May 25, 2018

Dr. G.P. “Bud” Peterson
President
Office of the President
Georgia Institute of Technology

sent via email

Dear Dr. Peterson:

My office recently completed a review of the circumstances surrounding the expenditure of morale funds for use by Georgia Tech Research Institute (GTRI) employees. Two primary concerns came to our attention with respect to this review. For the purposes of this report, I will categorize these concerns as follows: 1) Organizational Culture and Governance, and, 2) Adherence to Policy. I have provided a set of recommendations for your consideration at the end of this report. As you know, GTRI has had financial irregularities in the past.

Background
GTRI earns funds primarily through research contracts. GTRI is comprised of Georgia Tech employees; however, GTRI administration processes the majority of GTRI financial and contracting activities through the Georgia Tech Applied Research Corporation (GTARC). GTARC is a cooperative organization of the Board of Regents and is managed on a day-to-day basis by Georgia Tech employees. GTRI will generally be used to refer to GTRI and GTARC activities except where it is relevant to distinguish between the two entities.

GTRI is authorized under Federal Acquisition Regulations (FAR 31.2) to charge a fee on research contracts. GTRI Policy 6160 Proposing, Accumulating, and Expending Fees provides an accurate and thorough background with respect to these fees. However, an overly simplistic explanation is that these fees represent an amount designed to cover costs not allowable under the FAR and might also be thought of as “profit” albeit GTARC is a not-for-profit organization.

GTRI has allocated these fees per GTRI Policy 6140 Promotional Funds for various purposes to include “employee morale, business development, research support, and recruitment of new employees.” As of April 2018, GTRI had accumulated $14.1M in federal government fees on revenue of $348.8M in Fiscal Year 2018 and $778k in private industry fees on revenue of $11M. GTRI’s own policy states that these fee expenditures “should be consistent with the image of Georgia Tech and not excessive, overly expensive, or inappropriate for a state university” (emphasis added).

Organizational Culture and Governance
Georgia Tech Internal Audit issued a Special Review of the GTRI Advanced Concepts Laboratory (ACL) on October 27, 2014 in response to various policy and criminal violations that ultimately resulted in federal indictments of former GTRI employees to include senior ACL staff. This report states in part:

However, these positive aspects of culture were not adequately reinforced by a commitment to follow established procedures and comply with GTRI and Institute requirements, and appear to have been utilized by several individuals whose intent was to manipulate the system for personal gain. In addition, employees charged with overseeing and enforcing these policies did not consistently feel “supported” when raising issues.

This does not suggest that GTRI executive management encouraged or were in any way complicit in the alleged malfeasance; however, the absence of the appropriate support, tone and messaging as related to compliance contributed to an environment in which various “red flags” for malfeasance were not adequately addressed.

Compounding the cultural issues is the separation between fiscal and compliance staff within GTRI versus the Institute as a whole. The Institute’s overall structure is designed to provide adequate independence for accounting and compliance, while ensuring consistency in procedures and providing for ongoing internal oversight and auditing. Going forward, it is recommended that GTRI’s “back office” functions and relevant assurance functions be incorporated within the Institute’s policies, procedures, and structure as opposed to operating in a quasi-independent manner.

Georgia Tech EVP for Research Dr. Steve Cross and Executive Vice President for Administration and Finance Steve Swant implemented several changes in response to this report on October 31, 2014. These include “joint reporting” of the GTRI Finance Director to the Georgia Tech SVP for Administration & Finance and “dual reporting” of the GTRI Ethics and Compliance Officer (ECO) to the GTRI Chief of Staff and to the Georgia Tech Vice President for Legal Affairs and Risk Management.

GTRI’s Ethics and Compliance Officer reported as noted until the elimination of the Chief of Staff position at which point the ECO reported to the GTRI Deputy Director for Finance & Research Administration. GTRI altered this structure on July 1, 2017 with the ECO now reporting to the GTRI Director of Talent Management. The ECO raised both personal and substantive concerns with this structure in a discussion with the GTRI Director. Georgia Tech’s Vice President for Human Resources also raised substantive concerns with this structure.¹ These concerns were noted some months after the GTRI reorganization as

¹ Georgia Tech’s HR Vice President wrote in an October 5, 2017 memorandum in part:

GTHR Recommendations: GTHR does not support GTRI Ethics and Compliance reporting to GTRI Talent Management Department (“TMD”).

