



**U.S. Department of the Interior  
Office of Inspector General**

# **Audit Report**

## **Procurement Practices, Virgin Islands Port Authority, Government of the Virgin Islands**







# United States Department of the Interior

OFFICE OF INSPECTOR GENERAL  
1849 C Street, NW – MS 5341  
Washington, DC 20240

March 28, 2005

Mr. Darlan Brin  
Executive Director  
Virgin Islands Port Authority  
P. O. Box 301707  
St. Thomas, Virgin Islands 00803-1707

Subject: Final Audit Report “Procurement Practices, Virgin Islands Port Authority, Government of the Virgin Islands” (Report No. V-IN-VIS-0001-2004)

Dear Mr. Brin:

The attached report presents the results of our audit of procurement practices at the Virgin Islands Port Authority. The objective of our audit was to determine if the Port Authority was carrying out its procurement activities in accordance with applicable local and Federal laws and regulations.

The legislation, as amended (5 U.S.C. app. 3), creating the Office of Inspector General requires that we report to Congress semiannually on all reports issued, actions taken to implement our recommendations, and recommendation that have not been implemented. Therefore, this report will be added to the next semiannual report.

Please provide a response to this report by May 2, 2005. The response should provide the information requested in Appendix 4 and should be addressed to me at the above address, with a copy to our Caribbean Field Office, Ron deLugo Federal Building – Room 207, St. Thomas, VI 00802.

Sincerely,

Roger LaRouche  
Assistant Inspector General for Audits

cc: Governor Charles W. Turnbull  
Chairman, Governing Board, Virgin Islands Port Authority

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# INTRODUCTION

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## BACKGROUND

The Virgin Islands Port Authority was created in 1968 as an instrumentality of the Government of the Virgin Islands. The Authority is authorized to establish, acquire, construct, develop, and improve air and marine terminals; issue contracts and execute all instruments necessary in the exercise of any of its powers; accept grants and loans from and enter into contracts, leases, agreements, or other transactions with any Federal or Virgin Islands agency; and expend the proceeds of any grants or loans.

The Authority is governed by a nine-member Governing Board, and day-to-day operations are managed by an Executive Director appointed by the Board. The Authority has 299 employees. The Engineering Division, the Purchasing Office, and Accounting Office have responsibilities related to the procurement of services. The Engineering Division establishes and manages capital projects, the Purchasing Office processes requisitions for supplies and equipment initiated by other divisions, and the Accounting Office maintained files for purchases related to administrative goods and services.

During fiscal years 2002 and 2003, the Authority awarded 24 construction and/or project management contracts for 11 capital improvement projects totaling \$85.3 million. Additionally, the Authority paid six professional service providers a total of \$1.9 million over periods of up to 6 years and issued 2,158 purchase orders totaling \$3.9 million during fiscal years 2002 and 2003.

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## OBJECTIVE AND SCOPE

The objective of our audit was to determine if the Virgin Islands Port Authority was carrying out its procurement activities in accordance with applicable local and Federal laws and regulations. To accomplish the audit objective, we interviewed Authority personnel and reviewed budgets, purchase orders, contracts and agreements, contract files, payment documents, and other documents related to transactions during fiscal years 2002 and 2003, and other periods as appropriate for contracts that were active during 2003 and 2004.

We reviewed the contractor selection process for 11 capital improvement projects totaling \$85.3 million and performed more comprehensive reviews of the contracts for 9 of the projects totaling \$71.1 million. We also reviewed payments totaling more

than \$1.9 million made to six professional service providers and 50 purchase orders totaling \$881,954.

Our audit was conducted in accordance with the “Government Auditing Standards,” issued by the Comptroller General of the United States. Accordingly, we included such tests of records and other auditing procedures that were considered necessary under the circumstances. The “Standards” require that we obtain sufficient, competent, and relevant evidence to afford a reasonable basis for our findings and conclusions.

As part of our audit, we evaluated the internal controls related to procurement activities of the Authority to the extent we considered necessary to accomplish the audit objective. Internal weaknesses in these areas are discussed in the Results of Audit section of this report. The recommendations, if implemented, should improve the internal controls in these areas.

