinion from the Office of the New Jersey Attorney General to the effect that EDA’s participation in the proposed financing fell within the confines of its operating statute. Franzini told the Commission that beyond this level of analysis, the financing application generated little discussion among EDA staff and essentially received *pro forma* approval from the agency’s governing board based upon a four-page summary memorandum prepared at her behest by Lawrence Cier, the EDA’s Director of Investment Banking.

Franzini testified that EDA’s review did not include an evaluation of the financing proposal’s underlying revenue and cost assumptions. “We relied on the toll roads and their expertise,” she stated. Absent the True Up Agreement, she noted, her agency most likely would have carried out an analysis of “the primary sources of revenue.” But for EDA’s purposes, “it didn’t matter.” With the True Up, “we were relying on the strength

of the toll roads.” She stated that it was not unusual for proposed financing packages to arrive at EDA fully structured, thus requiring minimal staff attention before presentation to the agency’s governing board. In such instances, EDA often relies on outside entities, such as the applicant’s financial adviser, to have already conducted an expert analysis and evaluation. In the case of E-ZPass, the agency relied upon representation made by the Consortium as well as paperwork submitted by Newcourt Capital Inc., the financial adviser to MFS. When the application was presented to the EDA Board for final consideration on March 10, 1998 – the same date as the formal execution of the E-ZPass contract by the Consortium – Franzini said there was virtually no discussion before it received unanimous approval. With regard to the selling of the bonds, Franzini stated this was the sole responsibility of Newcourt Capital, the placement agent for the bond issue. The E-ZPass bonds required the firm to locate particularly sophisticated investors due to the complexity of the financing arrangement and the fact that it involved multiple public entities.

The bond counsel was selected by MFS from a list provided by EDA and received a lump-sum payment for services rendered of \$100,000 at the Consortium’s expense. She testified that the E-Z-Pass vendor, MFS Network Technologies, did that in connection with its financing application for \$300 million in taxable bonds:

*Q. Who would be the person who would have selected the bond counsel?*

*A. MFS.*

*Q. . . . Just [what is] the process of how normally bond counsel would have been assigned to this issue?*

*A. The borrower would select bond counsel off of our approved list. Bond counsel would submit a fee, and that would be approved by the Attorney General’s Office.*

**Q.** *So in this case, MFS looks at the approved list of EDA bond counsel, and in this case, they would have selected this law firm of Whitman [no relation], Breed, Abbott & Morgan, correct?*

**A.** *Correct.*

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During her sworn appearance before the Commission, Franzini was questioned about documents received by the Consortium from MFS and the firm's E-ZPass financial adviser, Newcourt Capital. The MFS document was an October 10, 1996 letter to Paul Carris wherein MFS opined that the self-funding approach might not be attainable. The Newcourt Capital document was a July 24, 1997 letter to Gross in which the firm characterized the potential revenue stream as speculative. Franzini testified:

**Q.** *Were you ever aware that . . . in written correspondence to Ed Gross, [Newcourt Capital] informed Ed Gross that they believed that the revenue stream would be speculative?*

**A.** *I have no knowledge of any letters to Ed Gross, Newcourt Capital.*

**Q.** *Would that be something that you or EDA would want to consider at the time where the financial advisor or a principal involved in the issuance of the bonds themselves is saying that the revenue stream is speculative?*

**A.** *That's a very important piece of information that we would have – I should have known and we should have divulged to our board members if that was being represented.*

## **Risks Disguised**

During the summer and early fall of 1996, representatives of Chase Manhattan Bank, a primary MFS partner in the procurement, staged a series of presentations to instruct Consortium officials about the intricacies of violation-revenue projections. These projections were based upon the effect of three factors working in concert with one

another: the market penetration rate, or the overall level of E-ZPass usage by motorists; the violation rate, or the percentage of all users who were violators; and the violation collection rate, or the percentage of total violations resulting in actual fines paid. To illustrate the full range of possible outcomes from interaction between this trio of changeable criteria, Chase constructed a matrix that came to be known internally as “the magic cube.”

Witnesses to these presentations, including Carris, Mortimer and members of the MET evaluation group, told the Commission in sworn testimony that Chase officials made it plain that the components of the magic cube were extremely volatile and that even relatively minor changes in one or all of the factors could have a drastic impact on the bottom-line revenue picture. Donald E. Mauer, then-Chief Engineer of the South Jersey Transportation Authority and a member of the MET, testified:

*Q. . . . Is it fair to assume that Chase Manhattan Bank during those presentations did not hide the fact that slight changes in various parameters could have drastic effects in the revenue projections?*

*A. They were very up front. [T]he presentation was very tedious, because . . . it was formula driven. A lot of formulas had to be vetted against different parts of the industry. . . It was a long presentation, but the thing I remember most about it is there [were] 900 and some points of entry into this cube, and anyplace you go in, you could come out in a drastically different place and the swing was hundreds of millions of dollars.*

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*They [Chase] wanted to present it to anybody who was willing to listen. They really believed in what the cube did, [but] they really wanted everybody to understand how many multiple possibilities there were.*

More than half of the magic cube configurations showed that at the end of the originally proposed eight-year contract, the Consortium would either just break even or sustain a deficit of increasing size depending upon the actual magnitude and mixture of the three criteria. In instances where administrative fines could be collected against 50 percent of all violations, the Consortium would stand to make a profit only if the actual violation rate remained above 1 percent, according to the Chase analysis.

Similar calculations were conducted by Lockheed, whose analysis showed an even more limited array of profit-making options under the violation-revenue approach. Among other things, Lockheed told the Consortium that the violation collection rate would need to exceed 70 percent to make this approach effective as a generator of substantial revenue.

According to various witnesses in this investigation, the data utilized by each vendor in making these calculations were provided by the Consortium. Louis A. Fuertes, the lead Chase official at the time, told the Commission that Consortium officials, during the negotiating process, singled out one set of criteria to be used by the vendors as the basis for preparing offers. The numbers specified by the Consortium were:

- 35 percent penetration rate
- .93 percent weighted violation rate
- 50 percent collection rate

As a result, the violation revenue projections submitted by both Lockheed and MFS at the time were similar in scope and magnitude.

During meetings and in the exchange of correspondence with representatives of MFS and Lockheed in late September and early October 1996, the Consortium received

multiple warnings with respect to the volatility of the revenue projections.<sup>45</sup> Indeed, during the course of preparing final offers in October 1996, MFS submitted violation-revenue projections for the overall project that fluctuated between an estimated surplus of \$8.5 million and a deficit of approximately \$12 million at the end of the contract.

The inherent uncertainty of this violation-revenue picture, however, was never adequately conveyed to those formally charged with the responsibility of voting to award the contract, that is, the Turnpike Authority's Board of Commissioners. According to Frank X. McDermott, the then-Chairman of the Turnpike Authority's Board, and Commissioner Joseph P. Miele, who served on the Consortium's Executive Council, the Turnpike's Board was never apprised of the full scope of the risk and volatility associated with the revenue projections, particularly as illustrated by analytical tools like Chase's magic cube. Indeed, there is no evidence to show that the Turnpike Board was ever presented with data suggesting that the two revenue streams upon which Consortium would be most reliant – fees from E-ZPass violators and the leasing of fiber-optic cable – could easily drain away into a deficit depending on the variables.

The Board's vote to award the contract to MFS was based primarily upon a summary PowerPoint presentation by Mortimer purporting to show that the self-funding approach was entirely viable and that the MFS offer would produce a surplus of \$159 million compared to a \$22 million deficit with Lockheed.<sup>46</sup> No such presentation was

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<sup>45</sup> See section entitled *Vendor Warnings Minimized* at p. 128.

<sup>46</sup> The Commission sought but was never provided with, and thus could not ascertain, supporting data for these projections, which differed substantially from projections made by the vendors in their best and revised final offers.

conducted in order to provide the Turnpike Board with the full panoply of potential risk and the volatility of the revenue factors.

### **Exclusion, Manipulation and Intimidation of Turnpike Personnel**

As lead agency for the regional Consortium, the New Jersey Turnpike Authority was assumed by many who participated in the E-ZPass procurement to have brought substantial expertise to bear on the project, particularly in the area of financial analysis, prior to the award of the contract.

