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# Audit of the Research Corporation of the University of Hawai'i

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A Report to the  
Governor  
and the  
Legislature of  
the State of  
Hawai'i

Report No. 15-07  
June 2015



**THE AUDITOR**  
STATE OF HAWAII

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## Office of the Auditor

The missions of the Office of the Auditor are assigned by the Hawai'i State Constitution (Article VII, Section 10). The primary mission is to conduct post audits of the transactions, accounts, programs, and performance of public agencies. A supplemental mission is to conduct such other investigations and prepare such additional reports as may be directed by the Legislature.

Under its assigned missions, the office conducts the following types of examinations:

1. Financial audits attest to the fairness of the financial statements of agencies. They examine the adequacy of the financial records and accounting and internal controls, and they determine the legality and propriety of expenditures.
2. Management audits, which are also referred to as performance audits, examine the effectiveness of programs or the efficiency of agencies or both. These audits are also called program audits, when they focus on whether programs are attaining the objectives and results expected of them, and operations audits, when they examine how well agencies are organized and managed and how efficiently they acquire and utilize resources.
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5. Health insurance analyses examine bills that propose to mandate certain health insurance benefits. Such bills cannot be enacted unless they are referred to the Office of the Auditor for an assessment of the social and financial impact of the proposed measure.
6. Analyses of proposed special funds and existing trust and revolving funds determine if proposals to establish these funds are existing funds meet legislative criteria.
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8. Fiscal accountability reports analyze expenditures by the state Department of Education in various areas.
9. Special studies respond to requests from both houses of the Legislature. The studies usually address specific problems for which the Legislature is seeking solutions.

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### THE AUDITOR

STATE OF HAWAII

Kekuanao'a Building

465 S. King Street, Room 500

Honolulu, Hawai'i 96813



Office of the Auditor  
465 S. King Street  
Rm. 500  
Honolulu, HI 96813  
Ph. (808) 587-0800

Jan K. Yamane  
Acting State Auditor  
State of Hawai'i

**"A research organization has got to be willing to take some risks, too."**

**—RCUH board chair**

Recommendations

Responses

Prior Audits

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# Audit of the Research Corporation of the University of Hawai'i

Report No. 15-07, June 2015

## *RCUH's weak plans and limited role reduce accountability for hiring and procurement exemptions*

### **Conservative, complacent business approach relegated RCUH's role to a university service bureau**

The Research Corporation of the University of Hawai'i (RCUH) was formed to play a proactive role in promoting the welfare of Hawai'i's people by initiating, stimulating, conducting, and coordinating research and training, as well as commercializing inventions and discoveries. We found, however, that RCUH acts primarily as a provider of services to UH, which constituted \$9 out of every \$10 in RCUH business in FY2014. The RCUH board recognized a need to expand UH services and pursue more non-UH projects in 2004. However, plans to do so were not implemented or updated because the RCUH Board of Directors lacked initiative, training, policies, and metrics needed to drive proper planning. This planning failure undermines RCUH's accountability for services provided and for achievement of the purpose for which the corporation was founded.

We further found that RCUH's executive director and board took a cautious business approach that ignored plans to pursue more non-UH projects. According to the RCUH board chair, from about 2002 through 2011, UH's research enterprise was growing rapidly, which provided the corporation with all the work it could handle. As a result, there was no pressing need to grow RCUH's non-UH business. Plans to pursue non-UH business also were undermined by RCUH efforts to avoid conflicts with a public sector union and private service providers.

### **Improved oversight of projects is needed to ensure the integrity of RCUH's services**

RCUH's broad purpose allows projects remotely associated with research or training to qualify for exemptions from state procurement and civil service laws. As such, strong management controls should be in place to ensure that projects qualify for RCUH's exemptions. During FY2014, the corporation had about 3,000 employees earning \$113.5 million in salary. We found that RCUH allows state agencies to circumvent contract requirements, secure services without proof of governor approvals, and forgo required evaluations of \$4.3 million in projects. We also found that the corporation lacks clear policies and procedures for the review and acceptance of direct projects, and the department in charge of administering those projects lacks staff to ensure adequate project vetting and monitoring. We further found that written policies and procedures could improve RCUH's oversight of intramural and revolving account projects. A lack of accountability for the flexibility afforded to RCUH raises the risk that RCUH's employment and procurement exemptions are inappropriately used, which in turn may expose the corporation to criticism and undermine the public's trust.

### **Agency response**

Neither the board chair nor the executive director disputed our findings in their responses to our audit. The chair said the board will review the corporation's mission and make changes as needed, but that the current mission was appropriate. He also said the board will work with the executive director to ensure policies and procedures are reviewed and updated. The chair agreed that RCUH needs strategic and long-range goals, objectives, and performance measures. The board chair also stated that our audit did not take into account the legislative intent of creating RCUH, or the statutory composition of the board, which both skew toward providing services to UH. The chair misses our larger point that the RCUH board adopted initiatives to grow and diversify the corporation's business in 2004, but failed to ensure their implementation.

The RCUH executive director disagreed with our recommendation that the Legislature amend Chapter 304A, HRS, to require RCUH to develop and provide annual reports with goals and objectives. He said it will be recommended to the next executive director to follow-up on our recommendations by enhancing board orientation, and establishing performance measure parameters. Additionally, the executive director said RCUH is updating its policies and procedures and is developing guidelines as needed. The executive director further stated that RCUH will not execute any direct project agreements or amendments without approval from the governor, and that all state agencies will be required to comply with the State/RCUH master agreement.

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Submitted by

**THE AUDITOR**  
STATE OF HAWAI'I

Report No. 15-07  
June 2015

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## Foreword

This report on our audit of the Research Corporation of the University of Hawai'i was conducted pursuant to Article VII, Section 10 of the Hawai'i State Constitution and Section 23-4, Hawai'i Revised Statutes (HRS), which require 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.

We wish to express our appreciation for the cooperation and assistance extended to us by members of the Research Corporation of the University of Hawai'i Board of Directors, the executive director and staff of the RCUH, and other individuals whom we contacted during the course of our audit.

Jan K. Yamane  
Acting State Auditor

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# Chapter 1

## Introduction

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This audit of the Research Corporation of the University of Hawai'i was conducted pursuant to Article VII, Section 10 of the Hawai'i State Constitution and Section 23-4, Hawai'i 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.

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## Background

In the early 1960s, Hawai'i's legislature sought to promote research to enhance the reputation of the University of Hawai'i (UH) and to advance the State's economic growth and development. To support UH's efforts to be a leader in research, the Legislature created the Research Corporation of the University of Hawai'i (RCUH). RCUH was designed to make UH more competitive in obtaining research grants by exempting the corporation from certain state procurement and employment laws. The flexibility was intended to allow RCUH to carry out federal government, UH, and state agency projects in a more effective and efficient manner.

In enacting Act 209, Session Laws of Hawai'i 1965, which created RCUH as a non-profit, public agency, the Legislature considered that the corporation would:

- Have trained specialists for negotiating contracts with federal and State agencies;
- Provide university-wide assistance in promotion and development of short- and long-range research opportunities from an interdisciplinary point of view; and
- Provide a mechanism for prompt and effective meeting of contingency research needs.

Among other things, RCUH was tasked with encouraging, initiating, aiding, developing, and conducting scientific investigations and research. RCUH is empowered to enter into and perform contracts; coordinate projects with state agencies for economic development purposes; stimulate and promote cooperative research projects; and retain patents, copyrights, and other rights arising from RCUH activities. RCUH also can set up a special account for depositing moneys received from either public or private contracts, or from private or public grants, awards, or gifts.



### ***RCUH's mission, organization, and projects***

RCUH's mission is to support UH's research and training programs and to enhance research, development, and training generally in Hawai'i. To this end, RCUH provides accounting, disbursements, human resources management, and procurement services, which in turn makes it possible for researchers to focus their efforts on research rather than administrative activities.

### **RCUH organization**

RCUH is a state agency attached to UH for administrative purposes. Its enabling legislation is codified in Chapter 304A, Sections 3001 to 3011, HRS. The affairs of RCUH are under the general management and control of an eight-member RCUH Board of Directors. RCUH is composed of the Executive Director's Office; Finance and Project Administration and Human Resources departments; and the Accounting, Procurement/Disbursing, and Project Administration sections.