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#### **PRIOR AUDIT COVERAGE**

During the past 5 years, the Office of Inspector General has not issued any audit reports on procurement activities at the Virgin Islands Port Authority. However, findings related to procurement activities were included in two reports issued by the Authority’s internal audit unit in December 2000 and August 2002. We found that the 11 recommendations made by the internal audit unit were not implemented. Further details on these prior audits are presented in Appendix 1.

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# RESULTS OF AUDIT

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## OVERVIEW

The Virgin Islands Port Authority did not always comply with applicable Federal and local procurement requirements and, as a result, did not have adequate control over its procurement function. Specifically, we found that the Authority did not:

- Adequately document the process used to select contractors for major capital improvement projects.
- Maintain complete contract files and require that contractors submit all necessary documents, including evidence of liability insurance coverage and appropriate business licenses.
- Adequately plan a major construction project so as to minimize the need for contract change orders totaling \$13.7 million.
- Use required competitive negotiations for all professional services to ensure that the most cost-effective combination of price and quality of service was obtained.
- Issue contracts for all professional services or, when issued, did not do so until the majority of work had been performed and significant payments had already been made to service providers.
- Solicit at least two price quotations for purchases of \$2,500 or less, and issue contracts to vendors for purchases over \$2,500, as required by internal policies.
- Deduct gross receipt taxes of \$846,653 from payments to contractors who performed services for the Authority, as required by the Virgin Islands Code.

Because the Authority did not comply with established policies and did not have adequate control over its procurement activities, it could not ensure the efficient and effective use of funds.

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## **CAPITAL IMPROVEMENT PROJECTS**

The Virgin Islands Code<sup>1</sup> and the Port Authority's Procurement Policy and Procedures Manual (procurement manual) provide local regulations for maintaining contract files, procuring goods and services, and deducting gross receipt taxes from payments to contractors and vendors. The Federal "Common Rules" for grant management<sup>2</sup> require grantees to follow local procurement regulations for grant-funded projects. In addition, Federal Aviation Administration (FAA) grant regulations contain requirements regarding audit access to contractor records and prior approval of contract change orders.

### **Lack of Support for Capital Project Contracting Undermined the Integrity of Procurement Actions**

The Authority did not follow requirements for documenting the procurement process. Contract files should present a complete history of the transaction to provide: a comprehensive background as a basis for informed decisions at each step in the acquisition process; support for actions taken; information for audits and investigations; and essential facts in the event of litigation.

Section XVII-A of the Authority's procurement manual lists 14 items that should be documented and included in the files for each capital improvement contract. However, we found that although file folders were set up for such items as "mailing lists of bidders," "contract," and "bid evaluation," the actual documents were often not contained within the folders. For example, we could not find documentation of bid analyses and evaluations for 10 contracts or bid abstracts for 6 contracts.

### **Competitive Was Not Sought or Documentation of Competition Was Lacking**

Section IV of the procurement manual requires that the Authority acquire services for capital improvement projects by soliciting competing bids or proposals and choosing the most favorable of the competing offers. This may be done by formal competitive bidding or by competitive negotiations.

We reviewed the contractor selection process for 11 capital improvement projects, 9 from fiscal year 2002 and 2 from fiscal year 2003. We determined that the Authority did not follow the competitive procurement requirements for 7 contracts valued at \$1.7 million and did not document the process for 9 contracts valued at \$46.4 million. Examples follow:

- No information was found in the files for the selection of the firm that performed marine-related services for most capital

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<sup>1</sup> Titles 29 and 33

<sup>2</sup> Issued pursuant to OMB Circular A-102



improvement projects, although seven contracts were awarded to the firm. A February 25, 2003 letter from the firm's president to the Authority stated that four of five listed projects had been put out on bid, but we could not confirm this statement because documentation was not available. We also found that the Authority did not require that the firm provide proof of liability insurance. Although five of the firm's seven contracts stated that upon execution the contractor must provide the Authority with certification of insurance, we did not find certificates of insurance in the contract files.