In reality, the Turnpike's own finance staff was out of the loop for months before the agency's governing board voted unanimously to award the contract to MFS in March 1997. Despite this lack of involvement, the Turnpike's Chief Financial Officer was pressured at the eleventh hour to certify the purported accuracy of cost and revenue projections. Furthermore, other Turnpike staffers – including senior officials who had been assigned direct roles in the procurement – told the Commission that, as the project proceeded toward implementation and beyond, they, too, were relegated to the sidelines under questionable circumstances.

The individual in charge of day-to-day operations at the Turnpike during this period was Edward Gross, the Authority's Acting Executive Director from 1994 until January 1997, when "Acting" was dropped from the title.<sup>47</sup> According to sworn testimony from multiple witnesses and a thorough review of the record, Gross's tenure during the E-ZPass procurement was marked by turmoil virtually from the start. In some instances, the turmoil was the result of events and circumstances beyond his control. It

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<sup>47</sup> Gross's tenure as Executive Director ended in January 2002 when he was discharged from the post by Governor James E. McGreevey.

was not Gross's decision, for example, to staff the procurement with individuals who, though Turnpike Authority employees, reported outside the agency to senior officials at NJDOT. Further, Gross was confronted internally with a series of difficult personnel issues. Witnesses told the Commission that key Turnpike employees simply did not get along, and simmering interpersonal disputes and rivalries periodically erupted into full-blown formal complaints.<sup>48</sup> In one such instance, an employee of the Authority's Budget and Finance Department, Francis K. O'Connor, accused the department head, Catherine A. Coryat, of pressuring him during the vendor evaluation process in a procurement unrelated to E-ZPass. An internal investigation produced no finding of wrongdoing. O'Connor, who meanwhile had been transferred to the Turnpike's central maintenance facility in Hightstown, filed a civil complaint alleging harassment. In late 1995, in an action coincident with settlement of that complaint, he was promoted, given the title of Special Project Control Administrator and assigned to the E-ZPass project as deputy to Paul A. Carris where his duties included controlling the flow of internal documents related to the procurement.

Individuals who worked at the Turnpike during this period testified that amid such personnel tangles, Gross made matters worse. They described him as an overbearing manager who tolerated little dissent and showed no patience with anyone or anything he perceived as an obstacle to rapid completion of E-ZPass. Gross himself testified that the

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<sup>48</sup> Gross himself was named as a plaintiff in three separate civil actions filed by senior employees of the Turnpike, including Chief Financial Officer Catherine A. Coryat (nee Schladebeck), who filed a complaint in October 1997 alleging she had been subjected to a hostile work environment. Coryat's complaint included a recitation of incidents related to the E-ZPass procurement.



peculiar resolution of the O'Connor matter ultimately was his doing, despite the longstanding record of friction between O'Connor and the Finance Department's Coryat.

Further, while Gross told the Commission he had no substantive involvement in the project prior to mid-November 1996, documentary evidence and the testimony of others show that he was aware of, if not directly party to, various significant milestones in the procurement process until that point. Gross also testified that he knew of the Finance Department's complaints of being left out of the process, but despite this, sought to have the department's director certify E-ZPass cost and revenue figures she claimed were unverified. The record also shows that after mid-November 1996, Gross assumed direct control over the negotiation process leading to the Consortium's final contract with MFS.

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During the early stages of the procurement, beginning in late 1995, the Turnpike's finance staff appeared, at least on paper, to be positioned for a central role. In a memorandum dated December 27, 1995, to Margro, Coryat sought to formalize staffing arrangements for the project: "As has been discussed on numerous occasions, implementation of Electronic Toll Collection will have a significant impact on the Finance & Budgets Department's operations," Coryat wrote. "I have assigned Pamela Varga and Donna Manuelli to represent this department. I would appreciate it if they were kept apprised of the process. They are also available for any input required for this process."<sup>49</sup>

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<sup>49</sup> See Appendix at p. A-42.

All three of these finance personnel, however, testified that their involvement was never more than sporadic through the spring and summer of 1996, and was virtually curtailed that fall and in the months immediately preceding the award of the contract by the Turnpike's governing board in March 1997. Addressing a key ramification of this disconnect, Coryat testified:

*Q. Do you know if anyone did an independent assessment of the underlying assumptions for the revenue projections?*

*A. No, I don't know.*

*Q. Would your department be capable of doing that kind of analysis . . . ?*

*A. Yes.*

*Q. Were you ever asked?*

*A. No, not until after.*

\* \* \*

*Q. . . [Y]ou were only asked to do any kind of analysis after the contract was already awarded to MFS?*

*A. Yes.*

Manuelli testified that a pattern of selective exclusion was established throughout 1996 leading to the contract-award recommendation that autumn by the MET team:

*Q. What was the level of cooperation you or the Finance Department were receiving from the ETC staff?*

*A. We weren't receiving any cooperation. We were, you know, frequently not invited to meetings, invited at the last minute. We didn't get the information. . . . We never got the information we needed. So it was not a very healthy, cooperative working relationship.*

\* \* \*

*Q. Did you ever complain to anyone about this?*

*A. Well, sure. I complained to my boss, Cathy Coryat.*

*Q. Do you know if she took any steps to rectify the situation?*

- A. *Yes. I believe she contacted – you know, initially she contacted Tom Margro, she contacted Ed Gross, she discussed it with Paul Carris. I know she did verbally and I believe she may have also done it in writing.*

According to documents obtained from the Turnpike Authority, Coryat alerted senior Turnpike officials, including Gross, about her department's frustration at least as early as August 1996 after Margro had announced his intention to resign as the Authority's Chief Engineer. In a memorandum to Gross dated August 23, 1996, Coryat stated, in part:<sup>50</sup>

*I believe Finance & Budgets has a very important role to play in the ETC procurement and have assigned two extremely competent professionals to this task. While the Authority has an ETC staff, I have been told that their purpose is to represent the Consortium as a whole, not the Authority. Since this is the case, I believe it to be critical that financial matters receive the attention they deserve. The best interest of the Consortium and the best interest of the Authority needs unbiased representation. We believe the ETC process to be important however, (sic) this is only one of many responsibilities of the Finance & Budgets representatives.*

*Overall, there have been activities where Finance & Budgets participation would have been very beneficial to the process. I realize that the ETC project has been an intense effort however (sic) you should know that this department is often left out of the loop. The lack of notice makes it extremely difficult to plan anything and reduces the opportunity to give things their proper attention. This department is repeatedly not informed of meetings or is asked to review things at the last minute. In fact, we were just invited today, Friday, to attend presentations on Monday. Most of the time we need to rely on information from our colleagues from other agencies since they usually receive information and prior notices.*

*I just want you to be aware of the extent of our efforts as well as our frustration.*

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<sup>50</sup> See Appendix at p. A-43.

One week later, in a follow-up memorandum dated August 30, 1996, Coryat complained to Carris that her staff's problems of access to meetings and information persisted. Referencing a Consortium presentation that had been held, Coryat stated, in part:<sup>51</sup>

*As you know, I have spoken to Tom Margro and Ed Gross several times, and Pam Varga has spoken to you, regarding not being properly notified about ETC meetings. Ed assured me on August 29, 1996 . . . that he had discussed this matter with you and there would no long (sic) be a problem. . . .*

*At the presentation, members of other Authority's information (sic) Donna that they were expected to be at the negotiation meetings and that they received a schedule for the next three weeks. We have not received any notification of the negotiations meetings or schedule. I would appreciate this matter being addressed once and for all.*

Gross testified that he was aware of these concerns at the time, that he discussed them with Carris and O'Connor, and that both individuals denied cutting Coryat and her staff out of the procurement. Gross acknowledged, however, he did not investigate further:

*. . . I recall more than once that Cathy Coryat advised me that they were not getting cooperation from Paul Carris and Fran O'Connor and were not able to do the work that was required of them. And I spoke to both Carris and O'Connor who claimed otherwise, saying that the[y] were always – they always were cooperative, the finance department was always invited to meetings, and there was a number of meetings where they didn't attend. And, you know, I said – my response to it is that I wasn't able to judge who was accurate and who was not accurate. I said, Just cooperate. Get this stuff done. You know, it's important for the finance department to look at the numbers.*

In their appearances before the Commission, Carris and O'Connor denied deliberately or knowingly frustrating efforts by the Finance Department staff to participate in the

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<sup>51</sup> See Appendix at p. A-44.

procurement. As to Gross' claim that he spoke to them about Coryat's complaints, however, both testified that they could not recall any such discussions.

