Audit of the Hawai‘i Health Connector’s Mansha Contracts: Connector Board and Management Wasted and Abused Millions in Public Funds

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

Report No. 15-10
September 2015

THE AUDITOR
STATE OF HAWAI‘I

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.

3. Sunset evaluations evaluate new professional and occupational licensing programs to determine whether the programs should be terminated, continued, or modified. These evaluations are conducted in accordance with criteria established by statute.

4. Sunrise analyses are similar to sunset evaluations, but they apply to proposed rather than existing regulatory programs. Before a new professional and occupational licensing program can be enacted, the statutes require that the measure be analyzed by the Office of the Auditor as to its probable effects.

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.

7. Procurement compliance audits and other procurement-related monitoring assist the Legislature in overseeing government procurement practices.

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.

Hawai‘i’s laws provide the Auditor with broad powers to examine all books, records, files, papers, and documents and all financial affairs of every agency. The Auditor also has the authority to summon persons to produce records and to question persons under oath. However, the Office of the Auditor exercises no control function, and its authority is limited to reviewing, evaluating, and reporting on its findings and recommendations to the Legislature and the Governor.

THE AUDITOR
STATE OF HAWAI‘I
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A Multitude of Missteps: Audit of the Hawai'i Health Connector's Mansha Contracts

Report No. 15-10, September 2015

Connector board and management wasted and abused millions of dollars in public funds

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State of Hawai'i

The Connector expected Mansha to be a "Swiss army knife" for the health exchange.

Management's hasty and inept procurement practices wasted more than $11 million in taxpayer moneys

Facing an April 17, 2013, federal deadline, the Connector first engaged Mansha Consulting LLC in March 2013 through an emergency sole-source procurement for $56,000 for IT system design review services. A month later, anticipating the federally required October 1, 2013, exchange go-live date, the Connector procured a second emergency sole-source contract with Mansha, for $12.4 million to oversee the integration of two IT systems into a single health insurance exchange.

We found that instead of taking steps to ensure it selected the most qualified vendor at the best price, the Connector awarded Mansha a multi-million dollar contract based on personal recommendations. In total, the Connector awarded $21.6 million in IT contracts to Mansha. The Connector also failed to sufficiently analyze Mansha's proposed fees to ensure contract amounts were reasonable, as required by federal procurement standards. Thus, the Connector could neither justify its selection of Mansha nor the fixed fees awarded for each of the two Mansha contracts. Furthermore, the Connector executed vague, poorly written contracts with flawed terms and conditions that prevented it from effectively monitoring and evaluating Mansha's performance.

Connector board's and management's inattention to contract administration abused public funds

We found that the Connector board and management paid little attention to contract administration and the Connector's organization lacked a contract administration function. By neglecting to establish a functional area dedicated to managing the Connector's numerous contracts, the board prevented staff from effectively administering any of its numerous contracts worth $176.7 million. Furthermore, the Connector was unable to demonstrate that the $15.3 million paid to Mansha were used as intended. The Connector did not approve its contract administration procedures until more than a year after the Mansha contracts were executed, and the former executive director did not ensure the administrator for the Mansha contracts was qualified.

The Connector also had no procedures for amending contracts. The former executive director executed a $168,000 contract amendment without the board's knowledge or approval. In addition, contracts were not amended to reflect changes in scope of work; and amendments that were made were not done timely. This led to higher contractual costs, further wasting public moneys, and could result in federal enforcement action. Such practices constitute abuse of public funds, which involves behavior that is deficient or improper compared to what a prudent person would consider reasonable and necessary business practice in the circumstances.

Agency response

The Connector agreed that our findings appeared consistent with material in our previous audit and information the Connector has made public during the last year. It said it shared our concerns about Mansha and other significant contractors and has worked to improve its procurement and contract management practices.

The Connector pointed out a number of items it considered inaccurate, including references to the executed versus effective dates of the contracts, our analysis regarding staffing requirements, and our conclusion regarding burden to taxpayers in the event of federal enforcement action. We addressed these and other minor technicalities prior to publication but stand by our findings.

Recommendations

Response

Prior Audits

For the full text of this and other reports, visit our website: http://auditor.hawaii.gov/

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

Submitted by

THE AUDITOR
STATE OF HAWAI‘I

Report No. 15-10
September 2015

Foreword

This is a report on our audit of the Hawai‘i Health Connector’s contracts with Mansha Consulting LLP. We conducted the audit pursuant to Section 435H-2(d), Hawai‘i Revised Statutes (HRS), which requires the Auditor to undertake annual audits of the Connector and submit the results to the Connector and the insurance commissioner.

We wish to express our appreciation for the cooperation and assistance extended to us by the members of the Hawai‘i Health Connector’s board, its executive director and staff, 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

During our previous *Audit of the Hawai‘i Health Connector* (Report No. 15-01), we encountered an area of concern that we were unable to follow up on and which warranted further study. Specifically, we could not determine whether or not fees paid to Mansha Consulting LLC (Mansha) were reasonable because the Hawai‘i Health Connector was unable or unwilling to provide requested information for these contracts, which totaled $21.6 million. This audit was conducted to assess the Hawai‘i Health Connector's procurement and monitoring of its contracts with Mansha.

This audit was also conducted pursuant to Section 435H-2(d), Hawai‘i Revised Statutes (HRS), which requires the Auditor to undertake annual audits of the Connector and submit the results to the Connector and the insurance commissioner. Section 23-9, HRS, also requires that the Auditor submit all reports to the Legislature and governor.

Background

In 2010, the federal *Affordable Care Act* (ACA), designed to expand access to health insurance and curb rising health care costs, became law. The ACA required every state to establish a health exchange to help qualified individuals and small employers shop for, select, and enroll in affordable private health plans.

The Hawai‘i Health Connector was established as the state's health insurance exchange to meet the requirements of the ACA. Created in 2011 under Chapter 435H, HRS, as a nonprofit corporation, the Connector's purpose was to:

- Facilitate the purchase and sale of qualified health plans and qualified dental plans;
- Connect consumers to the information necessary to make informed health care choices; and
- Enable consumers to purchase coverage and manage health and dental plans electronically.

The Connector's mission was "to create a health insurance exchange that conforms to the requirements of the (ACA), is responsive to the unique needs and circumstances of Hawai'i, and reduces the number of uninsured by providing a transparent marketplace, conducting consumer

education and assisting individuals in gaining access to assistance programs, premium assistance tax credits, and cost-share reductions." The Connector was also designed to provide information on all qualified health care plans, offer consumer assistance in a culturally and linguistically appropriate manner, and make plans available to qualified individuals and employers.

Hawai‘i chose to implement its health insurance exchange by using two separate information technology (IT) systems. One was the Connector's web-based portal, the Hawai‘i Health Insurance Exchange (HHIX), which determines applicants' eligibility and allows them to shop for and enroll in the exchange's health care plans. The other was the state Department of Human Services' (DHS) system, Kauhale On-line Eligibility Assistance (KOLEA), which is used to enroll applicants who are eligible for Medicaid or the Children's Health Insurance Program (CHIP).

Hawai‘i Health Connector organization

At the time of our audit, the Connector was governed by a 14-member Board of Directors, headed by an executive director appointed by the board, and had 30 full-time employees and 16 temporary hires.

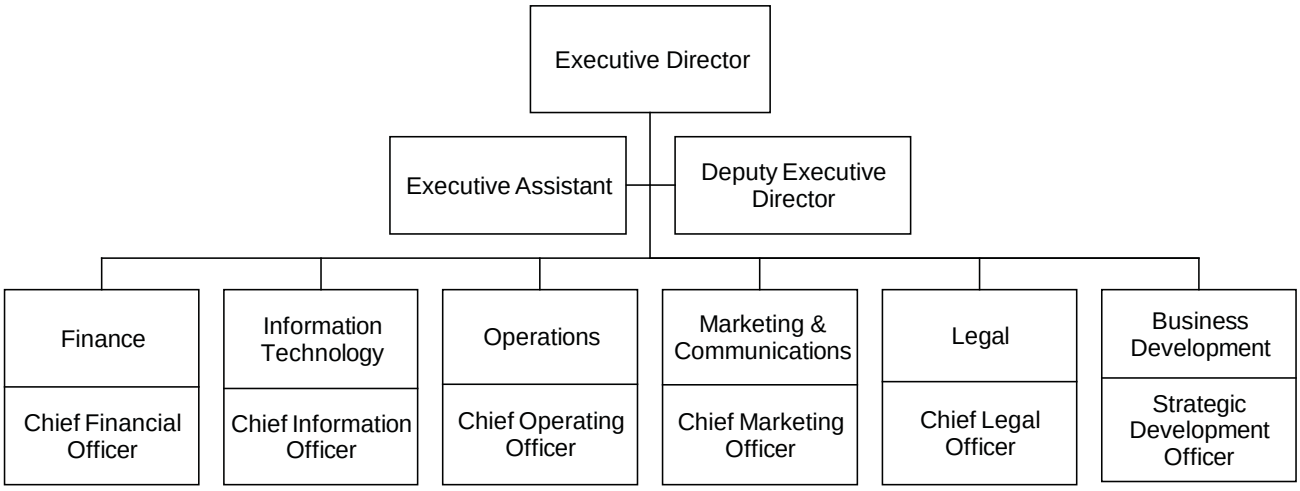
Board of Directors

Nine board members were appointed by the governor and five were ex-officio members. One ex-officio member was the State's formal representative on the board. The other four ex-officio members—who included the directors of commerce and consumer affairs, health, human services, and labor and industrial relations or their designees—were non-voting members. Members must have had education, training, or professional experience in at least one of nine areas specified in law, and served without compensation. Appointed board members served staggered terms determined by the governor; ex-officio members served for their entire term of office. The board elected its own chair, vice chair, treasurer, and secretary. Federal regulations required the Connector to have policies on ethics, conflict of interest, accountability and transparency, and disclosure of financial interests.

