

STATE OF NEW YORK
PUBLIC SERVICE COMMISSION

Case 09-M-0114 – Proceeding on Motion of the Commission to Examine the Prudence of Certain Capital Program and Operation and Maintenance Expenditures by Consolidated Edison Company of New York, Inc.

DEPARTMENT OF PUBLIC SERVICE STAFF'S PROPOSED PRIMA FACIE
SUBMISSION REGARDING THE PRUDENCE OF
CONSOLIDATED EDISON COMPANY OF NEW YORK, INC.,
IN ITS INTERNAL CONTROLS AND FAILURE TO DETECT FRAUD
WASTE AND ABUSE IN ITS CAPITAL PROGRAM
AND OPERATIONS AND MAINTENANCE EXPENDITURES

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Introduction

On January 14, 2009, the United States Attorney for the Eastern District of New York (US Attorney) announced the arrest of ten Consolidated Edison Company of New York, Inc. (Con Edison or the Company) supervisors and one retired supervisor.¹ Based on the US Attorney's investigation, the Con Edison employees were criminally charged with arranging for Con Edison to pay inflated claims by a contractor and with receiving from that contractor over \$1 million in bribes and kickbacks.

On February 12, 2009, the Public Service Commission (Commission) issued an Order initiating this case to investigate the prudence of the Company's

¹ The investigation revealed later that two the Con Edison employees had been arrested previous to January 2009 and had been cooperating with authorities making a total of 13 arrested Con Edison employees.

expenditures associated with Con Edison's construction program from 2000 to 2009, the years over which the US Attorney's investigation found that the illegal bribe and kickback schemes took place.² Additionally, via letter to Con Edison Chief Executive Officer Kevin Burke and a Request for Proposal, the Commission initiated an examination of Con Edison's internal controls surrounding its construction program to determine if the Company's control environment facilitated the fraudulent activities discovered through the US Attorney's investigation, and to determine the amount of any losses suffered by ratepayers due to such activity.³

At its August 2009 session, the Commission selected Charles River Associates International Inc. (CRA) to perform the investigative examination.⁴ The forensic investigation was divided into two parts. Part 1 focused on identifying any failure of Con Edison's internal controls that facilitated the arrested employees' illegal activity and to determine the magnitude of potential "at risk" transactions.

² Case 09-M-0114, Proceeding on Motion of the Commission to Examine the Prudence of Certain Capital Program and Operation and Maintenance Expenditures by Consolidated Edison Company of New York, Inc., Order Commencing Prudence Proceeding and Requiring Report (Issued February 12, 2009).

³ Case 09-M-0243, Comprehensive Investigative Accounting Examination of Consolidated Edison Company of New York, Inc., Letter to Kevin Burke, CEO dated April 21, 2009. Available on the Department of Public Service website at <http://documents.dps.ny.gov/public/Common/ViewDoc.aspx?DocRefId={615D6174-CC69-4809-830E-F85198A21807}>

⁴ Case 09-M-0243, Comprehensive Investigative Accounting Examination of Consolidated Edison Company of New York, Inc., Letter to Kevin Burke, CEO dated August 20, 2009. Available on the Department of Public Service website at <http://documents.dps.ny.gov/public/Common/ViewDoc.aspx?DocRefId={6F4B9765-4B06-49DD-90F3-7CF4F8576E95}>

Part 2 focused on calculating an estimate of the harm to Con Edison ratepayers due to fraud, waste and abuse related to the failure of the Company's internal controls, should the Company be found to have been imprudent.

In its Part 1 report,⁵ dated October 14, 2010, CRA concluded that Con Edison's actions (and inactions) related to its internal controls were imprudent in two respects. First, Con Edison failed to establish certain controls that a reasonable company would have in place designed to either prevent or detect fraud, waste and abuse by its employees. Second, Con Edison unreasonably failed to employ in a proactive manner certain controls that it did have in place that could have prevented, or detected much earlier, the fraud, waste and abuse that occurred. CRA found that the aggregation of the two control breakdowns created an environment, or culture, in Con Edison's construction management whereby the arrestees could perpetrate their fraudulent schemes resulting in ratepayer harm.

