
**Procurement Audit of the
Department of Business,
Economic Development and
Tourism**

A Report to the
Governor
and the
Legislature of
the State of
Hawaii

Report No. 97-12
October 1997

THE AUDITOR
STATE OF HAWAII

Procurement Audit of the Department of Business, Economic Development and Tourism

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the State of
Hawaii

Submitted by

THE AUDITOR
STATE OF HAWAII

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Foreword

This is a report of our procurement audit of the Department of Business, Economic Development and Tourism. The audit was conducted pursuant to Section 23-4, Hawaii Revised Statutes (HRS), which requires the Auditor to conduct postaudits of the transactions, accounts, programs, and performance of all departments, offices, and agencies of the State and its political subdivisions, and Chapter 103D, HRS, which requires the Auditor to periodically audit procurement practices within government to ensure compliance with the Hawaii Public Procurement Code and all applicable rules.

We wish to express our appreciation for the cooperation and assistance extended to us by the officials and staff of the Department of Business, Economic Development and Tourism.

Marion M. Higa
State Auditor

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Chapter 1

Introduction

This audit was performed pursuant to Section 23-4, Hawaii Revised Statutes (HRS), which requires the Auditor to conduct postaudits of the transactions, accounts, programs, and performance of all state and county agencies, and Chapter 103D, HRS, which requires the Auditor to periodically audit procurement practices within government to ensure compliance with the Hawaii Public Procurement Code and all applicable rules.

The Auditor initiated this procurement audit of the Department of Business, Economic Development and Tourism (DBEDT) because of concerns over the significant amount of the department's expenditure of general funds for service contracts. In our previous 1995 *Audit of Contract Administration and the Office of Space Industry in the Department of Business, Economic Development and Tourism*, Report No. 95-3, we found that the department entered into contracts without rigorous analysis of the need for contracting or identification of the intended benefits to the State. We also found that the department did not protect the interests of the State in administering contracts, paid contractors before any work was performed, allowed work to be done before the contract was executed, and allowed informal changes to the contract. Additionally, we found that the department did not adequately monitor contracts and reimbursed contractors for questionable costs or paid for work that was not performed.

Background on the Department of Business, Economic Development and Tourism

In 1963, the Legislature established the Department of Planning and Economic Development, now called the Department of Business, Economic Development and Tourism. The department's mission is "to support business, create jobs, and improve Hawaii's standard of living through diversifying the economy, expanding existing business, and attracting new economic activity." To accomplish this mission, the department engages in business support, investment attraction, product marketing, and loan activities.

In 1995, the department reorganized and consolidated its operations into four divisions: 1) Business Development; 2) Energy, Resources and Technology; 3) Research and Economic Analysis; and 4) Foreign-Trade Zone.

The **Business Development Division** helps new entrepreneurs, expands existing companies, and attracts jobs and capital to the state. It supports the formation and operation of small businesses in areas of licensing,

registration, and access to government markets. It promotes economic recovery in rural and distressed areas. The division serves as a business advocate within the executive branch and attracts new businesses and investment to the islands. It also promotes export opportunities for Hawaii products and services in Asia-Pacific markets.

The **Energy, Resources and Technology Division** supports statewide economic development and diversification by promoting Hawaii-based industries which engage in technological enterprises for the sustainable development of Hawaii's technology, energy, environment, and ocean resources.

The **Research and Economic Analysis Division** provides analysis and recommendations on economic and business issues, collects and catalogues data, and disseminates information.

The **Foreign-Trade Zone Division** encourages the expansion of international trade and the concomitant expansion of the commercial and economic base of Hawaii by providing a range of services to assist business and government agencies involved in international trade.

In addition to the four divisions, five offices support the department's operations. They are as follows:

- The Hawaii Tourism Office formulates long-range policy, advises the private sector on tourism-related activities, conducts research, establishes public informational programs, monitors complaints, and develops and implements the State's tourism marketing and promotion plan.
- The Honolulu Waterfront Project ensures that a long-range vision for the Honolulu waterfront is articulated and responsive to the current and future needs of residents.
- The Communications and Publications Office provides public information on state business and economic development and diversification initiatives.
- The Administrative Services Office (ASO) oversees the department's budget, contracts, personnel, property management, risk management, and other administrative matters.
- The Office of Planning assists the governor and the director of DBEDT in maintaining an overall framework to guide the development of the state through a continuous process of comprehensive, long-range, and strategic planning.