Connector staff

During the time period under audit, Connector staff were organized into six major functional areas: finance, information technology, operations, marketing and communications, legal, and business development. Exhibit 1.1 shows the Connector's organizational chart as of September 17, 2013.

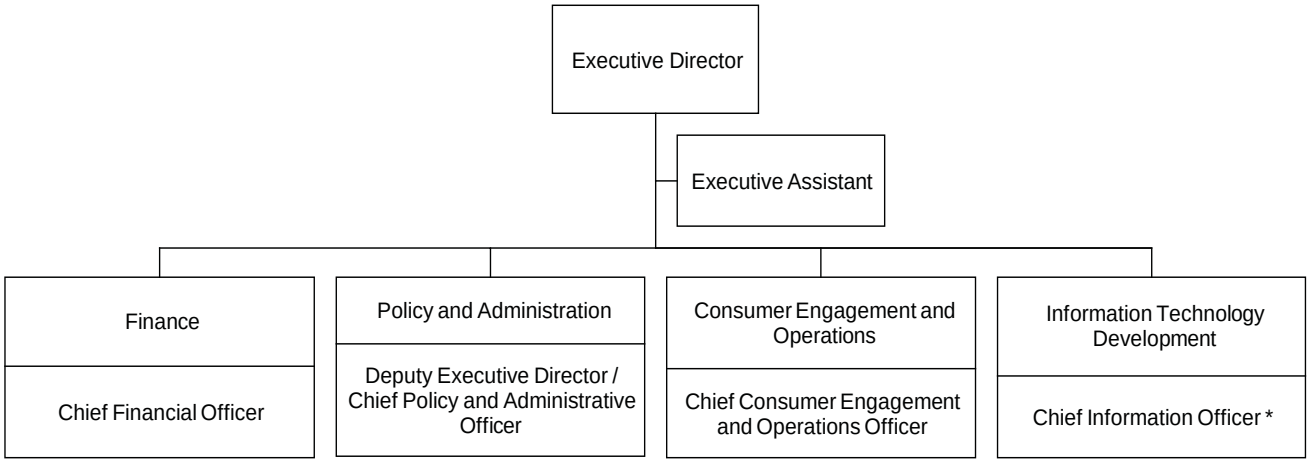
Exhibit 1.1
Hawai‘i Health Connector Organizational Chart as of September 2013



Source: CW Associates (Hawai‘i Health Connector’s independent auditor for fiscal years ended June 30, 2013 and 2014)

The Connector subsequently restructured; during our audit work, its staff were organized into four major functional areas: finance, policy and administration, consumer engagement and operations, and information technology development. Exhibit 1.2 shows the Hawai‘i Health Connector’s organization as of January 15, 2015.

Exhibit 1.2
Hawai‘i Health Connector Organizational Chart as of January 2015



* Contractor
Source: Hawai‘i Health Connector

Connector procurements

The Connector's procurement policy governed its purchases of equipment, goods, and services. The policy was established to ensure that materials and services were obtained in an effective manner and in compliance with federal procurement standards. It required all procurement transactions to be conducted in a manner that provides, to the maximum extent practical, open and free competition.

Procurements of less than $1,000 required only reasonable efforts to obtain the best value to the Connector. For procurements of $1,000 to $100,000, the executive director evaluated price or rate quotations from qualified sources and entered into contracts at his or her discretion. The board evaluated and authorized contracts for procurements more than $100,000, including amendments and multiple awards to the same vendor that exceeded $100,000. The executive director decided the procurement method to be used.

The Connector's policy allowed for five different methods of procurement:

- Procurements of *less than $1,000*;

- Procurement by *small purchase* procedures ($1,000–$100,000). In this relatively simple and informal procurement method for securing services, supplies, or other property that did not cost more than $100,000, a price or rate quotation had to be prepared for an adequate number of qualified sources;

- Procurement by *competitive proposals* (request for proposals). In this method, a request for proposals was advertised, proposals were solicited from multiple vendors, and either a fixed price contract or a cost reimbursement type contract was awarded. Generally, competitive proposals were used when conditions were not appropriate for sealed bids;

- Procurement by *noncompetitive proposals*. This method was for procurements more than $100,000 that were obtained by soliciting a proposal from only one source (*sole source*), or when, after soliciting quotes from a number of sources, competition was determined inadequate. For this method, a cost analysis verifying proposed cost data, data projections, and evaluation of specific cost and profit elements had to be prepared. This method could only be used when awarding a contract under one of the other procurement methods was infeasible, and either: the item was available only from a single source, public necessity or emergency would not permit delay resulting from competitive solicitation, the U.S. Department of Health and

Human Services (DHHS) authorized the noncompetitive method, or competition was determined inadequate after solicitation of a number of sources; and

- Procurement by *sealed bids*. In this method, bids were publicly advertised and a firm fixed contract (lump sum or unit price) was awarded to the responsible bidder whose bid, conforming to the material terms and conditions of the invitation for bids, was the lowest price.

Connector contract administration and monitoring

The Connector's Contract Administration Procedures were approved by its interim executive director on February 27, 2014. Pursuant to these procedures, a contract administrator, who was appointed by the executive director at the time a contract was executed, was responsible for:

- Preparing a written contract administration plan appropriate for the detail and complexity of the specific contract. Contract administration plans were to be consistent with contract terms and include a deliverables tracking list, expenditure budget data, and any other pertinent information. Copies of each plan were to be provided to finance staff and made easily accessible for internal monitoring and compliance;

- Preparing post-award orientation materials and documentation. This orientation occurred between the contract administrator and relevant Connector staff and vendor representatives after the contract was fully executed. The orientation was to ensure that all parties had a clear and mutual understanding of all contract deliverables and other requirements, the Connector's administration process, and the rights and obligations of all parties to the contract;

- Monitoring vendor progress based on contract terms and deliverables;

- Tracking and matching deliverables to invoices, receipts to expense reports, and reviewing them for disallowed costs;

- Producing all correspondence and communications with the vendor regarding invoices, deliverables, and disallowance of costs; and

- Closing the contract upon the vendor's completion of work. This included comparing the vendor's actual performance against the goals and objectives of the contract, documenting any deficiencies, and communicating any such deficiencies to the appropriate parties.

Connector funding and expenditures

Almost all of the Connector's funding came from federal grants. Since 2011, the DHHS provided the Connector three different grants totaling $204.3 million to build a health insurance exchange and develop infrastructure needed for the exchange's ongoing operations. As part of its grant conditions, the Connector was subject to DHHS oversight and had to abide by DHHS' Grants Policy Statement and award-specific requirements for each grant. The Connector was also subject to cost principles and administrative requirements set forth in various federal regulations. Exhibit 1.3 details how the Connector used its grant funds.

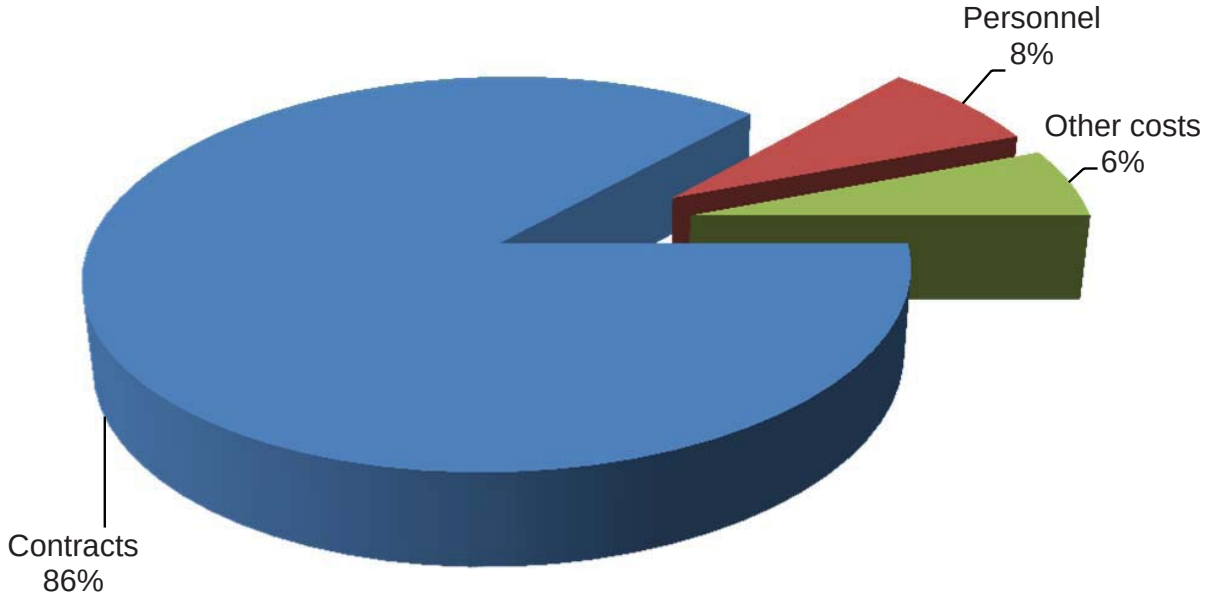
Exhibit 1.3
Connector Grant Fund Activity, November 29, 2011 through June 30, 2014

	Total Grant Award	Expended Funds	Obligated Funds	Unobligated Funds as of June 30, 2014
Contracts	$176,715,514	$86,447,951	$32,703,948	$57,563,615
Personnel	15,598,783	7,788,711	0	7,810,072
Other costs	12,027,973	10,131,536	0	1,896,437
Totals	**$204,342,270**	**$104,368,198**	**$32,703,948**	**$67,270,124**

Source: Hawai'i Health Connector 2014 Annual Report

As shown in Exhibit 1.4, the vast majority of the Connector's grant funds (86 percent) were used to hire contractors.

