

DATE: April 24, 2024

TO: Chair Nora Vargas, Board of Directors
Chair David Zito, Audit Committee
SANDAG Board of Directors
SANDAG Audit Committee
Coleen Clementson, Interim Chief Executive Officer
Ray Major, Chief Deputy CEO
Andre Douzdjian, Chief Financial Officer
Residents of San Diego County and Toll Users

FROM: Courtney Ruby, Independent Performance Auditor

SUBJECT: SANDAG Management Response to the OIPA's Investigation Report on SANDAG's State Route 125 Toll Operations

INTRODUCTION

SANDAG Executive Management (Management) provided a timely response to the Office of the Independent Performance Auditor's (OIPA) [SR 125 Investigation](#) released on March 25, 2024. In their response, Management acknowledged and agreed with all the report's findings and recommendations as well as accepted full responsibility for the failures of the toll operations system. In addition, Management provided a detailed discussion memo, project history, timeline, and response to SANDAG's Board of Directors' questions.

According to [Board Policy No. 039](#), the Independent Performance Auditor serves as the Board of Directors oversight function. As such, the purpose of this Memo is to identify areas in Management's response to the investigation that are inconsistent with the SR 125 Investigation findings and which require further clarification or additional information from Management.

To assist the Board, OIPA developed **Questions** included in called out boxes below, for the Board to consider during its discussion of Management's response to the OIPA's SR 125 Investigation. Each key area begins with the **Question** called out and is followed by information provided in Management's response or referenced in the

SR 125 investigation.

Management's responses have also been reproduced within the document and the corresponding pages from Management's actual response can be found in Attachments A and B. **Attachment A** includes pages from Management's response, *Attachment 3 - Project History* and **Attachment B** includes pages from Management's response, *Attachment 5 - Responses to Board Questions*.

AREAS OF MANAGEMENT'S RESPONSE THAT ARE INCONSISTENT WITH THE SR 125 INVESTIGATION

There are two attachments, as identified above, in Management's response that are inconsistent with the investigation's findings.

Management's responses in these attachments attempt to answer two key questions noted in the investigation: Why wasn't the Board made aware? and Why wasn't an RFP (request for proposals) prepared? However, their responses contradict themselves or are contrary to the investigation findings.

1

Management's response (Attachment A) states:

As noted above, at the Board meeting on April 22, 2022, the former CEO announced that SANDAG had retained the services of an industry expert (Fagan Consulting) in the prior month to conduct an operational risk assessment of the SR 125, and to provide guidance on improving tolling operations. One of Management's significant concerns at the time Fagan was retained was the fact that ETAN's contract contained an option to develop a back-office system for the future Otay Mesa East Port of Entry (OME) project; staff expressed concerns about exercising this option given ETAN's failure to deliver a fully operational system with all anticipated functions for the SR 125 and I-15 facilities.

As part of their risk assessment, Fagan was asked to provide a recommendation as to whether SANDAG should continue utilizing ETAN for the OME project or consider other vendors.

Fagan recommended that SANDAG continue the current contract with ETAN while procuring a new back-office system for the OME project, with a second future phase of that work to include a transition of the existing toll facilities to the same OME back-office system.

However, Fagan's recommendations are broader than the OME project. Fagan's SR 125 Toll Operational Risk Assessment report, Introduction section (Attachment C, page 1) states:

There are **four paths** forward for the SANDAG back office for I15, SR125, and Otay Mesa:

Fagan's report, Recommendations section (Attachment C, page 4), goes on to outline the pros and cons of each path and concludes:

We recommend SANDAG continue the current contract with ETAN while procuring a new back office. Continuing with ETAN is an interim step until you acquire and stand up a new back office system.

② Later, Management's response (Attachment A) further states:

"The work developing a RFQ (request for qualifications) for the Regional back office technical advisor began until it was determined that the delay in opening OME, a component of the system, provided additional time for Toll Operations to consider a vendor change because the ETAN contract was expiring."

Question 1

Did Management determine the back-office system would only need replacement if it was a part of the OME project? If not, why did the OME project dictate the procurement timeline and implementation for a new system?

The first three paragraphs below are consistent with Fagan's report recommendations. However, the last paragraph below indicates the OME project opening date was being used to establish the timeline for conducting the procurement and implementation of the replacement back-office system. As previously stated, Fagan's recommendations were broader than the OME project alone.

③ Management's response (Attachment B) states:

There have been ongoing challenges with implementation of the back-office system since before it was launched. At the same time, there was also a general expectation and assurances that ETAN would be able to resolve the issues to the extent needed to operate the system until another vendor could be identified.