Contrary to Gross' purported admonition that it was "important for the finance department to look at the numbers," Coryat and her staff testified that they had difficulty throughout the fall and winter of 1996-97 gaining access to key financial data related to the vendor proposals and were not active participants in the negotiations leading to submission of final offers. Further, they testified that they played no role in evaluating the accuracy of cost and revenue projections as submitted to the Consortium by the vendors, nor were they asked to review the New Jersey Highway Authority's December 1996 memorandum raising questions about the long-term accuracy of the violation-revenue estimates. The finance personnel also testified that they did not participate in presentations summarizing the vendor offers for review by the governing boards of the various Consortium entities, including the Board of Turnpike Commissioners, prior to the award of the contract.

Despite this lack of involvement, Coryat was asked by Gross to sign off on the accuracy and validity of revenue projections contained in the MFS proposal just days before the Turnpike Authority's governing board was to vote to award the firm the E-ZPass contract. The trigger for this incident was a proposed agenda that circulated at the Authority's headquarters the week before the board's March 25, 1997 meeting. MFS's contract offer was scheduled for a final vote, and the agenda item that embodied it bore a blank signature block above Coryat's name. Typically, the Authority's practice is to have the Chief Financial Officer sign or initial any item slated for a board action that may impinge upon the agency's operating or capital budgets. The object of this exercise is to

provide certification that adequate funds are available. Coryat testified that she was surprised to find that she would be required to sign the MFS item because the E-ZPass procurement, as structured, did not involve any immediate direct expenditure of Turnpike funds. More importantly, her department had not yet evaluated the firm's cost and revenue projections, particularly the bottom-line estimate of a \$159 million surplus.

Several days before the Turnpike Authority Commission's scheduled vote, Coryat was summoned to a meeting with Carris and Diane Scaccetti, then-Deputy Executive Director, at the behest of Gross, who was away from headquarters at the time. Also present was Manuelli. At this meeting, according to Coryat and Manuelli, Carris asked her to sign off on the MFS agenda item. Coryat described the session in sworn testimony as "very pressure-filled":

*Q. Why do you think the signature, your signature on that agenda item was important to Mr. Gross?*

*A. Well, because it would show that the financial person at the Authority certified those numbers.*

*Q. Certified, in that you believe those items to be accurate?*

*A. Yes.*

*Q. Did you believe the numbers to be accurate?*

*A. No.*

*Q. Why do you believe the numbers were not accurate?*

*A. There were too many discrepancies between what the proposal said and what their [MFS's] presentation said. There were too many variables. Even I wasn't comfortable saying that we were going to make that kind of money. I just didn't think that was going to happen.*

*Q. Why didn't you think the proposal was . . . going to make that kind of money?*

*A. I thought there were pieces missing. Financing costs, fiber maintenance, change in – a change in anything, a change in our tolls, change in the collection of those violations could throw it off, you know, significantly.*

At one point during the meeting, according to those present, Coryat asked whether the Authority's special services advisor, Phoenix, would be asked to sign the item. She testified that Carris scoffed at this suggestion, responding to the effect " 'they would never sign . . . those numbers.' And, I was like, but you expect me to?"

Carris testified that he had limited recollection of this encounter beyond the exchange concerning Phoenix:

*She expected Phoenix to independently evaluate the cost proposals and to sort of bless them as valid, and I said that wasn't their role. She had always complained about her staff – well, she was complaining about the process because, again, the time frames, the meetings getting called on short notice. I believe she had issues with the documents [being] in a locked room. I'd say a good portion of it was just, you know, complaining about the process that had been imposed on everybody.*

**Q.** *Did she ever voice to you during this meeting that she had a concern that she didn't think the numbers would work or the revenue stream would be foreseeable?*

**A.** *I believe so, yes.*

Coryat described the tone of the meeting as such that she feared consequences relating to her employment:

*I was very nervous. I was afraid, I will say that. I was afraid of what Ed would do when he . . . realized I wouldn't sign it. And, yes, I was very afraid.*

\* \* \*

**Q.** *Do you think . . . you were given time to adequately review the agenda item prior to signing it?*

**A.** *No.*

**Q.** *What would have been a reasonable amount of time?*

A. *I don't know what a reasonable amount of time is. We should have been involved throughout the whole process. Had we been involved, there wouldn't have been an issue to having to do this item, you know, overnight. If we had been involved in the process, we wouldn't have had any questions. Hopefully, those all would have been resolved before we got here.*

Manuelli corroborated the essential facts as recounted by Coryat:

*. . . Diane came with Paul Carris and . . . [they] wanted to sit there all day, if we had to, and get us comfortable so that Cathy could sign the agenda item.*

Q. *Get comfortable with what?*

A. *With the agenda item that says that the deal was going to make \$159 million and pay for itself.*

Q. *So, is – Ms. Coryat's objection was to the wording or the fact that they wanted her to sign off and certify that number?*

A. *Both of it. She could not certify that number, she was not comfortable with saying that it would – with the way it was written, to say that the deal was going to make \$159 million and not cost anything. It failed to state that, under a number of different conditions, the deal could cost us money.*

. . .

Scaccetti testified that her role in the meeting was minimal:

*. . . Notwithstanding the fact that Mr. Gross had previously, you know, presented a proposal that was supposed to result in revenue and no expenditure by the Turnpike, it was his desire to have that agenda item still signed off by the comptroller.*

*He happened to be out of the building; and he understood that Cathy Coryat did not want to sign the agenda item, and [he] asked me to go down and speak to her and to try to determine why that was and see if I couldn't resolve it. . . . I really didn't add much other than for me to be in the room while Paul explained to her what she said she had an understanding – understood through the entire process.*

*She felt she shouldn't sign it because there was no monies to be expended by the Turnpike Authority; and, therefore, she didn't believe*



*she had to sign it. Paul continued to try to persuade her; that, you know, it was not so much the monies but an endorsement of the financials and she wasn't prepared to do that.*

On March 25, 1997, the Turnpike Authority's governing board met and voted unanimously to award the E-ZPass contract to MFS. Subsequent to the board meeting, Coryat testified that she was confronted by Gross and, in the presence of Scaccetti, was admonished by him. Coryat testified that, despite the paper trail of prior memoranda to the contrary, Gross implied that she had never complained before about her lack of familiarity with the financial aspects of the procurement:

*After the Commission meeting, he called me up there, and he and Diane were there, and he told me that I was shirking my responsibilities, and I was out in left field. And I mean, it was a whole tirade he went through. And he told me that I never – I should have told him this before. And I tried to tell him, I told you numerous times before that I wasn't involved. And he just, you know, he went on yelling at me. There was no talking to him at this point, he was so angry, you know.*

\* \* \*

**Q.** *But you remember prior to being asked to sign this agenda item, you remember complaining to Mr. Gross that you are not being involved like you should be?*

**A.** *Yes, absolutely.*

\* \* \*

**Q.** *How did the meeting conclude?*

**A.** *He told me I had to make those numbers, you know, get myself to where I felt reconciled with the numbers and come back to him . . .*

**Q.** *But the contract was already awarded at this point, correct?*

**A.** *Yes.*

Scaccetti testified that during this meeting Gross appeared “definitely disappointed” with Coryat’s refusal to sign the agenda, “and he communicated that [to] her.” But according to Scaccetti, Gross “didn’t show a lot of emotion one way or the other, so it was kind of always the same.”