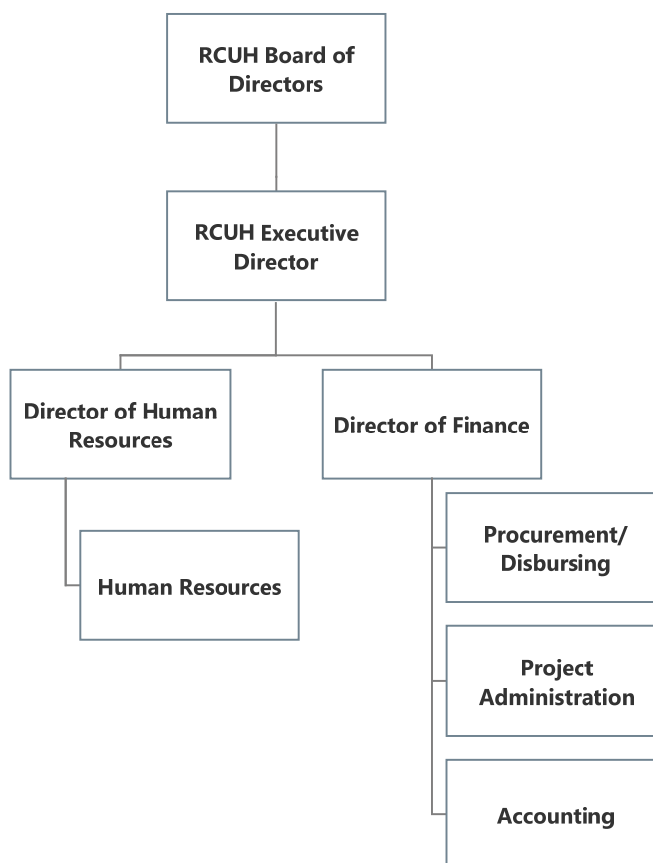
RCUH has a staff of approximately 40 employees. The **Executive Director's Office** is responsible for overall management RCUH's day-to-day affairs. It also provides support to the RCUH Board of Directors. The office is composed of two individuals, the executive director and corporate affairs/facility security manager.

The **Human Resources Department** is led by the director of human resources. The department is responsible for compliance with policies and employment laws and provides support on personnel matters including employment administration and support services, compensation administration, employee benefits, policy and regulatory administration and compliance, staff training and development programs, payroll administration, and human resources information management. On average, there are 3,000 project personnel on RCUH's payroll at any given time; the vast majority of personnel work on UH research and training projects. Because RCUH project lifespans vary, there is constant turnover, resulting in RCUH processing about 1,600 new hires and 1,600 terminations each year.

The director of finance oversees the **Procurement/Disbursing, Project Administration and Accounting section**. The Disbursing/Purchasing Department reviews all contracts and agreements regarding consultants, subcontracts, real property, leases, construction, and insurance. This department also coordinates and distributes requests for proposals.

The Project Administration section is responsible for establishing service order projects, direct projects, revolving accounts, and specialized service facilities projects at RCUH. The Accounting section is responsible for providing general accounting, financial and information systems support. Exhibit 1.1 depicts the corporation's organizational structure.

### Exhibit 1.1 Research Corporation of the University of Hawai'i Organizational Chart



Source: Office of the Auditor

### RCUH projects

RCUH's enabling legislation lends the corporation wide latitude for accepting projects. RCUH accepts four types of projects: UH extramural, UH intramural, UH revolving fund accounts, and direct.

**UH extramural projects** are external federal and non-federal sponsored contracts, grants, and other agreements.

**UH intramural projects** are internal sponsored programs or activities such as Research and Training Revolving Funds or Tuition and Fee Special Funds. UH intramural projects encompass staffing a gift shop at the Hanauma Bay Education Center (from 2002–2013), architectural and public relations consultants for the Regional Biocontainment Laboratory, and window replacement for UH facilities.

**UH revolving fund account projects** are self-sustaining, income-generating projects that are established to support a specialized service facility, recharge center, or other sales and service activities. UH Revolving fund account activities have included conferences, workshops, and supplying a photocopier to the UH School of Ocean and Earth Science and Technology.

**Direct projects** are assigned to and accepted by RCUH from non-UH organizations, including federal and state agencies, international organizations, and other not-for-profit organizations. A 1995 master agreement between RCUH and the State establishes criteria for determining the appropriateness of the State's use of the corporation's services. These projects normally remain under the general and technical supervision of personnel employed by the state sponsors; RCUH's responsibilities are limited to providing administrative services. Direct projects have included coordinating statewide early childhood education and care programs and services, and hiring and training a water treatment coordinator for the Hawai'i National Guard Youth Challenge Academy.

## ***Funding***

RCUH must be self-supporting. It receives no general funds and operates entirely on fees charged for its services. During the past three fiscal years, RCUH's total operating revenues averaged \$6.5 million while total operating expenditures averaged \$6.1 million. Exhibit 1.2 provides a three-year summary of RCUH finances.

### **Exhibit 1.2 Corporation's Financial Summary, FY2012–FY2014**

	<b>FY2012</b>	<b>FY2013</b>	<b>FY2014</b>
<b>Beginning Net Position</b>	\$8,963,915	\$9,055,000	\$9,418,429
Revenues	6,256,687	6,167,221	6,998,459
Interest	94,961	67,073	92,554
Expenditures	(5,962,816)	(5,870,865)	(6,331,146)
Investment expense	(297,747)	--	--
<b>Ending Net Asset Position</b>	<b>\$9,055,000</b>	<b>\$9,418,429</b>	<b>\$10,178,296</b>

Source: RCUH audited financial statements

For UH projects, the university pays RCUH a fee based on an agreed-upon formula. UH extramural projects make up the largest portion of RCUH's business, followed by UH intramural, UH revolving fund account, and direct projects. Direct projects such as those of other state agencies, federal agencies, and private organizations, are charged a fee to cover RCUH's administrative costs, based on the scope and volume of

services provided and represent a fraction of RCUH's business. RCUH volume of business (project expenditures) fell to about \$350 million in FY2014 following the conclusion of an RCUH construction project involving UH West O'ahu and UH Cancer Center. Exhibit 1.3 shows RCUH's volume of business and revenues by project type for FY2012–FY2014.

### Exhibit 1.3

#### Corporation Volume of Business and Revenues by Project Type, FY2012–FY2014

PROJECTS	Volume of Business			Revenues		
	FY2012	FY2013	FY2014	FY2012	FY2013	FY2014
UH Extramural	\$241,162,916	\$248,806,479	\$236,465,471	\$4,060,297	\$3,859,243	\$4,030,313
UH Intramural	164,441,161	92,399,670	39,101,095	264,920	424,616	677,380
UH Revolving Fund Accounts	42,339,782	42,056,058	41,123,155	887,264	919,906	1,210,437
Direct	36,770,793	33,531,091	32,950,285	1,044,206	963,456	1,080,329
<b>Total</b>	<b>\$484,714,652</b>	<b>\$416,793,298</b>	<b>\$349,640,006</b>	<b>\$6,256,687</b>	<b>\$6,167,221</b>	<b>\$6,998,459</b>

Source: RCUH

The State departments with the highest volume of direct project business and revenues were: (1) Department of Land and Natural Resources, (2) Department of Business, Economic Development and Tourism, and (3) Department of Health. Exhibit 1.4 shows contract volume and revenues by state agency for the prior three fiscal years.

**Exhibit 1.4****Contract Volume of Business and Revenues by State or County Agency, FY2012–FY2014**

	Volume of Business			Revenues		
DIRECT PROJECTS	FY2012	FY2013	FY2014	FY2012	FY2013	FY2014
<b>State Department</b>						
Business, Economic Development and Tourism	\$ 68,952	\$ 312,124	\$ 838,201	\$ 1,881	\$ 9,033	\$ 28,077
Health	877,811	686,384	774,429	23,914	16,676	23,032
Education	40,632	20,644	13,234	1,163	601	448
Land and Natural Resources	1,596,816	1,647,550	1,448,666	41,764	43,047	46,279
Defense	831,090	213,393	63,798	22,094	5,789	2,038
Accounting and General Services	32,099	89,365	94,995	935	2,603	3,212
Commerce and Consumer Affairs	32,099	89,366	94,996	935	2,603	3,212
Public Safety	132,587	155,806	209,400	3,486	4,096	6,689
Governor's Office	--	304,920	359,357	--	8,215	11,480
<b>Other State Agency</b>	--	29,214	--	--	835	--
<b>County</b>	--	--	172,900	--	--	13,545
<b>Total State and County</b>	<b>\$3,612,086</b>	<b>\$3,548,766</b>	<b>\$4,069,976</b>	<b>\$96,172</b>	<b>\$93,498</b>	<b>\$138,012</b>

Source: RCUH

**Prior Audits**

We conducted an audit of the corporation in 1993 and a follow-up audit in 1995. Our 1993 *Audit of the Research Corporation of the University of Hawai'i*, Report No. 93-10, found a lack of accountability and oversight in RCUH's operations, financial management, and contract administration. RCUH also lacked clear policies, criteria, and management controls for contracts with state agencies. Further, RCUH's financial statements were misleading. Finally, we found that RCUH's management fee structure for state agencies was arbitrary and not linked to services provided. We recommended that the corporation accurately report revenues and expenses in its financial statements. We also recommended UH ensure RCUH developed clear policies, criteria, and guidelines for the types of projects RCUH will accept from state agencies; developed management controls and a monitoring program to ensure that state projects do not circumvent state laws and contracts; formalized policies for a management fee for RCUH contracts with state agencies based on its administrative costs, and define the use of revenues derived from the fees.