The July 2022 report from Fagan Consulting, LLC (Fagan), a tolling-industry expert who had conducted an SR 125 Toll Operational Risk Assessment for SANDAG, confirmed this understanding. Fagan outlined four options for addressing Management's concerns about the ETAN Fastlane system, and

for achieving a back-office system for the existing I-15 and SR 125 facilities, and the soon-to-be constructed Otay Mesa East (OME) project.

After considering the pros and cons of the various options outlined by Fagan, the former CEO decided to pursue a parallel process which included 1) preparing for a procurement to select and implement a new regional back-office system, and 2) continuing the current contract with ETAN, focusing on fixing significant bugs and ensuring core functionality of the Fastlane system, but not attempting to achieve all requirements of the ETAN contract as “there is enough existing functionality in place to make this a feasible solution.”

Path 1: At the time, the former CEO had announced that the OME project was expected to open in September 2024. This established the timeline for conducting the procurement and implementation of the replacement back-office system. However, ongoing negotiations with our federal partners regarding the OME project continues to delay the finalization of the specifications of the OME back office.

Additionally, Fagan informed SANDAG (see slide below) that the RFP and system implementation takes 36 months. Based upon Fagan’s suggested timing, if the OME’s opening remained as 2024, the RFP would have needed to be initiated in 2021 and a procurement to replace ETAN’s BOS would have required immediate attention.

FAGAN’s June 23, 2022 briefing to SANDAG included the following slide:

INITIAL CONSIDERATIONS

- Begin to research alternative procurement options:
 - 1) Leverage other agencies back office. Sample questions:
 - Are they willing to consider processing SANDAG’s trips in their back office?
 - If yes, how and what would you charge for processing?
 - Would you have issues with SANDAG performing image review and posting fully formed rated trips to your back office?
 - What is your violation process?
 - What is the timeframe for transition completion?
 - 2) Streamline RFP Process to procure a new back office system
 - RFP and system implementation is usually 36 months
 - Phase 1: Core BO functionality including support for Otay Mesa plaza
 - Phase 2: Complete BO functionality, data migration and transition off ETAN BO

Question 2

What policies and procedures was Management following that prompted them to notify the Board in October 2023 of ETAN's inability to meet contractual requirements?

The investigation found ETAN was not able to produce required financial reports and was dependent upon workarounds and queries from the initiation of ETAN's SR 125 BOS through today.

④ Management's response (Attachment B) further states:

ETAN executives informed the SANDAG CFO and other SANDAG staff on August 25, 2023, that the Fastlane system would never be capable of producing the financial reports that had been specified in the project requirements. This admittance by ETAN prompted the CFO to immediately report the magnitude of the issue to the former CEO, and steps were initiated to advise the Board. A closed session item was held during the October 13, 2023, Board meeting regarding this matter.

Question 3

Why was the Board not notified immediately following the July 2022 CFO email to Ron Fagan, when the CFO implied that they would be? Further, why was a procurement not initiated at that time to replace ETAN?

The July 5, 2022 full email text from the CFO to FAGAN included in the investigation states:

Good morning Ron and Christine,

I know we are not to receive the final report until October, but after Hasan discussed your preliminary findings with the Executive Team last week, it was really determined that we need to move away from ETAN (in particular for the new OME Port of Entry, but also in time for SR-125 and I-15). So we need to take an item to our BOD sooner than later so that we can get the team moving in a direction to prepare a new tolling RFP or piggy back on someone else (i.e. BATA or TCA).

So can we carve out the portion of the report related to the viability/going concern of ETAN and get a preliminary report on that aspect this/next week. We would more than likely take these items in closed session to the Board, as we would need to keep this subject confidential for now for obvious reasons.

Thanks

SANDAG CFO

Question 4

Considering the procurement timeline of approximately 8 months to conduct an RFP/Q solicitation, as stated in Management’s sole source justification for Deloitte, why did Management not conduct an RFP/Q following the recommendation made by Fagan in July 2022? Why did Management wait until ETAN notified SANDAG of their inability to meet their contractual obligations?

Question 5

If Management was only researching products available to replace the current back-office system, why was Management inquiring about timelines for implementing such products? Isn’t this something that should have been conducted through a formal solicitation process, like an RFP/Q to determine the most suitable approach and service provider to meet SANDAG’s service needs?

Question 6


Considering that Management delayed taking action following Fagan’s recommendations and that the sole source justification requirements specify that a sole source procurement cannot be the result of failure or lack of planning, what alternative policy or process was followed to allow the sole source contract award to Deloitte?

5 Management’s response (Attachment B) further states:

When ETAN notified SANDAG that it would never be able to deliver a system to the specifications set forth in the contract in late August 2023, staff determined that a sole source would be necessary to mitigate the risk of continuing work with ETAN.