In his testimony, Gross admitted instructing Carris and Scaccetti to meet with Coryat for the purpose obtaining her signature on the MFS agenda item. Gross characterized his action in this regard as “not the right thing to do,” stating:

*. . . [W]hen I had asked Cathy to do that, it was not only premature, it was not proper for her to do that because it wasn’t out of the capital or operating budgets of the Turnpike.*

Gross also acknowledged confronting Coryat after the board’s vote but testified that he could not recall details of the conversation with regard to her doubts about the accuracy of the revenue estimates:

*What I – what I did do is I called her in and I said to her, If you weren’t prepared in going through the numbers, then you should have told me in advance. And I said to her, I need to know what you’re doing so that we work together and we don’t get surprised, and I had a conversation like that with her.*

\* \* \*

*. . . I don’t recall precise dialogue with her where she didn’t agree with the numbers. I recall her saying that she had not had adequate time and adequate backup to be comfortable with the numbers, I remember that.*

Nonetheless, Gross never informed the Turnpike Authority’s governing board of the signature incident, nor did he inform the board that the Authority’s own Chief Financial Officer had voiced concerns to senior staff about the accuracy of the MFS revenue

projections immediately prior to the board's vote to award the E-ZPass contract. Testifying on these points, Gross sought to minimize the actual contract-award decision, characterizing it as merely one step in a lengthy process:

*Q. Did it bother you at the time you were immediately going to the board . . . to award the contract to MFS and your controller at that point [is] saying, I don't have enough information to sign the agenda item?*

*A. Well, she shouldn't have signed it – I shouldn't have asked her to sign it.*

*Q. That's not my question. Did it bother you at the time that your chief financial officer is basically telling you right before the board meeting where the board is going to award the contract to MFS [that] she's not going to sign the agenda item because she doesn't have enough information to do so?*

*A. No, because we still had a long period of negotiations with MFS. We weren't – we weren't doing anything but designating them as the winner of the procurement process, and then we had a major undertaking to go through in connection with the financing, in connection with the contract terms. No it didn't – it didn't trouble me.*

*Q. So your chief financial officer is saying she doesn't have enough information or data to sign the agenda item for this proposal and yet you have no problem with continuing to put the proposal before the board of Turnpike commissioners to award the contract to MFS?*

*A. Well, I mean, it's difficult for me to respond to that by saying yes or no. What I'm saying to you is that the award of that – the award of that contract was a green light to proceed to negotiate a contract and to negotiate financing. That wasn't the final dispositive point in time for the commissioners to act.*

*Q. It was dispositive of which vendor gets the contract, either Lockheed or MFS, right?*

*A. Well, I mean, that – that – yeah, it was – you're absolutely right.*

Gross further testified that he could recall no prior occasion in which an agenda item either requiring, or presumed to require, the controller's signature went before the governing board without it:

**Q.** . . . *[A]s long as you were at the Turnpike, whether as acting executive director or executive director, all budget items – or all items which impacted [the] budget would be signed off on by the finance department or by the comptroller directly?*

**A.** *That – that is correct.*

\* \* \*

**Q.** . . . *Was this the first time that you asked the comptroller to sign something that she wouldn't sign and then you presented it to the commissioners?*

**A.** *I think that's true.*

\* \* \*

**Q.** . . . *[D]o we know . . . whether, when you presented this to the Turnpike commissioners, you said to them, "This has not been signed off on by the controller?"*

**A.** *I don't think I did say that.*

Key members of the Authority's governing board expressed surprise when informed of these events. Joseph P. Miele, at the time the board's representative on the Consortium's Executive Council, testified:

**Q.** . . . *Did anyone ever bring it to your attention that the comptroller refused to sign the agenda item certifying the accuracy or validity of the E-ZPass procurement [revenue estimates] prior to the commissioners' vote on March 25, '97?*

**A.** *No.*

\* \* \*

**Q.** *Do you think you should have been [told]?*

**A.** *Yes.*

Frank X. McDermott, the then-Chairman of the Turnpike Board of Commissioners, expressed the same view:

- Q.** *Is that something that the board should have been informed of, that the comptroller refused to sign the agenda item for the E-ZPass procurement?*
- A.** *Well, I think the board should have been informed by the Executive Director because that certainly was an important consideration.*

•   •   •

Turnpike Authority finance personnel testified, and documents show, that only after the contract was awarded – when the momentum of the procurement shifted into negotiations to hammer out the final terms – were they directed to conduct a detailed analysis of the revenue and cost projections. Indeed, it is noteworthy that subsequent to the contract-award vote, there is no record of additional complaints from the Authority’s financial personnel about being excluded from the process. However, a host of thorny questions lingered for months regarding the accuracy and underlying validity of the data contained in the MFS proposal, and the process of sorting it out continued virtually until the contract was executed on March 10, 1998. It was during this process that the projected surplus associated with MFS’s proposal – initially pegged at \$159 million – diminished to less than \$35 million.<sup>52</sup> Coryat testified:

- Q.** *. . . [B]asically, Donna [Manuelli] took the 159 million [surplus projection] and started working backwards?*
- A.** *Yes.*

\*   \*   \*

- Q.** *Have you ever been involved in any contract where a contract was awarded with all these open financial questions?*
- A.** *No.*

\*   \*   \*

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<sup>52</sup> See footnote at p. 90.

*I can't imagine ever going forward with the contract with so many questions unanswered.*

Manuelli, who was assigned to participate on behalf of the Turnpike Authority during much of the post-award negotiation phase, testified:

**Q.** *Shouldn't have all this accounting been done prior to the award of the contract?*

**A.** *Yes.*

\* \* \*

**Q.** *Did you or Ms. Coryat ever become comfortable with the numbers . . . ?*

**A.** *No, I don't think so. I don't think we ever – neither one of us ever – ever attested to the numbers, neither one of us ever said, "Yes, these are good, reasonable numbers." All we did was we found backup for most of the numbers. We found a sheet of paper that MFS submitted that at least told us where the numbers came from and put them together into a spreadsheet, but that was the extent of it. We never were asked to test them. . . .*

Coryat and Manuelli both took issue with statements made by Gross on this issue during the Assembly Transportation Committee's E-ZPass hearings. In unsworn testimony on May 2, 2002, Gross told the Committee that

*. . . between March of 1997 and the contract signing on March 10, 1998 the finance department of the Turnpike had fully reviewed and critiqued and signed off on the projections. . . . The department signed off on it.*

\* \* \*

*. . . [I]n addition, she (Coryat) indicated that she had not fully reviewed, signed off on the revenue projections and her staff was still working on it, and they were having some difficulty getting some of the underlying worksheets, which ultimately was straightened out. . . .*

*[A]s I said, over a period of time the Turnpike's finance department did all of their due diligence and signed off on it.*

Coryat, however, swore that neither she nor her department, ever fully reviewed, critiqued and signed off on the projections.

**Q.** . . . *[D]id you give anybody approval in your department to sign off on the revenue projections?*

**A.** *No.*

**Q.** *And you, yourself, didn't?*

**A.** *No.*

**Q.** *So how do you view Mr. Gross' testimony before the Assembly Transportation Committee?*

**A.** *I don't think it's true.*

Manuelli testified:

**Q.** *Is that (Gross's Assembly testimony) an accurate statement?*

**A.** *No, that's not an accurate statement. We never signed off. No one ever asked us to sign off on the projections.*

• • •

Confronted on this matter by the Commission, Gross testified:

**Q.** *Would it be surprising to learn that Coryat provided sworn testimony to the Commission that she was never comfortable with the projections so she never signed off on the project?*

**A.** *I'd be very surprised with that – with that testimony, I really would. I mean, I don't know where – within that statement I don't know where her discomfort – alleged discomfort would be, but I would be surprised by that.*

**Q.** *Would it surprise you to learn that Donna Manuelli made the same statement to the Commission?*

**A.** *Absolutely.*

• • •

Although Gross in his sworn testimony sought to minimize any role he might have played in connection with blocking the full participation of the Turnpike staff in the procurement process, several Turnpike personnel testified that they were subjected to intimidating treatment when he perceived that they were impediments to rapid completion of the contracting process.

Manuelli testified that after one meeting during the negotiations to iron out the final contract terms in the fall of 1997, Gross went to her superior, Coryat, and complained about Manuelli for pressing the vendor's representatives with questions about the deal's financial components. Manuelli testified:

*Q. What did [Coryat] tell you?*

*A. She told me that he was not happy with the way that I was asking questions, just what I said, that I was too aggressive, you know, he didn't like the tone of the way I was questioning them, and that I needed to back off and back down.*

*Q. Did you heed the advice –*

*A. Yes.*

\* \* \*

*Q. You didn't ask those questions?*

*A. No.*

*Q. Who was asking those tough financial questions during the time period after you stopped asking them?*

*A. No one.*

\* \* \*

*Q. . . . What [were] you thinking?*

*A. It's very intimidating . . . I just didn't ask some of things or push as I would have pushed.*



Gross testified that he recalled “one event at an early stage of a meeting with a lot of people in it where I thought Donna’s comments were a little aggressive.” He recalled “casually mentioning” this to Coryat but denied making it “a major issue.” Asked whether he tried to intimidate Manuelli into avoiding tough questions, Gross replied, “Absolutely not” and expressed surprise when informed that she testified to having felt intimidated by his action.