Exhibit 1.4
Connector Grant Fund Usage, by Percentage



Source: Office of the Auditor

Mansha Consulting LLC

Mansha Consulting LLC was the Connector's second largest contractor; it had more than $21.6 million in contracts with the Connector (25 percent of the Connector's spent or obligated grant funds as of June 30, 2014). The Connector paid $15.3 million to Mansha under its two contracts through August 2014. The Connector did not pay for services rendered and invoiced from July 1, 2014 through December 5, 2014, when Mansha withdrew its team from the Connector project. The firm was established in May 2011 as a small healthcare IT consulting firm specializing in assisting states to become state-based marketplaces, leveraging the federally administered marketplace to implement the ACA, and aligning strategies and implementing technology to adhere to the parameters of the ACA. The Connector entered into two different contracts with Mansha, each of which were amended to provide for additional services that significantly increased Mansha's fees. Exhibit 1.5 shows the Connector's maximum obligations to Mansha under both contracts and their amendments.

Exhibit 1.5
Connector's Maximum Contractual Obligations to Mansha

Contract or Amendment	Contract Period	Contract or Amendment Amount	Cumulative Contract Total
1) Agreement for Design Review Consulting Services (DRCS)	March 28, 2013 to April 15, 2013	$56,000	$56,000
Amendment 1 – Extended term and scope of services	April 16, 2013 to May 31, 2013	$168,000	**$224,000**
2) Integrated Project Management Office (IPMO) Contractor Agreement	April 26, 2013 to April 25, 2014	$12,360,650	$12,360,650
Amendment 1 – Added provisions related to the Social Security Act	No change	No change	$12,360,650
Amendment 2 – Removed provisions related to the IPMO governance structure	No change	No change	$12,360,650
Amendment 3 – Extended term and increased scope of services and fees	April 26, 2013 to April 25, 2015	$9,059,367	**$21,420,017**
Total Mansha contracts			**$21,644,017**

Source: Office of the Auditor

Agreement for Design Review Consulting Services

The Connector first engaged Mansha in March 2013 for $56,000 to provide consulting services to help the Connector prepare for a federal review of the HHIX system. This contract was amended in April 2013 to extend the contract term and increase Mansha's fees by a maximum of $168,000 because the federal review was delayed and additional services were required. The amendment also increased the scope of Mansha's

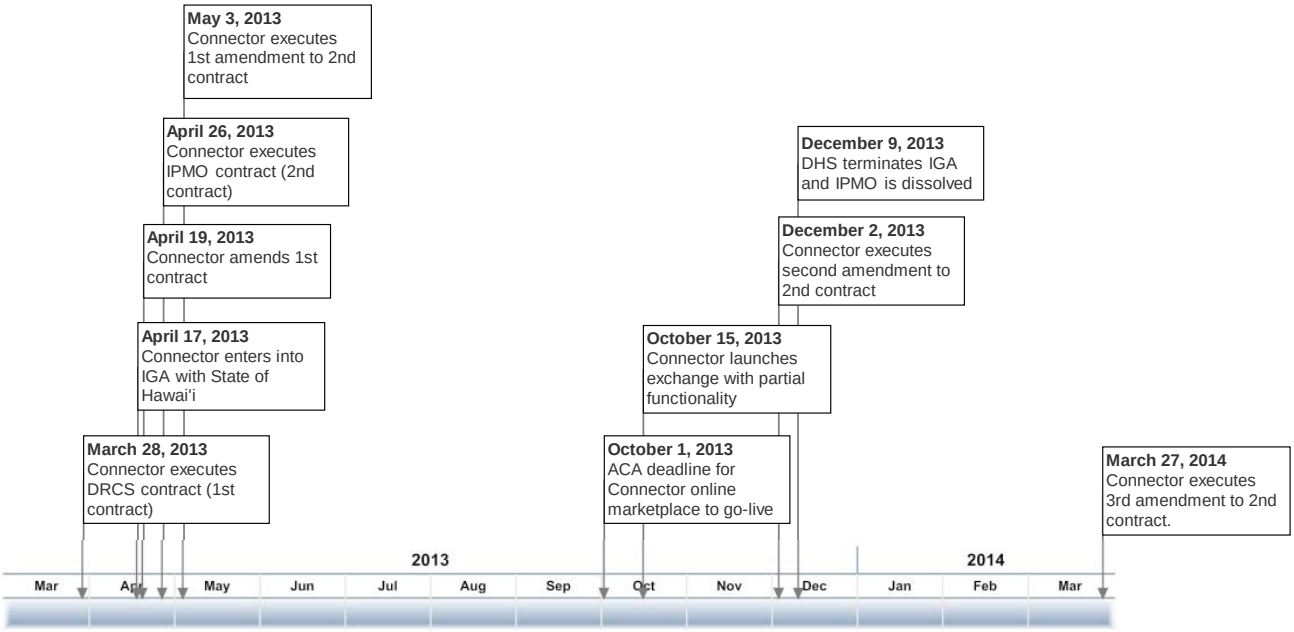
services to include implementing an Integrated Program Management Office (IPMO) to manage implementation of the HHIX.

Integrated Project Management Office Contractor Agreement

Seven days after it amended its first contract with Mansha, the Connector entered into a $12.4 million contract with Mansha to act as an IPMO. As IPMO, Mansha was to manage, facilitate, and oversee the decision-making process on, and to maintain transparency of, all matters related to integrating the Connector's HHIX system and DHS' KOLEA system. The Connector amended this second contract three times. The first amendment added a provision related to the Social Security Act. The second amendment removed provisions related to an Integrated Governance Agreement (IGA) that created the IPMO and its governance structure. The third amendment increased the original fees to $21.4 million, not including taxes and travel expenses, extended the contract term, and changed the scope of Mansha's work from being the Connector's IPMO to being its Project Management Office (PMO) and Systems Integrator.

Exhibit 1.6 illustrates key events related to the Connector's contracts with Mansha.

Exhibit 1.6
Timeline of Key Events Related to the Mansha Contracts, March 2013 to March 2014



Source: Office of the Auditor

Prior Audits

Our previous *Audit of the Hawai'i Health Connector* (Report No. 15-01), released in January 2015, found that the Connector Board of Directors' inadequate planning led to an unsustainable health exchange and the Connector did not have IT staff to manage the project's development or monitor contracts, relying on vendors to self-report their progress. We also found the Connector did not properly procure and administer its contracts and monitor costs, putting its federal grants at risk. We raised concerns over the reasonableness of fees paid to Mansha Consulting LLC, which we believed warranted further study.

The Connector also underwent three financial audits to comply with federal Office of Management and Budget (OMB) Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*, for the fiscal years ended June 30, 2012, 2013, and 2014. These audits were conducted by independent certified public accounting firms. The audit for fiscal year ended June 30, 2012, reported the Connector had not accrued certain costs for legal and other professional services that totaled approximately $479,000 as of June 30, 2012; did not have formal policies and procedures governing its procurement process until May 2012; and did not have formal policies and procedures in place to ensure compliance with OMB Circular A-122, *Cost Principles for Non-Profit Organizations*, or govern its cash management process. No findings were reported in the audits for fiscal years ended June 30, 2013, and June 30, 2014.

Objectives of the Audit

1. Assess the Hawai'i Health Connector's procurement of its contracts with Mansha Consulting LLC.
2. Assess the Connector's monitoring of its contracts with Mansha.
3. Make recommendations as appropriate.

Scope and Methodology

We examined the Hawai'i Health Connector's practices for administering and overseeing its federally funded contracts with Mansha Consulting LLC and payments under such contracts from FY2013 through FY2015. We evaluated whether the Connector's procurement practices resulted in appropriate contracts and contract amounts, and whether the Connector's practices held Mansha accountable for contract performance and allowed the Connector to manage related grant fund expenditures to ensure they were reasonable.

