

Semiannual Report to the Congress

October 1, 2004 – March 31, 2005

Volume 53



**Office of Inspector General
U.S. Department of Labor**

A Message from the Inspector General

This *Semiannual Report to the Congress* summarizes the significant activities of the Office of Inspector General (OIG) for the six-month period ending March 31, 2005. During this reporting period, our audits of Department of Labor (DOL) programs and operations resulted in \$5.6 million in questioned costs. Our investigative work led to 302 indictments, 217 convictions, and nearly \$50 million in monetary accomplishments. I am pleased to submit this record of our accomplishments. Among our most significant results this period was a decision by a DOL Administrative Review Board ordering Florida to reimburse the Department \$11.4 million in misspent job training funds previously questioned by an OIG audit. The Board reversed an administrative law judge ruling and allowed the costs.

Through our audit program we continue to focus on assessing programs or functions, identifying systemic problems, and recommending constructive solutions to improve the effectiveness and efficiency of DOL operations. Chief among our recommendations this reporting period is the need for the Department to separate its procurement functions from program functions by creating an independent acquisition office led by an Acquisitions Officer who reports directly to the Deputy Secretary. Our recommendation is based on findings in three comprehensive audits involving two major DOL agencies where we found problems with the award, documentation, monitoring, and/or contract termination processes.

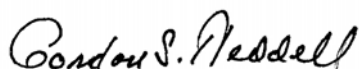
In another significant audit completed this reporting period we confirmed allegations that managers of the Kittrell Job Corps Center manipulated student records, potentially resulting in overpayments for their services. The OIG also found opportunities for improvement relative to Information Technology security controls involving some of DOL's most critical IT systems.

Our audits also identified areas where the Department has achieved success, most significantly in the financial management area, as evidenced by the Department receiving an unqualified opinion on its consolidated financial statements for the eighth year in row.

OIG investigations continue to combat abuses of DOL programs that serve American workers and to combat labor racketeering in the workplace. Among our recent successes were the guilty plea of a Gambino crime-family associate to conspiracy charges relative to a scheme in which he defrauded the Carpenter's and Laborer's Union benefit funds of more than \$7 million.

Also significant was the guilty plea of a union official to conspiracy charges related to a \$1 million embezzlement of the Hudson County District Council of Laborers and its benefit funds. Also notable were the indictments in Virginia of seven defendants on charges of conspiracy, visa fraud, and money laundering, where two of the defendants allegedly filed more than 900 fraudulent foreign labor certification applications on behalf of foreign nationals seeking entry into the United States; and the indictment of 32 members and associates of the Gambino Organized Crime family, including the acting boss, for alleged racketeering and other crimes, including extortion and union embezzlement in the New York City area.

The OIG will continue its efforts to promote the integrity and efficiency of programs that serve American workers and retirees by detecting and identifying ways to prevent waste, fraud, and abuse. In this regard, we will continue to work with the Secretary and officials of the Department to maximize the economy and effectiveness of DOL programs and operations.



Gordon S. Heddell
Inspector General

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Selected Statistics

Investigative recoveries, cost-efficiencies, restitutions, fines and penalties, forfeitures, and civil monetary action	\$49.6 million
Investigative cases opened.....	212
Investigative cases closed	164
Investigative cases referred for prosecution	314
Investigative cases referred for administrative/civil action	165
Indictments.....	302
Convictions	217
Debarments	88
Audit and evaluation reports issued.....	60
Total questioned costs	\$5.6 million
Outstanding questioned costs resolved during this period	\$1 million
Allowed ¹	\$200,000
Disallowed ²	\$800,000

Note: The OIG conducts criminal investigations of individuals that can lead to prosecutions based on criminal complaints, warrants, informations, indictments, or pre-trial diversion agreements. Successful prosecutions may carry sentences such as fines, restitutions, forfeitures, or other monetary penalties. The OIG financial accomplishments, which include administrative and civil actions, are further detailed and defined in the Appendix of this report.

¹ *Allowed* means a questioned cost that DOL has not sustained.

² *Disallowed* means a questioned cost that DOL has sustained or has agreed should not be charged to the government.

Significant Concerns

The OIG provides information and assistance to the Department and Congress in achieving efficient and effective management of DOL programs. As part of our effort to focus attention on mission-critical management problems and their resolution, the OIG has identified the following areas that we consider vulnerable to mismanagement, error, fraud, waste, or abuse.

The Permanent Foreign Labor Certification Program

The OIG is concerned about abuse of DOL's Permanent Foreign Labor Certification program. This abuse may result in the unlawful admission of foreign nationals and economic hardship for domestic workers. During this reporting period, an OIG audit found that the Employment and Training Administration's (ETA's) San Francisco regional office (SFRO) may be certifying inaccurate, deficient, or possibly fraudulent labor certification applications. These applications were submitted to SFRO through California's Employment Development Department, along with a warning from state investigators that the applications were flawed. We found no evidence that SFRO considered investigators' findings; however, the SFRO approved the applications in question.

New regulations, effective March 2005, provided for electronic submission of applications for the Permanent program directly to ETA national processing centers. A prior OIG audit cautioned that removing human review of applications by State Workforce Agencies, such as that provided by California investigators, might increase fraud due to reduced controls on application information. However, the new system does include some positive developments in the area of fraud detection.