• • •

Carris testified that at one point in the negotiations, Gross discouraged him from raising questions about whether MFS should offer the Consortium a discount in view of the potential profit the firm might earn from the leasing of fiber-optic cable. Carris stated that he pointed out during one negotiating session that by installing fiber along primary toll roads in New Jersey, MFS would complete a lucrative regional fiber-optic network stretching from Ohio through New York and down to the Atlantic coast. Carris memorialized his concerns in a memorandum to Gross dated May 13, 1997, on the subject of “Fiber Optic Negotiations Issues.” The memo stated, in part:

*It appears as though the MFS fiber people continue to look at the fiber component as their domain, independent of the rest of the ETC contract and are negotiating as if it were only a fiber contract. My impression is that [MFS Senior Vice President William] Thompson put together our multi-faceted, integrated deal back in October and now their fiber people are trying to steer clear of those linkages.*

Carris, in his testimony, amplified on his concerns and stated they were set aside by Gross:

*We were trying to get into background on where their costs – where their revenues were going to be coming from or how they were going to develop based on the components of right-of-way that we offered. In educating myself on the process with the fiber and what was going on in the industry, New Jersey was a main destination point for trans-Atlantic cables to come in. MFS basically was basically going to give us a ring of fiber in the State of New Jersey, but it became obvious to us during questioning them more and more that that ring was part of a bigger ring going out into the Midwest and then coming back. . . . I started to realize that, whatever, they were giving us, just by getting our right-of-way it was adding value to all of their contracts everywhere else that they had to complete this ring. And I put that on the table in front of Thompson and said, Well, if you're getting more money from . . . everybody else, why aren't we getting a piece of that, because we're giving you a completion of that loop. Mr. Thompson took great offense at that and got upset and Ed Gross turned to me and said, "Paul, I think you've gone too far with this," or something to that effect, and I shut up.*

- Q.** *But the bottom line, MFS never gave the price break to the Consortium that you –*
- A.** *No, there was never any follow-up to get any benefit of what I pointed out.*

Carris also testified that there came a time when Gross booted him from the negotiations on the grounds that they were not proceeding with sufficient speed. According to Carris, the incident occurred on or about the Memorial Day weekend in May 1997:

*I had to jump between the engineering back to the financial group and we got to the Friday of Memorial Day and I had the agency staff walking out getting ready to go away on a long weekend. MFS and Chase, their attorneys were starting to step out because they had planes to catch. . . . So my conclusion by Friday afternoon was we're not wrapping this up. Let's just suspend it, and then we'll get back with specific committee groups the following week. Once that was done and I remember – I just remember getting a call from Ed Gross saying, Get back to my office. And he took issue with my taking that upon myself to stop negotiations at that point.*

- Q.** *What happened when you got back to the Turnpike?*
- A.** *Fran [O'Connor] and I met him in his office and he basically yelled at me. He said I had no right to do what I did. I should have had*

*everybody working through the weekend to get it done. I tried to explain to him why I disagreed. I told him I thought the financial section of the contract was nowhere near where it had to be. . . .*

**Q.** *What happened after that point going forward?*

**A.** *I was taken out of the loop and Ed took over the negotiations. . . . I stayed around to basically serve as institutional memory . . . and Ed took over the negotiations, which culminated almost a year later.*

In separate testimony, O'Connor corroborated Carris' articulation of the essential facts of this encounter.

Carris submitted a notice of resignation to the Turnpike Authority on March 12, 1998, two days after execution of the E-ZPass contract. He did not have another job lined up.

. . .

Donald E. Mauer, who joined the Turnpike Authority as Assistant Chief Engineer in July 1997, testified that he was shunted onto the project's sidelines by Gross after writing a series of memos pointing out that work on the project had fallen behind schedule:

**Q.** *What caused you to become cut out of the loop?*

**A.** *I wrote a memo that said the job was not going to finish on time and here are the reasons why based upon, you know, my professional experience. That's all. And it was not a memo that [Gross] wanted to see or receive. I was called to task on it and that was it. It was the beginning of the end. I was cut out more than I was included on the construction of the job.*

**Q.** *But wasn't that memo within your sole area of expertise and –*

**A.** *Yes.*

**Q.** *– job duties?*

A. *It was my sole responsibility. When I joined the Turnpike as the assistant chief engineer, my obligation was to be the chief engineer for the consortium to execute the construction of the job.*

Gross testified that Mauer “absolutely was not cut out. . . . I never gave instructions to reduce his workload or not – or do anything different in connection with Don Mauer.”

### **Vendor Warnings Minimized**

Before and after the E-ZPass contract was awarded – but prior to its actual execution – officials in charge of the procurement received verbal and written notice from representatives of MFS and its financial advisor, Newcourt Capital, alluding to the genuine risk associated with the untested self-funding approach.<sup>53</sup> Collectively, these contacts should have served as an ever-widening signal that trouble lay ahead. In each instance, however, they were set aside, treated essentially as little more than a series of unwelcome and unwarranted impediments to speedy completion of the deal.

• • •

Daniel M. Morash, then-Senior Vice President of Newcourt Capital, told the Commission that his firm took the position “from day one” that the projected revenue streams associated with the Consortium’s self-funding approach were speculative and advised its client, MFS, of such beginning as early as the fall of 1996. As the

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<sup>53</sup> In addition to its role as financial advisor to MFS, Newcourt Capital organized and arranged the private-sector syndicate of lenders that eventually provided start-up capital for the E-ZPass project via bonds issued by the New Jersey Economic Development Authority.

procurement progressed, questions raised by both Newcourt and MFS were placed directly before the Consortium.

In a letter faxed to ETC Program Manager Paul A. Carris, on October 2, 1996, responding to a Consortium request for best and final offers (BAFOs) from vendors, MFS stated flatly it did not regard as viable a strategy reliant on uncertain revenue from E-ZPass violators without some mechanism to protect the firm from potential losses. The letter, signed by William P. Thompson, the firm's President and Chief Operating Officer, stated, in part:

*Our financial concern with the terms requested by the Consortium is based on our view that the E-ZPass project including potential revenues . . . is not likely to be self-financing. Our estimates for revenue from a fiber optic telecommunications system help narrow the financial gap, but do not change our fundamental conclusion. . . . If the violations rate falls below the Consortium's estimates, the MFS team faces increasing levels of financial risk, and will be in a money-losing position if the violation rate falls significantly below the Consortium's forecasts. We are only able to present a financial package of the sort the Consortium has requested (\$0 down, \$0 payment) if it guarantees to insulate the MFS team from losses . . .*<sup>54</sup>

As an alternative, MFS advanced a second approach in which the Consortium collectively would spend \$120 million on the project after the first two years of development. The firm characterized this modified pay-as-you-go alternative as one that would

*. . . Provide a financial backstop on the risks we face from lower than estimated violations rates, and – very importantly – align the Consortium's interests and ours in a number of important financial and operational ways. . . . We believe this very strongly, and have structured it so that it will be more attractive financially to the Consortium than Approach 1. We are recommending it for your serious consideration even though it yields lower returns to us . . .*

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<sup>54</sup> See Appendix at p. A-45.

Thompson told the Commission that he believed MFS did a “pretty good job” presenting the Consortium alternative funding approaches. As was testified to by Carris and other members of the MET vendor evaluation team, however, no alternative to self-funding ever received serious consideration or became the object of any rigorous comparative analysis. Further, Gross testified that neither he nor the Executive Council were ever presented with this second approach.