We reviewed the Mansha contracts, organizational bylaws, meeting minutes, policies and procedures, operating reports, grant documents, best practices, and other relevant documents and records in order to assess the board's and management's oversight of the Connector and its business operations. We also conducted interviews with board members, key employees, contractors, state government agency personnel, and other parties as appropriate.

Our work was performed from December 2014 through May 2015 and conducted pursuant to the Office of the Auditor's *Manual of Guides* and according to 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.

Auditor's access to information

The Office of the Auditor has broad authority to access information. Section 23-5, HRS, gives the Auditor authority to examine and inspect all accounts, books, records, files, papers, documents and all financial affairs of every department, office, agency, and political subdivision of the State. Although the Connector was established by law as a Hawai‘i nonprofit organization, Section 435H-2(d), HRS, requires the Connector to be audited annually by the Auditor, who is specifically permitted to access, inspect, and make copies of any documents, papers, books, records, or other evidence pertinent to the Connector's budgets and operations. The Connector's bylaws also require an annual audit by the Auditor and specify the Connector shall permit the Auditor to have access to, inspect, and make copies of any relevant documents.

Although the Connector cooperated with our requests for information, it produced very little documentation relating to the Mansha contracts. The Connector's former legal counsel told us his laptop contained files related to the Mansha contracts; however, the Connector was unable to prove such files existed. As a result, we had no assurance that documents were complete or in existence prior to our review.

Chapter 2

Connector Board and Management Wasted and Abused Millions in Public Funds

Hawai‘i’s Health Connector was awarded more than $204.3 million in federal funds since its inception in 2011, which it used to hire contractors and staff and establish a health insurance exchange to comply with the federal *Affordable Care Act* (ACA). By June 30, 2014, the Connector had allocated $176.7 million (86 percent) of those funds on contracts, and spent or obligated more than $92.2 million (45 percent) on information technology (IT). Approximately a quarter of its IT funds, $21.6 million, was awarded to Mansha Consulting LLC, making Mansha the Connector’s second largest contractor.

Our previous audit, which found that the Connector did not properly procure and administer its contracts or monitor costs, also found several issues with a $12.4 million, sole-source Mansha contract. For instance, the Connector selected Mansha despite serious concerns raised by the Connector’s board. Because the Connector did not provide us with cost information we requested, we were unable to determine whether or not Mansha’s fees were reasonable. And the Connector’s contract files were missing most required procurement records and contract administration documentation for many of its contractors. In response to our prior audit recommendations, the Connector reported it is in the process of adopting and implementing new policies and procedures governing procurement and contract administration that address deficiencies identified in that audit. However, the Connector did not expect to complete the documentation process for the new policies and procedures until the end of 2015 due to its constrained resources.

Our current audit likewise found that the Connector’s contract procurement and administration was seriously flawed, as embodied in its dealings with Mansha. The board’s and management’s ineptitude at overseeing and managing the Connector’s procurement and inattention to contract administration activities wasted and abused millions of dollars in public funds and left the Connector unable to demonstrate whether it complied with the terms and conditions of its federal grants.

During the course of this audit, the Connector’s board agreed to comply with the State’s corrective action plan to switch the Connector to a state-supported, federally facilitated marketplace. The transition will take place in three stages, and all Connector staff and contractors will be eliminated by May 2016. However, even as the Connector shuts down its operations, it is imperative that its activities be transparent and accountable and its records accessible.

Summary of Findings

1. The Hawai‘i Health Connector’s management failed to follow appropriate procurement practices, wasting more than $11 million in taxpayer moneys. The Connector had poor justification for selecting Mansha or determining contract amounts, and faulty contracts precluded the Connector from effectively monitoring Mansha’s performance. As a result, it is unclear whether Mansha fulfilled is contractual duties.

2. The Connector board’s and management’s inattention to contract administration constituted abuse of public funds. The board neglected to ensure staff effectively administered the Mansha contracts. Management was unable to demonstrate that the millions of dollars it paid to Mansha achieved the intended results, and the Connector had no procedures for amending contracts.

Management’s Hasty and Inept Procurement Practices Wasted More Than $11 Million in Taxpayer Moneys

Facing an April 17, 2013, federal deadline, the Connector first engaged Mansha in March 2013 through an emergency sole-source procurement for $56,000 for IT system design review services. A month later, anticipating the federally required October 1, 2013, exchange go-live date, the Connector procured a second emergency sole-source contract with Mansha, for $12.4 million, to manage and oversee the integration of two IT systems into a single health insurance exchange. If it missed these deadlines, the Connector risked losing its federal grants and the State would be forced to use the federally facilitated exchange.

We found that the Connector management’s procurement of Mansha’s services was hasty, inept, and wasted more than $11 million in taxpayer moneys. Instead of taking steps to ensure it selected the most qualified vendor at the best price, the Connector awarded Mansha a multi-million dollar contract based on personal recommendations. The Connector also failed to perform sufficient cost analyses of Mansha’s proposed fees to ensure contract amounts were reasonable, as required by federal procurement standards. Thus, the Connector could neither justify its selection of Mansha nor the fixed fees awarded for each of the two Mansha contracts. Furthermore, the Connector executed vague, poorly written contracts with flawed terms and conditions that prevented it from effectively monitoring and evaluating Mansha’s performance.

Connector had poor justification for selecting Mansha or determining the fees for each contract

The Connector awarded contracts to Mansha totalling about $21.6 million, making Mansha its second-highest paid contractor. Rather than ensuring Mansha possessed the qualifications and expertise necessary for managing and overseeing the integration of two IT systems, the Connector's former executive director primarily relied on personal recommendations to select this critically important vendor. Additionally, the Connector agreed to Mansha's fees without sufficiently analyzing them for reasonableness and in accordance with federal requirements for cost analyses. By our calculations, the Connector over-obligated itself to Mansha by $8.2 million (66 percent of the original second contract amount) and inappropriately obligated federal grant funds for questionable costs totaling $3.4 million, thereby wasting approximately $11.6 million in public funds.

Contracts should be fairly awarded to responsible vendors[1] who are able to successfully meet the terms and conditions of a proposed contract.[2] Federal procurement standards also require that cost analyses be performed prior to awarding a contract to ensure the amounts are reasonable.[3] Such practices ensure that organizations select the most qualified vendors at the best price. We found that the Connector's procurement policies mirrored federal requirements for small purchase procurements and noncompetitive proposals, but lacked specific guidance to help staff conduct procurements properly. For instance, policies lacked criteria for identifying potential vendors from whom to solicit proposals or for evaluating contractors for small purchases and sole-source procurements. These omissions likely contributed to the questionable process the former executive director used to award the Mansha contracts.

Federal procurement standards also require maintaining sufficient details of a procurement's history.[4] Records must include a rationale for the selected procurement method, justification for any noncompetitive procurements and the basis for contractor selection and award amount.[5] The Connector's own policies also require contract files to contain all source documents supporting any given transaction, including a record of a cost or price analysis, to ensure a clear and consistent audit trail.[6] Contrary to these standards, the Mansha contract files contained very little information validating the Connector's determination that Mansha was best suited to meet the Connector's needs and its proposed fees were reasonable.

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[1] National State Auditors Association, *Contracting for Services, A National State Auditors Association Best Practices Document*, June 2003, p. 2.

[2] Title 45 Code of Federal Regulations Part 92.36 and Hawai‘i Health Connector Procurement Policy, Article V, Section 4.

[3] Title 45 CFR Part 92.36.

[4] Ibid.

[5] Ibid. and Title 2 CFR Part 215.46.

[6] Hawai‘i Health Connector Procurement Policy, Article IX, Sections 1 and 2.

Connector's former executive director primarily relied on personal recommendations to award contracts to Mansha

Mansha Consulting LLC was established in 2011 as a start-up healthcare IT consulting firm, operated out of a single-family home in Virginia. We found scant other information available about this relatively new company. Despite it being a small, young company with a limited track record, the Connector's former executive director selected Mansha based on a list of recommended vendors from the Connector's former IT consultant and Mansha's reputation with the federal Centers for Medicare & Medicaid Services and the state of Maryland. According to a procurement memo, Mansha was selected because of its prior experience implementing ACA-compliant health insurance exchange information systems, which the Connector confirmed with officials from the federal Center for Consumer Information and Insurance Oversight (CCIIO) and the Maryland Health Benefits Exchange.

However, the Connector was unable to provide us with sufficient evidence that it ensured, prior to awarding the contracts, Mansha possessed the expertise and qualifications needed to successfully complete the work for either contract. The Connector's files contained very little information substantiating Mansha's expertise and qualifications for the required services, the nature and extent of the Connector's actions to confirm Mansha's past performance and experience, or how the Connector determined that Mansha was capable of performing the required services and meeting the Connector's needs under the proposed contracts.

Further, the Connector did not really know what it wanted out of a contractor. The Connector's former legal counsel acknowledged that the Connector did not know "exactly what level of effort or skill sets would be required" to complete the work when it awarded the second ($12.4 million) contract to Mansha. We question how the Connector was able to determine that Mansha was qualified without first identifying the scope of work needed to complete the project, what specific qualifications would best address the project's needs, and the criteria for evaluating potential vendors.