Under the new rule, ETA will verify whether employers seeking certifications are bona fide business entities with employees on the payroll. Using selection criteria based on potential fraud indicators, the electronic system will identify applications for audit. In addition, the OIG will be informed of possible fraud cases. These improvements are the result of the cooperative efforts of ETA, the OIG, and others. What remains for the Department is to diligently implement changes so that expediting the processing of backlogged applications does not come at the expense of certifying fraudulent applications.

Additional regulatory changes to the program are also needed. For example, although the approved labor certification bears the name of a specific alien worker, that certification may be used to hire another worker. Our investigations have shown that this practice, known as substitution, encourages fraud involving the sale of approved certifications to foreign workers for up to \$20,000. In addition to prohibiting substitution, we believe regulations should limit the life of a certification to 90 days to discourage abuses.

Procurement and Systems Planning Concerns

Improperly managed and awarded procurements by the Department of Labor are of concern to the OIG. This concern is compounded in cases where the Department, as a result of poor systems planning, is not using millions of dollars' worth of purchased products. Based on our recent audit work, the OIG identified actions the Department should take to improve this situation.

In the case of a DOL sole-source contract awarded to Meganet Corporation for encryption software and services, our audit found that the contract was not properly awarded, modified, or managed. This was largely due to inadequate separation between DOL's information technology (IT) program function and procurement function, which currently fall under the jurisdiction of the same DOL official. We recommended that DOL separate its procurement function from program functions by creating an independent acquisition office.

This audit also found that DOL did not use \$3.8 million worth of encryption purchases from Meganet and could not support its reasons for abandoning that investment. We therefore recommended that the Department establish a process for an independent review and approval of decisions to abandon contracts or to not use products already purchased. The need for this process is further illustrated by a prior OIG audit that found the Occupational Safety and Health Administration (OSHA) invested millions in the redesign of a mission-critical data system that resulted in no benefit to the Department.

Finally, our audit of Mine Safety and Health Administration procurement found that the agency demonstrated a pattern of disregard for acquisition requirements and did not adhere to the principle of full and open competition. Here too we concluded that lack of separation of the procurement function allowed program staff to exert undue influence over the procurement process. Recurrent problems such as these highlight the need for improving DOL-wide procurement practices to prevent violation of acquisition requirements and wasteful spending.

Oversight of Grantees and Contractors

The OIG has raised concerns about grant and contract accountability in the Department, and ETA has undertaken an initiative to improve grant administration. The bulk of DOL expenditures on employment and training take the form of grants. Direct Federal oversight of these grants is difficult because a large share of the funding is passed down through the states to subgrantees and contractors. During this reporting period, OIG audits found that grantees and contractors continued to charge unallowable costs, manipulate performance data, and otherwise fail to meet program requirements, as outlined in the examples below.

For example, the State of Arkansas improperly allocated \$860,000 in WIA grant funds to Nestle Corporation for purposes prohibited under the act. Funds intended for upgrading the skills of incumbent workers were used to train new hires. Before Nestle's Jonesboro, Arkansas, facility was built or employees hired, the funds were improperly promised to Nestle as an

incentive for the company to locate in Arkansas. In addition, the State improperly used almost \$350,000 in Unemployment Insurance grants to pay for vacant office space. We recommended that DOL recover these costs.

In another example, the Kittrell Job Corps Center of North Carolina improperly manipulated student attendance and training records to improve the center's reported performance. This not only violated program requirements, but it also had a financial impact on Job Corps, because centers are reimbursed for operating expenses, receive bonus and incentive payments, and are awarded contract option years based on performance data. In response to a related OIG audit, ETA is now requiring its regional staff to validate Job Corps data as part of their routine monitoring procedures.

As a final example, an OIG audit identified compliance problems with the Indiana Department of Labor's management of an OSHA safety and health consultation program from October 1999 through September 2002. The OIG found instances of funds not expended in accordance with regulations, unallowable costs, and noncompliance with provisions with their agreements with DOL.

The OIG is reviewing ETA's efforts to improve overall grant accountability, with the aim of determining whether ETA's planned improvements are being implemented.

Major Management Challenges at DOL

The Reports Consolidation Act of 2000 (P.L. 106-531) requires the OIG to identify the most serious management challenges faced by the Labor Department. These challenges and the Department's response to them are published in the Department's annual report. The challenges identified by the OIG in DOL fiscal year 2004 annual report are:

- reduction of improper payments,
- Unemployment Insurance safeguards,
- integrity of foreign labor certification programs,
- financial and performance accountability,
- systems planning and development,
- information systems security,
- security of employee benefit plan assets,
- accounting for real property, and
- Workforce Investment Act reauthorization.

The challenges in their entirety are on the OIG's Web site (www.oig.dol.gov).

Procurement

In FY 2003, DOL spent \$1.5 billion on procurement activities and initiated more than 12,000 procurement actions. With this amount of dollars at stake, it is important for the Department to examine its procurement policies. As a result of hotline complaints received by the OIG, we conducted two comprehensive audits related to departmental procurement issues during this period and provided substantive comments to a revised internal DOL policy directive related to grant and procurement authority. Of greatest concern to the OIG in this area is the need to separate procurement duties from operational or program duties. To improve the performance and ensure the accountability, the OIG recommended a number of changes to the existing procurement program.