• • •

Eight days later, on the morning of October 10, 1996, MFS sent Carris a revised final offer. The firm reiterated its position that a self-funded E-ZPass system would be viable only if the Consortium assumed full responsibility for associated risk. Otherwise, MFS warned, it would be difficult if not impossible to obtain up-front financing from lenders. “If revenues are insufficient to cover capital and operating costs,” the firm stated, “the Consortium will need to make payments at the conclusion of the project to make up for the shortfall.” Further, MFS told the Consortium that its “updated financial assumptions” projected a likely deficit of at least \$12 million for violation-revenue alone at the end of the contract’s proposed eight-year term. According to this MFS communiqué:

*Due to the unique nature of the project (i.e. lack of precedence for violation revenue collection for a toll facility) coupled with the fact that this same violation revenue will be relied upon significantly to pay down the debt, MFS strongly believes financing for this project will be unattainable on a \$0 down, \$0 payment basis without the Consortium’s support in the manner outlined above.*

MFS went on to point out that it had not yet fully analyzed possible outcomes associated with the alternative funding approach it had recommended approximately one week earlier. “Time limitations preclude us from presenting the same scenarios for Approach 2, although we clearly believe them worthy of consideration should the Consortium choose to continue discussions with the MFS team with regard to the particular approach.”

• • •

After the contract was awarded to MFS by the Turnpike Authority’s governing board on March 25, 1997, the firm entered into negotiations to hammer out final contractual terms. As part of that process, Newcourt Capital, as MFS’s financial adviser, began sounding out the financial markets for investor receptivity to the proposed self-funding strategy. According to Newcourt Capital’s Daniel M. Morash, the investor community was lukewarm to the Consortium’s approach and made that plain in various meetings. In a letter to Turnpike Executive Director Edward Gross dated June 13, 1997, Morash and another Newcourt executive, Johannes G.M. Derksen recounted the substance of discussions with the lending community at that juncture. Among other things, Morash and Derksen told Gross that there may be difficulty obtaining timely receipt of letters of commitment from various investors who had expressed tentative interest in underwriting the project. A key sticking point cited by the Newcourt executives in this letter were concerns surrounding the revenue projections, and they told Gross that a substantial “reserve” account would have to be established in order to complete the deal. They wrote on June 13, 1997, in part:

*The uncertainty of actual levels of fiber optic and violations collection revenues necessitates that large reserves be built into the Transaction. Newcourt is evaluating how to achieve the necessary reserves at a minimum cost to MFS NT and the Consortium, and is prepared to consider all alternatives that reduce costs while meeting the objectives of the parties.*

Morash told the Commission that the Consortium, through Gross, its chief representative, was not receptive to Newcourt Capital's concerns. Morash testified:

*. . . [W]e were being put under a lot of pressure to provide firm financing commitments to a transaction that had not yet been properly and finally scoped out. So, you know, we were very concerned about . . . being pushed into something before we were ready to do so. You know, once we agreed to the transaction we were going to have to deliver other commitments and we had to make sure that other financial institutions were comfortable with the structure, and what this [letter] says is that these issues haven't been adequately vetted for purposes of financial institutions giving credit approval.*

**Q.** *Do you remember any kind of discussion . . . in response to this letter?*

**A.** *Just, you know, more pressure to get a final resolution.*

. . .

Approximately six weeks later, in a letter dated July 24, 1997, Morash informed Gross that while the firm had begun to line up institutional investors to provide start-up capital, problematic issues remained with regard to risk and costs. Morash stated that three major banking institutions with a significant presence in New Jersey – PNC Bank, Chase Manhattan and First Union – had declined invitations to participate. According to Morash, the banking community still regarded the financial structure as uncertain, despite the fact that it was anchored by the so-called “True Up” agreement obligating the



Consortium to cover all costs, including money owed to lenders, in the event of a revenue shortfall. In this letter, Morash wrote, in part:

*These banks are not only large New Jersey/New York stakeholders, they are also banks with whom Newcourt has close business relations. Each gave the [E-ZPass] financing full and careful consideration. Furthermore, we approached the project finance and public finance lenders at several additional commercial banks who have also declined to participate to date. The primary reason for the commercial banks' discomfort is the potential for non payment of interest without the ability to accelerate the True-up prior to maturity, and other terms of the Financing which are necessary in order to comply with the "nothing down, nothing for eight years" requirement of the MFS NT contract.*

In this letter, Morash also alluded to concerns that Newcourt Capital had expressed about the mechanism chosen by the Consortium for raising the start-up capital: a taxable, private-sector placement of loans bearing a mix of fixed and floating interest rates. During the negotiations, Newcourt had recommended instead the issuance of some form of tax-exempt public debt that would carry lower interest rates and thus be less costly to the Consortium over the long run. The tax-exempt approach, however, was vetoed by the Consortium – unilaterally by Gross, according to Morash's sworn testimony – because it would have taken too much time and because it was fundamentally incompatible with the Consortium's goal of having E-ZPass project eventually pay for itself.<sup>55</sup> Morash told the Commission the tax-exempt approach

*. . . was set aside by Ed Gross in no uncertain terms. He said, 'stop trying to save us money,' would be the more direct quote.*

**Q.** *Ed Gross said stop trying –*

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<sup>55</sup> Because the long-term goal of a self-funded E-ZPass system was reliant, in part, on projected revenues from the commercial leasing of fiber-optic cable to private-sector interests, the vehicle for raising start-up capital, by law, could not be tax-exempt.

A. *Stop trying to save us money.*

Q. *That's an unusual concept, isn't it?*

A. *I was a little shocked by it. This [July 24 letter] was a more diplomatic way of saying that we looked at this [tax exempt approach], you [the Consortium] decided not to do it. Ultimately, it was bona fide that the transaction was not pursued on a tax exempt basis, because there was no way to have private sector revenues coming in, you know, the fiber-optic revenues, and still have a structure that was legitimately tax exempt.*

Q. *Unless there was a way to separate both transactions?*

A. *Right, exactly.*

Q. *Anybody thought of that or was it considered?*

A. *We thought it was our job to raise that and to run it – what I would call, run it to ground. In other words, keep pursuing it until, you know, you get a stoplight that you can't find a way to structure around. Time was of the essence the way that these negotiations went and the way it was presented to us at that point in time. And the consortium ruled it out, Ed Gross ruled out the tax exempt alternative.*

Morash testified that that he interpreted Gross's remark – "Stop trying to save us money" – in the context that the Consortium "had concluded definitively that they could not arrange tax exempt financing, so he wanted to stop talking about it."

## **Frustration of Private-Sector Scrutiny**

According to Morash and MFS's William P. Thompson, Gross during the summer and fall of 1997 personally dominated the contract negotiations on the Consortium's behalf and sought throughout the process to eliminate anything he regarded as an obstacle to rapid closure of the deal. Among the purported obstacles were mechanisms typically incorporated into contractual documents governing such projects to protect investors, ensure due diligence and provide adequate public disclosure.

When Newcourt Capital drafted a term sheet calling for standard lender controls, for example, Gross unilaterally vetoed it and drove the point home by tearing up the draft, threatening to nullify the contract-award and walking out of the negotiating session. Lender controls are designed to protect the interests of those who supply capital financing by providing checks and balances against things that might go wrong – and thus possibly delay loan repayment – during contract implementation. In this instance, the controls proposed by Newcourt would have established a timetable for municipal court disposition of administrative fees assessed against E-ZPass violators and would have blocked payment to the vendor for non-performance. The controls sought by Newcourt Capital also would have required extensive pre-operational testing to verify the E-ZPass system’s viability and functionality, particularly its ability to weed out so-called “false positives,” that is, to distinguish legitimate E-ZPass customers from actual violators. Questioned on this point, Morash testified:

*Q. Wasn't that [false positives] one of the major problems in the implementation of this project?*

*A. In retrospect.*

*Q. Would this have short-circuited that problem, do you believe?*

*A. Based on my experience in other project financings, the [lender control] structure works to assure delivery of a system on time and on budget.*

Ultimately, Newcourt and MFS acceded to Gross’s demand for removal of lender controls from the final financing term sheet. Their reasoning, according to Morash, was that the Consortium had already agreed to assume the bulk of the risk via the “True-Up” arrangement obligating the toll authorities to cover any deficit.