Mansha's proposed fees were awarded without sufficient cost analysis, and renewal violated federal grant condition

The Mansha contracts were subject to federal procurement standards and the Connector's own procurement policy. Both required a cost analysis for every procurement and contract modification.[7] Cost analyses should include verifying proposed cost projections and evaluating specific cost and profit elements to ensure that a contract amount is reasonable

[7] Title 45 Code of Federal Regulations Part 92.36 and Hawai'i Health Connector Procurement Policy, Article VII, Section 1.

and contract files for procurements exceeding the $100,000 simplified acquisition threshold should also include a record of the basis for costs awarded and a supporting cost analysis.[8]

The Connector was unable to demonstrate that it performed a cost analysis for either Mansha contract or their amendments that both substantiates the contract amounts and complies with applicable federal procurement standards. Mansha's first contract, for $56,000, was later increased by $28,000 per week up to $168,000 for additional services, but the Connector could not provide any evidence of a cost analysis for this contract or its amendment. Likewise, and much more alarming, Mansha's second contract, originally for $12.4 million, for project management and system implementation services, was later increased to $21.4 million, yet the limited documentation the Connector provided failed to demonstrate that the cost analyses performed adhered to the applicable requirements. For the first contract, we found neither support for the original or renegotiated contract amounts, nor evidence that costs were analyzed for reasonableness in accordance with federal procurement standards and the Connector's own policies. For the second contract, fees were analyzed for the original and renegotiated contracts, but the limited documentation in the contract files did not demonstrate the analyses complied with federal procurement standards and the Connector's own policies.

Our analysis identified discrepancies in the award amounts that resulted in excessive contract costs. Mansha's second contract ($12.4 million over 12 months, with an option to extend) reflected the fixed price and period that Mansha proposed, which contemplated a team of 20 people working for a year. However, the Connector subsequently agreed to a staff of 16 but did not reduce the contract price by the cost of those four excluded positions. In addition, the project was to be completed, tested, implemented, and ready to accommodate and process open enrollment on October 1, 2013, just five months after the contract's effective date, rather than one year as contracted.

By subtracting four positions and seven months from the contract, we calculated that the Connector over-obligated itself to Mansha by $8.2 million (66 percent of the $12.4 million contract) when it entered into a one-year contract for a project that was to take only five months and which erroneously included costs related to four eliminated positions. The one-year contract term was unnecessary and excessive because the contract allowed the Connector to renew and extend the contract for up to one year should unforeseen issues delay completion of the integration project and require project management services beyond October 1, 2013.

[8] Title 45 CFR Part 92.36 and Hawai'i Health Connector Procurement Policy, Article VI, Section 4 and Article IX, Section 2.

Furthermore, in March 2014, the Connector exercised its renewal option and extended Mansha's second contract through April 2015 for an additional $9 million. Mansha's services under the renewal included operating and maintaining the Connector's IT system beginning in 2015. However, obligating federal grant funds for such services violated ACA's prohibition on using exchange establishment grant funds for continued operations. The Connector obligated $3.4 million in federal grant funds for Mansha's services that were to be rendered between January and May 2015—at a monthly fee of $677,843. This was not an allowable use of federal funds.

The Connector's former legal counsel acknowledged the Connector's contract cost analyses were generally weak, attributing it to the Connector's lack of information and desire to expedite procurements to meet tight deadlines. He said the Connector included in its contract a "termination for convenience" clause that it used as leverage to renegotiate any part of the contract. Furthermore, we found that the former executive director relied on the federal CCIIO and state Office of Information Management Technology (OIMT) to review the contract costs for reasonableness. However, neither of these approaches absolves the Connector from performing its own cost analyses. If the federal government denies the Connector the use of grant funds for the questionable costs it paid to Mansha, the Connector must repay grant funds with funds from another source—funds it currently does not have.

Contract terms and conditions prevented the Connector from effectively monitoring Mansha's performance

Contracts are a key mechanism for holding vendors accountable for their performance and reducing the risk of making improper payments. Terms and conditions should protect an agency's interests, identify each party's responsibilities, and define what is to be delivered as well as document the mutuality, substance, and parameters of the parties' agreement.[9] Contract administration should start with developing clear, concise, performance-based statements of work.[10]

However, we found that Mansha's second ($12.4 million) contract lacked clearly defined performance requirements because the Connector did not have a clear idea of what it wanted Mansha to do. As a result, the Connector executed a poorly written, vague contract that contained few performance standards, which prevented it from effectively monitoring Mansha's performance. Connector payments to Mansha were based on a contractual payment schedule rather than successful completion of agreed milestones and deliverables. Furthermore, the Connector also overlooked its responsibility to review the Mansha contracts for propriety and to amend or remove flawed provisions.

[9] National State Auditors Association, *Contracting for Services, A National State Auditors Association Best Practices Document*, June 2003, p. 3.

[10] Office of Federal Procurement Policy, *A Guide to Best Practices for Contract Administration*, October 1994.

Because the Connector was unable to adequately monitor Mansha's performance, it is unclear whether Mansha successfully completed its contractual duties. The former state chief information officer (CIO) thought Mansha accomplished its work to assist with implementing and integrating the state's health insurance exchange, and even recognized Mansha as contractor of the year in 2013. On the other hand, the succeeding state CIO said Mansha's efforts to implement the electronic file system transfer necessary to integrate the Connector system with the state Department of Human Services' Medicaid eligibility system, KOLEA, were unsuccessful. A contract with clearly defined contractual obligations and performance expectations would have precluded such disparate interpretations of Mansha's performance.

Lack of clarity on Mansha's roles and responsibilities led to vague, poorly written contracts

The federal CCIIO noted deficiencies in the Mansha contracts' scope of work descriptions and sought clarity on the nature of some tasks required of Mansha. CCIIO also commented that some provisions lacked verbs to clearly describe the work to be performed. As illustrated in Exhibit 2.1, one contract did not specify whether Mansha was meant to manage, design, change, and/or oversee development of a website.

Exhibit 2.1
Contract Provisions That Do Not Describe Action To Be Taken

1.1 In House Master Systems Integrator. The Contractor will:

(c) Business website www.hawaiihealthconnector.com, internal technical infrastructure related to SharePoint, Project Server, etc.

1.2 PMO. The Contractor will:

(a) Business website www.hawaiihealthconnector.com, internal technical infrastructure related to SharePoint, Project Server, etc.

Source: Third amendment to IPMO contract agreement with Mansha Consulting LLP

These flaws reflect management's poor planning and inability to clearly and accurately describe the scope of work it required of Mansha. The Connector's former legal counsel acknowledged that the scope of work in Mansha's second contract was "very broadly" stated. He reported this was due to management's lack of clarity on how much work was needed at the time the contract was drafted, combined with a mindset that Mansha would serve as the "Swiss Army knife for the state's exchange program."

Management failed to properly review and modify contracts prior to execution

Although the Connector properly leveraged the technical expertise of its IT consultant when developing the scope of work and related provisions for the second Mansha contract, management was unclear what Mansha's roles and responsibilities were to be and did not properly review and modify the Mansha contracts prior to their execution.

We found that the Connector's legal department drafted the second Mansha contract using the Connector's standard terms and conditions. The Connector then consulted with one of its IT contractors and others to develop the scope of work and related provisions. The Connector's former legal counsel reviewed the contract for compliance with federal guidelines, and briefed the board and its executive committee on the contract's terms, including the statement of work. However, we found no evidence that counsel or the executive committee reviews of the contract terms ensured they included provisions recommended by best practices that would allow the Connector to effectively monitor and evaluate Mansha's performance.

The second Mansha contract was also missing key provisions. Neither Mansha's second ($12.4 million) contract nor its amendments contained performance requirements such as work product standards; and provisions describing acceptable deliverables, measurable outcomes, and a schedule for completing work and deliverables were inadequate. While the contract's third amendment identified deliverables, it neither specified a timeline for completion nor indicated the frequency with which all but one of the deliverables were to be submitted. In fact, the amendment's pages-long list of deliverables were merely examples, and not actually required. Further, the amended contract required Mansha to produce monthly progress reports but did not specify what the reports were to contain. Contracts should include specific, measurable, required deliverables.[11] As a result of reviewing contracts merely for federally required provisions, management never identified or rectified inappropriate or missing contract provisions that should have adequately described Mansha's responsibilities and work requirements.

Moreover, the Connector sought CCIIO's feedback on provisions in the third amendment and CCIIO identified several "significant shortcomings." In neglecting to correct the deficiencies by further amending the contract, management failed to protect the Connector's—and therefore taxpayers'—interests and define specific, measurable deliverables. Ultimately, the Connector was unable to properly monitor Mansha's performance and determine whether it fulfilled its contractual obligations.

[11] National State Auditors Association, *Contracting for Services, A National State Auditors Association Best Practices Document,* June 2003, pp. 2, 3.

Connector Board's and Management's Inattention to Contract Administration Abused Public Funds

The Connector spent 86 percent of its budget on numerous contractors to support its operations, including information technology, call center management, health exchange solution management, independent verification and validation, human resources and payroll, legal services, and marketing. Thus, contract administration should have been among its core functions.