\$3.8 Million Contract Improperly Awarded for Encryption Products

Following receipt of a hotline complaint and a subsequent memorandum from the Assistant Secretary for Administration and Management, the OIG initiated an audit of DOL's contract with Meganet Corporation to purchase file-encryption software and related services. The objectives were to determine:

- whether the sole-source contract awarded to Meganet was in compliance with government-wide procurement regulations and DOL procurement policies;
- whether DOL provided adequate justification for not using the products purchased through the Meganet contract and, if so, whether DOL adequately justified not attempting to recover the \$3.8 million paid to Meganet; and
- the current status of DOL's file and e-mail encryption capability.

We found significant irregularities in DOL's process for awarding the Meganet contract. Specifically, there was:

- no documentary evidence that the need to purchase encryption software was reviewed by DOL's Technical Review Board, which is composed of IT executives from DOL agencies;
- inadequate documentation of the evaluations of pre-proposal submissions;
- no written justification for the use of a sole-source contract;
- a lack of disclosure by the then Deputy Chief Information Officer of an apparent conflict of interest; and
- a possible bias in preparing the Statement of Work.

We also found that the Department's reasons for deciding not to use the products purchased from Meganet were not supported. Although DOL officials stated that the software did not perform as expected, there were no test results or other documentation to support these assertions. The OIG tested the software in a configuration described in the Meganet contract and found the software did function. We concluded that the Meganet contract was

not properly awarded, modified, or managed because of a lack of organizational separation of duties, inadequate oversight, and insufficient internal controls. Furthermore, individuals knowingly made decisions and took actions that violated government regulations and DOL policies and that may not have been in DOL's best operating or financial interests. As a result, the contract may have been improperly awarded on a sole-source basis, \$3.8 million in Meganet products have gone unused without adequate justification, and DOL spent an additional \$1.6 million (as of December 2004) on another product to satisfy some of the same technical requirements that Meganet's products solved.

Currently the Office of the Assistant Secretary for Administration and Management (OASAM) is responsible for DOL's procurement function and for its IT function. Among our recommendations were that DOL should properly separate its procurement and programmatic responsibilities and put effective controls in place, including a process for an independent review and approval of decisions to abandon contracts or to not use products already purchased. The OIG believes that unless such recommendations are implemented, DOL will continue to be at risk for wasteful and abusive practices, as evident in its handling of the Meganet contract. DOL responded that it has already made some policy and staffing changes, plans to implement additional controls, and will "give careful consideration" to the reasons behind our recommendation that procurement and programmatic responsibilities be separated. ([Report 05-05-005-07-720, issued March 31, 2005](#))

MSHA Procurements Disregarded Acquisition Rules

To determine the merits of a series of allegations received by the OIG Hotline, the OIG audited the Mine Safety and Health Administration's (MSHA's) procurement and contracting procedures, as well as related personnel matters, for June 1, 2000, through December 31, 2002. Within the Department, MSHA is one of only two agencies that has acquisition authority for the purchase and lease of Federal information-processing resources. Our audit found the following:

- MSHA did not always ensure that the government received best value or that vendors were treated fairly in the award of contracts.
- MSHA circumvented requirements to procure office furniture and travel management services from specific sources.
- A potential conflict of interest existed in the award of contracts to a company owned by a contracting officer's spouse.
- Excessive unauthorized commitments and ratifications were made.
- Deficiencies existed in how MSHA administered some of its contracts.

The overall cause for the problems we identified was a long-term history of MSHA management that accepted and fostered a lack of commitment to procurement principles, which was facilitated by a lack of separation of the procurement from the program function. This lack of separation of duties allowed program staff to exert undue influence over procurement personnel—an environment that resulted in MSHA being unable to ensure that contracts were in the government's best interest and that all eligible contractors were afforded a fair opportunity to provide supplies or services to MSHA.

Prior to the issuance of our report, the OIG reviewed contract files for procurements made by MSHA in FYs 2003 and 2004. We observed a degree of file documentation that, had MSHA documented its procurement actions and rationale for its choices of procurement instruments to the same extent during the period included in our audit, would have addressed some of the findings in this report.

We recommended that DOL rescind MSHA's procurement authority, reassign such authority, and ensure that said authority is completely independent of MSHA. The Department responded that it would be important to assess the full breadth and effectiveness of recent procurement reforms in order to make a more informed judgment on our recommendation. In addition, DOL indicated that MSHA has instituted procurement reforms. ([Report 25-05-001-06-001, issued October 29, 2004](#))

Weaknesses in OASAM Procurement

As indicated in the Financial Management section of this report, during our audit of the Department's financial statements, we noted four new reportable conditions. One of these involved weaknesses found in our testing of the OASAM procurement office. The procurement office processed approximately \$296 million of the \$622 million of new FY 2004 procurements for supplies and services. We identified weaknesses in the areas of file documentation, file organization, and compliance with Federal Acquisition Regulations requirements regarding contract competition.