In its Part 2 report, dated January 11, 2013, CRA found that Con Edison's imprudent actions regarding its creation and use of its internal controls resulted in significant ratepayer harm. Based on its review of a sample of construction files over the course of the almost ten years during which the arrestees activity was allowed to continue, CRA estimates with reasonable confidence that Con Edison

⁵ Both of CRA's reports were filed in Case 09-M-0243, and are wholly incorporated herein by reference and attached hereto as Attachment A and Attachment B, respectively. Staff adopts their findings as the factual basis for its Prima Facie imprudence case.

was overcharged in the two areas of Construction–Street Work and Interference by almost \$210 million due to fraud, waste and abuse.⁶

Importantly, in its Part 2 report, CRA also concluded from its review that other contractors, contracts, and transactions exhibited patterns similar to those examined during its Part 1 review that was limited strictly to the single contractor implicated in the US Attorney’s investigation, Felix Associates. CRA opined that the consistency of the investigation variances found during the Part 2 review supported and enhanced its findings in Part 1 that Con Edison’s imprudent management of its construction program through its unreasonable implementation of internal controls facilitated fraud, waste and abuse resulting in overpayments to contractors.

The findings of CRA, as contained in its two reports, serve as the basis for Staff’s Prima Facie case against Con Edison. As such they are attached hereto as Attachment A and Attachment B, respectively, and are wholly incorporated by reference into Staff’s Prima Facie Statement. The following Statement distills these reports to highlight the Company’s most egregious failures, but is not intended to supersede or eliminate any other failings identified by CRA or by Staff as part of Staff’s case for a finding of imprudence. Based on CRA’s findings, Staff maintains

⁶ The ratepayer harm stemming from these overcharges has not yet been quantified. Additionally, the overcharges CRA found were those related to payments made only in one Con Edison accounting database, COMPASS. Con Edison also employed another database for making payments during the time of the fraudulent activity, PMS. A Part 3 investigation to look at the PMS database is under consideration. Additionally the amount of overcharges found does not contain any evaluation of overcharges made under a third construction category, Special Projects.

that a Prima Facie case of imprudent management and control has been established regarding Con Edison's construction spending over the years 2000 to 2009 that resulted in significant ratepayer harm.

Legal Standard

New York Public Service Law §65(1) requires the Commission to set just and reasonable utility rates. In doing so, the Commission may "consider all factors which in its judgment have any bearing on determining just and reasonable prices, rates and charges as to utility costs."⁷ The Commission has the authority to determine whether a utility's costs of service should be borne by the utilities' ratepayers or its shareholders – shareholders are held responsible for those costs that a utility "imprudently" incurred in carrying out its obligation to provide safe and adequate service.⁸ "It would be neither just nor reasonable for a utility's customers to bear the cost of inefficient management or poor planning."⁹

The Commission must determine whether "the utility acted reasonably, under the circumstances at the time, considering that the utility had to solve problems prospectively rather than reliance on hindsight" and the burden,

⁷ See Matter of Abrams v. Public Serv. Comm'n of State of N.Y., 136 A.D.2d 187, 189 (3d Dept. 1988); see also Public Service Law, Article 4, §65 (1), §66(12), §72).

⁸ Matter of Long Island Lighting Co. v. Public Serv. Comm'n of State of N.Y., 134 A.D.2d 135 (3d Dept. 1987).

⁹ Id. p. 143, quoting Consolidated Edison Company of New York, PSC Opn. No. 79-1 (issued January 16, 1979).

ultimately, is on the utility to “justify its conduct.”¹⁰ In the first instance, however, Staff is obliged to demonstrate a tenable basis for imprudence.¹¹

Staff submits that the information provided below demonstrates the imprudence of Con Edison’s decision-making and its failure to follow through with properly conducted and coordinated internal investigations culminating in the arrests of several of its construction management employees for activity that inflated the costs of construction projects from 2000 to 2010 when Con Edison strengthened its internal controls as a result of information learned from the underlying arrests.