At another juncture in the negotiations, Gross resisted Newcourt's demand that Consortium produce signed letters of accounting from the member authorities delineating their obligations under the True Up agreement. The firm also insisted that an outside entity be retained by the Consortium to examine the performance of the E-ZPass revenue streams on an annual basis after implementation of the contract and to revise the projections as warranted based on changing circumstances. Morash testified:

*Q. What was the significance of . . . the accounting letters?*

*A. That if the process started to get out of control, the annual review would surface, would shine light on the situation, so that we didn't get to the end of eight years and then discover there was a problem.*

*Q. Why would that be an important factor for you?*

*A. Because then to the extent there was a problem, it would come to light early. And an appropriate response and solution would be put in place before it was too late.*

*Q. What was Mr. Gross' response to this?*

*A. Well, . . . he objected strenuously to it and only agreed to it once we said it was a condition of closing.*

*Q. Is it true that such letters of accounting are typical or standard in such projects and are critical to ensuring public disclosure of the key terms?*

*A. Yes.*

Gross also opposed Newcourt Capital's plan to hire an outside accounting firm, Coopers & Lybrand, to conduct a thorough assessment of the proposed E-ZPass self-funding structure, including the viability of fiber-optic and violation-fee revenue projections, on behalf of the syndicate of lenders that was being organized to provide start-up capital. Morash testified:

*Q. [Would] you characterize [hiring Coopers & Lybrand] as an effort to effect . . . private sector due diligence on this particular project?*

- A. Right. Because at the time the only information we had was the pro formas that MFS had prepared and, you know, it's a normal due diligence matter for private lenders to get their own independent consultant. So we insisted that Coopers review the structure. And, again, there was a lot of pushback from Ed Gross on that because he said, well, if you have our guarantee at the end of eight years, what do you need a report for. And we said: Well, you know, we need a report as normal matter of diligence, so therefore, the nature of the report was negotiated at length.*
- Q. Would you say that Mr. Gross opposition to this initially was adamant?*
- A. Yes. And we had to insist that we would not proceed with the transaction without this.*
- Q. So this would have been a deal breaker for you if you could not have done this?*
- A. Right. Because we knew that the other investors in the Consortium – in the syndicate that we put together would require this, that their credit departments would require this . . .*

When it became apparent that Newcourt Capital would go forward with Coopers & Lybrand despite Gross' objections, Morash testified, Gross insisted that the terms of the study be negotiated in advance. “. . . [H]e wanted to put limitations on the – what constituted an acceptable report . . .,” Morash stated. For example, at Gross' insistence, it was agreed that the scope of work by Coopers would be subject to unusually stringent budgetary and time constraints. Moreover, the MFS revenue projections were to be deemed viable even if the results of the Coopers evaluation concluded that those projections, in reality, could deviate by as much as 30 percent. Morash testified the 30 percent figure was a compromise and that Gross initially sought 50 percent.

- Q. What was the time limitation?*
- A. I think, you know, we had started them up and they had to produce a report within . . . I think it was a two-week or three-week period of time. It was shorter than the normal review period.*

*Q. What would you have expected the time limit to have been?*

*A. Four to six weeks instead of two or three.*

*Q. At the least?*

*A. Yes.*

*Q. What about the restriction on cost?*

*A. Well, the restriction in the cost means that the consultant would limit the hours and, therefore, the depth of analysis. And ironically at the time the big difference that came out – the big dispute that came out of the Coopers report was a difference between their analysis of the fiber revenues, which came in at about 40 million dollars, versus MFS' estimate of fiber revenues, which came in at about 120 million dollars. Interestingly enough, the actual revenues were about 80 million dollars, halfway in between the two estimates. That also gives you a sense for what we were talking about when we said the revenue streams were speculative. You got one person saying 120 million, another saying 40 million, the actual is 80 million; that's a wide discrepancy in what was ultimately – what was both estimated up front and collected; which, you know, is why from the start we said that the [True Up] guarantee was needed.*

\* \* \*

*Q. Based upon your experience, is this a normal business practice?*

*A. No.*

In its review of this matter, the Commission obtained documentary evidence suggesting that, in addition to the negotiated constraints that were placed upon the Coopers due diligence study, efforts were undertaken to restrict the firm's access to key personnel. Coopers employees seeking data and information for the evaluation, for example, were instructed in writing to funnel all communications through the Turnpike Authority in the person of Francis K. O'Connor rather than contacting the appropriate Consortium officials directly.

Coopers delivered a 20-page "letter report" to Newcourt Capital on September 10, 1997. The results were mixed. With respect to the violation revenues, the firm stated, in

part, that “[w]hile the analysis of the projections made by the MFS team is generally favorable (in aggregate), the unprecedented size of the project magnifies even small changes in the assumption values.” Echoing the “magic cube” risk assessment made nearly a year earlier by Chase Manhattan Bank, the report concluded, “small deviations in assumptions, taken in aggregate, can have a significant impact. Therefore, even small changes in multiple key variables may cause Violations Revenue to decline significantly.” As to the MFS projections for the other major revenue source, the leasing of fiber-optic cable, Coopers suggested “a likely scenario” would be a yield “in the range of \$31 to \$52 million versus the \$118.7 million projected in the plan.” Although Coopers characterized its own calculations as conservative and did not rule out the possibility that the MFS projections could be achieved, it stated that MFS’ fiber outlook “cannot be proven adequately to be fully included in the outlook for purposes of due diligence.” The report’s bottom line: “Overall, a likely scenario is that projected Violations and Fiber Revenues will be within 20% of that projected by the MFS team.”

In his testimony before the Commission, Morash characterized the report, given the constraints under which Coopers had been instructed to operate, as minimally sufficient to satisfy the requirements of lender due diligence. He described the document as “weak, shallow and proscribed” and stated that it possessed “the form of an independent review but not the substance.” Nonetheless, once the Coopers report was completed, and purported to show that the violations projections fell within the 30 percent deviation rate set forth in the exercise’s negotiated guidelines, Gross asked for a copy because, according to Morash, the document appeared to “support his position.” Morash testified that Newcourt Capital resisted this request on the grounds that the

report, though commissioned at the Consortium's expense, constituted proprietary material prepared for Newcourt on behalf of prospective lenders. Gross testified he requested the report but swore he never saw it.

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In December 1997, the Consortium retained the firm of Public Resources Advisory Group, Inc. (PRAG) to assist in the final E-ZPass contract negotiations. After the contract was executed on March 10, 1998, PRAG was given the added responsibility to conduct an annual review of the cost and revenue projections and to calculate how those projections would affect the Consortium's obligations under the True Up Agreement. These annual reviews showed from the start that the Consortium faced an ever-widening deficit. PRAG's initial report, dated November 30, 2000, projected a deficit of \$64.8 million at the end of the contract period in 2008 – a reversal of nearly \$100 million from the \$34.9 million surplus projected at contract execution. A year later, on November 30, 2001, PRAG projected a deficit of \$161.7 million. In February 2002, revised figures showed the deficit increasing to at least \$300 million. In April of that year, further adjustment to the PRAG data boosted the deficit projection to \$469 million.



## ***Referrals and Recommendations***

The Commission refers the full record of this investigation to the following agencies of government for whatever action they deem appropriate:

- The Governor, Legislature and Attorney General of New Jersey
- New Jersey Department of the Treasury, Division of Purchase and Property
- New Jersey Turnpike Authority, South Jersey Transportation Authority and Port Authority of New York and New Jersey
- State of Delaware, Department of Transportation

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Based upon the investigative record, the Commission makes the following recommendations for statutory and regulatory reforms:

### ***1. Safeguarding Procurement Integrity***

The E-ZPass contract procurement was doomed to mismanagement and thrown open to manipulation from the start because it was founded upon a wholly inappropriate process, it was mismanaged and manipulated, and it was subjected to little in the way of due diligence or accountability. The facts established by this investigation provide a basis for significant reforms aimed at fundamental weaknesses that render the present state procurement system vulnerable to wholesale abuse, either by design or by default, and that undermine the state's ability to maintain proper and effective financial oversight.