Our 1995 *Follow-up Report on an Audit of the Research Corporation of the University of Hawai‘i*, Report No. 95-9, found that RCUH had made progress in implementing our recommendations, including accurately reporting revenues and expenses, capitalization and annual depreciation expenses of fixed assets, and investment income and total expenses for research assistantships. In addition, RCUH had drafted a proposed master agreement for RCUH and state agencies to establish the terms and conditions under which state agencies and the RCUH may enter into contractual arrangements.

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## Objectives of the Audit

1. Assess the adequacy of the Research Corporation of the University of Hawai‘i’s planning and oversight.
  2. Assess the adequacy of the corporation’s vetting and monitoring of projects.
  3. Make recommendations as appropriate.
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## Scope and Methodology

Our audit focused on RCUH’s planning, oversight, and vetting and monitoring of projects during FY2014. We interviewed board members, office personnel, and a legislator. We reviewed strategic plans, contracts, performance measures, and other documentation as appropriate; and judgmentally sampled items to test compliance with applicable policies, procedures, and other relevant criteria.

Our audit was conducted from January 2015 through April 2015 pursuant to the Office of the Auditor’s *Manual of Guides* and generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe the evidence we obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

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# Chapter 2

## RCUH's Weak Plans Limit Role, Reduce Accountability for Hiring and Procurement Exemptions

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The Research Corporation of the University of Hawai'i (RCUH) was formed to play a proactive role in promoting the welfare of Hawai'i's people by initiating, stimulating, conducting, and coordinating research and training, as well as commercializing inventions and discoveries. To aid in this broad purpose, RCUH was empowered to provide procurement and employment services that are exempt from state laws. During FY2014, the corporation had about 3,000 employees earning \$113.5 million in salary. The University of Hawai'i (UH), the State, counties, and federal agencies can use RCUH's flexibility to make purchases and hire personnel with business-like efficiency. We found, however, that RCUH acts primarily as a provider of services to UH, which constituted \$9 out of every \$10 in RCUH business in FY2014. The RCUH Board of Directors recognized a need to expand UH services and pursue more non-UH projects in 2004. However, plans to do so were not implemented or updated because the RCUH board lacked initiative, training, policies, and metrics needed to drive proper planning. This planning failure undermines RCUH's accountability for services provided and for achievement of the purpose for which the corporation was founded.

We also found RCUH lacks written policies and procedures and staff to ensure adequate oversight of \$4.3 million in direct projects with state agencies closed in FY2014. This impedes the corporation's accountability and enables the improper use of RCUH's flexible procurement and employment services by state agencies. Although direct projects currently represent a fraction of RCUH's business, it is a segment that board members have targeted for growth. Pursuit of non-UH projects will help RCUH fulfill its broad mandate to serve research and training efforts statewide, while also diversifying its business base.

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### Summary of Findings

1. Complacency and weak planning by the Research Corporation of the University of Hawai'i's Board of Directors and executive director have resulted in a reactive approach to supporting research and training that focuses support services on University of Hawai'i activities. In addition, plans do not address RCUH's mandate to initiate, stimulate, conduct, and coordinate research and training generally in Hawai'i.



2. RCUH project oversight deficiencies jeopardize the integrity of the corporation's services.

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## **Board and Director Have Relegated RCUH's Role to a University Service Bureau**

The Legislature created RCUH with a broad range of purposes and powers, and envisioned a proactive agency that would initiate and perform research and training and coordinate such activities in Hawai'i. We found RCUH's fulfilment of this mandate is constricted by a complacent, conservative business approach that relegates the corporation to providing employment and purchasing services primarily for UH projects. RCUH's passive approach towards initiating and stimulating research and training, coupled with inadequate planning, has resulted in the corporation's near complete dependence on UH, which is imprudent and contrary to legislative intent.

## ***Complacent planning results in the self-supported corporation's near complete dependence on UH research projects***

RCUH is a unique state agency in that it receives no general funds and relies on fees, contracts, and grants to support its operations. Despite this autonomy, RCUH remains dependent on UH for about 90 percent of its nearly \$350 million in FY2014 project expenditures. In 2004, RCUH adopted a strategic plan that identified a need to expand services and diversify revenues beyond UH; however, key elements of the plan were not implemented. Follow-on efforts in 2008 and 2011 to develop a new strategic plan and financial sustainability, respectively, also were not implemented. Further, RCUH has not developed an annual report establishing goals and objectives as required under Act 100, Session Laws of Hawai'i (SLH) 1999. Because RCUH lacks both an Act 100 plan and a relevant strategic plan, it operates without goals, objectives, and metrics needed for measuring performance. As a result, RCUH cannot account for its service provider performance or determine if it is accomplishing its statutory purpose.

## **RCUH's 11-year-old strategic plan to expand and diversify its business has never been implemented**

Government agency strategic plans should have a mission, goals, and objectives. The strategic plan is the foundation of an agency's planning system as it provides direction for all programmatic and management functions used to execute the strategies needed to reach goals. An agency's strategic goals and objectives should be used to align resources and guide decision-making to accomplish priorities to improve outcomes.

Generally, goals are statements of what a program is striving to achieve, and objectives are statements of what a program expects to achieve within a defined period. The importance of goals, objectives, and performance measures is recognized in Act 100, SLH 1999. The act

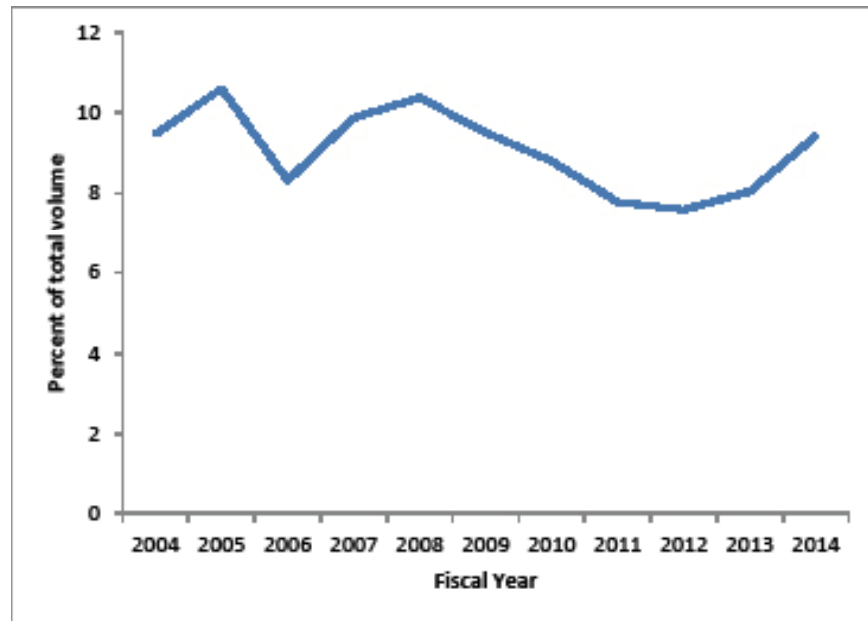
requires all departments and agencies to identify their goals, objectives, and policies to provide a basis for determining priorities and allocating limited public funds and human resources to assist the Legislature in evaluating budgetary needs. The development of goals and objectives by agencies is essential for determining priorities, guiding their decisions, and measuring the effectiveness of their programs and services. To this end, Act 100 requires that *every* department and agency of the State develop and submit to the Legislature an annual report with short- and long-term goals, objectives, performance measures, and a timetable indicating how objectives and policies will be implemented.

We found that RCUH, which is a state agency, has no Act 100 plan. The RCUH executive director was unaware of the requirement until we inquired about the existence of such a plan. He said RCUH subsequently consulted its advising deputy attorney general who determined that the corporation was not subject to the requirement because it received no general funds. We further found that RCUH's most recent 2004-adopted strategic plan has been largely ignored. That plan included a strategy to fill gaps in UH research and training infrastructure and enhance interconnection with government and the private sector. The five-year plan contained six objectives and one performance measure. Board members, however, were unfamiliar with the plan, and key objectives to expand services to better meet UH and state research and training needs were not implemented by the executive director.

According to the 2004 plan,

increased volume of non-UH activities at RCUH will provide enhanced capabilities and expertise that will benefit the UH, and will reduce the absolute financial dependence of RCUH on the University as UH evolves rapidly in the face of various challenges.