Seven agencies are attached to the department for administrative purposes. They include the Aloha Tower Development Corporation, Convention Center Authority, Hawaii Community Development Authority, Hawaii Strategic Development Corporation, High Technology Development Corporation, Land Use Commission, and Natural Energy Laboratory of Hawaii Authority.

Objectives of the Audit

The objectives of the audit were to:

1. Determine whether the department's purchases of goods and services comply with the provisions of the Hawaii Public Procurement Code.
2. Determine whether the department's contract administration process ensures the efficient and effective use of state resources.
3. Make recommendations as appropriate.

Scope and Methodology

This audit focused on purchases from July 1994 to May 1997. We sampled purchases from the four divisions and four offices of the department. We did not review purchases of the administratively attached agencies or the contracts with the Hawaii Visitors and Convention Bureau.

We selected a sample of the department's purchases of goods and services and tested them for compliance with the provisions of the Hawaii Public Procurement Code and related administrative rules. We performed specific tests to determine compliance with the provisions governing small purchases and purchases of \$10,000 or more. We examined purchases made through competitive sealed bids, competitive sealed proposals, emergency, and sole source methods. We also examined the department's purchase of professional services.

We also selected 20 contracts using a judgmental sampling method. Our sample represented about 54 percent of the total dollar value of departmental contracts. The sample was tested to determine whether the department performed adequate analyses to determine the need for contracting, developed scopes of services that were sufficiently specific to ensure expected outcomes and benefits, and developed clearly defined monitoring and evaluation procedures.

Exhibit 1.1 shows the expenditures and encumbrances for those divisions and offices covered within the scope of our audit from FY1993-94 through FY1995-96. The total amounts have declined substantially over the past three years—from \$24.0 million to \$11.7 million.

Exhibit 1.1
Operating Expenditures and Encumbrances
FY1993-94 to FY1995-96

Division/Office	FY1993-94	FY1994-95	FY1995-96
Business Development Division	\$ 11,103,884	\$ 7,661,132	\$ 5,124,944
Energy, Resources and Technology Division	1,218,065	937,986	730,772
Research and Economic Analysis Division	614,430	590,529	519,111
Foreign-Trade Zone Division	1,501,513	1,298,247	1,461,661
Hawaii Tourism Office*	6,778,694	5,955,273	1,642,452
Communications and Publications Office	970,818	892,615	808,523
Administrative Services Office (Includes the Office of the Director)	<u>1,813,640</u>	<u>1,694,120</u>	<u>1,395,458</u>
Total	<u>\$ 24,001,044</u>	<u>\$ 19,029,902</u>	<u>\$ 11,682,921</u>

*Excludes contract with Hawaii Visitors and Convention Bureau.

Source: DBEDT fiscal office; includes only division/office within audit scope.

We interviewed department management and representative officials of the affected divisions and offices. We also reviewed relevant laws, available policies and procedures, and previous audits.

We followed up on significant findings and recommendations from our 1995 *Audit of Contract Administration and the Office of Space Industry in the Department of Business, Economic Development and Tourism*, Report No. 95-3, that affected our current audit objectives.

Our work was performed from December 1996 to May 1997 in accordance with generally accepted government auditing standards.

Chapter 2

Manuals and Improvement in Contract Administration Needed

The Hawaii Public Procurement Code (codified as Chapter 103D, Hawaii Revised Statutes), was enacted to ensure fiscal integrity, responsibility, and efficiency in the procurement process. In this chapter, we assess the Department of Business, Economic Development and Tourism's (DBEDT) compliance with the code. We also assess the efficiency and effectiveness of the department's contract administration process.

Summary of Findings

1. The centralized procurement process of the Department of Business, Economic Development and Tourism fosters a high degree of compliance with the provisions of the Hawaii Public Procurement Code. However, compliance is jeopardized by the lack of a detailed procurement manual.
2. Although the department has made progress in planning for and drafting contracts since our 1995 audit, improvement in the department's monitoring and evaluation of contracts is still needed.

DBEDT'S Centralized Procurement Environment Promotes Compliance with the Procurement Code but a Procurement Manual Is Needed

The final approval of all procurement, as well as oversight for compliance with Chapter 103D, HRS, is highly centralized. This centralization of oversight responsibility has resulted in a high level of compliance with the provisions of the Hawaii Public Procurement Code. However, the lack of a detailed procurement manual puts this level of compliance at risk.