Changes Needed in DOL Procurement Regulations

The Department is currently revising its internal policy and procedures regarding procurement. Because of recent audit work in this area, we provided input and made suggestions on how to address our audit findings through changes to DOL policies and procedures.

Within the Department of Labor, OASAM has overall responsibility for DOL's procurement functions, as well as overall responsibility for all major administrative functions. This creates an organizational conflict of interest whenever a procurement action involves products or services. The OIG believes the lack of separation of duties does not allow for sufficient oversight or accountability for procurements and increases the risk that operational needs and desires will override sound procurement practices.

The OIG's overarching concern is the need for separation of duties. As described in this section, recent OIG audits have shown that problems arise when program officials, instead of contracting experts, drive procurement policy and decisions. It follows that officials who have procurement authority should not also have responsibility for operational or program areas. To address these concerns, the OIG's comments on the proposed DOL policy revision on procurement include a recommendation that procurement executives be higher than, and organizationally separate from, program and operations officials.

Information Technology

The Department operates sensitive systems comprising major applications, general support systems, and mission-critical systems. DOL relies on these critical information systems to monitor and analyze the nation's labor market and economic activities, manage workforce services, and protect and compensate American workers. The Department continues to focus on improving its information security program. For example, the Department was proactive in establishing IT security work groups to develop better policies and procedures in logical access control, change control management, and contingency planning.

Last year, the OIG noted that the Department had weaknesses in both risk assessment and certification and accreditation processes. We continue to test in both areas to determine whether progress has been made.

Stronger IT Controls Needed Over Financial Systems

The OIG assessed IT application controls over the Department of Labor Accounting and Related Systems (DOLAR\$), the Department's core financial and accounting system that supports the financial statements. The OIG also assessed the general and application controls of PeoplePower, the Department-wide human resource/payroll system. We also tested and updated the audit findings and recommendations identified in previous years. Moreover, the OIG issued a report to summarize all audit work performed in support of the FY 2004 DOL financial statement audit.

DOLAR\$ Application Controls

Regarding DOLAR\$ application controls, we noted that the Office of the Chief Financial Officer (OCFO) has made progress in addressing IT control weaknesses identified in prior years. However, we also noted recurring recommendations, originating in FY 2002, that have not been fully implemented. Based on the current year testing results, we found weaknesses in application security controls over the DOLAR\$ system. We also made 17 new findings and 36 associated control recommendations for improvements in general, application, and security controls.

PeoplePower

Regarding PeoplePower, we found weaknesses in the design and implementation of security and application controls. We identified 16 application control findings and made 37 related recommendations for DOL to reduce the risk over payroll subsystems and data. Among our findings, we noted that PeoplePower had an incomplete security plan, lacked a segregation of duties policy, and was weak in monitoring procedures and password controls. For input and output controls, the system had weak edit checks and reconciliation procedures, as well as weak retention and storage procedures over sensitive output. We also found problems in certification and

accreditation, audit trails, and processing controls. Although we found security and application control weaknesses, we did not identify any significant issues with the integrity of data in PeoplePower.

We recommended that OCFO establish procedures and controls to ensure full compliance with the federal IT security standards. In general, OCFO agreed with our recommendations and proposed action plans that address the security issues raised in our findings.

Summary Report

This report summarized all audit work performed in support of the FY 2004 DOL financial statement audit, some of which was reported previously. We assessed the effectiveness of IT general, application, and security controls over 14 systems operated by 7 agencies in support of DOL financial statements. The audit provided DOL with information on weaknesses in key security controls, as well as with recommendations to improve IT security.

The summary report described weaknesses in the design and operation of internal controls, which could adversely affect the reliability of financial and performance reporting, and in the system's compliance with laws and regulations. To correct the problems, we recommended that DOL strengthen controls over access to and protection of financial information by implementing appropriate controls for application, logical security, and business continuity recovery.

Based on our recommendations, DOL has developed new policies and procedures to address the weaknesses noted above, including (1) revising the Department's IT security policy and procedures to provide improved logical access and technical control guidance; (2) developing a technical standards manual that serves as a repository of approved enterprise security standards; (3) revising DOL security test and evaluation procedures; (4) developing an internal independent verification and validation process; and (5) coordinating application processing priorities to improve disaster recovery and contingency planning.

These weaknesses were a reportable condition in the DOL FY 2004 financial statement audit, which is discussed in the Financial Management section of this report.

We determined that the recommendations in this summary report are resolved based on the actions and time frames described in DOL's response. To ensure complete implementation of corrective actions, which is necessary to close out these recommendations and reportable conditions, the OIG will continue to monitor the progress and conduct follow-up testing during its audit of the FY 2005 DOL financial statements. ([Report 23-05-004-07-001](#), issued October 18, 2004; [Report 23-05-022-13-001](#), issued October 18, 2004; and [Report 23-05-002-13-001](#), issued October 18, 2004)

Financial Management

Consolidated Financial Statement Audit

The OIG issued an unqualified opinion on DOL's consolidated financial statement for the eighth consecutive year. We found that DOL substantially complied with the standards of the Federal Financial Management Improvement Act (FFMIA). The act's standards require agencies to implement and maintain systems that provide timely, accurate, and useful information upon which to base decisions and to ensure accountability on an ongoing basis.