The plan included adopting a comprehensive approach to providing pre-award as well as commercialization services, and expanding RCUH's infrastructure to support a 100 percent increase in direct grants and contracts, which were \$24.7 million (9.5 percent) of \$260.4 million in total project volume in FY2004. Neither of those objectives were implemented, and a decade later, FY2014 direct project volume was \$33 million (9.4 percent) of \$349.6 million in total project volume. Exhibit 2.1 illustrates the percentage of RCUH direct project volume to total volume having remained relatively unchanged since FY2004.

**Exhibit 2.1****Percentage of RCUH Direct Project Volume, FY2004–FY2014**

Source: RCUH provided data

In the absence of a long-term strategic plan, RCUH operates under a two-year “strategy and workplan,” which is used to develop budget initiatives and for evaluating the executive director’s performance. We reviewed the FY2014 plan and found it did not contain strategic goals. The executive director told us that a separate document created in 2007 or 2008 articulated these strategies. However, he could not find that document, and instead provided us a copy of a 2009–2011 strategy and workplan with two goals aimed at improving services to facilitate client growth. That plan contained no objectives or performance measures.

**“High priority” effort to develop a new strategic plan is in its eighth year**

In September 2008, the RCUH board approved a strategy and workplan for fiscal years 2010 and 2011 that included a “high priority” initiative to develop RCUH’s next strategic plan by the end of June 2011. The strategic planning initiative also was labeled a high priority in the subsequent FY2012–2013 and FY2013–2014 strategy and workplans. The FY2014–2015 strategy and workplan also contains a strategic planning initiative as a high priority, but with no completion date. In actuality, development of a new strategic plan was not a high priority, according to the RCUH board chair and executive director.

We found that the executive director and board members disagreed over the need for a strategic plan. There are opportunities for RCUH to grow its non-UH business, and to provide added services to UH, according to the executive director. However, the executive director said RCUH's ability to expand was constrained by a lack of resources and a need to maintain services to UH. He said he did not see a solution to that problem absent expanding services to existing clients, expanding existing services to new clients, charging UH and the State more for services, or finding new clients. Despite this dilemma, the executive director did not see a need for RCUH to have a strategic plan.

Board members, who are responsible for managing and controlling the corporation, disagreed with the executive director. They said they recognize a need for a strategic plan and to diversify and grow RCUH's non-UH business. However, the RCUH board chair said such a plan will need to be conducted by a new executive director. RCUH's executive director will retire in June 2015.

Strategic planning, and regular strategic reviews, are a foundational tool for identifying opportunities and establishing priorities to address RCUH's resource needs. The lack of such planning undermines RCUH's ability to prioritize resources to expand services and better fulfill its purpose of promoting and initiating research and training statewide.

According to the Office of Management and Budget (OMB) *Circular No. A-11*, an annual strategic review should look at opportunities for productivity gains using a variety of analytical, research, and evaluation methods. The circular describes requirements under the Government Performance and Results Modernization Act and requirements for federal agency strategic plans, annual performance plans, and reports. The act serves as a foundation for helping government-sponsored agencies focus on their highest priorities to create a culture where data and empirical evidence support policy, budget, and management decisions.

A potential model for RCUH strategic planning is San Diego State University (SDSU) Research Foundation strategic plan. Like RCUH, the SDSU Research Foundation is a non-profit organization chartered to further the educational, research, and community service objectives of San Diego State University. Its strategic plan has priorities that include:

- Strengthening communication to support business goals and enhance reputation;
- Providing quality, timely services at a lower cost; and
- Helping enhance SDSU's national prominence in research.

Exhibit 2.2 provides excerpts from SDSU's financial stability strategic priority.

## Exhibit 2.2

### San Diego State University Research Foundation Strategic Plan Priority

#### SDSU strategic priority: Build and sustain financial sustainability

Invest and/or reallocate resources to achieve strategic goals.

- Demonstrate effective and efficient use of resources.
- Increase and diversify revenue streams.

Identify new entrepreneurial projects to generate funds.

- Research new collaborations and partnerships.
- Develop strategies for new resource acquisition.
- Pursue major funding opportunities that focus on emerging national and international trends.

Source: San Diego State University Research Foundation strategic plan

### **Without metrics, RCUH cannot measure service performance or determine mission achievement**

According to the Governmental Accounting Standards Board (GASB) *Suggested Guidelines for Voluntary Reporting*, effective Service Effort and Accomplishment Performance Information reports focus on key measures that provide a basis for assessing the performance of the programs and services. The guidelines were developed to assist state and local governments in providing effective external communication of performance information. The building blocks of performance management and reporting are goals and objectives. Preferably, objectives are quantifiable and measurable, in order to be compared to a target government expects to achieve.

RCUH does not adhere to a set of strategic plan-derived goals and objectives; therefore, our analysis of RCUH's performance monitoring focused on determining how the RCUH board monitored performance in achieving the corporation's mission. We interviewed four RCUH board members and the executive director and determined that performance is monitored via a variety of financial measures and feedback from UH.

We also found that UH feedback is tracked on an anecdotal, not quantitative basis. Further, RCUH's financial reports are not adequate for monitoring achievement of the corporation's mission. According to the GASB guidelines, traditional financial statements are adequate for providing financial performance information about a government's fiscal and operational accountability. However, those statements

are inadequate for determining the degree to which the government successfully provided services to maintain or improve the well-being of citizens. Therefore, effective reports focus on key measures, providing a basis for assessing the performance of the programs and services being reported and the achievement of major goals and objectives.

In a budget plan adopted in June 2011, the RCUH board identified a need to develop performance measures and timelines and reporting measures. The budget plan included a research investment initiative goal that directed development of a financial sustainability plan to invest RCUH profits to support UH and state projects consistent with RCUH's legislative mandate and mission. The board considered the plan might include performance measures and timelines and reporting measures, and would identify ways to improve RCUH's financial outlook. However, no such plan was developed, and no review was conducted.

Without performance data and benchmarks, board members cannot make informed decisions on how to allocate funding and ensure long-term sustainability of operations because they cannot determine whether RCUH achieves goals and objectives.

### **RCUH lacks a framework to drive proper strategic planning**

We found the RCUH board is not equipped to perform its policy-making and oversight roles. The board lacks a formal training program, and the packet of information provided to new board members does not contain RCUH's 2004 strategic plan or the executive director's strategy and workplan. The board does not have access to a compilation of past policies. Additionally, the board, which meets quarterly, held just three general meetings in FY2014, none of which included a discussion of strategic plans, according to a review of board minutes. The most recent meeting of a board strategic planning committee was in 2004.

According to Cyril O. Houles' *Governing Boards*, a board should approve and periodically revise long-range institutional plans to ensure that the overall mission of a program remains in focus and that objectives are in harmony with the mission and that objectives are achieved in the best fashion possible. An institution's ability to achieve its mission is hampered by trustee ignorance or apathy; therefore, the whole board has the obligation to stimulate, guide, and assist each member. Formal opportunities for learning are crucial in helping a board and its members fulfill the specific missions of their agency. A compilation of past policy decisions can help board members focus on important matters.

RCUH also lacks policies and procedures to drive and guide strategic planning, and no one is specifically responsible for developing a strategic plan. Board members said RCUH's executive director is responsible

for developing such a plan. The executive director acknowledged this responsibility was his; however, his position description states only that the executive director is to direct, manage, and administer RCUH's affairs.

***RCUH's mandate to proactively support Hawai'i research and training is undermined by conservative practices***

RCUH's purpose to initiate, develop, and conduct training, research, and study is strengthened via powers that include rights to conduct research, coordinate activities with state agencies for economic development purposes, promote cooperative research projects, and retain patents and copyrights arising from RCUH activities. Among other things, the Legislature considered that RCUH would have a staff of trained specialists for negotiating contracts with federal and private agencies, and assist UH in promoting and developing short- and long-range research opportunities from a broadly-based, interdisciplinary point of view.

In contrast with this proactive mandate, RCUH pursues a passive mission that calls for supporting UH research and training programs and enhancing research, development, and training generally in Hawai'i. RCUH acts as a service bureau that hires personnel, procures goods and services, handles accounts payable/receivable, and provides training primarily for UH clients. Exhibit 2.3 includes RCUH's own description of its service provider role.

**Exhibit 2.3**  
**RCUH's Self-Described Role as a Service Bureau**

**RCUH IS AKIN TO A SERVICE BUREAU.** Its services include accounting, disbursements, human resources management, and procurement. Because of its exemption from State statutes relating to special funds, procurement, civil service, compensation, public employment, and the retirement system, RCUH has the flexibility to function more like a business. Accordingly, RCUH has its own personnel, payroll, accounting, procurement and disbursing systems, independent of the state and University systems. This makes it possible for RCUH to process transactions expeditiously, which in turn makes it possible for the researchers to focus more of their efforts on research rather than administrative activities.