Centralized review and approval authority enhances compliance with procurement rules

The contract specialist and fiscal officer within the Administrative Services Office (ASO) have oversight responsibility over department compliance with the Hawaii Public Procurement Code.

To initiate a request for contract services, a division or office submits a “Request for Project Proposal” to the ASO’s contract specialist. The request outlines the objectives, goals, justification, description, and measures of effectiveness of the proposed project. The division or office also sends a request for the governor’s approval, and, if appropriate, a request for sole source procurement.

The contract specialist reviews each request for adherence with the mission of the department and for compliance with the provisions of Chapter 103D, HRS. The contract specialist may then forward the request to the director with a recommendation for approval or deny the request and return it to the division or office.

If the request is approved by the director, the contract specialist oversees all steps of the procurement process to ensure compliance with Chapter 103D, HRS. The contract specialist also develops forms for the division or office to monitor and evaluate the contractor’s services. The contract specialist periodically audits the contract administration of the division or office to ensure compliance with proper monitoring and evaluation procedures.

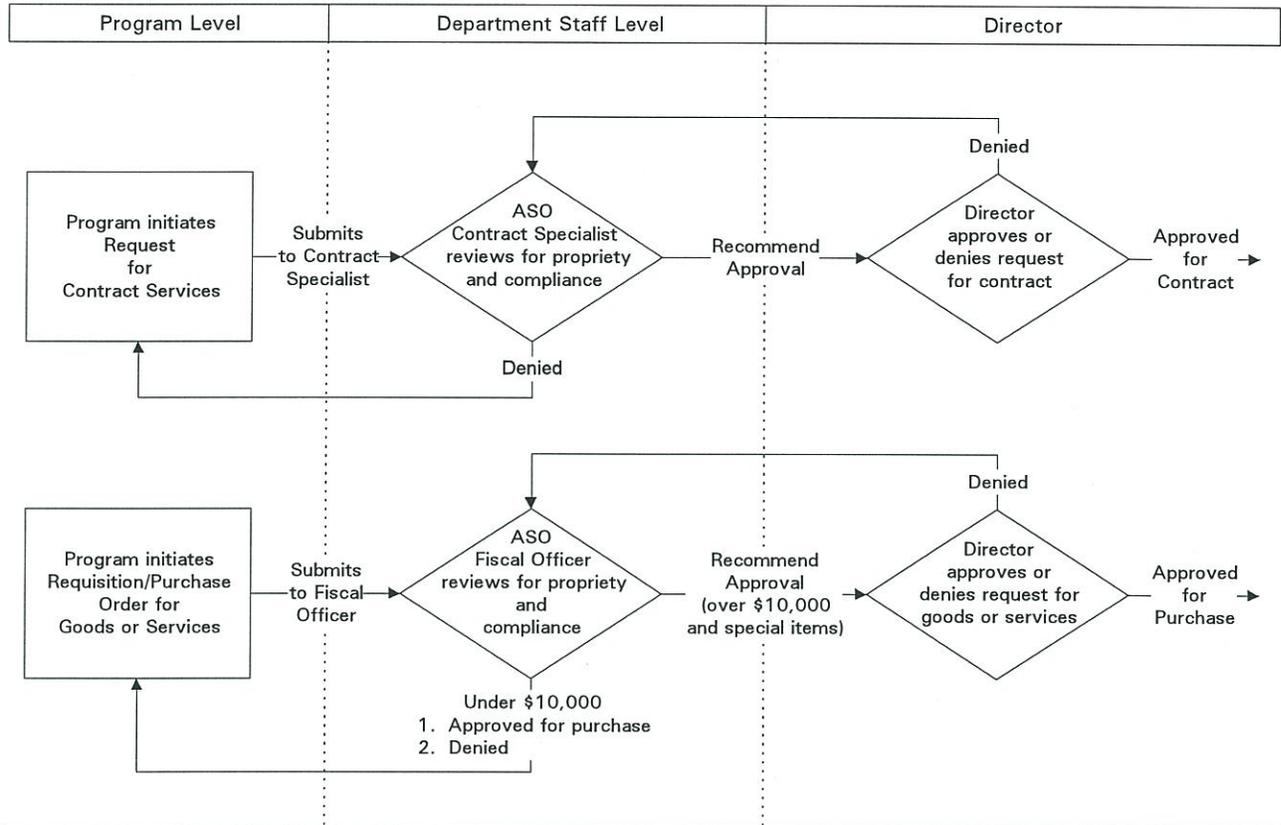
For purchases not requiring a formal contract, a requisition/purchase order is completed and must be approved by the division/office head or a designee. The purchase order and any supporting documents are then sent to the ASO’s fiscal officer. The fiscal officer reviews the purchase order and documents to ensure compliance with the Hawaii Public Procurement Code and all applicable policies and rules. The purchase order may be denied and returned to the division or office for correction and reprocessing. The fiscal officer approves the purchase order when all requirements have been met. The fiscal officer retains a copy of the purchase order and returns the remaining copies to the requisitioner who then initiates the purchase.