Reportable Conditions

We noted four new areas involving internal controls that we consider to be reportable conditions, although we do not consider them to be material weaknesses. We also noted seven outstanding reportable conditions from prior years that continue to require management's attention. The new reportable conditions, including any subsequent agency action are discussed in the Office of Workers' Compensation Programs, Information Technology, and Procurement sections of this report, respectively.

New Reportable Conditions

- Inaccurate Federal Employees' Compensation Act (FECA) Medical Bill Payments
- FECA Medical Bill Receivables
- Stronger IT Controls Needed Over Financial Systems
- Weaknesses in OASAM Procurement

Outstanding Reportable Conditions

The outstanding reportable conditions from prior years include Job Corps real property, FECA payments, IT security controls over financial information, deficiencies in accounting for grants, capitalized assets, UI benefit overpayments, and implementation of managerial cost accounting.

In IT security controls over financial information, continuing weaknesses were identified with the Department's technical security standards and policies; logging, monitoring, and response controls; system administration procedures; and the overall security framework. DOL has not coordinated comprehensive disaster recovery tests to ensure the Department's network and applications can be recovered in the case of a disaster. Testing conducted in FY 2004 identified that DOL agencies were in varying stages of disaster recovery plan development and testing. In addition, the Department had not coordinated disaster recovery efforts across all agencies or conducted a Department-wide test of disaster recovery plans. The Department has indicated that it has taken or is undertaking corrective action. In order to close out these reportable conditions, the OIG will evaluate the corrective actions during our audit of the FY 2005 DOL financial statements. ([Report 22-05-004-13-001, issued November 15, 2004](#))

Employee Misconduct Investigations

The OIG investigates allegations of wrongdoing by those entrusted to carry out departmental programs and activities. Below is an example of this type of investigation.

DOL Contractor Sentenced for Falsifying Employment Application

A former MSHA computer contractor, Salahuddin Khattak, pled guilty on March 10, 2005, to charges of making false statements and was sentenced to three months plus two years' probation for falsifying documentation regarding his security background information on more than one occasion. Khattak failed to disclose two trips to Pakistan, and he had falsely stated his place of birth on the form. He also misrepresented his marital status. In addition, Khattak falsified information on a Federal application when he applied for permanent employment with DOL. This was a joint investigation with the FBI and the State Department's Diplomatic Security Service. *U.S. v. Khattak* (E.D. Virginia)

Audit Resolution

When the OIG questions costs claimed by a grantee, the Department reviews the expenditure and determines whether it was allowable under the applicable rules and regulations. If the Department determines that the costs were unallowable, a debt is established. The grantee has appeal rights both within and outside the Department. Below is an example of the audit resolution process.

Florida Ordered to Repay \$11.4 Million in Misspent Funds

In February 2005, the Department's Administrative Review Board ordered the State of Florida to reimburse the Department \$11.4 million in job training funds questioned in a 1998 OIG audit report. The Board asserted that the State failed to show that Job Training Partnership Act funds were spent for lawful purposes. The 1998 OIG audit found that Florida used the funds to supplant adult education costs that should have been borne by the State. Although ETA disallowed the \$11.4 million, a DOL administrative law judge ruled that the expenditures were proper and reversed the disallowance. This ruling was appealed to the Board. ([Report Number 04-98-005-03-340; issued September 25, 1998](#))

The OIG at the Department of Labor is unique among inspectors general in that it has an “external” program function to conduct criminal investigations to combat the influence of labor racketeering and organized crime in the nation’s labor unions. Labor racketeering is the infiltration, domination, and/or use of a union or employee benefit plan for personal benefit by illegal, violent, or fraudulent means. Organized crime is defined as activities carried out by groups with a formalized structure whose primary objective is to obtain money through illegal activities. Traditionally, organized crime has been carried out by La Cosa Nostra (LCN) groups, also known as the “mob” or the “Mafia.” According to the Department of Justice, however, there has been a rapid rise in transnational organized crime groups engaging in new criminal enterprises. There are now organized crime groups that include people from Asia, Russia, Eastern Europe, Nigeria, and West Africa.

Labor racketeering activities carried out by organized crime groups affect the general public in many ways. Because organized crime’s exercise of market power is usually concealed from public view, millions of consumers unknowingly pay what amounts to a tax or surcharge on a wide range of goods and services. In addition, by controlling a key union local, organized crime can control the pricing in an entire industry. The public also suffers when organized crime orchestrates illicit strikes and work slowdowns or resorts to violence to maintain its operation of labor rackets.

Over the past two decades, the OIG has conducted extensive criminal investigations of labor racketeering. Traditionally, organized crime has been involved in loan-sharking, gambling, benefit plan fraud, violence against union members, embezzlement, and extortion. OIG investigations have uncovered millions of dollars of workers’ dues and benefit monies that have been siphoned off by organized crime through embezzlement or more sophisticated devices, such as fraudulent loans or excessive fees paid to corrupt union and benefit plan service providers. Our investigations continue to identify complex financial and investment schemes used to defraud pension assets, resulting in millions of dollars in losses to plan participants.