Source: RCUH 2014 annual report

The UH Board of Regents also sees RCUH's role as a facilitator to UH research. According to the OMB, strategic goals should reflect the statutory mission of the agency. However, RCUH's passive, supportive

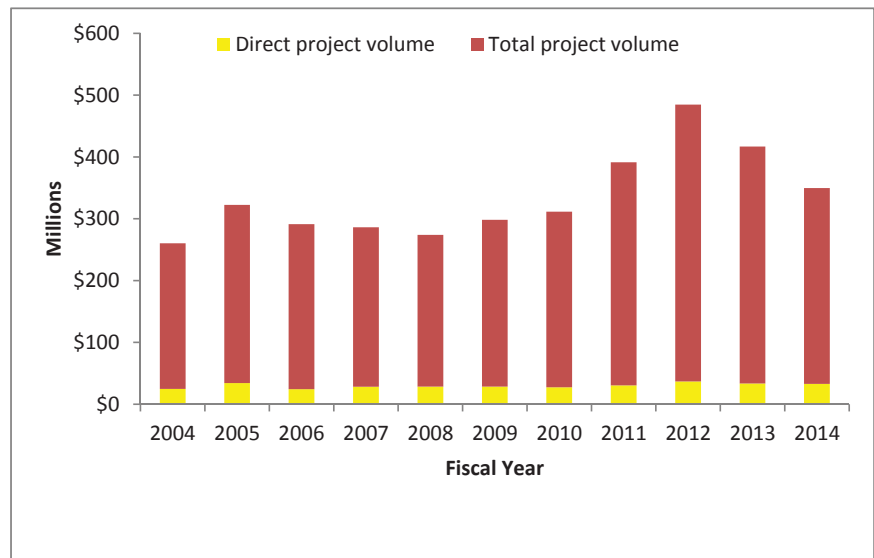


role, which focuses on hiring and employment exemptions for UH, does not align with the proactive role envisioned by the Legislature as expressed in its committee reports and legislation.

We found that RCUH's executive director and board took a cautious business approach that ignored plans to pursue more non-UH projects. According to the RCUH board chair, from about 2002 through 2011, UH's research enterprise was growing rapidly, which provided the corporation with all the work it could handle. As a result, there was no pressing need to grow RCUH's non-UH business. However, federal budgets have since contracted, reducing that growth and causing RCUH to need to find opportunities elsewhere, according to the chair. Another RCUH board member said the board has been too comfortable with this status quo and therefore failed to develop and implement an updated strategic plan that targeted growing and diversifying RCUH's business.

As illustrated in Exhibit 2.4, RCUH's direct and total project volume has declined in recent years, in part because of reduced construction project costs for UH West O'ahu and the UH Cancer Center.

**Exhibit 2.4**  
**RCUH Total Project Volume, FY2004–FY2014**



Source: RCUH-provided data

Plans to pursue non-UH business also were undermined by RCUH efforts to avoid conflicts with a public sector union and private service providers. According to a 2014 new markets proposal prepared by the RCUH executive director, the corporation has been cautious about promoting more use of its services by state agencies following complaints by the Hawai'i Government Employees Association to the



Legislature asserting that many RCUH employees should be state or UH employees. He further wrote that RCUH should be cautious in marketing its staffing and procurement services to county governments lest the public-sector unions “crank up” their attempts to restrict employment through RCUH. He also wrote that marketing services to non-profit organizations might put RCUH in competition with private sector companies.

The board chair acknowledged that the RCUH executive director has taken a risk-averse approach to business development. However, the chair said, “A research organization has got to be willing to take some risks, too.”

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## **Improved Oversight of Projects Needed to Ensure the Integrity of RCUH's Services**

RCUH's broad purpose allows projects remotely associated with research or training to qualify for exemptions from state procurement and civil service laws. Accordingly, strong management controls should be in place to ensure that projects qualify for RCUH's exemptions. Procurement laws are meant to ensure fair, competitive access to government contracts, while civil service laws support a merit-based system of public employment. We found that RCUH allows state agencies to circumvent contract requirements, secure services without proof of governor approvals, and forgo required project evaluations. We also found that the corporation lacks clear policies and procedures for the review and acceptance of direct projects, and the department in charge of administering those projects lacks staff to ensure adequate project vetting and monitoring. We further found that written policies and procedures could improve RCUH's oversight of UH intramural and UH revolving fund account projects. A lack of accountability for the flexibility afforded to RCUH raises the risk that RCUH's employment and procurement exemptions are inappropriately used, which in turn exposes the corporation to criticism and undermines the public's trust.

### ***RCUH's permissive management enables improper use of procurement and employment flexibility by the State***

We identified a need for RCUH to improve contract administration in 1993. At the time we reported that RCUH lacked clear policies, criteria, and management controls for contracting with state agencies, which jeopardized the integrity of the corporation's services. RCUH developed criteria to address oversight deficiencies identified more than two decades ago; however, our audit found that RCUH applied the criteria haphazardly.

### **Twenty-year-old State/RCUH agreement was meant to increase accountability**

Our 1995 follow-up audit of RCUH determined that the corporation and the State were in the process of developing a master agreement to establish criteria for determining the appropriateness of the State's use of the corporation's services. Executed in April 1995, that master agreement set guidelines for determining whether a State project can seek RCUH services. Among other things, state agencies must provide a concise justification and statement of reasons for the use of RCUH services. Exhibit 2.5 shows criteria a proposed state project must meet to qualify for RCUH services.

#### **Exhibit 2.5 State/RCUH Master Agreement Acceptance Criteria**

**A project qualifies for RCUH services if it has all of the following characteristics:**

- The scope of the work is beyond the existing capacity of the requesting agency;
- Contracting with RCUH is more efficient than contracting with the private sector;
- The work involved requires university-level research or investigation;
- The project's funding requirements exceed \$25,000;
- The project does not involve classified research;
- Assistance is required in the development of the project's scope, formulation, or implementation; and
- Private sector assistance would be inappropriate.

Source: State/RCUH Master Agreement

The master agreement also identifies the project administration responsibilities of both the State and RCUH. For example, the agency requesting RCUH services must obtain the governor's prior written approval on all initial requests for services, as well as amendments and supplements to such requests. RCUH also is required to periodically review state direct projects to ensure they remain acceptable for use of the corporation's exemptions.

### RCUH improperly approved and amended state project agreements

Direct projects with the State require governor approval before execution of an agreement with RCUH, and before approval of any subsequent project amendments. RCUH requests proof of the governor's approval of agreements and amendments prior to project acceptance; however, RCUH does not ensure receipt of these documents. We reviewed the vetting and monitoring of all seven state direct projects closed in FY2014 and found four project files did not contain evidence of the governor's approval. Overall, we found RCUH amended 13 of 18 total project agreements without proof of the governor's approval. Exhibit 2.6 details all state direct project files closed in FY2014, amendments made, and whether RCUH had evidence the governor approved the amendments.

#### Exhibit 2.6 State Projects Missing Governor's Approvals

State Department	No. of Project Amendments	Proof of Governor's Approval for Each Amendment
Business, Economic Development and Tourism	1	None found
Office of Information Management & Technology	0	N/A
Human Services	1	None found
Defense	4	None found for 3 of 4
Land and Natural Resources	10	None found for 6 of 10
Education	2	None found
Health	0	N/A

Source: Office of the Auditor

We further found RCUH allowed two state agencies to circumvent master agreement requirements, which undermined accountability. Six of seven projects we reviewed contained standard form contracts with all requisite terms and conditions needed to satisfy statutory requirements and the master agreement. However, we found that the Department of Education (DOE) contracted for RCUH services via a Memorandum of Agreement (MOA) in which the DOE was allowed to dictate its own terms and conditions, contrary to the master agreement terms and conditions. For example, the DOE contract does not require documentation of a governor's approval for the execution of the MOA or two subsequent amendments. DOE's position was that the department did not need governor's approval to utilize RCUH because the master agreement was not applicable. Additionally, the master agreement was not incorporated or referenced in the MOA, and there was no evidence that DOE justified the project qualified for RCUH services. RCUH provided administrative and research services to support a fiber optic network project in DOE schools under a \$65,490 contract.

RCUH also allowed the Department of Business, Economic Development and Tourism (DBEDT) to sidestep the master agreement's requirement for governor approval. That contract, in which RCUH provided administrative support for an internship program between August 2011 and June 2013, amounted to more than \$65,209 in expenditures. Requirements of the master agreement can be amended only by mutual agreement between the corporation and the State. However, we found that RCUH improperly accepted DBEDT's assertion that the contract did not require the governor's approval. Although the project is outside the scope of our audit, we note that RCUH provided services to DBEDT for a separate project in which DBEDT again took the position that it was exempt from obtaining governor approval.

