

OVERVIEW

Investigation of Specific Issues of the Department of Business, Economic Development & Tourism

Report No. 10-01, January 2010

Summary

Prompted by concerns over the management of federal grant funds and the State's 2005 trade mission to China and Korea, the Legislature requested the Office of the Auditor investigate the Department of Business, Economic Development & Tourism, including the department's Out-of-State Offices. Although we initially attempted to track the reallocation of \$50,000 appropriated for Community-Based Economic Development (CBED), the attempt proved futile as the moneys were not restricted to specific program use. In tracking CBED monetary transfers into the Chinese office bank accounts, however, we noted the existence of federal funds related to the federal Market Development Cooperator Program (MDCP) under the International Trade Administration of the U.S. Department of Commerce. We found certain aspects of the Out-of-State Offices merited closer examination and refocused the scope of the investigation. Also in accordance with our standard procedures, we reviewed departmental comments on our draft report. As part of the process, we re-visited areas in the draft with which the department disagreed and made adjustments in the final report as merited by our investigation.

During 2003-2004, the department requested approval from the director of finance, the governor, and the Legislature to spend funds from a \$399,500 award it received from the federal Market Development Cooperator Program (MDCP). Our investigation found that the department failed to fully disclose to the director of finance and to lawmakers that the MDCP was a reimbursement program. The department did not make clear that it would use general funds to obtain the reimbursement moneys and that the reimbursements would be under no federal spending requirements or restrictions. In essence, the department would get to keep and spend the reimbursement funds at its discretion.

Our investigation found the department has spent tens of thousands of dollars in reimbursement funds to support the operations of its out-of-state office in Beijing and to cover budget cuts to its overseas offices. This non-disclosure to key decision makers of the impact the reimbursements would have on the department's general fund expenditures tainted the approval process and enabled the department to essentially pad its general fund appropriation. We found no documentation that shows the department provided to lawmakers a clear and accurate characterization of the program that enabled the department to spend the reimbursement funds as it saw fit.

In addition, our review of financial records from the Out-of-State Offices also found a deposit of \$35,000 of private funds into the Taipei office's bank account. The transfer of private funds directly into the office's account jeopardized its non-profit status and threatened its ability to function as a government office.



Moreover, our investigation found that the transferred funds were money solicited by the department from private companies to sponsor the 2005 mission and that the transfer was requested by the department.

We also found that the department provided incomplete or misleading information to the State Procurement Office which enabled the department to expend mission funds outside the procurement code with no restrictions and without any effective internal controls. We found the department withheld from state lawmakers fiscal records associated with the mission and provided incomplete and misleading information to state agencies about the mission model.

Finally, we found that ineffective oversight of expenditures and reporting requirements of the Out-of-State Offices created opportunities for fraud and abuse. We found that the invoices and receipts used to verify expenditures by the Beijing office are primarily in Chinese and often have vague or illegible English descriptions or no descriptions at all, contrary to department requirements. Department officials who review these documents admitted they could not read Chinese, were unable to independently verify the information, and simply “trust” or “assume” that the invoices and receipts are legitimate and justified.

Recommendations and Response

We recommend the department halt all activity regarding its MDCP reimbursement funds and consult with the Legislature and the Department of Budget and Finance as to the appropriate course of action. We also recommend the State Procurement Office request records from the Pacific and Asian Affairs Council related to the 2005 mission and contact key stakeholders involved in the planning and implementation of the mission to determine whether its prior opinions regarding the mission were tainted and procurement laws were circumvented.

In its written response, the department asserted the issues addressed in the report regarding the 2005 mission had been thoroughly reviewed by the Legislature and that two state agencies ruled no procurement or criminal law violations had occurred. However, as noted in our report, the conclusions reached by the Legislature and the state agencies that reviewed the 2005 mission were based on incomplete, misleading, or erroneous information provided by the department. Therefore, the issues merit further review. The department also noted that the transfer of private funds into its Taipei office was in error but contended that the action did not adversely affect the office’s operations. The department added that the report provides no substantiated finding of actual abuse or impropriety regarding its Out-of-State Offices. The department misses our point. Our report addresses the lack of effective internal controls regarding the Out-of-State Offices and the need to mitigate that risk.

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