- We also found that there was no documentation regarding the selection of the construction contractor for the Henry Rohlsen Airport terminal building on St. Croix or for the selection of project management consultants for the marine port projects at Red Hook, St. Thomas and Enighed Pond, St. John.
- Additionally, we were unable to determine who evaluated the proposals and selected the construction contractor and project management consultant for the Ann Abraham pier project on St. Croix.

### **Contract Change Orders for the Rohlsen Airport Construction Contract Were Not Properly Administered**

The initial \$22.5 million construction contract for the Rohlsen Airport terminal was prepared by the contractor and contained open-ended provisions that, in our opinion, favored the contractor's interests over those of the Authority. For example, 17 change orders were issued to significantly change the scope of the project. This resulted in an \$8.4 million, or 37 percent, increase in total construction costs and an extension of the contract period from 26 months to 55 months. Change order no. 12 compensated the contractor \$2.1 million for additional costs related to extensions of the contract period made by prior change orders.

An Authority official advised that the prior Executive Director, because of limited funding, originally intended to construct the basic shell of the terminal building and have the airlines and other tenants of the building design and finish their individual areas. However, because of the downturn in the airline industry after the September 11, 2001 terrorist attacks, the Authority changed its plans and decided to construct and finish all tenant areas. Most of the change orders for the construction contract resulted from this change in construction plans. A total of 17 change orders valued at \$8.4 million were issued for this major alteration to the project.



**Figure 1.** The Henry E. Rohlsen Airport terminal building on St. Croix (Virgin Islands Port Authority photo)

**The Rohlsen Airport  
Project Management  
Contract Was  
Increased by  
\$5.3 Million**

On June 23, 1994, the Authority issued a project management contract for the Rohlsen Airport terminal in the amount of \$1.5 million. Our review of the contract files revealed that the original completion date was August 1997, but the completion date was extended to August 2002. A total of 12 amendments raised the total contract cost to \$6.8 million – an increase of \$5.3 million, or 368 percent. We also found that one of the amendments was approved by the Authority’s Governing Board on July 19, 2000, to continue management services at an additional cost of \$964,020, but the Authority paid the contractor \$38,561 more than the approved amount. We further found that the contractor later gave the Authority a credit of \$28,106, but \$1,124 in applicable gross receipt taxes that the Authority had previously included in payments to the contractor was not also credited to the Authority’s account.

**Federal Grant-Related  
Guidelines Were Not  
Always Complied With**

Compliance with grant terms and conditions is a prerequisite for receiving FAA and other Federal grants. However, there are other general conditions with which the Port Authority should also comply. For example, the FAA’s construction projects guide states that sponsors need prior approval for contract change orders that add or delete work from the basic grant scope. Despite this requirement, the Authority did not request prior approval for a \$1 million change order issued on February 20, 2003, to add work

items to the contract for the rehabilitation of the Cyril E. King Airport on St. Thomas. Although the change order form included a section for FAA approval, this section was not signed by an FAA representative. In fact, the FAA did not approve the change order until December 17, 2003, almost 8 months after the project was completed on April 29, 2003.

Additionally, the FAA's guidelines on recordkeeping responsibilities state that any cost reimbursement contracts executed in conjunction with a Federal grant should include a clause allowing access to contractors' books, documents, and records by the Comptroller General of the United States or any of his authorized agents. Despite this requirement, our review of major contracts issued by the Authority revealed that this clause was not included. For example, the contract for the construction of the Rohlsen Airport terminal building provided for access to the contractors' cost accounting records only by the "owner" – the Port Authority.

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## **PROFESSIONAL SERVICES**

Section IX of the procurement manual specifies that the Authority must initiate requests for proposals for specialized (professional) services and that if the projected cost of the services is \$50,000 or more, the proposal must be reviewed and evaluated by an authorized officer and the Director of Administration and Finance or by the Bid Evaluation Committee. The procurement manual also states that a contract shall be awarded for the best proposal and be approved by the Authority's Governing Board if the contract exceeds \$50,000.