According to the master agreement, issues regarding requirements, applicability, and exceptions to the agreement should be addressed by the Department of the Attorney General. However, RCUH did not seek assistance from counsel regarding DOE's purported exemption from the master agreement. We found that RCUH does not have a clear understanding of the requirements and applicability of the master agreement and that guidance related to compliance with statutory and contractual obligations are not clearly communicated to agencies requesting services. This unclear understanding of the applicability of master agreement requirements increases the risk that a state agency will violate the agreement, which exposes RCUH services to improper use.

### **Evaluations of \$4.3 million in state direct projects are not conducted**

The master agreement requires the State and RCUH to periodically review projects to ensure RCUH's continued administration is appropriate and conforms with the agreement's criteria for qualifying uses of RCUH services. Periodic reviews are to be conducted upon each project's renewal and at least every two years. We found no record of a periodic review of any of the \$4.3 million in state direct projects we examined. RCUH's project administration manager acknowledged that such periodic reviews should be conducted, but were not. Although the need for periodic reviews is clear under the master agreement, there are no RCUH policies or procedures for performing periodic reviews. A lack of periodic reviews to determine whether state agencies continue to qualify for RCUH services provides agencies the latitude to evade state requirements related to position ceilings, fund lapsing, and purchasing.

### **RCUH needs policies, procedures, and staff to ensure adequate acceptance and review of state projects**

RCUH's considerable flexibility from state purchasing and personnel requirements behooves the corporation to develop and implement clear policies and strong management controls over its state direct projects. As a contract administrator RCUH is responsible for retaining complete contract files that provide sufficient documentation to allow reconstruction of a contract and understand its history, in the absence of a contract administrator. A complete contract file should include the contract, invoices, and amendments, and meeting minutes. We found RCUH lacks written project management policies and procedures, and procedures for direct project approval acceptance.

RCUH procedure requires preliminary clearance from RCUH before the initiation of a state direct project request. RCUH accomplishes this through preliminary meetings with the requesting state agency. The purpose of this preliminary meeting is, among other things, to establish whether a proposed project qualifies for RCUH services prior to executing a project agreement. This important meeting, however, is rarely documented. One of seven project files reviewed documented that a preliminary approval meeting was held. Additionally, RCUH lacks internal policies or procedures requiring documentation of the preliminary approval meeting or for general file maintenance. The RCUH director of finance informed us the corporation recently adopted a direct project request form in 2014, which requires agencies to provide written justifications that projects are eligible for RCUH services. However, we note that use of this form is not required under RCUH's policies and procedures.

RCUH policies incorporate the acceptance criteria in the master agreement by reference but do not clearly enumerate the criteria. For example, RCUH policies refer to the need for state agencies to receive appropriate approvals but do not identify the parties with approval authority. In comparison, RCUH policies for UH revolving fund account projects contain explicit acceptance and approval criteria.

We also found that the corporation's project administration section lacks staff resources to ensure adequate acceptance and review of state direct projects. The RCUH project administration department comprises three individuals. Both the RCUH director of finance and project administration management said more staff are needed to handle all workload responsibilities. The RCUH director of finance said employees cannot be added because of budget constraints.

***Written policies and procedures could improve RCUH's oversight of UH intramural and UH revolving fund account projects***

RCUH provides accounting, disbursements, human resources management, and procurement services for approximately 400 UH intramural and 600 UH revolving fund account projects. We reviewed 29 intramural and 31 UH revolving fund account projects, which represented all projects closed in FY2014, and found that RCUH's process for accepting service orders, monitoring monthly cash balances, and closing out projects was adequate. However, we noted that RCUH lacks internal written project policies and procedures for establishing, monitoring, and closing these accounts. RCUH's lack of internal written policies and procedures unnecessarily increases project management risks because only two people service approximately 1,000 UH intramural and UH revolving fund account projects. RCUH could be left without policies and procedures if either, or both, of those employees left the corporation.

According to the U.S. Government Accountability Office (GAO) *Standards of Internal Control in the Federal Government*, internal control activities help ensure management's directives are carried out and are effective and efficient in accomplishing an agency's control objectives. Control activities are the policies and procedures, techniques, and mechanisms that enforce management's directives and ensure that actions are taken to address risks.

UH establishes intramural and revolving fund account projects at RCUH through service orders. These service orders also are required for all account updates for funding, extensions, renewals, amendments, and terminations. For UH intramural projects, a service order form is completed and approved by UH, then sent to RCUH for review and acceptance. Exhibit 2.7 shows the circumstances projects must meet to qualify for RCUH services.

## Exhibit 2.7

### Justifications for Qualifying for RCUH Services

**Intramural service order forms detail justifications to qualify a new project for RCUH services:**

- Involving a private organization;
- With unusual procurement problems, such as major items of special equipment, or complex equipment construction;
- In which much of the operation will lie outside the State;
- In which there are human resource problems which might be handled more effectively outside the State or UH personnel system;
- With a substantial amount of ship operations, technical shop-type operations, computer services, involvement with other RCUH projects, etc.;
- Involving research facility management where any combination of the above mentioned problems exist; or
- With other special problems that may be better resolved through the services of the RCUH.

Source: RCUH intramural project service order form

UH project personnel are required to identify any applicable justifications and provide a brief explanation of the project's scope of work.

For UH revolving fund accounts, a service order request form is completed and approved by UH, then sent to RCUH for review and acceptance. The service order should include a description of the project, anticipated users, distribution base, annual operating budget, annual recharge rates, and variance adjustments.

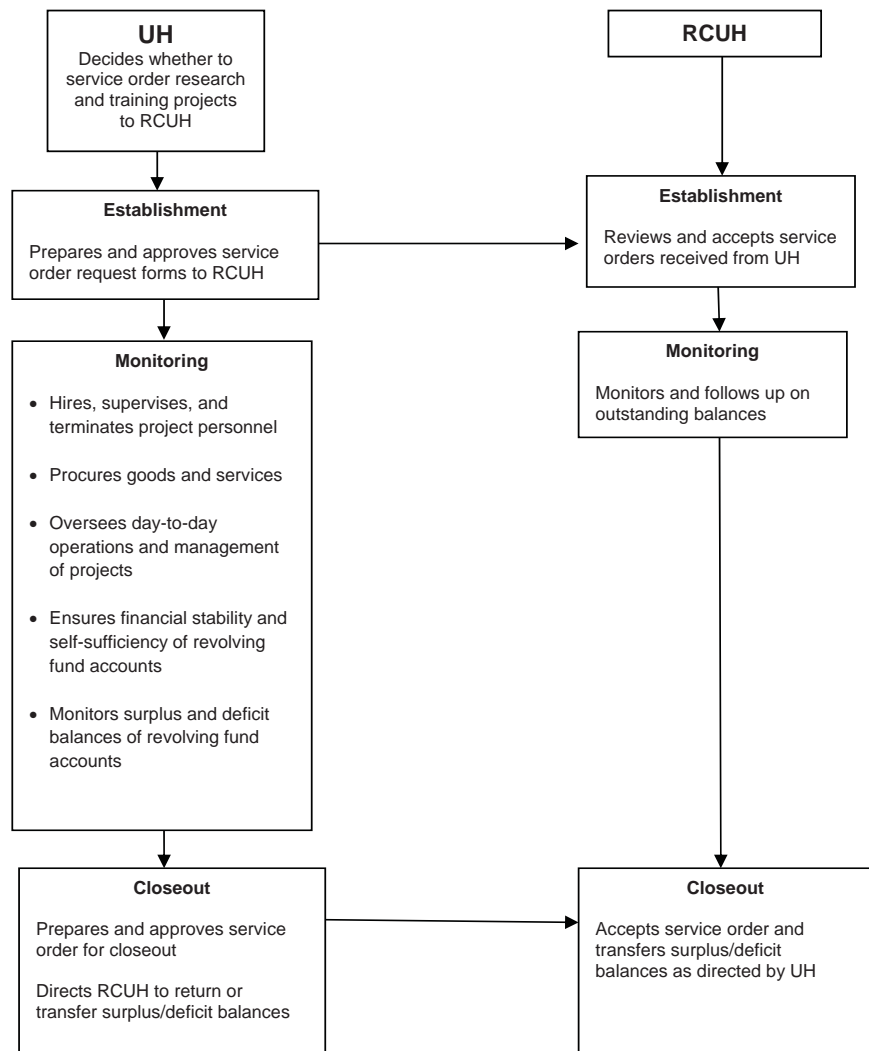
Based on interviews conducted with RCUH staff, we found the director of finance reviews UH intramural and UH revolving fund account service orders to ensure that they relate to research or training and are signed by all parties. For UH intramural projects, the director of finance reviews the service order form to ensure that at least one justification box is checked and the scope of work relates to that justification. Upon review by the director of finance, the service orders are accepted and logged.