The Commission is particularly concerned about the need to ensure that the procurement framework is used properly and appropriately and that the state is equipped with credible tools to evaluate, monitor and audit all key financial and programmatic

elements that are part of the public-project procurement process – from design assumptions through operational performance. Too much is at stake for New Jersey and its citizens ever again to be subjected to the cost, inconvenience and embarrassment of a public project undertaken, in effect, with blinders on. The Commission, therefore, recommends that the Legislature and Governor:

- **Tighten the Definition of “Professional Services”**

E-ZPass was designated from the outset an integrated professional-service procurement and, as such, was exempt from a host of statutory and regulatory rules that govern open, competitive public bidding. The issue is not that professional-service arrangements necessarily constitute bad public policy; rather, the issue is: what constitutes a professional service? The Legislature has never explicitly defined the term or considered the need for limiting its use. That a massive capital undertaking such as E-ZPass could be placed for procurement purposes in the same category as legal or engineering consulting with no enhanced controls or oversight to safeguard fairness and guarantee a level playing field for vendors raises serious questions that go to the heart of whether the public’s best interests are properly served by current law. Indeed, the professional-service procurement process was never designed or intended for use in such instances. Given that the Appellate Division of New Jersey Superior Court actually upheld the professional-service designation for E-ZPass based upon the law and the facts as presented to it, the Commission believes it is all the more vital that the Legislature and the Governor take action to tighten the definition of this term. By doing so, they will not only protect taxpayers and

consumers; but they will also provide proper and reasonable guidance to the courts.<sup>56</sup>

- **Strengthen Accountability under the Public Contracts Law**

In January 1999, after the E-ZPass procurement was completed, legislation was signed overhauling the state and local government contract law (*N.J.S.A 52:34-12*). Though hailed at the time as a means to enhance procurement integrity and to balance administrative efficiency with public accountability, the revised statute contains a provision which, in light of what is now known about the E-ZPass procurement, could be self-defeating. Subsections (f) and (g), state<sup>57</sup>:

*(f) for any procurement, the State Treasurer or the [Division of Purchase and Property] director may negotiate with bidders, after bid opening, the final terms and conditions of any procurement, including price; such ability to so negotiate must be expressly set forth in the applicable invitation to bid;*

*(g) award shall be made with reasonable promptness, after negotiating with bidders where authorized, by written notice to that responsible bidder whose bid, conforming to the invitation for bids, will be most advantageous to the State, price and other factors considered.*

This language was intended to promote flexibility in obtaining the best deal at the best price on behalf of the taxpayers, but the Commission is concerned that it is so broad as to constitute an invitation to abuse. In effect, it opens the way for every procurement to be treated such that the lowest responsible bid no

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<sup>56</sup> It is the Commission's contention that if all of the facts uncovered by this investigation had been known to the Appellate Division prior to its rendering of the decision in *Nachtigall v. N.J. Turnpike Authority*, 302 N.J. Super. 123 (App.Div. 1997), the conclusions reached therein may have been markedly altered.

<sup>57</sup> Underlined material denotes language added to the statute as part of the changes enacted in 1999.

longer is necessarily paramount in any instance. Further, the statute as written authorizes private discussions, i.e. “negotiations”, with select vendors prior to the award of the contract without any explicit mechanism to ensure that such discussions are carried out in the public’s interest. Given the troubled history of both the enhanced emissions-inspection and E-ZPass procurements, the Commission recommends that the relevant sections of this statute be reviewed at the earliest possible date and amended to incorporate appropriate checks and balances without undermining or forestalling negotiated procurements deemed proper and legitimate.

- **Establish a New Process for Achieving Unique Procurements**

New Jersey’s contract procurement system as presently constituted provides an inadequate regulatory framework for the proper promulgation and administration of unique, technically difficult and financially complex procurements, such as E-ZPass, that may involve an elaborate mix of capital components and services. The state, therefore, needs to formulate a process to deal with those types of procurements requiring custom treatment and special oversight. A task force should be established immediately to develop such a process and to recommend to the Legislature and the Governor a practical methodology for implementing it. A key function of this task force would be to establish core criteria for determining whether a given procurement qualifies for this unique category either because its scope is beyond that of conventional competitive public bidding or does not fit the definition of a negotiated

professional-service procurement, or because it is a hybrid of the two, thus requiring its own process.

- **Reorganize Government Oversight or Create an Independent Comptroller's Office for Procurement Auditing**

The documented failures of the E-ZPass and enhanced emissions-inspection procurements point to the critical need for a central state-level entity to ensure that the public-project contracting system throughout New Jersey is subject to proper and thorough financial and programmatic oversight. The Legislature and the Governor should take appropriate steps to review the current fragmented oversight structure and either reorganize it or create an independent auditor/comptroller with authority to consolidate and expand procurement oversight functions, and properly charged with auditing and reporting thereon. The goal in either case would be to establish and administer a practical system for auditing, monitoring and certifying all public-project procurements pursued by the state or by the various authorities to which the state is a party, with the following critical tasks in mind:

- Review the feasibility of large, unique and complex procurements
- Ensure that proper procurement procedures are followed
- Examine the financial and programmatic viability of proposed public-project contracts prior to contract execution
- Certify the accuracy and propriety of cost and revenue projections associated with public-project procurements
- Perform specialized public-project auditing functions

## ***2. Conflicts of Interest***

New Jersey's conflict-of-interest statute should be amended to require that state employees whose positions bring them into contact with private vendors relative to the state contract procurement process be barred from taking employment with such vendors, subsidiaries or otherwise related companies for at least two years following termination of state service.

At a minimum, legislation should be enacted that explicitly requires disclosure of a pre-existing or current professional or personal relationship between a state official and a vendor or consultant with involvement in a state procurement. Such disclosures should contain details sufficient to identify the exact vendor or consultant, regardless of any subsidiary relationship with a larger entity.

## ***3. Due Diligence: New Jersey Economic Development Authority***

Statutes governing the operations of the New Jersey Economic Development Authority (NJEDA) should be amended to require that the NJEDA conduct authoritative and independent financial due diligence evaluations on all financing arrangements in which it agrees to participate as a "conduit" for the sale of bonds or with which it otherwise is integrally involved.

## ***4. Vendor Protests***

During the E-ZPass procurement, the losing bidder, Lockheed Martin IMS, filed a formal protest claiming the contract was unfairly awarded. The protest was dismissed

following two separate hearings presided over by the top administrative officials of the New Jersey Turnpike Authority, which was the lead agency in the procurement. In one instance, the presiding officer – at the time the Turnpike Authority’s Chief of Staff – was a reluctant participant who testified to being ill-prepared and denied the assistance of outside counsel. Thus, the Commission is concerned not only about the appearance of a conflict of interest associated with a protest proceeding conducted by an agency directly involved in a procurement, but also about the experience and qualifications of personnel who preside over such proceedings.

To address these issues, legislation should be enacted specifying that such protest claims be filed with and heard by a qualified, experienced and independent arbitrator.

## ***5. Vendor Evaluations***

The State Division of Purchase and Property should adopt regulations explicitly requiring that all vendor evaluation committees established pursuant to the state contract procurement process, particularly as it relates to large capital projects, include at least two members proficient in matters related to public-project financing. This is essential in those procurements where substantial sums of money are involved or nontraditional financing approaches are contemplated. In instances where appropriate and necessary expertise is not available within the government, the responsible agency should seek to obtain objective resources through the private sector at reasonable expense.

Further, to safeguard the integrity of the evaluation process, a reliable mechanism should be established to evaluate the suitability of candidates for membership on evaluation committees. Individuals found to have a current or past relationship with a

prospective vendor, or with the principal of a prospective vendor, should not be considered for evaluation assignments to which such a vendor is a party.

## **6. *Transparency***

In the interests of public disclosure, legislation should be prepared and enacted requiring that once a matter has entered the procurement process, any contact related to the procurement between state employees and representatives of active or prospective state vendors be memorialized in writing so that a public record of all such contacts can be maintained.

## **7. *Service of Process***

Legislation should be enacted to require that all foreign and domestic entities doing business in New Jersey relative to any public project – including consultants, contractors and subcontractors – complete, maintain and keep current the New Jersey Division of Revenue’s “*Public Records Filing For New Business Entity*” form that includes the designation of a registered agent and regional office within this state for the service of process (subpoena) for any legal action or inquiry, civil, criminal or otherwise. Further, proof of such filings should be required by the public entity prior to the award of any public contract. The Commission is constrained to point out that it repeatedly has made this recommendation over the course of a number of its investigations in recent years, and it seems to have fallen on deaf ears.

The Commission also recommends that the “Uniform Act to Secure the Attendance of Witnesses From Without a State in Criminal Proceedings” (N.J.S. 2A:81-



18 *et. seq.*) be amended to allow for compulsory attendance by out-of-state witnesses in investigations conducted by the SCI.