Staff’s Prima Facie Case

Staff’s investigation, conducted by CRA, determined that Con Edison exhibited imprudent management and oversight of its construction program in two distinct ways. First, the Company failed to have adequate and reasonable controls in place to prevent fraud, waste and abuse, and to discover in a timely manner any such activity. Second, that Con Edison failed to reasonably enforce even those controls that were in place that could have deterred fraud, waste and abuse from occurring, or discovered and stopped such activity in a timely manner mitigating the harm suffered by ratepayers.

- A. Con Edison’s Inadequate Internal Controls Facilitated Construction Employees’ Illegal Activity Both in Allowing Such Activity to Occur and in Failing to Discover Such Activity in a Timely Manner.

¹⁰ Id. p. 143-144.

¹¹ See Id. p. 144.

Had Con Edison implemented reasonable internal controls related to its construction management policies and procedures, a failure that ultimately led to at least \$210 million in overcharges related to fraud, waste and abuse, the Company could have prevented or reduced the impact of such activity. Con Edison's specific failure to establish internal controls that a reasonable comparable company would employ consisted of (1) the ability of construction employees to manipulate worksheet items and overwrite system records without leaving an auditable trail in the Company's official database, COMPASS;¹² (2) the lack of a formal employee rotation policy; (3) the lack of a systematic or periodic assessment of fraud risk exposure or an identification of particular fraudulent schemes, events and risks that are pertinent to construction; and (4) the lack of independent monitoring of requests and approvals for an extension of time or increase in money to complete construction jobs.¹³ Given the mandate in the Public Service Law that its rates remain just and reasonable, as well as its implicit obligation thereunder to take all reasonable efforts to prevent inflated costs due to fraud, waste and abuse from

¹² CRA found that Con Edison employed six major computer systems to manage the lifecycle of construction work at Con Edison. Part 1 and Part 2's scope included only payments made through its Construction Management Payment and Support System (COMPASS) database. See Attachment A at ¶5.3.24. Additional construction payments were made through the Company's Procurement Management System (PMS) database. A Part 3 investigation is under consideration to examine overcharges related to fraud, waste and abuse from payments made through the PMS database.

¹³ CRA summarizes its findings regarding Con Edison's internal control deficiencies and failures in Section 5.2 of its Part 1 Report (Attachment A), before detailing each finding more specifically in Section 5.3.

becoming embedded in the rates charged to its customers, Con Edison either knew, or should have known, that its failure to provide a reasonably robust internal control environment to deter and detect such fraud, waste and abuse, was unreasonable and imprudent.

1. Con Edison's Lack of Internal Controls Requiring an Audit Trail for any Modifications Made in its COMPASS Database was Unreasonable and Imprudent.

CRA found that the fraudulent transactions were carried out by a series of data manipulations and falsification of records that occurred at various stages of the contract administration process. In particular, many of these data manipulations occurred at the payment requisition and approval process. This indiscriminate manipulation of data activity was not reasonably constrained to limit the personnel allowed to make such changes, or to maintain a log of changes made, the employee making such changes or reasons for any changes.

Thus, CRA found that due to the lack of an audit trail, it was possible that the responsible official recorded in the respective databases for procurement, control oversight, modification, and payment was not necessarily the person who actually performed or approved the action attributed thereto. CRA also found that employees involved in the initial approval of payments were often not recorded within the COMPASS database. This failure of record keeping allowed employees to essentially make anonymous modifications at will to the documents that supported contractor construction payments.

The COMPASS database did not, at the time of the fraud, keep an audit trail for modifications made to the payment invoices contained therein. Thus, any historic changes to the database erased the record of when the change was made, by whom such change was made and even what change was made. Accordingly, unless hard copies were available, and Con Edison's controls did not require the maintenance or retention of any such hard copies, it would not be possible for the Company or any auditor to verify the accuracy of the user details or payment data that appeared at any given time in the database.