a) The GTRI Ethics and Compliance group is responsible for monitoring and reviewing ethical violations within all GTRI departments and therefore should not have a direct reporting relationship and thus be solely accountable to any one department. Sole oversight by TMD in particular may substantially inhibit employees from raising ethics concerns that involve TMD, even tangentially. Specifically, it may inhibit the ability (or at least the perception of such) of Ethics and Compliance to conduct a full and fair review of leadership decisions that may involve TMD partners (in the scope of providing Human Resources advice, counsel, and transactional support).

b) Dual reporting (to TMD and possibly Legal Affairs and Risk Management) has been proposed as an alternative solution. This would, however, require Ethics and Compliance to remain accountable to TMD,
GTRI did not obtain Georgia Tech HR authorization prior to announcing the organizational change. GTRI’s Director did consult with the Georgia Tech Vice President for Legal Affairs and Risk Management but was not advised to either alter the structure or maintain as is – ultimately it was left to the GTRI Director’s discretion. GTRI’s director also obtained approval for the organizational change from his supervisor but was instructed to obtain the required approvals; no formal action was taken with respect to the GTRI Director’s failure to obtain Georgia Tech HR approval.

Interviews with multiple Georgia Tech and GTRI administrators and my own assessment as the individual charged with USG compliance and ethics is that this structural change was a mistake. Ethics and Compliance officers should report at a level where they can effectively discharge their responsibilities and are seen as having adequate scope and authority. While technically reporting to a direct report of the GTRI Director, the ECO did not perceive she had the necessary authority or access to raise significant issues or concerns within GTRI. These challenges were raised with GTRI leadership but were not effectively addressed.

Elements of organizational culture include the symbolic, e.g., relative placement on an organizational chart (or lack thereof), sitting on leadership committees, etc. all send messages as to the importance leadership places on certain activities. Given GTRI’s history, emphasizing the importance of ethics and compliance is that much more relevant. The changes made to the ECO’s reporting are both substantively and symbolically misaligned with the emphasis on ethics and compliance reflected in Board Policy 8.2.20 USG Ethics Policy and 7.16 Compliance Policy.

Another issue that arose during the course of our review that speaks to the ethical tone around compliance with Board Policy. Dr. Bo Rotolini was appointed Deputy Director, Finance, Operations & Information Systems on July 1, 2017. However, Dr. Rotolini’s spouse is employed within his division. This directly violates Board Policy 8.2.3. GTRI leadership and their chain of supervision was aware of this policy violation but nevertheless authorized the structural change resulting in this Board Policy violation. Equally concerning is the message this sends to the organization, i.e., Board Policy represents optional guidance which can be set aside if leadership deems necessary.

The net result of these organizational and cultural issues was that your office was not informed of the issues associated with morale expenditures until well after the issue had been raised, discussed, and seemingly dismissed internally. This lack of overall awareness likely also contributed to the initial Georgia Tech statement which implied support for the morale expenditures from both internal audit and GTRI Ethics and Compliance. Quite specifically, communications was not aware that both Georgia Tech internal audit and GTRI Ethics and Compliance had raised concerns about the expenditures in question. Finally, given the nature of the issues, there was insufficient, timely engagement with the system office.

### Adherence to Policy
GTRI’s policy on use of promotional funds states, in part:

particularly as this proposal does not include an actual managerial relationship between Ethics and Compliance and another department.

c) The committee recommends a more direct line of oversight by GTRI leadership into potential ethics complaints in addition to a dual reporting relationship. …
All expenditures should be consistent with the image of Georgia Tech and not excessive, overly expensive, or inappropriate for a state university. See Section 2.3 below. Any questions with regard to whether an expenditure is reasonable or appropriate should be addressed with the GTRI Director of Ethics and Compliance prior to incurring the expenditure.

The policy is reasonable on its face; however, multiple personnel with responsibility for implementing and/or interpreting policy were not aware of this statement. Also lacking was a context to determine whether “morale expenditures” were “inappropriate for a state university”. Additionally, the ECO’s review was generally limited to transactions already undertaken by GTRI management. The ECO did effectively prevent certain individual transactions. However, prior GTRI management had indicated (with respect to the ECO’s question about purchasing $48-50 shirts with a GTRI logo): “If this is how they choose to spend their employee morale budget, I think it’s appropriate.”