Through interviews and reviewing documentation, we found that in 2022 and 2023, SANDAG staff was acting with a sense of expediency given the concerns regarding ETAN’s viability, poor performance, and failure to deliver system requirements. This process included SANDAG speaking with Transportation Corridor Agencies (TCA) to see if they could immediately take over transaction processing if ETAN could no longer perform. This also included contacting potential vendors, scheduling software demos, and planning on-site visits to see actual “live” tolling systems.

As previously mentioned, Management was advised by Fagan in July 2022 to initiate a solicitation. In November 2022, a procurement had still not yet begun, and Fagan was advising the department director on alternatives to shorten the procurement process. The sole source justification form for Deloitte’s contract was dated October 31, 2023, 16 months after Fagan’s recommendations. The form provided the following instructions for completion, and the initial section was completed as follows by the department director:

	
Version 3.0	SOLE SOURCE JUSTIFICATION
<p><i>Contracting without providing for full and open competition is prohibited unless justified on one or more of the bases below. This form is required if Sole Source is selected as the Competition Type in the Solicitation or Contract record in CMS. Complete the form and attach to the CMS record by uploading as the Sole Source Justification Form. The form will be routed electronically as a CMS Business Review for review/approval by the appropriate Department Director and the Director and Legal Counsel of Contracts and Grants (DLC). By approving the transaction in CMS, the Department Director certifies that the information on this form is correct and approves of the justification used for this sole source.</i></p>	
THE FOLLOWING MUST BE ANSWERED AFFIRMATIVELY (CAN BE USED FOR ALL FUNDING SOURCES)	
By marking the boxes below, you are affirming that the following statements are true.	
<input checked="" type="checkbox"/>	The need for a sole source is not due to a failure to plan or a lack of advanced planning.
<input checked="" type="checkbox"/>	The need for a sole source is not due to concerns about the amount of federal assistance available to support the procurement (for example, expiration of federal assistance available for award).

Additionally, the sole source justification form for Deloitte’s contract included the following explanation provided by the department director:

SANDAG’s technical staff began researching other products available in the tolling industry that could replace the existing BOS on an expedited basis and determined that only 6 vendors had systems with the ability to meet the agency’s needs. Of those vendors, only Deloitte and A To Be had the ability to deliver a system within an acceptable time-frame; the remaining vendors would require several years of development before a new BOS would be operational, which would have left the region’s tolling facilities with the inability to process the collected tolls for several years. The vendors noted a best case would be 24 to 36 months, the amount of time we allotted for the current vendor, to get their systems up and ready to process the collected tolls.

Deloitte and A To Be will be able to deliver a new BOS in 7 months, rather than several years, so as to minimize disruptions to toll operations and

OTHER INFORMATION REQUESTS

There are areas in Management's response that include new or expanded information related to the investigation.

OIPA requested additional supporting documentation last week from Management to determine the accuracy of the statements presented below. Management provided the information on April 24, 2024 and the OIPA is in the process of reviewing it.

6

Management's response (Attachment B) states:

SANDAG has implemented a robust and thorough sampling process to confirm customer account balances to a 99% confidence level. Since early January 2024, staff have been analyzing, confirming, and resolving any discrepancies or anomalies in customer accounts to ensure they are accurate. This work is expected to be completed in July 2024.

During the June 2022 migration to the ETAN Fastlane system, the technology used to transfer customer account balances functioned as expected and the moment-in-time transfer from the old system was successful. Although it is an industry standard, moment-in-time approaches require review and correction of accounts that had transactions during the migration. The transfer period contained a three weeks lag where customer transactions weren't initially captured. Consequently, we made corrections to reflect the accurate activity in this period, ensuring the beginning account balances were updated to include all transactions that occurred during the migration process.

CORRECTION

7

Management's response (Attachment B) states:

There is documentation that shows the history of the 64/36 split between the SR-125 and I-15 which is updated on an annual basis based on the active FasTrak accounts on each roadway. There has been turnover in the Accounting Department and the accountant that was asked to provide the documentation was not aware of the split. Once the question was elevated to the Manager, the documentation was provided to OIPA.

However, the Finance manager stated the following directly to the OIPA:

"In regards to this, unfortunately no we have not been able to pull up any clear documentation of this, but we did sit down with people who were here during the transition and noted that the split was based on active Fastrak

accounts at the time the roadways were merged. Attached is a recalculation showing the percentages per year. “

CLARIFICATIONS FOR MANAGEMENT RELATED TO THE OIPA AND AUDIT COMMITTEE RECOMMENDATIONS

There were two recommendations that are broader in scope than reflected in Management’s response to OIPA. We are providing clarification so that Management may incorporate this information into future recommendation updates.