We found, however, that the Connector board and management paid little attention to contract administration. For example, the Connector's organization did not even include a contract administration function. By neglecting to establish a functional area dedicated to managing the Connector's numerous contracts, the board prevented staff from effectively administering any of its numerous contracts worth $176.7 million.

Furthermore, the Connector was unable to demonstrate that the millions of dollars it paid to Mansha were used as intended. The Connector did not approve its contract administration procedures until more than a year after the Mansha contracts were executed, and the former executive director did not ensure the administrator for the Mansha contracts was qualified.

The Connector also had no procedures for amending contracts. We found the former executive director amended large contracts without the board's knowledge or approval. In addition, contracts were not amended to reflect changes in scope of work, and amendments that were made were not done timely. This led to higher contractual costs, further wasting public moneys, and could lead to federal enforcement action. Such practices constitute abuse of public funds, which involves behavior that is deficient or improper compared to what a prudent person would consider reasonable and necessary business practice under the circumstances.[12]

Board and management failed to establish a contract administration function

Federal procurement standards require, and best practices recommend, that agencies maintain a system for contract administration to ensure contractors meet contractual requirements and agencies have received what they paid for.[13] However, agencies often devote more time to awarding contracts than administering them. This frequently leads to contractor performance problems, cost overruns, and delayed delivery of goods and services. Effective contract administration is therefore

[12] U.S. Government Accountability Office, *Government Auditing Standards*, December 2011, Section 6.33.

[13] Title 2 Code of Federal Regulations Part 215.47, and Office of Federal Procurement Policy, *A Guide to Best Practices for Contract Administration*, October 1994.

essential to safeguarding public funds from waste and abuse. We found that the organization lacked a functional area dedicated to contract administration, reflecting board and management neglect of this critical core function.

During our audit period, the Connector was organized into six functional areas (finance, information technology, operations, marketing and communications, legal, and business development) as illustrated in Exhibit 1.1. Although its organizational structure later evolved (as shown in Exhibit 1.2), it still did not include a functional area dedicated to administering contracts.

Instead, contract administration duties were individually assigned by the executive director to designated operational staff. Best practices recommend assigning a contract monitor who has the authority, resources, and time to ensure contracts are properly monitored.[14] We found that high turnover at both the Connector's leadership and staff levels, as well as staff reductions, negatively impacted the time and resources that contract monitors were able to allocate to their contract administration responsibilities.

Management was unable to demonstrate $15.3 million paid to Mansha was used as intended

From May 2013 through August 2014, the Connector paid Mansha $15.3 million. Yet we found little evidence that contract administrators approved and accepted Mansha's deliverables or substantiated Mansha's performance before authorizing those payments. Both contracts with Mansha gave the Connector the right to dispute invoices for inappropriate charges and terminate the contracts for cause. But insufficient contract monitoring precluded administrators from identifying and properly addressing Mansha's performance issues and inappropriate charges. As a result, the Connector was unable to withhold payments, terminate Mansha's contracts, or undertake other actions to protect its interests with respect to Mansha's performance; most importantly for public transparency, the Connector could not demonstrate that the $15.3 million it paid to Mansha was used as intended.

Contributing to this problem was the fact that the Connector's contract administration procedures were not approved until more than a year after it began hiring contractors. Furthermore, despite the complexity and significance of the health insurance exchange IT system implementation project that Mansha was hired to assist with, the former and interim executive directors failed to ensure the Mansha contracts were monitored by staff with adequate expertise and qualifications.

[14] National State Auditors Association, *Contracting for Services, A National State Auditors Association Best Practices Document*, June 2003, p. 4.

The only evidence in the Connector's contract files that staff monitored the Mansha contracts was progress reports, invoices, and vendor payment vouchers signed by the contract administrator. There were no reports or other documents to demonstrate that the contract administrator or others responsible for overseeing Mansha's work had reviewed and accepted Mansha's deliverables and deemed Mansha's performance satisfactory prior to approving payments, nor was there evidence that any potential instances of Mansha's unsatisfactory completion of services and deliverables were addressed. Without effective monitoring, the Connector impeded its ability to meet federal grant requirements that it report on accomplishments against established goals and objectives and any developments that had a significant impact on activities supported by the grant.

Contract administration procedures were not approved until February 2014

Federal standards required the Connector to maintain a system for contract administration to verify contractors met the terms, conditions, and specifications of their contracts and that all purchases were followed up adequately and timely. Although we found the Connector's contract administration procedures met federal procurement standards and generally followed best practices, this framework was not in place until February 2014, more than a year after the Connector began executing contracts in late 2012. Prior to February 2014, contract administrators' roles and responsibilities were never clearly defined. In the absence of formal guidance, the administrator for the Mansha contracts took it upon himself to develop the Connector's contract administration procedures. His draft was completed in August 2013 but was not approved by the interim executive director until February 2014.

The existence of procedures does not equate to implementation; they must be followed to be effective. For example, best practices and the Connector's procedures require contract administrators to document all monitoring activities in a contract file. Contract files should include contract administration plans, all correspondence and communication with a contractor, and contract closeout checklists.[15] However, administrators for the Mansha contracts never included such documentation in their contract files. Our prior audit of the Connector likewise found that other contract files were missing required documents. The absence of documentation was one of the reasons we engaged in this audit of the Mansha contracts.

We found that although management did provide some contract administration oversight, it was limited to contract administrators' weekly reports of contractors' significant performance issues, coupled

[15] Hawai'i Health Connector Contract Administration Procedures, Sections II and VIII.

with review and approval of invoices by the contract administrator, the chief financial officer, and the executive director. Reviewing and approving invoices is only one aspect of contract monitoring and does not guarantee that contract administrators have adhered to procedures.

Executive director did not ensure administrator was qualified to monitor Mansha contracts

It is essential that those responsible for safeguarding an agency receives what it paid for are competent in contract administration practices and aware of, and adhere to, the authority granted to them. It is also essential that contract administrators are technically competent and possess specialized qualifications. However, the Connector's management assigned an administrator to the Mansha contracts who was ill-prepared to adequately monitor such a technical project, even though he was considered the best person available. Management did not require or provide training to the Mansha contract administrators. The former interim executive director acknowledged that contract administrators generally had to rely on on-the-job training.

Furthermore, the former executive director did not make certain that the Mansha contracts administrator possessed the necessary expertise to monitor these IT contracts. Based on our review of comparable private sector positions, the Mansha contract administrator should have had experience in contract and vendor management and procurement for IT system implementation projects, and possessed a strong understanding of commercial and legal terms in IT contracts. Instead, the former executive director assigned the Mansha contract to someone experienced in contracting and legal affairs but who lacked IT expertise.

The Connector also lacked in-house staff with the technical competence and skills needed to review and evaluate Mansha's deliverables and services provided. As a result, the contract administrator relied on the State CIO and the Connector's acting CIO—who was also a contractor—to provide technical oversight of Mansha's work. When the acting CIO resigned in May 2014, Mansha's own principal served as the Connector's new acting CIO until Mansha withdrew from the Connector in December 2014. Thus, for more than half a year Mansha's principal was responsible for overseeing his own company's work, a clear conflict of interest.

Connector lacked procedures for amending contracts

We also found the Connector had no formal policies and procedures for amending contracts, including any guidance on when it is appropriate to amend a contract and seek approval from the board or the federal DHHS. Under its grant terms, the Connector was required to obtain prior approval from or notify DHHS of certain contract modifications.

Without policies and procedures for amending contracts, Connector staff could easily overlook these federal requirements. In addition, we found that the former executive director amended large contracts without the board's knowledge or approval. We estimate that one of these amendments wasted almost $3.9 million in public moneys.

Furthermore, the Connector amended its contracts with Mansha belatedly, which led to higher costs, further wasting public moneys. For example, the second Mansha contract was amended to revise the scope of work to include services that were also being provided by other contractors. By the time CCIIO questioned this, the Connector had already executed the amendment. The Connector never rectified this or other deficiencies that CCIIO identified.

Connector's amendments of large contracts wasted an estimated $3.9 million

Both Mansha contracts were amended in ways that significantly increased their duration and fees. The Connector's practice for amending contracts was to obtain board approval for proposed amendments that increased a contract's amount to more than $100,000 or an amount exceeding whatever was previously approved by the board. However, the Connector could not demonstrate that it adhered to this practice when amending the first Mansha contract, and we found that the Connector violated this practice when amending the second contract.

We found no evidence that the former executive director sought and obtained the board's approval for the $168,000 amendment to the first Mansha contract for additional services to plan for the implementation of the Integrated Project Management Office (IPMO). Although this amendment exceeds the $100,000 threshold for board approval, we also found that in April 2013, the board authorized and directed the former executive director to take all actions necessary or appropriate, including negotiating and executing contracts, to develop and establish an IPMO. However, it is not clear if this approval applies only to the IPMO contract or extends to all agreements necessary for implementing the IPMO, which would include the amendment to the first Mansha contract. In addition, the effective date of the amendment was *after* the original contract had terminated.

Likewise, the former executive director did not seek and obtain board approval when the Connector amended the second Mansha contract to remove an automatic termination clause. As originally worded, the second contract would have automatically ended when the Integrated Governance Agreement (IGA) terminated on December 9, 2013. Because Mansha's automatic termination clause was no longer in place, the Connector was obligated to pay Mansha through April 2014—five

additional months—as originally contracted. We determined these additional payments amounted to nearly $3.9 million.