Our current investigations are finding that nontraditional organized crime groups are engaging in racketeering and other crimes against workers in both union and nonunion environments. Moreover, they are exploiting the Department of Labor’s foreign labor certification and Unemployment Insurance programs. The following cases are illustrative of our work in helping to eradicate both traditional and nontraditional labor racketeering in the nation’s labor unions, employee benefit plans, and workplaces.

Benefit Plan Investigations

The OIG is responsible for combating corruption involving the monies in union-sponsored benefit plans. These pension plans and health and welfare benefit plans comprise hundreds of billions of dollars in assets. Our investigations have shown that this money remains vulnerable to corrupt union officials and organized crime influence. Pension plan service providers to pension plans continue to be a strong focus of the OIG's investigations.

LCN Associate Pleads Guilty to Embezzling \$7 Million from Benefit Plan

On November 22, 2004, Mario Garafola, a Gambino Crime Family associate and company owner, pled guilty to conspiracy charges for a scheme that involved embezzling employee benefit plan funds and laundering money. The investigation revealed that Garafola defrauded the Carpenter's Union and the Laborer's Union benefit funds of more than \$7 million. He circumvented a collective bargaining agreement by operating one of the companies as a nonunion shop while using the same employees and equipment as the unionized one. By doing so, he avoided paying benefits to union benefit funds. This investigation was conducted jointly with the FBI. *U.S. v. Garafola* (E.D. New York)

Former Union Benefit Fund Director Charged in Embezzlement Scheme

A former executive director of the National Plastering Industry's Joint Apprenticeship Trust Fund, located in Landover, Maryland, and the Trust Fund's former office manager were charged on March 15, 2005, with defrauding the fund, the Department of Interior, and DOL's Job Corps program of more than \$917,000 over a five-year period. They were charged with bank and mail fraud and money laundering. The trust fund is a nonprofit training entity governed by the Operative Plasterers' and Cement Masons' International Association to provide pre-apprenticeship career training for disadvantaged youth at Job Corps centers.

The investigation found that the two former employees allegedly generated checks to current, former, and fictitious vendors for nonexistent expenses. They also took funds from unions belonging to the association, the Union's trust funds, and contractors and employers in the form of employee benefit contributions. The two former employees then deposited the funds in a hidden account to be used for personal expenses. This investigation was conducted with the IRS Criminal Investigations Division (CID), the Department of Interior OIG, and DOL's Employee Benefits Security Administration (EBSA).

Internal Union Investigations

Our internal union cases often involve instances of corruption, such as union officers who abuse their positions of authority to embezzle money from union accounts for their own benefit. Investigations in this area also focus on situations in which organized crime groups control or influence a labor organization, frequently to exercise influence in an industry for corrupt purposes or to operate traditional vice schemes, such as drug dealing and theft. Following are examples of our work in this area.

Union Official Pleads Guilty to Embezzling More Than \$1 Million

On January 7, 2005, Carmelo Sita pled guilty to conspiracy charges related to an embezzlement of just over \$1 million from the Hudson County District Council of Laborers and its benefit funds and to falsifying reports of a benefit plan covered by the Employee Retirement Income Security Act (ERISA). Sita admitted that from January 1995 through March 1999, he conspired with others, who have previously pled, to take more than \$1 million from eight bank accounts that were maintained for union members and plan participants. This investigation was conducted jointly with EBSA and the FBI. *U.S. v. Sita* (D. New Jersey)

Former Union Presidents Convicted of Embezzlement

Joseph Nardone Sr., the founder and retired president of Local 148 of the Novelty and Production Workers Union, and his son, Joseph Nardone Jr., were both convicted at trial for their embezzlement scheme against Local 148. The Nardones were indicted in October 2002 and charged with conspiracy to embezzle in excess of \$350,000 in welfare funds and union funds as a result of a multifaceted fraud scheme. From 1996 through 2001, the Nardones created unnecessary construction projects at the union's Jersey City office building. They conspired with Stanley Rothman, a contractor who had previously pled guilty, to skim \$250,000 from the inflated costs of the construction projects.

As a result of this investigation, numerous other Local 148 officers and business agents have also been convicted. Local 148 is presently under a Federal Court-ordered trusteeship because of corruption and abuse of fiduciary powers. This investigation was conducted jointly with the Department of Housing and Urban Development OIG and EBSA. *U.S. v. Nardone, et al.* (D. New Jersey)

Company Owners Plead Guilty in Complex Scheme

On March 29, 2005, Carlos Gomez and Mary Gildea, the owners of Lanco Scaffolding, pled guilty to charges of conspiracy, mail fraud, and making false statements on pension plan documents covered under ERISA. The investigation revealed that they had allegedly evaded paying payroll taxes,

workers' compensation premiums, and payments to both the Carpenter's Union and the Laborer's Union ERISA benefit funds. In addition, one of the owners was charged with submitting false tax returns.

The scaffolding company supplied, erected, and dismantled scaffolding equipment for construction projects. Because the company had collective bargaining agreements with both the Laborer's and the Carpenter's Unions, it was required to make payments to the benefit funds. As a result of the above crimes, the losses to the various benefit funds, insurance companies, and the IRS is estimated to be more than \$4.7 million. This investigation was conducted jointly with the IRS CID, the FBI, EBSA, and the Insurance Fraud Bureau of Massachusetts. *U.S. v. Gomez, et al.* (D. Massachusetts)

Defendant Caught in Kickback Scheme

Jeffrey Respler, owner of Plumbing Solutions Inc., pled guilty on December 3, 2004, to conspiring with Donald Sclafani, president of Plumbers' Union Local 1, to sell property at an inflated rate and kick back the \$1.3 million difference to Sclafani. The money used to pay for the inflated property came from the Plumbers' Union Trade Education Fund. Respler also pled guilty to bribing New York City plumbing inspectors and to committing perjury.