OIPA Recommendation 7:

We recommend SANDAG immediately implements daily monitoring to ensure all systems are operating and communicating with each other correctly.

Clarification: This recommendation refers to daily monitoring to ensure all systems are operating and communicating with each other correctly. This is monitoring of all tolling systems, not just between RSS and BOS.

Audit Committee Recommendation 3:

The Board should consider development of a policy for all multimillion-dollar projects that includes a timely reporting of the status of the project to the Board, whether or not errors or delays are identified.

Clarification: The Audit Committee’s recommendation, as provided above, is broader than the OIPA’s recommendation number 4.

NEXT STEPS:

QUESTIONS 1 - 6: The questions are included for the Board's consideration during its discussion of Management's response to the Office of the Independent Performance Auditor's SR 125 Investigation. Next steps will be determined by the OIPA, Board and Audit Committee.

INFORMATION REQUEST: The OIPA is reviewing information provided by Management on April 24, 2024, and will report any notable differences, or further information required to the Board, Audit Committee and Management.

trips beginning on June 1, 2022, putting ~~\$450 million~~ \$50 million of revenue at risk and jeopardizing the outstanding bonds on the 125 freeway. Staff noted that it would balance these competing risks by reducing the level of functionality in the back-office system for go-live only, and continue to monitor system reports and customer service issues to identify and mitigate any resulting impacts.

The ETAN system, known as Fastlane, went live for SR 125 on June 5, 2022. In the 'Combined Roadway/Back Office System Project Status Report,' dated June 27, 2022, staff note that "*We are identifying issues, which ETAN is addressing, as they continue to turn on new functions in the back office.*" The report also notes that ETAN was working to address reporting issues and SANDAG staff were meeting with ETAN every day to discuss progress.

2022 – April 2024

1

As noted above, at the Board meeting on April 22, 2022, the former CEO announced that SANDAG had retained the services of an industry expert (Fagan Consulting) in the prior month to conduct an operational risk assessment of the SR 125, and to provide guidance on improving tolling operations. One of Management's significant concerns at the time Fagan was retained was the fact that ETAN's contract contained an option to develop a back-office system for the future Otay Mesa East Port of Entry (OME) project; staff expressed concerns about exercising this option given ETAN's failure to deliver a fully operational system with all anticipated functions for the SR 125 and I-15 facilities.

As part of their risk assessment, Fagan was asked to provide a recommendation as to whether SANDAG should continue utilizing ETAN for the OME project or consider other vendors. Fagan's report, included as Attachment 5, is notable in that it acknowledges that while certain features/requirements had not yet been implemented, "*the back-office system is installed and operating at SANDAG with no significant issues to date.*" Fagan recommended that SANDAG continue the current contract with ETAN while procuring a new back-office system for the OME project, with a second future phase of that work to include a transition of the existing toll facilities to the same OME back-office system.

Fagan's assessment, which also reflected SANDAG's concerns about ETAN's resourcing, also recommends that SANDAG not attempt to achieve all requirements of the ETAN contract and focus on fixing significant bugs in the system, as "*there is enough existing functionality in place to make this a feasible solution.*" Fagan further cautioned SANDAG to tread lightly on the issue of withholding liquidated damages from ETAN, as a punitive approach could force ETAN to walk away from the project at any time leaving SANDAG without any effective means of collecting tolls on the SR 125.

2

As the OIPA Investigation Report notes, the Fagan report was shared with Senior Executive Management in July 2022. Consistent with the Fagan recommendations, Senior Executive Management also instructed toll operations staff to continue to work with ETAN to maintain system functionality. Also, in line with Fagan's assessment and recommendations, OME project staff were informed ETAN's system was not scalable to include the facility. The work developing a RFQ *for the Regional back office technical advisor began* until it was determined that the delay in opening OME, a component of the system, provided additional time for Toll Operations to consider a vendor change because the ETAN contract was expiring.

Serious System Failures Uncovered

SANDAG staff focused on working with ETAN to identify and fix bugs in the Fastlane system. As the OIPA Investigation Report acknowledges, the volume of work tickets began to build after the implementation of SR 125 in June of 2022. These issues came to a head in Spring 2023 when SANDAG's Accounting and Finance staff began preparing year-end financial statements for the annual audit and identified issues regarding the accuracy of deferred revenue and accounts receivable. When pushed to resolve these errors on a priority basis, ETAN was unable to identify a solution and, in August

financial reports from November 2020 through 2021; thus, staff used some of the reliable reports from Fastlane and other source documents for financial reporting while ETAN was continuing to fix bugs.