Exhibit 2.2 shows the estimated amounts paid to Mansha from the date the IGA terminated—when the Mansha contract should have automatically terminated—through the end of Mansha's original contract date, April 25, 2014.

Exhibit 2.2
Payments Made to Mansha After the Contract Should Have Terminated, December 10, 2013 through April 25, 2014

Month	Payment
December 2013	$585,388
January 2014	824,864
February 2014	824,864
March 2014	824,864
April 2014	824,864
Total	**$3,884,844**

Source: Office of the Auditor

Contracts were not amended to reflect changes in scope of work

As Mansha's responsibilities changed and grew, the Connector fell short in executing new contracts, amending the existing contract to reflect new scopes of work, and renegotiating existing fees. According to a contract justification report to the Connector's board, after the October 2013 health exchange launch, it was determined in November 2013 that Mansha had fulfilled its original responsibilities under its second contract. The Connector then obtained board permission to use Mansha to help develop and implement its health exchange IT systems. This was a significant shift in Mansha's responsibilities. Instead of terminating the second contract and executing a third contract, however, the Connector merely amended Mansha's second contract to change the scope of work. Furthermore, the amendment was not executed until March 2014—nearly four months after the change in Mansha's responsibilities, a clear violation of best practices.

Mansha's services continued to evolve. In May 2014, its principal began serving as the Connector's acting CIO, and from August 2014, Mansha provided all internal IT functions and a security officer and managed other contractors' independent verification and validation (known as IV&V) and testing contracts. However, the Connector never amended Mansha's contract to reflect these added responsibilities.

The Connector's failure to amend Mansha's contract in a timely manner was not isolated to Mansha. Another contractor also reported that contract amendments for several IT vendors did not keep pace with changes in vendors' scope, schedules, and requirements. Changes to services agreed to verbally and via email were not formalized in contract amendments, putting the Connector's interests at risk and impeding public transparency.

Failure to amend contracts timely wasted at least $1 million

Because the Connector did not amend its contracts with Mansha in a timely manner, it may also have overpaid for Mansha's services by at least $1 million. At the time the second contract was executed, in April 2013, Mansha's billing rate included a 30 percent risk premium to cover uncertainty regarding the level of effort that would be needed to complete the work required at the time. By the time the contract renewal was negotiated in January 2014, that risk had significantly decreased; Mansha's estimate for the new work was lower than for the initial work. However, for nearly five months (from November 2013 to April 2014), the Connector continued paying Mansha the higher fees it had paid for the initial work—even though the contract did not prevent the Connector from renegotiating a lower price. The amendment also provided for an advance $1 million "rapid mobilization payment" at the start of the renewal period to allow Mansha to rapidly deploy its resources. We question the need for such a payment when Mansha was already in place and serving the Connector. The Connector was unable to provide evidence to support the need for the rapid mobilization payment or to demonstrate that the renewal price was reasonable.

Conclusion

The Connector awarded contracts totaling $21.6 million to Mansha Consulting LLP, a vendor whom it could not demonstrate was qualified to integrate the state's health insurance exchange IT systems. In addition, the Connector entered into seriously flawed contracts with Mansha, precluding the Connector from effectively monitoring Mansha's performance and wasting more than $11.6 million in taxpayer moneys. Because of its lackadaisical approach to contract administration, the Connector was unable to demonstrate that the $15.3 million it ultimately paid to Mansha was used as intended.

The multitude of missteps and failures in procuring and administering the Mansha contracts exemplifies the Connector's failure to adequately safeguard public funds. In addition, the Connector's failure to comply with certain federal procurement standards and terms and conditions of its federal grants may result in enforcement action by the federal government, including the Connector being denied the use of grant funds for any portion already used to pay for the Mansha contracts.

Any amounts the federal government deems ineligible for grant funding would have to be paid from the Connector's other revenue sources. However, the Connector has been unable to generate enough revenues to achieve self-sufficiency. Instead, it has relied on State general fund appropriations of $1.5 million for FY2015 and $2 million for FY2016 to provide partial operational funding. In addition to the $3.5 million already provided by the Legislature, the Connector estimated it needs a minimum of $5.4 million to remain viable in FY2016. Should the Connector require additional general funds to comply with any federal enforcement action, Hawai'i's taxpayers will have to shoulder the burden.

By May 1, 2016, the Connector will cease to exist, having transitioned its state-based exchange operations to a federally facilitated marketplace. However, the lessons learned from the Connector's experiences apply to any agency with responsibility for the use of public funds. Namely, (1) proper planning is imperative to ensure agencies contract for appropriate services; (2) agencies must be able to demonstrate that contracts were awarded to qualified consultants and that negotiated fees are reasonable; (3) contracts must be drafted with appropriate deliverables and performance indicators to allow adequate monitoring; (4) contracts must be monitored and contractors' performance evaluated throughout the contract period; (5) adequate records must maintained to support all actions taken regarding a contract; and (6) changes in scope of work must be appropriately and timely reflected as contract amendments. Following these steps is crucial to safeguard public funds—ultimately, taxpayers' moneys that have been entrusted to government.

Recommendations

1. The Hawai'i Health Connector Board of Directors needs to designate a custodian of record with responsibilities to maintain, conserve, and make available as needed by federal, state, and other appropriate entities any and all records relating to the business of the Hawai'i Health Connector from inception through dissolution.

2. The Legislature may wish to consider amending or repealing as appropriate the relevant sections of Chapter 435H, HRS (*Hawai'i Health Insurance Exchange*), to reflect the dismantling of the Hawai'i Health Connector.

Response of the Affected Agency

Comments on Agency Response

We transmitted a draft of this report to the Hawai‘i Health Connector’s executive director and its board on July 21, 2015. A copy of the transmittal letter to the executive director is included as Attachment 1. The executive director’s response, dated July 27, 2015, was received on July 29, 2015 and is included as Attachment 2.

Unauthorized release of draft report by agency

As reflected in Attachment 1, our audit process affords agencies an opportunity to respond to our confidential draft report. We explicitly state, however, that:

> [s]ince 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.

This direction was affirmed by the Connector in its response to our draft report, which states, in part, that “the Auditor specifically instructed the Connector not to share the contents of the Draft report with former employees or directors.” We find it troubling, however, that on August 4, 2015, we received an email from the former executive director’s private attorney that stated, in part, “I know a report on the Connector is coming out soon” and asking whether “the clarifications/corrections regarding [the former executive director] will be made in that Report.” The attorney also sent us two additional emails and further asked whether he and his client would be permitted to comment on the draft report. We contacted the attorney by telephone on August 6, 2015, and reiterated that, in accordance with our office procedures, we do not release draft reports to anyone other than the agency responsible for responding to the report and its recommendations. Although the attorney denied having seen a copy of the draft report, we question the timing of his contact with our office and his assertion that there are or were errors in the draft report that needed correcting. We seriously question whether the Hawai‘i Health Connector either provided a copy of the draft report or, at the least, provided a copy of its response to the draft report to the attorney, in contravention of our express embargo on releasing the draft report.

The confidentiality of draft reports helps ensure that we provide accurate final reports. Any breach of this confidentiality does a disservice to the public and to agencies under review by our office. In accordance with

our office procedures, we reviewed the Connector's response to our confidential draft and made minor changes for accuracy and clarity in the final report.

Agency's response to draft report

The Connector thanked us for our efforts and said that our findings appear to be consistent with the material in our previous audit and with information the Connector has made public during the past year. The Connector said its board and management have shared our concerns about Mansha and other significant contractors and have worked to improve their procurement and contract management practices.

The Connector believed that all references to execution dates throughout the report should be clarified to "effective" dates. We did not distinguish between execution and effective dates for the Mansha contracts because for all but the original design review contract, the contracts state that "the parties have executed this agreement as of the effective date." The original design review contract states "the parties have executed this agreement as of the first date above written," which is the effective date.

Regarding our finding that the initial staffing requirement was unclear and 20 Mansha staff were contemplated but later changed to 16, the Connector asserted that the State Office of Information Management and Technology (OIMT) largely oversaw Mansha's performance and specified staffing levels. According to the Connector, OIMT essentially imposed Mansha and many of the contracts' terms and conditions on the Connector and its board. We maintain that OIMT's involvement did not absolve the Connector of its responsibility as a party to the contract with Mansha to ensure that those terms and conditions, including specified staffing levels, were appropriate.

The Connector did not believe the report accurately describes Mansha's contractual staffing requirements. According to the Connector, the initial contract provided for 16 staff, either as a placeholder or in error, while the number of staff required was still being negotiated. The Connector cited a May 22, 2013 budget that reflects an agreed-upon staffing level of 22 that was approved by the federal government. However, our report clearly states that the April 26, 2013 contract amount reflects Mansha's proposed price for a 20-person team. If the staffing level of 16 in the contract was in error, the Connector should have, but did not, amend the contract to reflect the staffing level agreed upon after the contract was executed.