For purchases of \$10,000 or more, or for travel and equipment purchases, the purchase order is sent back to the requisitioner after it has been reviewed by the fiscal officer and approved by the director.

Exhibit 2.1 illustrates the functions within the department for purchase approval and compliance oversight.

The department has made serious efforts to improve its contracting practices over the past two years. Also, the contract specialist has tried to enforce strict compliance with the Hawaii Public Procurement Code by working closely with the State Procurement Office and the fiscal officer.

Exhibit 2.1
Departmental Review Process for Contract Services and Goods and Services



Testing reveals general compliance with procurement rules

We sampled purchase orders and contracts from four divisions and four offices and tested for compliance with various aspects of the Hawaii Public Procurement Code. We found that the department, with a few exceptions, was in general compliance with the code.

The code and the administrative rules adopted by the Procurement Policy Office establish different compliance requirements for the purchase of goods or services based on the size of the purchase. Purchases under \$10,000 are termed “small purchases” by the code. For purchases of \$10,000 or more, further distinctions in compliance requirements are made depending on whether the purchase is made through competitive sealed bids, competitive sealed proposals, sole source procurement, emergency procurement, or a procurement of professional services. For construction work, expenditures of less than \$25,000 are considered small purchases. Our tests for compliance took these differences into account.

Certain purchases are exempt from the code by virtue of statute, administrative rule, or approval of a chief procurement officer. The code also provides that most compliance aspects are automatically met if a purchase is made from a state price list. A price list is an indefinite quantity contract that provides for fixed prices of goods and services over a specific period of time. Twenty-two of the initial 52 purchases we sampled were exempt from the procurement code or on the state price list.

Exceptions noted in compliance with small purchase requirements

For small purchases, three quotes must be solicited from vendors and be recorded and placed in a procurement file. The most advantageous quote is selected based on various factors such as quality, warranty, deliverability, and price. If the quote selected is not the lowest of those submitted, a written justification must be placed in the file. If it is not practical to solicit three quotes, the reason must be recorded and placed in the file. Furthermore, the rules state that small purchases shall not be parceled by dividing the purchase of same, like, or related items of goods or services so as to evade the statutory competitive bidding requirements.

In our initial sample of 27 small purchases, we found two instances of non-compliance with the provisions of the Hawaii Public Procurement Code. The department purchased shipping services for \$3,273 without soliciting the required three quotes and did not provide a reason. In the second case, the department used a state price list to circumvent proper small purchase procedures. The department purchased a computer system from a state price list but spent an additional \$1,580 to upgrade the monitor. The department should have sought approval from the State Procurement Office and followed small purchase procedures to upgrade the monitor because it was outside the price list.

To determine whether these two instances of non-compliance were isolated cases, or evidence of a larger trend, an additional sample of purchase orders was reviewed. This sample produced one more instance of non-compliance where the department made a small purchase without soliciting three quotes. Based on both samples, we concluded that instances of non-compliance were isolated and rare.

Competitive sealed bidding requirements were observed

We tested the following requirements governing competitive sealed bids: (1) negotiations with bidders are prohibited after the receipt and opening of bids, (2) proper public notice of invitation for bids must be given, (3) bidder information must be witnessed and recorded at the time of the bid opening, and (4) the award is made to the lowest bidder whose bid met the requirements and criteria set forth in the invitation for bids.

The department was in general compliance with the tested requirements of competitive sealed bids, with one exception. The department classified an \$11,650 repair of a building's air conditioning system as construction and did not solicit bids. Department officials reasoned that this major repair constituted construction and was therefore considered a small purchase under the \$25,000 ceiling. However, we questioned whether this repair actually constituted construction. The object code used by the department on the purchase order classified the repair as "repairs and maintenance" rather than as a "fixed asset." It is reasonable to assume that all construction costs be capitalized, that is, added to the fixed asset records. Since it was not capitalized, we question whether this repair was truly construction. If it were not construction, then the expenditure exceeded the \$10,000 limit set for small purchases of goods and services and should have been subject to bid.

