

OVERVIEW

Procurement Audit of the Department of Education: Part 2

Report No. 09-04, February 2009

Summary

The Office of the Auditor and the certified public accounting firm of Grant Thornton LLP conducted a procurement audit of the Department of Education, State of Hawai'i, for the fiscal year July 1, 2006 to June 30, 2007. The audit examined the procurement process, policies, and transactions of the department and included inquiry, analytical procedures, and inspection of relevant records and documents to assess the department's compliance with state procurement laws and regulations.

The initial phase of our audit uncovered numerous reportable findings and deficiencies in the department's leadership and oversight related to its procurement process. We also identified a material weakness involving the department's lack of monitoring of internal controls over compliance with procurement requirements. These results are presented in Report No. 09-03, *Procurement Audit of the Department of Education: Part 1*.

Given the high volume of violations and the identification of several risk factors and fraud indicators in the initial phase of work, we were compelled to expand the scope of our audit. As part of our expanded work, we reviewed department emails and detailed project files to better understand the decisions made and actions taken with respect to select contracts. We also interviewed numerous department employees to gain further insight into the specific facts and circumstances surrounding each contract. The results of the additional work performed are presented in this second report.

The second phase of our audit revealed an organizational culture of disregard for procurement rules in the Office of School Facilities and Support Services (formerly known as the Office of Business Services and referred to herein as the "Office of School Facilities"). That culture has allowed office directors, managers, and staff to believe they have the discretion to unilaterally determine whether compliance with procurement laws and rules is in the best interest of the department.

We encountered numerous instances of department personnel manipulating the professional services selection process and awarding contracts to predetermined consultants. For instance, for a \$300,000 construction management project selection, the Project Control Section head bypassed established procedures by hand-picking the selection committee members and recommending a specific firm. The public works administrator then led the committee as its chair, documented the results selecting the recommended firm, addressed the results to himself as public works administrator, and approved the results on behalf of the branch.



We discovered several other alarming practices within the Office of School Facilities that appeared to be fraudulent and unethical. In one example, a high-ranking department official instructed a consultant to hire a specific sub-consultant in exchange for additional contract funding, thereby evading the competitive procurement process. The sub-consultant, who has close ties with the department, performed work under a department program that was unrelated to the contract's scope. Another inappropriate action involved selection committee members agreeing via email to change a prior selection decision to award the project to a vendor who was previously unranked, but had been improperly allowed to begin work on the project. The committee then falsified the selection documents to reflect the modified decision as the original selection.

The Office of School Facilities' regular outsourcing of large-dollar program and construction management contracts appears to be inefficient and wasteful. A key example is the most recent phase of the department's Whole School Classroom Renovation Program, which was appropriated \$160 million in 2006 to renovate 96 schools. The department has executed four management contracts totaling \$20,964,000 to oversee and manage the \$160 million. The management contracts outsource basic management functions that should be performed in-house, including responsibility for overseeing, evaluating, and negotiating with other vendors. On top of the inherent conflicts of interest, the poorly planned and structured contracts also lacked competition and had the potential for abuse. For example, a project management consultant assisted the department in procuring these significant management contracts while simultaneously competing for some of the work, and ultimately was awarded a related \$2.4 million program management contract.

The inappropriate procurement practices and culture of disregard in the Office of School Facilities are the indirect result of the lax tone from department leadership and the resulting weak environment, discussed in detail in the first report. In addition, the assistant superintendent of the Office of School Facilities perpetuates the culture by demonstrating to his staff that compliance with procurement rules is secondary to getting the job done.

Recommendations and Response

In addition to the recommendations to improve the department's leadership and oversight of its procurement process, we recommended that the department conduct detailed investigations into the specific procurement violations, and the outsourcing of program and construction management services, cited in this report and take appropriate and visible action.

The department generally welcomed our recommendations, described steps already taken to address some of our findings, and expressed its commitment to adopting procurement best practices.

Marion M. Higa
State Auditor
State of Hawai'i

Office of the Auditor
465 South King Street, Room 500
Honolulu, Hawai'i 96813
(808) 587-0800
FAX (808) 587-0830