The Connector also expressed concern about Hawai'i's taxpayers having to shoulder the burden if the federal government denies the Connector's use of certain grant funds already paid to Mansha. The Connector asserted that our conclusion assumes Mansha is owed money; but that

Section 435H-2, HRS, protects the State from the debts and liabilities of the Connector, which was established as a nonprofit corporation. However, we do not make any assertion that the Connector owes Mansha any money. Furthermore, any amounts the federal government could deem ineligible for grant funding would have to be paid from the Connector's own revenues. Because the Connector is not financially self-sustainable, it has relied on state general funds totaling $3.5 million for FY2015 and FY2016 to support its operations. Therefore, should the Connector require additional general funds to comply with any federal enforcement action, Hawai‘i's taxpayers will have to shoulder the burden.

Finally, the Connector pointed out what it considered to be certain other errors and inconsistencies in the report. Accordingly, we made minor technical changes for accuracy and clarity prior to publication. However, we stand by our findings.

ATTACHMENT 1

STATE OF HAWAI'I
OFFICE OF THE AUDITOR
465 S. King Street, Room 500
Honolulu, Hawai'i 96813-2917

JAN K. YAMANE
Acting State Auditor

(808) 587-0800
FAX: (808) 587-0830

July 21, 2015

COPY

Mr. Jeffrey M. Kissel
Executive Director
Hawai'i Health Connector
201 Merchant Street, Suite 1810
Honolulu, Hawai'i 96813

Dear Mr. Kissel:

Enclosed for your information are three copies, numbered 6 to 8, of our confidential draft report, *Audit of the Hawai'i Health Connector's Mansha Contracts: Connector Board and Management Wasted and Abused Millions in Public Funds*. We ask that you telephone us by Thursday, July 23, 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 12 noon, Wednesday, July 29, 2015.

The Board members of the Hawai'i Health Connector, 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,

Jan K. Yamane

Jan K. Yamane
Acting State Auditor

Enclosures

July 27, 2015

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OFC. OF THE AUDITOR
STATE OF HAWAII

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

Dear Ms. Yamane,

The Board of Directors and Management of the Hawaii Health Connector "Connector" thanks the Auditor for its efforts on behalf of the Governor, Legislature and the people of the State of Hawai'i for the material presented in the Draft Report to the Governor and Legislature on the Audit of the Hawai'i Health Connector "Draft" as of July 2015 and submitted for review by the Connector on July 23, 2015.

The findings appear to be consistent with the material presented in the previous Audit dated January 2015. They are also consistent with the information that Connector Management and Board have made public during the past year. As you will recall, the Connector Board and Management shared your concerns about Mansha and the other significant contractors, last year and not only adopted all of the Auditor's recommendations from the 2014 Report, but also went further to establish even greater control of the contracting process.

These actions were reported to your office and to our Board as they were implemented. It is unclear as to why no mention of these changes in procedures was made in the current Report, nor was there any mention made of the fact that Connector Management has recommended that Mansha **not** be paid for any services rendered from the period between September 25, 2014 and December 5, 2014, when the Connector's relationship with Mansha ended.

In addition, there appear to be certain errors and inconsistencies in the Report that the Connector would like to bring to the attention of the Auditor and the public as follows:

1) Since the Report, in large part, focused on the actions of the previous Management and Board of Directors of the Connector, the Connector did not have an opportunity to validate certain statements made by the Auditor. In fact, the Auditor specifically instructed the Connector not to share the contents of the Draft

report with former employees or directors; therefore we are uncertain how the Auditor came to the following conclusion;

a. Specifically the statement on Page 24: "The Connector determined in November 2013 that Mansha had fulfilled its original responsibilities under the second contract."

b. We do not believe the foregoing comment is accurate, as no such official determination was made. Accordingly we request that either the Auditor advise the Connector of the facts and circumstances that support this statement, or that it be withdrawn.

2) As the Report acknowledges, the Connector made available to the Auditor all of the reports and records of the work that Mansha performed relating to their performance and level of effort.

a. We note and request that the Report explicitly state that it does not express an opinion on their performance or Mansha's level of effort, nor does it reference any industry standards with which to compare Mansha's fees and charges.

b. It is more than somewhat difficult, therefore to follow the Auditor's logic in determining an amount that was "over obligated" and/or wasted when the Auditor elected to assume, without consultation with the Connector, or apparently any other State Based Exchange, or Healthcare.gov, that the Project Management Services should have ended on the same day as "open enrollment" began, October 1, 2013. This is an obvious error since: 1) no IT projects can be considered "complete" on the first day of operations, and 2) the project did not meet the definition of "complete" pursuant to the underlying contract with the System Integrator, CGI, that Mansha was supposed to supervise. Since the Auditor had full access to the CGI contract, and it was, in fact the subject of the 2014 Audit, this error should be corrected as well in the Report.

3) Exhibit 1.6 (and throughout the Report) references execution dates. It is our belief that the Report is generally referring to the effective dates of the agreements and amendments, not to the execution dates, and we believe this clarification should be made. This is an important clarification since the execution dates are inconsistent with the dates that services were required to be rendered.

4) On page 14 and 15, the Report states that the initial staffing requirement was unclear and that 20 Mansha staff were initially contemplated, but later changed to 16. It is critically important to note that the Connector was not fully in control of this process or providing project oversight. The State Office of Information Management and Technology (OIMT) was largely driving this process, overseeing Mansha's performance, specifying staffing levels and other terms and conditions;

a. The Report largely ignores the fact that OIMT essentially imposed Mansha and many of the terms and conditions in the contracts on the Connector and its Board. This is especially troubling since, at the time,

the State held four voting positions on the Connector Board,[1] its consultants and the State CIO are on record, in public, as having endorsed both Mansha, and a closed procurement process that was both inconsistent with the State and Connector policies in place at the time.

b. Moreover, we do not believe the Report accurately describes the contractually required staffing. We do not make in this comment our "legal" argument on this point, but we do refer you to our May 22, 2013 budget, a copy of which was provided to your staff. We also note, in this regard, that:

1. The initial agreement provided for 16 staff, either as a placeholder or perhaps in error, but the number of staff under the agreement was still being negotiated between the OIMT, Mansha, and the Connector.

2. Under an early budget, the staffing level was increased to 20 by deleting certain more highly compensated positions and adding additional positions at lower compensation levels.

3. Under Section 4.1 of the IPMO Contractor Agreement and the May 22, 2013 budget, the Connector, OIMT, and Mansha eventually agreed on a contractually required staff of 22 staff. This is the staffing level that was presented to and approved by the federal government (CCIIO) and the Connector's Board until the staffing plan of the IPMO Contractor Agreement was amended effective January 15, 2014.

4. We believe that applying appropriate legal principles of contract interpretation would yield the conclusion that the contractually required staffing was materially higher than 16 (as described above).

5) The last sentence of the Conclusion on page 25 of the Report states: "If the federal government denies the Connector the use of grant funds for any portion used to pay for the Mansha contracts, Hawaii's taxpayers will have to shoulder the burden."

a. This "Conclusion" appears surprising, since the Auditor clearly has access to the Hawaii Revised Statutes and they contain the language of the enabling legislation for the Hawaii Health Connector. It was established as an independent Corporation, specifically not funded by the State. Haw. Rev. Stat. § 435H-2 provides "The connector shall be a Hawaii nonprofit corporation organized and governed pursuant to chapter 414D, the Hawaii nonprofit corporations act. <u>The debts and liabilities of the connector shall not constitute the debts and liabilities of the State."</u>

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[1] The Connector's enabling statute (Act 205), identified four ex-officio voting members or their designees to serve on the Connector's Board, including the director of health, the director of human services, the director of labor and industrial relations and the director of commerce and consumer affairs. The State Legislature changed the Board composition during the 2014 legislative session (Act 233), reducing the State's number of voting members to one member, identified by the Governor.

b. The Connector does not believe Mansha is owed money. In addition, the aforementioned assertion in the Report is inaccurate because it assumes 1) that Mansha is owed money, and 2) that if the CCIIO denies funds to the Connector to pay Mansha, the State of Hawaii's taxpayers will be responsible. Unless the Auditor is aware of separate contractual commitments made by the State to Mansha, then the Connector knows of no way that the Auditor's conclusion can be considered accurate or representative of the current facts and circumstances.

c. Again, the Connector believes that this is a serious error and has the potential to mislead the people of the State. We request that the aforementioned information be corrected.

As we said in our response to the Audit Report last year "*With respect to the "Issue for further study," the Board and Management shares the concern expressed by the Auditor. At the December meeting the Board authorized an independent investigation into the outstanding balance that the named contractor asserted was due, owing and unpaid as well as certain other matters. The federal agencies controlling the grant were notified appropriately, as were the members of the Legislative Oversight Committee.*"

During the past year we have fulfilled that commitment, improved processes, and conducted the aforementioned study in order to improve our existing procurement and contract management practices. The results are being reviewed by our Board for appropriate action.

We certainly appreciate the seriousness of this matter, but hope that the Report will be adjusted to accurately represent the facts and circumstances, and provided the analysis and appropriate commentary on the Connector's adoption of the Auditor's previous recommendations.

The Board and Management are committed to improving the governance and business processes and will continue to work with the Auditor to assure satisfactory compliance.

Sincerely,

Jeffrey M. Kissel
Executive Director