In a May 2022 project report, staff noted that they had reservations regarding unproven elements of the ETAN system so close to "going live." However, staff also recognized that further delays to launch would impact the ability of Kapsch to complete the replacement of the legacy roadside equipment on SR-125 (which could result in revenue losses if the old equipment continued to fail) and beginning December 2022, the legacy system could no longer be certified to transmit or store credit card information resulting in SANDAG losing the ability to process credit cards transactions. This would lead to a potential loss of \$50 million in tolling revenue per year. Eventually SANDAG would not have sufficient funds to make principal and interest payments on the bonds and would trigger a payment default. The Agency would most likely lose its AAA rating making future borrowings much more expensive for other SANDAG projects.

Countering this was the fact that ETAN had provided the critical elements needed for the system to function; such as the ability to set up accounts, hold deposits, process payments, send out notices/correspondence/statements, track transactions, interface with banks, track inventory, etc.

Ultimately, staff concluded that they would balance these competing risks by reducing the level of functionality in the back-office system for go-live only, and continue to monitor system reports and customer service issues to identify and mitigate any resulting impacts going forward.

4. What happened between July 2022 and October 2023? Why wasn't the Board made aware and why wasn't an RFP prepared?

3 There have been ongoing challenges with implementation of the back-office system since before it was launched. At the same time, there was also a general expectation and assurances that ETAN would be able to resolve the issues to the extent needed to operate the system until another vendor could be identified.

The July 2022 report from Fagan Consulting, LLC (Fagan), a tolling-industry expert who had conducted an SR 125 Toll Operational Risk Assessment for SANDAG, confirmed this understanding. Fagan outlined four options for addressing Management's concerns about the ETAN Fastlane system, and for achieving a back-office system for the existing I-15 and SR 125 facilities, and the soon-to-be constructed Otay Mesa East (OME) project.

After considering the pros and cons of the various options outlined by Fagan, the former CEO decided to pursue a parallel process which included 1) preparing for a procurement to select and implement a new regional back-office system, and 2) continuing the current contract with ETAN, focusing on fixing significant bugs and ensuring core functionality of the Fastlane system, but not attempting to achieve all requirements of the ETAN contract as "*there is enough existing functionality in place to make this a feasible solution.*"

Path 1: At the time, the former CEO had announced that the OME project was expected to open in September 2024. This established the timeline for conducting a procurement and implementation of the replacement back-office system. However, ongoing negotiations with our federal partners regarding the OME project continues to delay the finalization of the specifications of the OME back office. However, ongoing negotiations with our federal partners regarding the OME project continue to delay the finalization of the specifications of the OME back office.

Path 2: To hold ETAN accountable, SANDAG began to withhold payments (liquidated damages) from ETAN in July 2022 due to the delay of delivery of the back-office system. A new Director of Regional Transportation Services was also hired to oversee the ongoing implementation and acceptance of the new system. The Director established project goals and expectations for consultant performance, and in

2023, started exploring options for contracting with another California Toll Operators Committee (CTOC) vendor to assume operations.

SANDAG staff worked diligently and in good faith with ETAN for an extended period of time to achieve the expected system functionality. In the months following go-live of Fastlane in June 2022, Accounting and Finance staff, and other project team members, continued to meet with ETAN on a regular basis to discuss and address functional issues that were preventing them from obtaining data necessary for periodic reconciliations and other accounting functions. There were also monthly project status meetings between SANDAG Management, SANDAG staff, and HNTB representatives. At ETAN's continued assurance, staff trusted that the system issues would eventually be resolved.

In early July 2023, SANDAG staff began to express serious doubts about ETAN's ability to produce the necessary financial reports and were concerned about upcoming FY 2023 year-end reporting activities. SANDAG's Chief Financial Officer (CFO) intervened and immediately instructed ETAN to prioritize the financial reporting components of the Fastlane system. ETAN responded by assigning additional resources to the project. As part of this response, a lead accountant from ETAN worked onsite at SANDAG for three days in late July 2023, side-by-side with Accounting and Finance staff, to fully understand the issues and requirements. In addition, a senior-level certified public accountant from HNTB who had also been the CFO of SBX and had a unique depth of familiarity with SR125 financial operations and the Fastlane system issues, was asked to work exclusively on assisting and overseeing the accounting reconciliation work until it was complete¹.

4 Despite these additional resources and work efforts, ETAN was unable to resolve the programming errors in the Fastlane system. ETAN executives informed the SANDAG CFO and other SANDAG staff on August 25, 2023, that the Fastlane system would never be capable of producing the financial reports that had been specified in the project requirements. This admittance by ETAN prompted the CFO to immediately report the magnitude of the issue to the former CEO, and steps were initiated to advise the Board. A closed session item was held during the October 13, 2023, Board meeting regarding this matter.

5 When ETAN notified SANDAG that it would never be able to deliver a system to the specifications set forth in the contract in late August 2023, staff determined that a sole source would be necessary to mitigate the risk of continuing work with ETAN.