The ECO also raised concerns specifically regarding the Six Flags event with a Georgia Tech internal audit staff member. The Georgia Tech institutional chief auditor subsequently raised these concerns with GTRAC leadership and the Vice President for Legal Affairs and Risk Management. The Georgia Tech institutional chief auditor was not aware that the ECO had raised the concerns. Both GTRAC management and the Vice President for Legal Affairs and Risk Management reportedly opined that the transactions were within management’s judgment. The Georgia Tech institutional chief auditor reports on a day-to-day basis to the Vice President for Legal Affairs and Risk Management and did not raise the issue further. It appears that responsible, senior officials who were aware of the expenditures failed to accept responsibility for determining what was appropriate. Senior leaders all have a duty to exercise good judgment to protect the image and integrity of Georgia Tech.

A more complete analysis of GTRI’s adherence to its own policies should have resulted in direction to GTRI management to alter practices with respect to employee morale. Quite specifically, the USG Ethics Policy requires USG employees to “Act as good stewards of the resources and information entrusted to our care.” The USG Business Procedures Manual Section 19.7 and 19.8 specify instances in which institutional funds can be used to purchase food for employees. GTRI’s morale fund expenditures do not meet the BPM Standards; as such, they are “inappropriate for a state university.” For example, BPM 19.7.1 generally limits expenditures to state per diem limits.

One might argue that GTRI funds are held by GTRAC and are, therefore, not subject to these requirements. This is problematic for two reasons. First, GTRI’s own policy introduces the concept of ensuring expenditures are “consistent with the image of Georgia Tech and not excessive, overly expensive, or inappropriate for a state university.” Second, the funds “earned” by GTRI through its contracts largely represent taxpayer funds that would otherwise be paid directly to Georgia Tech in exchange for the research conducted by Georgia Tech employees, under the Georgia Tech name, and largely using Georgia Tech facilities.

There are sound business reasons for maintaining these funds within GTRAC so as to enable efficient and effective functioning of the GTRI; however, there is no legitimate institutional or state purpose in...

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2 In the interest of full disclosure, I previously supervised the Georgia Tech institutional chief auditor in my previous role of Vice Chancellor for Internal Audit. My supervisory responsibilities for internal audit ended December 2016.
maintaining these funds outside of Georgia Tech for the purpose of providing entertainment for employees and their families. It is conceivable that Georgia Tech may use donated, private dollars to support otherwise unallowable but objectively necessary expenditures in support of employee morale and team-building. However, authorization to use these funds presumably should be part of a consistent and modest program that is accessible across Georgia Tech (and not limited to certain centers or departments) and tied to specific human resources or management objectives.

Recommendations
I recommend the following immediate actions:

1) Integrate GTRI’s support functions (e.g., Finance, Operations & Information Systems and Talent Management) within Georgia Tech operations and organize support functions and reporting lines directly under the respective Georgia Tech division. This would significantly strengthen compliance operations going forward. GTRI’s Ethics and Compliance Officer also should be positioned outside of the GTRI management structure but may be assigned primarily responsibility for GTRI activities given the level of expertise required with respect to GTRI-specific requirements. Immediately address the nepotism issue associated with the Finance, Operations & Information Systems division noted previously in this report.

2) Alter the Georgia Tech institutional chief auditor’s reporting structure to be fully consistent with Board Policy, i.e., directly to the institutional president and the USG Vice Chancellor for Internal Audit. You may wish to delegate purely administrative tasks to the Chief of Staff or similar role, e.g., approving travel expense statements and purchase requests. However, performance evaluation and regular oversight should be provided directly by you and continue to be provided by the USG Vice Chancellor for Internal Audit. This will help to ensure that potential risks are raised with your office directly and timely so you can ensure your senior officials are handling matters appropriately and that the system office is properly engaged.

3) Substantively revise GTRI Policy 6140 Promotional Funds to ensure it is fully consistent with Georgia Tech and University System guidelines governing use of institutional funds.

4) Consider implementing an “ethics audit” or similar assessment, perhaps using external resources, to thoroughly assess the ethical tone across Georgia Tech and take the necessary steps to address any potential issues or findings raised during this process.

Thank you for your consideration of this report. Please advise if you have any questions or would like to discuss further.

Sincerely,

John M. Fuchko, III
Vice Chancellor for Organizational Effectiveness

JMF/
cc:  Dr. Steve Wrigley, Chancellor
    Regent Sachin Shailendra, Chair, Committee on Internal Audit, Risk, & Compliance
    Tricia Chastain, Executive Vice Chancellor for Administration
    Edward Tate, Vice Chancellor for Legal Affairs
    Wesley Horne, Director of Ethics & Compliance