This investigation was conducted jointly with EBSA, the New York State Attorney General Office's Organized Crime Task Force and the New York City Department of Environmental Protection OIG. *State of New York v. Respler*

Father and Son Charged for Defrauding Union Association

On December 2, 2004, a father and son were charged after an investigation found that they used Unity House, Inc., for personal benefit at the expense of its members. Unity House is a labor support organization that provides services to three union locals in Hawaii. The men were charged with mail fraud, wire fraud, filing false tax returns, making illegal payments to a labor union, and forfeiture allegations. One of the defendants was also charged with witness tampering. The investigation found that one of the individuals conspired to shift control of Unity House from its members by converting it into a non-membership-based nonprofit organization.

In addition, the father, who was president of Unity House, allegedly approved a \$40,000 loan to a former state lawmaker without the knowledge of the organization's board of directors. The lawmaker later introduced legislation favorable to the defendant. The son was named as the listing agent for two residential properties sold by Unity House, which generated \$15,000 in commissions. He also allegedly caused Unity House to make two unlawful loans worth a total of \$35,000 to a new labor union called the Hawaii Hospital and Health Care Workers Union. Both loans were alleged to be illegal payments under the Taft-Hartley Act. This was a joint investigation with DOL's EBSA and Office of Labor Management Standards, the FBI, and the IRS.

Ringleader Pleads Guilty and Associate Is Convicted in Multiple Schemes

On January 10, 2005, the principal defendant, James Duff, pled guilty to charges of RICO conspiracy, money laundering conspiracy, mail fraud, wire fraud, money laundering, and filing false tax returns for multiple fraud schemes. In February 2005, one of Duff's associates, William Stratton, a former business agent of Liquor and Allied Workers Union Local 3, was convicted of all these charges except wire and tax fraud. Between 1990 and 2002, Duff's associates were awarded City of Chicago contracts and subcontracts in excess of \$100 million based on fraudulently obtained women- and minority-owned business status. The investigation was conducted with the IRS, the FBI, DOL's Office of Labor Management Standards, and EBSA. *U.S. v. Duff, et al.* (N.D. Illinois)

Former Union President Sentenced to Nearly Six Years in Prison

On February 18, 2005, Walter Browne, former president of the National Federation of Public and Private Employees, was sentenced to 70 months' incarceration and 3 years' probation. Browne's sister, Patricia Browne Devaney, a former administrative assistant to the union, received a sentence of 27 months in jail and 5 years' probation. Both are barred from any union activity for 13 years each. In addition to the forfeiture of nearly \$600,000 ordered in December 2004, Devaney was ordered to pay more than \$87,000 to the union.

Browne and Devaney were convicted in June 2004 on charges that included RICO violations, embezzlement of union assets, Taft-Hartley Act violations (stemming from the unlawful receipt of more than \$300,000 from multiple employers), bank fraud, mail fraud, theft of honest services, and record-keeping violations. The investigation found that from 1994 through 2002, Browne and Devaney engaged in racketeering by using their positions within the union to dominate and control its operation for their personal gain through various means, including credit card abuse, issuing unauthorized payroll checks, and submitting false vouchers. *U.S. v. Browne; U.S. v. Devaney* (S.D. Florida)

Labor-Management Investigations

Labor-management relations cases involve corrupt relationships between management and union officials. Typical labor-management cases range from collusion between representatives of management and corrupt union officials to the use of the threat of “labor problems” to extort money or benefits from employers.

LCN Crime Family Leadership Charged with Racketeering and Extortion

On March 2, 2005, in the Southern District of New York, 32 members and associates of the Gambino Crime Family were charged in a 53-count indictment for allegedly conducting wide-ranging racketeering crimes and other offenses spanning more than a decade. A president of the United Food and Commercial Workers Local 305 and a trustee of the local’s benefit funds were also charged with union benefit embezzlement and related fraud charges. The criminal offenses included assault, extortion of various individuals and businesses, loan-sharking, union embezzlement, illegal gambling, trafficking in stolen property and counterfeit goods, and mail fraud. The investigation found that this group allegedly infiltrated, controlled, extorted, and defrauded businesses and labor organizations, such as construction companies, a radio station, trucking companies, and restaurant and club owners. This was a joint investigation with the FBI and the Bronx District Attorney’s Office.

Mob Leaders and Union Officials Charged

On February 3, 2005, a Genovese LCN Family capo and three officers of the International Longshoremen’s Association (ILA) were charged with conspiracy, mail fraud, and theft of honest services. The investigation found that Genovese members allegedly directed the placement of Genovese associates into powerful positions with the ILA. Once in these positions, these individuals were instrumental in awarding benefit fund-related contracts to companies with ties to the Genovese LCN Family. This investigation is part of an ongoing initiative with the FBI and the Waterfront Commission of New York Harbor.