5. What is the status of customer accounts? Who is affected by the tolling software failures?

6 SANDAG has implemented a robust and thorough sampling process to confirm customer account balances to a 99% confidence level. Since early January 2024, staff have been analyzing, confirming, and resolving any discrepancies or anomalies in customer accounts to ensure they are accurate. This work is expected to be completed in July 2024.

During the June 2022 migration to the ETAN Fastlane system, the technology used to transfer customer account balances functioned as expected and the moment-in-time transfer from the old system was successful. Although it is an industry standard, moment-in-time approaches require review and correction of accounts that had transactions during the migration. The transfer period contained a three weeks lag where customer transactions weren't initially captured. Consequently, we made corrections to reflect the accurate activity in this period, ensuring the beginning account balances were updated to include all transactions that occurred during the migration process.

We are aware of isolated incidents of customers being mischarged, which we addressed as soon as we were made aware (i.e. the 100 transactions cited in the Investigation Report and December 8, 2023,

¹ Accounting and Finance staff performed FY 2022 year-end financial reporting activities using data from the prior legacy system; this explains the 12-month timeline between go-live and the determination of system failure.

2022 Notification

The SANDAG PM was notified by email on July 20, 2022, that HNTB had concerns about signing cover sheets included in the requests for payment/invoices submitted by ETAN due to ETAN's statement in the invoice submittal that all work reflected in the invoice had been completed to contractual specifications while HNTB and SANDAG had concerns about ETAN's performance. HNTB recommended adding an explanatory note to the invoice cover sheets to clarify that the authorization to invoice did not constitute approval of the milestones referenced in the invoice, and that SANDAG had approved the deferral of certain requirements to after go-live but before system acceptance. Additionally, HNTB recommended that the cover sheet note the liquidated damages incurred to date.

HNTB's recommendations were shared by the PM with a SANDAG attorney and the SANDAG CFO. As a result, neither SANDAG nor HNTB signed the ETAN invoice. Instead, SANDAG stated its concerns about ETAN's performance on the work reflected in the invoice in a letter dated June 22, 2022, to ETAN, noting that because of ETAN's deficiencies SANDAG was withholding fifty percent of the invoiced amount as liquidated damages and reserving all rights to pursue additional amounts including additional liquidated damages, damages for breach of contract and damages for defective workmanship.

7. How was the 64/36 revenue split between SR 125 and I-15 determined?

7 There is documentation that shows the history of the 64/36 split between the SR-125 and I-15 which is updated on an annual basis based on the active FasTrak accounts on each roadway. There has been turnover in the Accounting Department and the accountant that was asked to provide the documentation was not aware of the split. Once the question was elevated to the Manager, the documentation was provided to OIPA.

8. Why was the DMV hold not operational?

The DMV hold process does not work in the ETAN Fastlane system. SANDAG continues to issue debt notices to violators and these amounts are being recorded in SANDAG's financials (Aging Report). If the debt goes unpaid by violators, SANDAG will send notices to the DMV in the future to assist in recovering payment. Once DMV accepts the violations for the hold, they are added to the car registration for that year. The hold will prevent customers from obtaining a valid registration unless all fines and fees are paid.

We have asked Deloitte/A to Be to provide options and related costs to expedite the DMV Hold functionality in the new system and will keep the Board updated. It is currently scheduled to be available in 2025.

9. Can we stop tolling on the SR 125? / Bond Situation?

SANDAG currently has \$167 million in Series A SANDAG South Bay Expressway Revenue Bonds. One of the legally binding covenants of those bonds is that SANDAG maintain at least 1.5 times debt service coverage ratio (DSCR); that is, at least \$1.50 in net toll revenues (after the payment of operating and maintenance costs) against \$1.00 in annual debt service. If SANDAG stops collecting tolls on the roadway, the agency would not be able to maintain its DSCR and would be in default on its bonds. Additionally, SANDAG eventually would not have sufficient funds to make principal and interest payments on the bonds and would trigger a payment default.

If SANDAG defaults on our bonds, the agency would be downgraded by the rating agencies (Fitch and S&P) and subject to lawsuit(s) from the Trustee on behalf of bondholders to exercise the rights and remedies available to them. A default event could also make future borrowings much more expensive.



Draft Report

Draft Report for the State Route – 125 (SR-125) Toll Operational Risk Assessment



Contract No: S1000973
Agency: SANDAG
401 B Street, Suite 800
San Diego, CA 92101
Date: July 7, 2022



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1. BACK OFFICE ALTERNATIVE CONSIDERATIONS AND OPTIONS

1.1 INTRODUCTION

SANDAG asked Fagan to conduct an operational risk assessment of their back office project with ETAN. The SANDAG staff is concerned about ETAN's ability to fully deliver the current system. Additionally, the Otay Mesa project is scheduled to open in two years. Given the issues encountered on the current project, the SANDAG staff has reservations that ETAN will deliver for Otay Mesa.