RCUH's role in monitoring UH intramural and UH revolving fund account projects involves reviewing monthly reports. The project administration manager reviews reports and follows up with project personnel on outstanding balances through telephone calls and emails. UH is also responsible for the day-to-day operations and management of the intramural and revolving fund account projects. UH staff are responsible for procurement and hiring decisions for RCUH-serviced projects. At the end of a project, UH project personnel submit a service order to RCUH to request closeout with instructions on what to do with surplus or deficit balances. As directed by UH, account balances or deficits are transferred to similar RCUH accounts or returned to UH.

Exhibit 2.8 shows the service order process that directs RCUH servicing of UH intramural and UH revolving account projects.



## Exhibit 2.8 RCUH and UH Responsibilities for Intramural and Revolving Fund Account Projects



Source: Office of the Auditor

## Conclusion

The Legislature provided RCUH a broad mandate and accompanying powers to stimulate research and training. The Legislature intended that RCUH would play a proactive role to benefit Hawai'i's citizenry. In this, our second audit of RCUH, we found that a complacent, conservative leadership has resulted in a passive service provider that is almost entirely dependent on UH. We urge RCUH to renew its strategic planning efforts, which will enable it to better fulfill its mandate. The planning should include an accountability framework with goals, objectives, and performance indicators that can be used to assess

RCUH service quality and measure the extent to which the corporation accomplishes its mission. We also urge RCUH to improve its oversight of direct contracts with state agencies, particularly since board members have targeted this segment for growth.

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## Recommendations

1. The Research Corporation of the University of Hawai'i's Board of Directors should:
  - a. Adopt a mission that more accurately reflects the corporation's statutory responsibility to initiate and promote research and development statewide. If the board no longer thinks RCUH can fulfill its broad mandate, it should request that the Legislature redefine the agency's role;
  - b. Adopt a strategic plan that conforms to Act 100, SLH 1999, requirements by containing proper objectives and accounts for organizational changes needed to ensure fulfillment of all mandated duties;
  - c. Adopt and implement strategic planning and performance reporting policies and procedures;
  - d. Explicitly identify the corporation's executive director as being responsible for developing and implementing a strategic plan; and
  - e. Develop and update policies to ensure projects are accepted in conformance with Chapter 304A, HRS, the UH/RCUH Internal Agreement, and the State/RCUH Master Agreement.
2. The corporation's executive director should:
  - a. Implement a training program for board members that familiarizes them with their oversight roles and responsibilities;
  - b. Develop, adopt, and report on performance measures for assessing RCUH's accomplishment of its goals, objectives, and mission;
  - c. Consider and document whether added resources are needed to review incoming projects to determine whether they fall under the scope of RCUH services, and to monitor ongoing projects;

- d. Develop and implement procedures that include:
    - i. Detailed guidance for monitoring all projects;
    - ii. Ensuring periodic review of direct projects; and
    - iii. Reviewing and approving projects;
  - e. Ensure that requirements of the State/RCUH master agreement are complied with by agencies requesting services; and
  - f. Request the Department of the Attorney General issue a written opinion on whether certain state agencies are exempted from the State/RCUH Master Agreement.
3. The Legislature should consider amending Chapter 304A, HRS, to require RCUH to develop and, provide Act 100, SLH 1999, annual reports to the Legislature with goals, objectives, and policies; an action plan and timetable; and the process the corporation will use to measure program performance in meeting its goals and objectives.

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## Responses of the Affected Agency

### Comments on Agency Responses

We transmitted a draft of this report to the Research Corporation of the University of Hawai‘i and its board on May 19, 2015. A copy of the transmittal letter is included as Attachment 1. On May 27, 2015, we received responses from the board chair, and the executive director, which are included as attachments 2 and 3, respectively.

#### *Board chair’s response*

In his response, the board chair did not dispute our findings. The chair said the board will review the corporation’s mission and make changes as needed, but that the current mission was appropriate. He also said the board will work with the executive director to ensure policies and procedures are reviewed and updated. The chair agreed that RCUH needs strategic and long-range goals, objectives, and performance measures. However, he said it is RCUH’s position that Act 100, 1999 Session Laws of Hawai‘i, does not apply to RCUH because the corporation does not receive legislative appropriations. We note that Act 100 applies to every department and agency of state government. Our report recommends the Legislature amend Chapter 304A, Hawai‘i Revised Statutes (HRS), to require RCUH to develop an Act 100 annual goals and objectives report in order to ensure RCUH fulfills its strategic planning responsibilities.

We also found that RCUH’s inadequate planning, coupled with a passive business approach, resulted in the corporation’s near complete dependence upon UH. Our report noted that RCUH’s current UH service-provider role does not comport with the Legislature’s intention that the corporation proactively promote and enhance research and training. The board chair stated that our audit did not take into account the legislative intent of creating RCUH, or the statutory composition of the board, which both skew toward providing services to the University of Hawai‘i (UH). The chair misses our larger point that the RCUH board adopted initiatives to grow and diversify the corporation’s business in 2004, but failed to ensure their implementation.

#### *Executive director’s response*

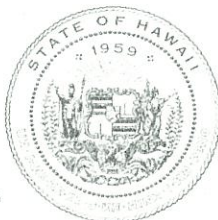
The RCUH executive director, in his response to our audit, did not dispute our findings; however, he disagreed with our recommendation that the Legislature amend Chapter 304A, HRS, to require RCUH to develop and provide annual reports with goals and objectives. He said it will be recommended to the next executive director to follow-up on

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our recommendations by enhancing board orientation and establishing performance measure parameters. Additionally, the executive director said RCUH is updating its policies and procedures and is developing guidelines as needed. The executive director further stated that RCUH will not execute any direct project agreements or amendments without approval from the governor, and that all state agencies will be required to comply with the State/RCUH master agreement.

Accordingly, we stand by our findings but made minor technical changes for accuracy and clarity.

STATE OF HAWAII  
OFFICE OF THE AUDITOR  
465 S. King Street, Room 500  
Honolulu, Hawaii 96813-2917



JAN K. YAMANE  
Acting State Auditor  
(808) 587-0800  
FAX: (808) 587-0830

May 19, 2015

**COPY**

Mr. James Karins  
Chairman  
Board of Directors  
Research Corporation of the University of Hawai'i  
2800 Woodlawn Drive, Suite 200  
Honolulu, Hawai'i 96822

Dear Mr. Karins:

Enclosed for your information are eight copies, numbered 6 to 13, of our confidential draft report, *Audit of the Research Corporation of the University of Hawai'i*. We ask that you telephone us by Thursday, May 21, 2015, on whether or not you intend to comment on our recommendations. Please distribute the copies to the members of the board. If you wish your comments to be included in the report, please submit your hard copy response to our office no later than 4:30 p.m., Thursday, May 28, 2015.

The Research Corporation of the University of Hawai'i, Governor, and presiding officers of the two houses of the Legislature have also been provided copies of this confidential 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,

A handwritten signature in cursive script, reading "Jan K. Yamane".

Jan K. Yamane  
Acting State Auditor

Enclosures



**The Research Corporation of the University of Hawaii**

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May 27, 2015

Ms. Jan K. Yamane  
Acting State Auditor  
State of Hawaii  
Office of the Auditor  
465 S. King Street, Room 500  
Honolulu, HI 968132917

**RECEIVED****2015 MAY 27 AM 11:14****OFF. OF THE AUDITOR  
STATE OF HAWAII**

Dear Ms. Yamane:

SUBJECT: Audit of the Research Corporation of the University of Hawaii

In 1965, the Legislature, in its wisdom, created the Research Corporation of the University of Hawaii (RCUH) "for the purpose of conducting and developing research projects . . . when it is determined that the University of Hawaii or any other State agency cannot as effectively and efficiently carry out such research projects." [Senate Standing Committee Report 836, 1965]

RCUH was established for the main purpose of serving the University of Hawaii (UH), as UH's entry into basic and applied research sponsored by the Federal government was growing rapidly, requiring a more agile operational environment, with less restraints of governmental regulations. Thus, RCUH is administratively attached to the UH per HRS § 26-35.

From inception, RCUH's Board of Directors was heavily skewed with University representation. RCUH's enabling legislation (Act 209, SLH 1965) outlined the Board composition as consisting of nine members, four of whom were from the UH:

- President
- Vice President of Academic Affairs
- Vice President of Business Affairs
- Director of Research

The State of Hawaii Director of Planning and Economic Development and four Gubernatorial appointees composed the rest of the Board back then.

Throughout the years, with amendments to the RCUH statute, the Board composition changed, and there were periods when UH representation decreased.

In 1995, the Legislature increased UH's presence on the Board to 50%, when five of the ten-member Board positions were reserved for UH Board of Regents' members. The statute further mandated that the President of UH also be the President of RCUH.