Chicago City Officials and Trucking Company Owners Charged in Bribery Scheme

Twenty-eight individuals have been charged in an investigation of the City of Chicago’s Hired Truck Program (HTP), including charges of RICO conspiracy involving bribery, extortion, mail fraud, and perjury. The HTP allowed four Departments (Streets and Sanitation, Transportation, Water, and Sewers) to hire trucking services on an as needed basis to supplement construction projects and daily operations. On March 9, 2005, Martin McDonagh pled guilty to charges of lying to federal agents about bribing a city employee to get into the HTP. Over a period of years, McDonagh paid more than \$35,000

to the city employee in order to receive preferential treatment for his trucking company. Another trucking company owner was accused of mail fraud for allegedly obtaining \$6.6 million in HTP work by giving campaign contributions and cash to city officials and falsely claiming his firm was eligible for jobs set aside for women-owned businesses.

The RICO conspiracy indictment of February 24, 2005, charged 14 individuals, including 6 former Chicago city employees, 10 trucking company owners (2 of the owners were also city employees), and an accountant with offenses related to HTP corruption. Several city employees allegedly operated Chicago's Departments of Water, Sewers, Streets & Sanitation, and Transportation as a racketeering enterprise by engaging in a pattern of fraud, extortion, bribery, and obstruction of justice between 1993 and 2004. HTP permitted the city to hire private trucking companies for projects in a no-bid process, spending \$40 million annually on the 172 trucking companies that participated in the program. Several HTP trucking companies were owned by either alleged mobsters or the family members of reputed mob figures. The investigation uncovered that city employees allegedly solicited trucking companies for cash, gifts, political contributions, or private labor in exchange for preferential treatment.

The OIG became involved with the investigation due to the trucking companies' affiliation with several unions and due to allegations of Minority Business Enterprise/Women's Business Enterprise fraud. This is a joint investigation with the FBI, the United States Postal Inspection Service (USPIS), and the IRS CID. *U.S. v. McDonagh* (N.D. Illinois)

Union Officials Charged with Taft-Hartley Violations

On November 29, 2004, an executive secretary-treasurer and the former president/executive director of the Michigan Regional Council of Carpenters (MRCC) were charged with conspiring to solicit and receive prohibited payments (Taft-Hartley Act violations) in the form of discounts from six different construction companies whose employees were represented by the MRCC. The investigation found that from January 1998 to December 1999, the former union officials allegedly conspired to solicit and obtain discounts exceeding \$147,000 on building materials, labor, and related costs in order to reduce the cost of constructing a new personal residence for the executive secretary-treasurer in Grosse Pointe Park, Michigan. This case was investigated with the FBI and EBSA.

Retired Union Official Charged with \$1.5 Million Extortion

A retired international representative of the United Food and Commercial Workers (UFCW) Union was charged on November 18, 2004, with Hobbs Act extortion, mail fraud, wire fraud, and interstate travel in aid of racketeering. The investigation also found that the former UFCW union official allegedly extorted approximately \$1.5 million from a supermarket chain from 1989 until the time of his arrest in September 2003 to keep the union from organizing the company. This investigation was conducted jointly with the FBI and the Boston Police Department.

Foreign Labor Certification

The Department's foreign labor certification (FLC) programs provide American employers access to foreign labor. The Permanent Foreign Labor Certification program allows an employer to hire a foreign worker to work permanently in the United States. Administration of this program is the responsibility of three Federal departments: Labor, Homeland Security, and State. Prior OIG audits have identified vulnerabilities in the FLC program, and our investigations continue to identify fraud against these programs.

FLC Applications May Have Been Approved Despite Notifications of Potential Fraud

We conducted an audit based on a complaint alleging that ETA's San Francisco regional office (SFRO) did not consider warnings, notification of potential fraud, or other application deficiencies identified by the State of California's Employment Development Department. The complaint also alleged that SFRO certified and/or processed as many applications as possible to reduce the backlog and to meet regional goals or quotas, with little or no regard to warnings of abuse, potential fraud, or application deficiencies.

At the time of the audit, the State reviewed FLC applications before they were forwarded to SFRO for approval. If the State identified problems with the application, a form was attached stating the investigative results and the finding. We reviewed a judgmental sample of 35 applications for which California had prepared the form. According to the State, the applications and forms were forwarded to SFRO. We found the following:

- Although SFRO received the forms, we did not find any of these forms in the application files. The OIG was unable to make a definitive determination, but we believe that because this form was missing from the files and there was no other evidence of a Notice of Findings or other action taken on the application, SFRO may not have heeded warnings of potential abuse and/or fraud identified by California.
- In some cases, SFRO certified applications within a day or two of receipt, even though the State had found problems with the application.
- The SFRO Certifying Officer did not review subordinates' work to ensure that only bona fide applications were certified.
- Application files were purged of critical documents that should have been considered in the analysts' decisions to certify or deny applications.
- SFRO appeared to be working under a regionally mandated quota system, driving them to ignore questionable applications in order to achieve numerical results, with little or no management oversight. SFRO's emphasis was on reducing the FLC application backlog, as opposed to certifying only bona fide applications.