DBEDT complied with competitive sealed proposal requirements

Contracting through competitive sealed proposals is permitted if the head of a purchasing agency determines in writing that this method is more appropriate than competitive sealed bidding because bidding is either not practicable or not advantageous to the State. A request for competitive sealed proposals must receive proper public notice and a register of proposals must be maintained. Proposals are ranked by a formal evaluation process. The contract is awarded to the responsive, responsible offeror whose proposal is determined in writing to be the most advantageous to the State.

We assessed several proposals and the reasons given to contract through competitive sealed proposals rather than competitive sealed bidding. We compared the given reasons with those approved by Hawaii Administrative Rule 3-122-43 and found no conflicts. Department documentation showed that proper public notices of requests for proposals were given and that registers of proposals were maintained. An examination of the formal evaluation processes also showed that the contracts were awarded to the offerors whose proposals were ranked as the most advantageous. We found the department has complied with the provisions governing competitive sealed proposals.

The department complied with sole source procurement requirements

A sole source purchase may be made when there is only one available source from which a particular good or service may be obtained. Using a State Procurement Office form called a "Request For Sole Source," the heads of purchasing agencies must certify to the best of their knowledge that the form's information is true and correct before submitting it to the chief procurement officer for approval. The State Procurement Office

and the purchasing agency must post a copy of a “Notice of Sole Source” in publicly accessible areas at least seven days prior to any approval action. The posting requirement allows individuals to object to the request for sole source and to possibly reveal alternative vendors.

Amendments to sole sourcing that would change the original scope of the contract, or increase the original contract price by ten percent or more, must be approved by the chief procurement officer. A “Notice of Amendment to Sole Source Contract” must also be posted in publicly accessible areas at least seven days prior to any approval action.

Based on our review, we found that the department was in compliance with the requirements governing sole source procurement.

No problems were found in emergency procurement and professional services

The department rarely contracts for emergency procurement and the lack of any such contracts in our sample confirmed this.

According to Hawaii Administrative Rule 3-122-62, “professional services” are services within the scope of the practice of architecture, landscape architecture, professional engineering, land surveying, real property appraisal, law, medicine, accounting, dentistry, or any other practice defined as professional pursuant to Section 415A-2, HRS, or the professional and scientific occupation series contained in the United States Office of Personnel Management’s Qualifications Standards Handbook.

Purchasing agencies are required to invite persons who provide professional services to submit current statements of qualifications and expressions of interest to the agency at least annually. A review committee of three qualified agency employees is designated to evaluate the information and to compile a list of qualified persons who provide particular types of professional services. When the agency requests to contract for professional services, the screening committee provides the head of the purchasing agency with the names and qualifications of the three most qualified persons. The head of the purchasing agency ranks these persons in order of preference and, starting with the top ranked, negotiates until an agreement can be reached with one of the three. If agreement cannot be reached with any of the three, the head of the purchasing agency can request additional names of qualified persons from the screening committee. Other rules govern the purchase of professional services costing less than \$10,000.

Only one of the department contracts sampled was for the purchase of professional services over \$10,000. Our review of this contract found that the department was in compliance with the requirements governing professional services purchases over \$10,000.

Centralized oversight for compliance with the Hawaii Public Procurement Code within the department has been highly effective and the efforts of the contract specialist and fiscal officer are to be commended.

A procurement manual is needed

Although the department has a manual developed by the State Procurement Office that addresses the major procurement issues governed by the Hawaii Public Procurement Code, DBEDT needs to supplement this with its own procurement manual. For example, department policies regarding construction can affect whether a purchase is classified as a “small purchase.” A uniform written policy is needed in order to determine which provisions of the procurement code are applicable.

The department is currently developing a procurement policies and procedures manual, but in the absence of a completed manual, the current level of compliance is in jeopardy. The instances of non-compliance that were noted may have been avoided if the department had a detailed manual. A manual will also ensure uniformity and continuity in procurement requirements and processes.