As CRA found, the absence of such a control was integral to the arrestees' continued perpetration of their fraud as demonstrated in the affidavits of the arrested employees made in conjunction with the US Attorney's investigation, as well as by Con Edison's own internal investigation instituted after the arrests by its contracted auditor KMPG.¹⁴ Con Edison knew, or should have known, that the failure to maintain an audit trail of modifications made to its contractor payment invoices could lead to abuse by anyone with access to the database, yet it unreasonably and imprudently failed to institute any such control until after the January 2009 arrests.

2. Con Edison's Lack of a Formal Rotation Policy for its Construction Personnel was Unreasonable and Imprudent.

¹⁴ It should be noted that CRA's investigation was hampered by the fact that items of documentation requested by both KPMG and CRA could not be produced by Con Edison and that the Company was unable to explain or account for such absences. See Attachment B at ¶¶14-15.

CRA found that during the time in which the Con Edison construction employees were engaged in their fraudulent schemes, the Company had no formal rotation policy in place. Indeed, CRA concluded that the lack of a prescribed staffing rotation policy indicated that any moves made were at the sole election of the employees or the result of promotions and not the result of any formal process to ensure that Con Edison's personnel remained objective and independent.

This absence of an internal control mandating that employees be rotated on a regular basis was an essential breakdown. As CRA found, such absence permitted an environment whereby Con Edison's construction management responsible for contractor oversight and payment could develop relationships with contractors such that their independence was compromised and facilitating collusion between the two parties to seek personal monetary gains. Moreover, as discussed below, the Company allowed employees to continue to serve in the same capacity without rotation after receiving and investigating allegations of inappropriate or fraudulent behavior pertaining to their interactions with contractors under their oversight. Con Edison knew, or should have known, that its lack of a formal employee rotation policy was not in conformance with industry norms and was unreasonable and imprudent.

3. Con Edison's Lack of a Systematic or Periodic Assessment of Fraud Risk Exposure Pertinent to Construction Management Allowed the Fraud to Continue for an Unreasonable Period of Time.

CRA found that Con Edison failed to have any systematic or periodic assessment of fraud risk exposure or an identification of particular fraudulent

schemes, events and risks pertinent to construction management. This was a critical failure in two ways. First, by failing to conduct regular periodic assessments of fraud risk, employees and Company vendors could be given the impression that the Company was not concerned with identifying and preventing fraudulent activity or encouraging employees to be vigilant in identifying and reporting potentially existing fraud. Second, by failing to conduct systematic and periodic assessments, Con Edison lost opportunities to identify and strengthen control weakness such as those identified by CRA and KPMG¹⁵ that could have deterred fraud or to identify any potentially existing fraud.

4. Con Edison's Lack of Independent Monitoring of Requests and Approvals to Complete Construction Jobs was Imprudent.

CRA also found that Con Edison's internal controls did not provide for any independent monitoring of requests and approvals for an extension of time or increase in money to complete construction jobs. Thus, the personnel directly responsible for contractor oversight were allowed to make the ultimate decisions as to whether any such requests should be granted. Moreover, the effect of the absence of any independent oversight of extensions or increases was exacerbated by Con Edison's failure to employ any measures that would trigger a review when purchase

¹⁵ The details learned by CRA of Con Edison's own internal investigation regarding the underlying events leading to the arrests are included in Section 4.3 of CRA's Part 1 Report. KPMG LLP was hired by Con Edison's outside counsel Davis, Polk and Wardwell LLP to produce some quantification of loss sufficient to support restitution and forfeiture claims of the US Attorney, recoveries related to civil actions, and proof of claims related to insurance recoveries. Attachment A at ¶4.3.2.

order amendments exceeded a specified threshold above an originally authorized amount. Thus, no independent review was prescribed.

This lack of independent review unreasonably eliminated any checks or balances that could have mitigated the effects of having no rotation policy or other policies that facilitated the development of close relationships between the contractors and those employees charged with the oversight of such. Given that this absence could help to contain runaway inflated costs regardless of any illegal motives by identifying areas of waste, Con Edison's failure here was imprudent and not in conformity with industry standard practices.