The most recent Board change took place in 2013 when the Legislature removed the UH President as President of RCUH and the Board composition changed to eight members:

- 2 Members of the UH Board of Regents
- 3 Gubernatorial Appointees:
  - 1 = business sector representative
  - 1 = UH research faculty representative
  - 1 = non-UH research organization representative
- 1 Senate President Appointee
- 1 House Speaker Appointee
- 1 UH Vice President for Research (ex-officio, non-voting)

So today, the UH is still heavily represented on the RCUH Board, owing to the fact that the University remains as RCUH's major client. The audit report does not take into account the legislative intent of creating RCUH or the statutory composition of the RCUH Board, which has been heavily weighted with representation from the University of Hawaii.

With the latest legislative action which affected the Board composition, the current Board has been in place for less than a year.

#### Auditor's Recommendations for the Board of Directors:

- We believe RCUH's current mission, "to support the research and training programs of the University of Hawaii and to enhance research, development, and training generally in Hawaii" remains appropriate. It provides the necessary latitude for RCUH to support the research enterprise of the University of Hawaii and the State of Hawaii.

RCUH's statute provides a broad spectrum of powers to the Corporation, and the Board exercises its discretion to set policy directions for RCUH within available capabilities and resources. The value of RCUH has been in the area of administrative support services, so that has continued to be a crucial role for RCUH. RCUH provides quality and timely service in a very efficient manner and at a reasonable cost. The University's/State's research enterprise depends heavily on RCUH because of its ability to meet the unique needs of research.

The Board will continually review the RCUH mission, evaluate and identify areas of growth/enhancement, and consider changes as necessary. The Board must ensure that RCUH remains relevant and continues to meet its statutory purposes.

- The current Board did discuss the need for a strategic/long-range plan. However, because the membership of the Board changed so significantly and the incumbent Executive Director also announced his intent to retire this year, the Board determined it would make more sense to develop the plan working with the new Executive Director. Therefore, the Board agreed to continue the practice of previous Boards to have the Executive Director annually submit a Strategy and Work Plan, which has been used as the basis for RCUH's goals and objectives for the short term.



The Board will be appointing a new RCUH Executive Director in June 2015. The Board's first task for the new Executive Director will be the development of a planning document, to include strategic/long-range goals and objectives for RCUH, including performance metrics. The Board is keenly aware of the need for a definitive road map and action plan for RCUH going forward, as such a plan will assist the Board in evaluating RCUH's performance as well as the Executive Director's effectiveness.

- The Board will continue to work closely with the Executive Director to ensure that RCUH policies and procedures are reviewed and updated on a regular basis and appropriate policies are in place to conform to all operational requirements.
- RCUH does not receive any appropriations from the Legislature. Therefore, the Board and its legal counsel do not believe that Act 100, SLH 1999, is applicable to RCUH because the Act's purpose is "to provide a basis for determining priorities and allocating limited public funds and human resources" for the Legislature.

Thank you for the opportunity to provide these comments on the report.



James P. Karins  
Chairman, Board of Directors

NOTE: Given the short turn-around time required to submit a response and because the Board must comply with the Sunshine Law, it has not met as a whole to discuss the report and this response.

**The Research Corporation of the University of Hawaii**

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May 27, 2015

Ms. Jan K. Yamane  
Acting State Auditor  
State of Hawaii  
Office of the Auditor  
465 S. King Street, Room 500  
Honolulu, HI 96813-2917

**RECEIVED****2015 MAY 27 AM 11:14****OFF. OF THE AUDITOR  
STATE OF HAWAII**

Dear Ms. Yamane:

SUBJECT: Audit of the Research Corporation of the University of Hawaii

Thank you for the opportunity to provide comments on the subject report's recommendations. Management of RCUH has prepared a response, which is attached. As noted in the attached, the RCUH Chairman will be responding separately on the items relating to the Board.

We are also attaching a list of technical corrections for your consideration.

Our thanks to Sean Hao and the rest of the audit team for their professionalism and courtesies throughout the audit.

Sincerely yours,

A handwritten signature in black ink, reading "Michael P. Hamnett".

Michael P. Hamnett  
Executive Director

Attachments



RCUH Management's Response  
to the Audit of the Research Corporation of the University of Hawaii  
The Auditor, State of Hawaii  
May 2015

The fundamental mission of the Research Corporation of the University of Hawaii (RCUH) is to **support** the research and training programs of the University of Hawaii (UH) and to enhance research, development, and training generally in Hawaii.

Through its fifty-year existence, RCUH has played a major supporting role to the University's and the State's research enterprise. RCUH's ability to remain flexible/adaptable and its exemption from certain state statutes has allowed it to perform more like a business by providing timely and efficient services, as the Legislature had intended.

The audit report references the 2004 Strategic Plan quite extensively and singles out the fact that no effort was made to expand and diversify RCUH's business.

Some parts of the 2004 Plan were implemented, including establishment of more training programs; piloting a new research facilitators program; assisting the University with their implementation of an electronic research administration system; and enhancing RCUH's on-line systems for financial and human resources management. We agree that other objectives in the 2004 Plan were not implemented. Attempts were made, but they proved to be unfeasible. Some progress was also made to expand RCUH's base of direct projects, although it was not a dramatic increase. RCUH's priority over the years was to continue to focus its services on the UH, its main client, in keeping with its legislative intent.

In 2009, RCUH established a two-year rolling strategy development and planning process linked to preparation of the RCUH budget. It was organized around the objectives of the 2004 Strategic Plan. It facilitated implementation of the 2004 objectives and provided a mechanism to update the Strategic Plan on an annual basis.

The authorities granted to RCUH in its statute are indeed very broad. However, in order for RCUH to provide more services and take a more proactive role, more resources are necessary. RCUH currently does not have the staff capabilities nor the financial resources to expand its scope of services to cover everything the statute provides. But perhaps this may be a reality in the future based on the priorities set by the Board of Directors and as additional resources become available.

Management's response to the applicable Report Recommendations follows. The Board of Directors will be responding to the Recommendations related to item 1.

Recommendations (pages 27-28)

2. The corporation's executive director should:

- a. Implement a training program for board members that familiarizes them with their oversight roles and responsibilities.

*Response: Board members are provided an orientation, which includes an overview of RCUH's enabling legislation, mission, Bylaws, operations, organizational structure, relationships, and other governance matters. It will be recommended that the new Executive Director work with the Board to further enhance the orientation process to provide the Board with a better understanding of its oversight roles and responsibilities.*



- b. Develop, adopt, and report on performance measures for assessing RCUH's accomplishment of its goals, objective, and mission.

*Response: It will be recommended that the new Executive Director work closely with the Board to establish the parameters for this recommendation based on a to-be developed strategic/long-range plan for RCUH.*

- c. Consider and document whether added resources are needed to review incoming projects to determine whether they fall under the scope of RCUH services, and to monitor ongoing projects.

*Response: The Project Administration section currently has a staff of 2 to handle the day-to-day operations encompassing approximately 500 UH Revolving, 400 UH Intramural, and 80 Direct projects. An additional staff position has been requested and is pending approval of our FY16 budget.*

- d. Develop and implement procedures that include:
  - i. Detailed guidance for monitoring all projects;
  - ii. Ensuring periodic review of direct projects; and
  - iii. Reviewing and approving projects.

*Response: RCUH is in the process of updating its policies and procedures as well as developing additional guidelines as needed. We expect to complete the revisions and additions in FY16. Earlier this fiscal year, we implemented a process that requires a Direct Project Request Form to be completed to ensure that there is proper justification and review prior to RCUH's acceptance of direct projects.*

- e. Ensure that requirements of the State/RCUH master agreement are complied with by agencies requesting services.

*Response: RCUH will not execute any project agreements or amendments without the required Governor's approval. For continuing projects, a Direct Project Continuation Request Form to document the continued need for RCUH services will be implemented and appropriate reviews with State agencies will be undertaken. Policies and procedures will be updated to ensure compliance with the State/RCUH Master Agreement.*

- f. Request the Department of the Attorney General issue a written opinion on whether certain state agencies are exempted from the State/RCUH Master Agreement.

*Response: All State agencies will be required to comply with the State/RCUH Master Agreement. Agencies requesting exemption shall be required to provide adequate justification and documentation. An Attorney General's written advice will be obtained for any exceptions prior to acceptance of the project.*

- 3. The Legislature should consider amending chapter 304A, HRS, to require RCUH to develop and provide Act 100, SLH 1999, annual reports to the Legislature with goals, objectives, and policies; an action plan and timetable; and the process the corporation will use to measure program performance in meetings its goals and objectives.

*Response: We do not believe this is necessary as Act 100 is not applicable to RCUH since we do not receive any legislative appropriations.*