The Department Has Made Progress In Contract Administration but Improvements are Still Needed

Our 1995 *Audit of Contract Administration and the Office of Space Industry in the Department of Business, Economic Development and Tourism*, Report No. 95-3, found a number of weaknesses in the department’s contract administration. An objective of the current audit was to determine whether the contract administration process ensures efficient and effective use of resources. Our follow-up found that the department has made progress in planning for and drafting contracts, but weaknesses remain in the areas of contract monitoring and outcome evaluation.

Improvements made since our 1995 audit report

A contract administration process that ensures efficient and effective use of resources includes sufficient planning, the development of a clear and results-oriented contract, effective performance monitoring, and final outcome evaluations. Since our prior report, the department has made noticeable progress in planning for and drafting contracts.

Improved planning prior to soliciting a contractor

The planning phase of the contracting process includes drafting a need statement, making cost projections, preparing a “Statement of Work,” and establishing evaluation factors.

The need statement is the first building block of the contracting process. The need statement begins with a clear definition of the issue, problem, or need leading an agency to contract for services. It should also clearly

state the quantitative and qualitative results desired. The “Request for Project Proposal” currently used by the department to initiate a contract fulfills the requirements of a need statement. For example, a proposal to initiate a cultural tourism program states that product development is an essential element of the state tourism strategy and will play a vital role in the future growth of Hawaii’s visitor industry. Cultural tourism strengthens, diversifies and adds value to Hawaii’s “tourism product” and helps to meet changing consumer needs. The proposal defines the issue, criteria and the qualitative results expected. The program is also projected to provide high quality cultural and historical experiences to all visitors and generate repeat visits and endorsements. Ultimately, the program supports and stimulates business and creates new jobs. Cultural tourism programs such as the Aloha Festivals and the Merrie Monarch Festival are two such examples.

Cost projections related to specific service activities are needed as a base for cost analysis of a bid, possible proposal negotiations, and determination of deductions for non-performance. In instances where the prospective contractors were given latitude in describing how required results would be achieved, the department required them to submit detailed budgets for analysis. In other cases we found that the department made adequate cost projections where appropriate.

The “Statement of Work” provides an accurate description of the essential and technical requirements for services. It is a thorough effort to clearly understand all aspects of the required service and is the foundation for the final contract and specifications. The “Statement of Work” establishes performance indicators, standards, and acceptable quality levels. We found planning elements in various documents which accompany department contracts that have the elements of a “Statement of Work.”

A final step in the planning process is to determine the evaluation factors (other than price) that will be used to make the contract award and their relative weight. Evaluation factors that may be considered include contractor experience, responsibility, responsiveness, and the quality of staff. After all criteria have been identified and weighted, a consensus on the importance of price is reached. Since our previous audit, the department has implemented an adequate and well documented evaluation process in making contract awards.

Contract documents are competently drafted

Contracts for the purchase of services are formal, written documents. They should protect the interests of the State, clearly identify the responsibilities of the parties to the contract, and define expected outcomes. The technical elements include a precise definition of the service to be rendered, schedules, timetables, benchmarks, status reports and presentations, and deliverables, if any. The effective price or prices

and the method and schedule of payments are detailed. The contract should also include the format or scenario for contract administration by the agency. Mutual agreement to the contract terms is confirmed by the signatures of those properly authorized to contract.

Our tests confirmed that the department competently drafts contracts and adequately addresses all necessary elements. Notably, the scopes of services in department contracts are now clear and specific. Contracts routinely incorporate the request for proposals or invitation for bids and the contractor's response as integral parts of the contract. The expected outcome and benefits are thoroughly communicated.

***Monitoring of contracts
still needs improvement***

Assessment of results is an ongoing process throughout the contract period. This process begins with a start-up conference to allow the contractor to meet the project manager and to provide the opportunity to explain the project manager's role in the administration of the contract. The project manager monitors disbursements against the budget and tracks work progress against schedules. The start-up conference also provides the opportunity to address potential work scheduling problems and to discuss property storage and security. The start-up conference also allows for a final review of specifications, terms, and conditions of the contract before work begins. The start-up conference lays the groundwork for smooth contract administration, however, we found that the department does not regularly conduct start-up conferences.

Project managers should have operational plans and a monitoring process to ensure that progress is made according to schedule and that quality of service conforms to established benchmarks. Where appropriate, the operational plan should require the project manager to make regular on-site visits or to obtain the views of a representative number of clients or direct beneficiaries to determine whether contract goals are being met. If the "products" of a contract for services include data, documentation, or reports, the operational plan should require the project manager to ensure that they are prepared in the prescribed format and are submitted on schedule. The project manager should also address disputes and take appropriate action when a contractor does not perform, or performs in a substandard fashion.