B. Con Edison's Inadequate Enforcement of those Internal Controls it did Have Facilitated Construction Employees' Illegal Activity Both in Allowing Such Activity to Occur and in Failing to Discover Such Activity in a Timely Manner.

As described previously, Con Edison's internal controls were inadequate and severely deficient. Irrespective of CRA's finding regarding the inadequacy of the Company's internal controls, Con Edison's actions during the time of the fraudulent activity were likewise imprudent in that they allowed the fraud to continue for an unreasonably long time before being discovered.

Had Con Edison properly enforced those controls that it did have, the Company could have prevented or reduced the impact of such fraudulent activity. Con Edison's specific failure to enforce its internal controls consisted of (1) the failure to perform periodic cost audits; (2) the failure to improve the quality of the

Company's trenching manual;¹⁶ (3) the failure to coordinate investigations related to employee whistle blower complaints; and (4) the failure to train employees in the proper use of the databases the Company employs for construction management. As with Con Edison's lack of adequate internal controls, given the mandate in the Public Service Law that its rates remain just and reasonable, as well as its associated obligation to take all reasonable efforts to prevent inflated costs due to fraud, waste and abuse from becoming embedded in the rates charged to its customers, Con Edison either knew, or should have known, that its failure to enforce the controls in place to prevent such fraud, waste and abuse, was unreasonable and imprudent.

1. Con Edison's Failure to Perform Periodic Cost Audits was Imprudent and Allowed the Fraudulent Activity to Remain Undetected for an Unreasonable Period of Time.

CRA's findings regarding the Company's failure to perform cost audits on its contractors as permitted by the Company's standard contract terms are extremely troubling. The failure to enforce this available control mechanism allowed more than ten employees to continue to conduct their fraudulent schemes for almost ten years without ever being detected by the Company. Instead, the activity was only discovered when the activity of the contractor involved was noticed by a United States law enforcement agency that caused it to investigate further. Had Con

¹⁶ Con Edison's Trenching Manual contains the reference material used by the Company's construction management personnel to essentially homogenize descriptions and payments applied to day to day construction work. More detail regarding the Trenching Manual is contained in Section B.2, below, as well as Attachment A at ¶¶5.3.10 through 5.3.12 and, in general, Attachment B.

Edison employed regular periodic cost audits as it was entitled to so do under the Standard Terms and Conditions of every one of its construction purchase orders, the Company could have discovered inconsistent information that would have mitigated the loss to its ratepayers through fraud, waste and abuse.¹⁷

CRA found that, in the absence of a dispute between the contractor and Company personnel, Con Edison failed to perform any periodic construction inspection and audit of a contractor's books and records, or even any on the job audits or post job audits. As CRA notes, this is an industry standard control that was embedded in the Company's construction purchase orders, but of which it did not avail itself.

Had the Company exercised its rights to such audits, it could have significantly improved its ability to uncover overcharges, unusual or suspect payments, and any circumvention of processes and procedures that were taking place. CRA found that this lack of control enforcement contributed to the fact that the activity continued as long as it did, remaining undiscovered for almost ten years. Moreover, CRA found that Con Edison's failure to perform such audits when coupled with the absence of the audit trail identified in Section A.1., above, would have provided the Company an ability to verify and ensure that payment

¹⁷ This particular Con Edison failure to perform audits is even more troubling when one considers the level at which Con Edison's construction spending increased over the years that the fraudulent activity was occurring. The Company has identified payments to construction contractors of \$5.362 billion during the years 2000 through 2008. Moreover, Con Edison's annual spending on construction contractors almost tripled during these years from \$306 million in 2000 to \$801 million in 2008. See Attachment A at ¶6.2.2. Despite such rapid increase, the Company did not strengthen its audit or review of its spending.

information entered into the COMPASS database contained an accurate representation of the work actually performed. Finally, CRA found that the deployment of such periodic independent contractor audits would have greatly increased the deterrence level for fraudulent activity.