The Fagan team had discussions about the project with the SANDAG staff. We also reviewed project documentation extensively. After the workshop debrief, SANDAG tasked us with providing a report on their options with ETAN and recommendations. This document explores four options for moving forward with the SANDAG back office.

There are four paths forward for the SANDAG back office for I15, SR125, and Otay Mesa:

1. Continue with ETAN
2. Outsource all back office processing to an existing agency in the State of California
3. Acquire a new back office system while contracting with an existing back office provider in California in the interim
4. Continuing with ETAN as an interim solution until the new back office system is ready

In the following section, we discuss the pros and cons of each of these approaches.

1.2 CONTINUE WITH ETAN

Pro:

1. The back office system is installed and operating at SANDAG with no significant issues to date
2. Training was completed for SANDAG staff
3. SANDAG staff indicates ETAN is providing good operational support when needed

Con:

1. SANDAG staff indicates ETAN performance issues remain to be resolved
2. SANDAG staff acknowledges there are efficiency issues with some operational features of the ETAN system
3. Integration with the new Kapsch SR125 roadside system is not anticipated before December 2022
4. ETAN and SANDAG agreed to descope the delivered system to achieve an operational state
5. There is an extensive list of deferred features/requirements yet to implement
6. ETAN owes millions of dollars in LDs to SANDAG and another project
7. System delivery to SANDAG was significantly late
8. ETAN's other significant project is years behind schedule
9. ETAN required considerable support from SANDAG staff to test and bring their system online
10. ETAN software development staff is limited (possible single point of failure if that person leaves ETAN)
11. ETAN seemed to significantly under-estimate the actual development cost of the project, leaving them in a precarious financial position on this project
12. Based on a review of the project-level documents, it is not clear that ETAN knows how to manage a project of this magnitude
13. Much of the project and technical documentation is poorly written
14. ETAN has limited experience in this type of software development (i.e., only two (2) operational back office systems projects)

15. ETAN has been reluctant to commit to guaranteeing they will continue to work with SANDAG (either for the current project or for Otay Mesa)
16. It is uncertain if ETAN can deliver new development required for Otay Mesa on schedule
17. Toll system operations software is not a significant product line for ETAN
18. ETAN seriously misrepresented the amount of development needed to implement SANDAG's system (RFP compliance matrix indicated >90% of the SANDAG requirements existed in their baseline software, while SANDAG staff told us that > 90% new development was a more realistic assessment)

Continuing with ETAN for Otay Mesa and beyond creates significant uncertainties and carries significant risk. One of the most significant concerns is ETAN's viability in the toll industry. Further, based on our review of documents such as their Project Management Plan, Master Test Plan, and Disaster Recovery Plan ETAN lacks an understanding of project management and system engineering principles.

We know of at least two projects on which ETAN repeatedly failed to meet project milestones. It would be demanding for any integrator to work through existing deferred requirements while simultaneously preparing for and implementing Otay Mesa-specific requirements. ETAN appears to struggle with resources, decreasing the likelihood of a successful outcome. SANDAG's justifiable reluctance to pay ETAN any additional monies given the amount of the existing LDs owed may be the breaking point either for ETAN as a tolling company or ETAN's continued work with SANDAG. Continuing with ETAN for Otay Mesa, based on our experience, seems the riskiest of all options.

1.3 OUTSOURCE BACK OFFICE SYSTEM

Pro:

1. Immediate solution
2. Mature back office systems are available in California
3. All the specialized interfaces (e.g., print house, DMV, collection agencies, etc.) are already in place
4. Ensures the scheduled Otay Mesa opening occurs on time

Con:

1. Cost per trip unknown currently
2. Violation processing and escalation solutions may differ from SANDAG's preferred approach
3. SANDAG staff will need training on the outsource back office system
4. The back office will implement Otay Mesa-specific requirements, which will cost money and time
5. SANDAG and the partner agency would need to resolve the logistics of account management and the role of SANDAG staff
6. SANDAG prefers to have an in-house back office system
7. Outsourced entity would have to modify existing software to interface to Kapsch roadside systems, further raising costs
8. Need to work out the coordination of the ETAN transition

The cost for this option is unknown, both in any system software development and the transaction processing rates. Additionally, SANDAG would need to adjust some operational logistics, processes, and procedures to conform with the outsourced system solution. SANDAG expressed a desire to have its own back office. Moving solely to another agency's back office would not meet that objective. However, this option carries the least risk of successful completion.