The department's contract specialist developed a "Contract Administration Verification Report" form to ensure contract deliverables. This report is customized for each contract, provides the essential elements of an operational plan, and establishes the accepted departmental procedures for contract administration. The project manager signs and dates the report as the deliverables are provided by the contractor. Contractor payments are based on the receipt of the established deliverables.

About half of the project managers were not using the forms to ensure contract deliverables. This resulted in poor accountability over the contractor and led to weak controls over incremental contract payments. For example, in at least one instance we found payment being made even though contractual milestones had not been reached. The Contract Administration Verification Report was developed to correct contract monitoring concerns identified in our prior report and the department should ensure that all project managers utilize the form.

Agency fails to perform sufficient contract outcome evaluation

The project manager is responsible for evaluating the outcome of a contract. A thorough evaluation upon the completion of a contract establishes whether the intended objectives of the contract were achieved and whether the fiduciary responsibility of the department to effectively and efficiently manage public resources has been fulfilled. An outcomes evaluation answers the following questions: (1) Did the State receive what it paid for? (2) Should action be taken against the contractor for substandard performance? and (3) Should the contractor be recommended for future contracting needs?

The Contract Administration Verification Report contains a section outlining the established procedures for contract evaluation. This section reiterates contract objectives, evaluates contractor performance in achieving the objectives, and provides recommendations for follow-up or future activities. However, in over 60 percent of the completed contracts we reviewed, project managers failed to evaluate contractor performance.

Problems result from the lack of a contracting manual and insufficient oversight

The department's weaknesses in contract management and evaluation may be due to the lack of a contract administration policies and procedures manual and central oversight of project managers. The department has indicated that it is in the process of developing a contract administration manual.

A high priority should be given to complete a manual. Without a manual to ensure uniform requirements and processes, improvements may be jeopardized with the loss of key personnel. As indicated earlier, improvements in contract planning and drafting, and compliance to the Hawaii Public Procurement Code have resulted through the efforts of the contract specialist. A manual and increased centralized oversight will be useful in training and encouraging project managers to monitor and evaluate contracts.

Conclusion

The department has achieved a high degree of compliance with the Hawaii Public Procurement Code through a review and approval process that is highly centralized. However, the level of compliance gained since 1995 is

put at risk by the lack of a detailed procurement manual. The department has also made progress in planning for and drafting contracts, however, weaknesses still exist in the areas of contract monitoring and outcome evaluation. Without sufficient contract management and evaluation, the efficient and effective use of state resources is not ensured.

Recommendations

1. The Department of Business, Economic Development and Tourism should develop a detailed procurement manual for use by all operating units.
2. The department should:
 - a. Develop a contracting policies and procedures manual for use by all project managers;
 - b. Ensure that all project managers are properly trained in contracting policies and procedures; and
 - c. Audit project managers for compliance with departmental contracting policies and procedures.

Response of the Affected Agency

Comments on Agency Response

We transmitted a draft of this report to the Department of Business, Economic Development and Tourism on September 4, 1997. A copy of the transmittal letter to the department is included as Attachment 1. The department's response is included as Attachment 2.

The department concurs with the findings and recommendations of the audit. It is currently in the process of enhancing its project management system through training of key departmental personnel and by integrating this system with an on-line automated tracking system. In addition, the department recognizes the importance of documenting its policies and procedures and has begun drafting a project management section as a part of its policies and procedures manual.

Finally, the department made several clarifying remarks regarding our audit statements on the department's contract management and evaluation practices. However, a review of our working papers confirms the accuracy of our statements and thus, we stand by our report.

ATTACHMENT 1

STATE OF HAWAII
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MARION M. HIGA
State Auditor

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September 4, 1997

COPY

The Honorable Seiji F. Naya, Director
Department of Business, Economic Development and Tourism
No. 1 Capitol District
250 South Hotel Street
Honolulu, Hawaii 96813

Dear Dr. Naya:

Enclosed for your information are three copies, numbered 6 to 8 of our draft report, *Procurement Audit of the Department of Business, Economic Development and Tourism*. We ask that you telephone us by Monday, September 8, 1997, on whether or not you intend to comment on our recommendations. If you wish your comments to be included in the report, please submit them no later than Thursday, September 18, 1997.

The Governor and presiding officers of the two houses of the Legislature have also been provided copies of this draft report.