Given that this industry standard control was in place during the entire time identified by the US Attorney that the fraudulent activities were taking place, but that the Company failed to take advantage of it at all, let alone use it effectively, Con Edison's conduct completely failed any reasonable test of prudent construction management practice.

2. Con Edison's Failure to Address Deficiencies in the Company's Trenching Manual Was Imprudent.

Con Edison's Trenching Manual contains a listing of payment items that describe the scope of work to be performed, the nature of such work and the associated unit of payment. It is intended by the Company to provide a standard by which to evaluate and account for the cost of most construction scenarios. To provide reimbursement for work performed, a Con Edison field inspector is supposed to match the observed work with the appropriate Trenching Manual item code.

CRA reviewed the Trenching Manual and found that while the Trenching Manual had a valid purpose, the configuration, quantity and quality of the descriptions in the trenching Manual were deficient and subject to abuse. Specifically, CRA found that the Trenching Manual's deficiencies provided an

opportunity to overpay a contractor by either referencing items with more expensive unit rates than a more appropriately applicable item (called “upcoding”) or by charging what should be two mutually exclusive items for the same job.

CRA specifically found that the opacity of the configuration, quantity and quality of the descriptions in the trenching manual combined with the failure of the Company to perform the audits identified in Section 2.A., above, to verify the accuracy and applicability of the item codes being used was a proximate cause of the arrested employees’ fraudulent schemes. Had Con Edison reviewed and updated its Trenching Manual to remove or clarify the descriptions contained therein, the Company or another investigative unit would have been able to more clearly identify where fraud, waste or abuse was occurring. Thus, Con Edison’s failure to review how the manual was used and update it where it identified deficiencies was imprudent.

3. Con Edison’s Failure to Coordinate Investigations Related to Employee Whistle Blower Complaints was Imprudent.

Even where the Company was made aware through the use of complaints regarding suspected fraudulent activity by the eventual arrestees, CRA found that the Company did not consistently adhere to its policies and procedures related to the collection, collation and assignment of those investigations such that the Company missed significant opportunities to identify and stop the activity. CRA expressed the concern that there appeared to be a lack of transparency and communication between the Internal Audit and the Security Services Units despite

the existence of Con Edison's comprehensive policy regarding the flow of information among the two units and the responsibility for investigating complaints made against employees. The Company's failure to enforce this policy is demonstrated by the fact that information regarding complaints made against employees that were eventually arrested was not shared between the two units so that appropriate follow through never occurred. Despite the complaints and allegations of fraudulent or inappropriate behavior made against certain employees, these employees were left in their respective positions when they could have been rotated to other positions.

A company can have the most robust policies on the books available, but its actions must likewise be judged on its implementation and execution of those policies. In this case, the Company's policy regarding the collection, collation and assignment of investigations related to complaints of possible employee misconduct appears to be comprehensive; however, the Company's failure was in that the policy was not executed properly in conformance of the written policy. Thus, the Company's actions were imprudent and failed to identify the fraudulent activity taking place even where those employees that were eventually arrested were the subject of employee whistle blowing complaints.

4. Con Edison's Failure to Instruct Employees in the Use of the Construction Management Databases was Imprudent.

CRA also found that the COMPASS database system in conjunction with another database system, the Construction Layout Tracking System (LOT), served as the central communication tool between Project Planning and Project

Management. The interplay between these two systems was critical to providing proper contractor payment. It is, therefore, essential that information in COMPASS and LOT be accurate and complete to provide an effective control for prudent construction management.

CRA found that despite the essential requirement that only accurate and complete information be included in the databases, no Con Edison systematic program of instruction existed for employees such as formal training material, training schedules or certification procedures for employees allowed to input data into these systems. Likewise, CRA found that there was no material that indicated to employees the consequences of information not being entered truthfully, accurately, completely and in a timely manner. Thus, although the databases could provide for a good control mechanism to measure cost increase or modifications between the project planning and the construction and management phases, the control ultimately failed in that role as providing for, and maintaining, accuracy of the information input there was not sufficiently mandated.