1.4 ACQUIRE A NEW BACK OFFICE SYSTEM WITH AN INTERIM OUTSOURCED SYSTEM

Pro:

1. Opportunity to correct issues encountered in previous acquisition, including required features, timelines, project management, testing, etc.
2. Acquire a system (and an integrator) SANDAG can rely upon
3. Ensure the scheduled Otay Mesa opening occurs on time
4. The previous RFP identified Otay Mesa as an option, not a commitment
5. All the above Pros for an outsourced back office system

Con:

1. Additional acquisition costs may be significant
2. Costs for transitioning to an existing back office in the interim are sunk if SANDAG procures a back office later.
3. A revised (and expedited) RFP and procurement process would be required, including Otay Mesa specific requirements
4. May need to revise existing management and communication approaches to ensure the new project timelines are met
5. SANDAG staff will need training on the interim and the new back office
6. Need to work out the coordination of the ETAN transition
7. Need to assess ETAN's motivation to cooperate if SANDAG takes this path
8. Interim system provider may be reluctant to take on short-term work
9. The interim system provider may be unwilling to undertake any system software development for SANDAG
10. SANDAG may need to contract with Kapsch to adapt the output of the RSS to meet interim system interface requirements

SANDAG expressed a desire to have its own back office and this approach would achieve that goal. All funds spent on the interim back office will be sunk costs once SANDAG transitions to its new back office. The same unknowns exist concerning transaction processing costs, operational processes, logistics, and procedures. It is unclear whether any of the existing back office providers/agencies would be willing to work with SANDAG on such a short-term solution so this option might be unfeasible.

1.5 ACQUIRE A NEW BACK OFFICE SYSTEM CONTINUING WITH ETAN IN THE INTERIM

Pro:

1. Opportunity to correct issues encountered in previous acquisition, including a reduction in requirements, reduction in business rules, required features, timelines, project management, testing, etc.
2. Acquire a system (and an integrator) SANDAG can rely upon
3. Ensure the scheduled Otay Mesa opening occurs on time
4. All the above pros and cons for continuing with ETAN remain, but with a defined expiration date (i.e., Otay Mesa)

Con:

1. ETAN might cease supporting SANDAG once you make a vendor selection if it is not ETAN
2. Additional acquisition costs may be significant

3. SANDAG would need to use an expedited RFP and procurement process, including Otay Mesa specific requirements
4. Need to manage the new project to ensure the vendor meets the timelines
5. SANDAG staff will need training on the new system
6. Need to work out the coordination of the ETAN transition

SANDAG expressed a desire to have its own back office and this approach would achieve that goal. Mitigate timeline risks with careful planning to address how you will manage the new acquisition. A phased procurement could have the vendor deliver core functions for Otay Mesa online as Phase 1, with subsequent functionality in Phase 2. A significant plus is that SANDAG increases the chances of acquiring a system and an integration partner you can trust. Managing ETAN in the interim could be tricky; ETAN might walk away if they thought SANDAG would push them out eventually.

The LDs owed could cause ETAN to quit the project at any time. Contractors typically must report all terminated contracts going forward. No contractor wants that in their history as it would be the end of ETAN in the tolling industry. If ETAN foresees a long-term commitment to the toll industry, they will work out a solution with SANDAG. If ETAN does leave the project, SANDAG would need to keep the system running on its own until the new back office is ready. In either case, SANDAG should plan on minimal work with ETAN going forward, i.e., do not attempt to incorporate deferred requirements and only fixing significant bugs. This would be the lowest risk long-term solution if ETAN continues the project. Even if ETAN drops out, there is enough existing functionality in place to make this a feasible solution.

1.6 RECOMMENDATIONS

We recommend that SANDAG continue the current contract with ETAN while procuring a new back office. Continuing with ETAN is an interim step until you acquire and stand up a new back office system.

Do not authorize ETAN to fix anything beyond significant processing and customer-facing deficiencies. Do not attempt to incorporate the full set of remaining and deferred requirements. Remind ETAN that Otay Mesa was always an option in the contract and that SANDAG decided to issue a separate RFP for that project. The new procurement will incorporate lessons learned into a more efficient acquisition process. Advise ETAN that they may submit a proposal on the new procurement.

Rethink/revise the Otay Mesa BOS RFP to emphasize detailed, in-depth demonstrations showing actual system capabilities instead of brief written descriptions of how the system works. The RFP should have a focus on “show me” versus “tell me.” Develop a performance-based RFP that tells the proposer to what level the system must perform. We recommend not using a prescriptive RFP approach. Tell the vendors what you need and let them determine how best to deliver.

Finally, SANDAG may want to consider some concessions on liquidated damages. These may be enough to keep ETAN involved in the current project.