Since this report is not in final form and changes may be made to it, access to the report should be restricted to those assisting you in preparing your response. Public release of the report will be made solely by our office and only after the report is published in its final form.

Sincerely,

Marion M. Higa
State Auditor

Enclosures



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September 22, 1997

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STATE OF HAWAII

Dear Ms. Higa:

Thank you for the opportunity to respond to the draft *Procurement Audit of the Department of Business, Economic Development, and Tourism*.

Upon arrival at DBEDT in 1995, I was very concerned with the findings of your just completed audit of the department which pointed out many weaknesses regarding our procurement practices. I was determined to implement your recommendations and made it one of my top priorities. As such, I take great pride in the progress you acknowledge regarding my Department's compliance with the provisions of the Hawaii Public Procurement Code in the report I have just received.

I charged my Special Assistant to oversee the implementation of our efforts in this regard. Given the reputation of the State Auditor for thorough and rigorous examination of governmental departments, I am extremely pleased the efforts of my Special Assistant in conjunction with the contracts specialist and fiscal officer resulted in the conclusions contained in your report. They include:

- *"Centralization of oversight responsibility has resulted in a high level of compliance with the provisions of the Hawaii Public Procurement Code"*
- *"The Department has made serious efforts to improve its contracting practices over the past two years"*
- *"The Department, with a few exceptions, was in general compliance with the code"*
- *"Based on both samples (of small purchases), we concluded that instances of non-compliance were isolated and rare"*
- *"Competitive sealed bidding requirements were observed"*
- *"DBEDT complied with competitive sealed proposal requirements"*
- *"The Department complied with sole source procurement requirements"*

- *"No problems were found in emergency procurement and professional services"*
- *"Centralized oversight for compliance with the Hawaii Public Procurement Code within the department has been highly effective and the efforts of the contract specialist and fiscal officer are to be commended."*
- *"Since our prior report, the department has made noticeable progress in planning and for and drafting contracts"*
- *"Improved planning prior to soliciting a contractor"*
- *"We found that the department made adequate cost projections where appropriate"*
- *"Since our previous audit, the department has implemented an adequate and well documented evaluation process in making contract awards"*
- *"Contract documents are competently drafted"*
- *"Our tests confirmed that the department competently drafts contracts and adequately addresses all necessary elements. Notably, the scopes of services in department contracts are now clear and specific. Contracts routinely incorporate the request for proposals or invitation for bids and the contractor's response as integral parts of the contract. The expected outcome and benefits are thoroughly communicated."*

I can assure you that DBEDT will continue its efforts to improve its procurement and contract management processes. We are enhancing our project management system by providing training to key departmental personnel. Using "smartware" programs, this project management system will be integrated with online automated tracking systems, thus further streamlining and coordinating the oversight of all projects.

DBEDT recognizes the importance of documenting its policies and procedures and has begun drafting a project management section as part of DBEDT's Policies and Procedures Manual. This manual will include all phases in the development, administration and evaluation of departmental projects. The manual cannot be completed, however, until the entire project management system is in place and operable.

In addition, I would like to clarify some of the audit statements regarding weaknesses in contract management and evaluation:

- *"Though the Department requires a written evaluation upon the completion of a contract, the audit cites 60% of examined "completed" contracts deficient in this area."*

Our review of all examined contracts, referred to above, indicates that all of these "deficient" contracts were still open, thus final written evaluations were

not required. Final written evaluations will be completed upon closing of the contracts.

- *"Though the Department requires all project managers to track the progress of contracts using a "Contract Administration Verification Report," (which lists all requirements, deliverables, payments, and serves as an operational plan to monitor the contract) about half of the project managers were not using the form."*

Each project manager is required to complete this form upon closing the contract and making final payments. Some project managers might not post information on the form on a timely basis during the course of administering the contract, but may complete periodic postings instead. The Department randomly audits open contracts to ensure project managers are in compliance with departmental contracting policies and procedures. Audits are, however, are contingent on the availability of resources. The Department recognizes the value of such audits in identifying deficiencies and training project managers.

DBEDT values the responsibility entrusted upon it to ensure proper planning and the prudent expenditure of public funds. As indicated above and throughout the audit report, DBEDT has and will continue to make great strides in fulfilling that trust.

Sincerely,

A handwritten signature in black ink, appearing to read 'Seiji F. Naya', with a long horizontal flourish extending to the right.

Seiji F. Naya