C. Con Edison's Other Internal Control Failures that Facilitated the Fraud and Extended the Length of Time Such Fraud Continued.

In addition to the most important failures detailed in Sections A. and B., above, CRA found other control deficiencies that also facilitated perpetration of the fraudulent schemes by the arrestees or lengthen the time such fraud was allowed to continue undiscovered. These failings all contribute to a finding that Con Edison

acted imprudently in managing its construction program and are contained within the CRA Part 1 and 2 reports attached hereto.

Specifically, CRA found that as part of Con Edison's overall failure to use appropriate tools designed for fraud detection or deterrence, the Company failed to: include key fraud risk indicators in variance reports, trend analyses, or risk and controls documentation; perform compliance audits of contractors' certified payrolls; develop and promote fraud awareness campaigns; extend Sarbanes-Oxley certification assessments to include an evaluation of inherent construction fraud exposure; and segregate duties between and among its construction management employees.

CRA also found as a general matter that the failures of Con Edison's accounting systems and process, some specifically detailed above, created an overall environment wherein unsubstantiated payments were allowed to made to contractors. This general failure is inexcusable in a Company that is required to present a capital plan and budget for Commission review and inspection as part of its regular course of business in establishing just and reasonable rates through Commission judged rate cases. For Con Edison to employ a system of accounting procedures that allowed for unsubstantiated payments to occur was clearly a breach of prudent management practices.

Additionally, during its investigation, particularly in Part 2, CRA noted that it requested a number of construction files to review that Con Edison was unable to produce despite the Commission's record retention requirements. Although such

failure more significantly impacts the assessment of damages, it is important to liability in that such failure demonstrates the lack of Con Edison to either implement regulatory required controls, or to enforce such controls adequately.

Finally, as to damages, Staff notes that CRA's Part 2 Report estimate of almost \$210 million in fraud, waste and abuse is conservative. The Part 2 estimate, instead of being based on CRA's Part 1 sampling methodology, was based on a "check the checker" approach, meaning that CRA audited a subset of the construction jobs previously reviewed by Con Edison's own auditor, KPMG, and was therefore limited by the KPMG reviewed sample population. Moreover, CRA did not make disallowances where supporting documentation for the file, or even the entire construction file, was missing. In fact, because CRA's task was to "check the checker," CRA could not disallow unsupported and undocumented construction jobs because those jobs had been excluded by KPMG's review. The confidence levels associated with CRA's estimate would likely have been much greater were there unlimited funds available to support further transaction review, however, Staff submits that given the reality of fiscal responsibility CRA's estimate is within acceptable confidence levels.

Conclusion

Based upon the evidence provided above, Staff has met its burden of presenting a *prima facie* case of Con Edison's imprudence in managing its capital and operations and maintenance programs resulting in ratepayer harm reasonable estimated by CRA in its Part 2 Report at almost \$210 million attributable to fraud,

waste and abuse related to construction street work and interference. Since Con Edison's rates are established on a cost of service basis, ratepayer harm is a necessary consequence of the overcharges identified. Thus, Con Edison should be required to defend its failure to implement reasonable internal controls related to its construction management policies and procedures, and its failure to adequately execute and enforce those internal controls it did have in place. Any one of the aforementioned failures discussed within the body of this Statement is enough to find that Con Edison's management fell severely short of prudent practice. The combination of all of the identified failures described herein and in the CRA Reports, created an environment or culture, where criminal activity could flourish resulting in the imposition of rates that were neither just nor reasonable.

Finally, the failures identified above clearly and proximately caused the harm to ratepayers. Each failure of internal control either facilitated the fraudulent activity resulting in the unprecedented number of New York utility employees arrested on a single day in January 2009 or allowed the schemes to continue and thrive for the unreasonably long period of almost ten years as identified by the US Attorney's investigation.

Respectfully submitted,

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