### **Requirements for Competition and Contracts Were Disregarded**

Despite these requirements, the Authority did not use competitive negotiations during the selection of four of the six service providers we reviewed. Additionally, for the same service providers, the Authority either did not issue any contracts (five instances) or issued contracts after the majority of work had been performed and payments had already been made (one instance). These service providers collectively received payments totaling more than \$1.9 million over periods of up to 6 years. Details follow:

**Computer Consulting Services - \$957,119.** The Authority did not obtain competitive proposals from other vendors and did not issue a formal contract for computer software and consulting services. In place of a contract, the Authority used a one-page proposal from a vendor who had previously provided computer-

related services. The proposal was attached to two memoranda, dated August 15, 2000, from the Authority's Accounting Manager to the former Director of Administration and Finance. This package was approved by both the former Executive Director and former Director of Administration and Finance. One memorandum stated that the services to be provided consisted of installation of human resource management software and training and maintenance for the software. The second memorandum provided justification for the new software. The proposal had incorrect price computations, did not include the name of the vendor, and did not include a time schedule for providing the services.

We could not determine the actual cost of the project because the proposal was not dated at the time of approval and invoices submitted by the vendor included the cost for maintenance and other miscellaneous services not related to this proposal. The firm was paid a total of about \$957,000 for all services provided during fiscal years 2000 through 2004 (as of January 2004).

Furthermore, on January 7, 2004, the same vendor submitted another proposal to (1) design and install a wireless cash collection system on all three islands, (2) upgrade the Authority's network structure to current Microsoft technologies, (3) integrate the St. Croix purchasing function into the St. Thomas accounting system, and (4) train St. Croix purchasing staff on the use of the Solomon IV software – all for \$49,400. Subsequent to the start of the project, the proposed cost was increased to about \$98,000. Because of the lack of documented justification for the increase, we believe the initial projected cost may have been stated at \$49,400 to circumvent the \$50,000 threshold for requiring the approval of the Authority's Governing Board.

The Authority again accepted this proposal without issuing a formal contract. The schedule of tasks attached to the proposal listed services to be performed from July 24, 2003 through March 15, 2004, but the document was approved only by the Executive Director on January 9, 2004, 5 months after the performance period started. The document was not signed by a representative of the firm. Finally, an official of the Authority stated that the firm was selected for this project without any competition and that, although she knew another firm that could offer the same services, the Authority wanted this particular firm to perform the services.

We also learned that during the past 15 years the Port Authority hired this firm, without competition or formal contracts, to provide various computer-related services. This was done despite the fact that the Authority had an employee on staff who may have had the expertise to perform at least the less technical tasks (such as routine maintenance) assigned to the service provider. This employee was the Authority's Information System Coordinator, who was certified in Microsoft software. The employee advised that he was underutilized by the Port Authority and could have performed some of the tasks that were provided by the outside consultant. He said that he was not allowed to participate in any of the activities performed by the outside consultant. In addition, he told us that about 7 years ago he requested training in the Solomon accounting software used by the Authority so that he could perform many of the tasks that were being performed by the outside consultant at an hourly rate of \$130. The Authority denied the training. We later learned that the Authority terminated the employee subsequent to the completion of our audit.

**Auditing Services - \$333,000.** The Authority did not issue a formal contract for independent auditing services but instead used a proposal from its long-time auditing firm to perform auditing and related services for fiscal years 2001 through 2003. No other proposals were solicited or received for these services. The February 12, 2001 proposal offered services to (1) perform financial statement and single audits, (2) review compliance with bond indentures, and (3) provide recommendations to improve internal controls. The proposal also stated that the Authority's internal audit staff must be utilized to perform audit review tasks to lower audit costs. The total proposed cost for auditing services totaled \$333,000. However, we found no documentation to show whether the Authority was given a discount for work performed by its internal audit staff.

In addition, at the time of our review, the firm which had audited the Authority continuously over the last 30 years did not have a current Virgin Islands business license, as required by the Virgin Islands Code. The firm's prior business license had expired in 2001 and was not for the type of services it provided to the Authority.

**Legal Services - \$6,846.** There was no evidence of competition and the Authority did not issue a formal contract to an attorney who provided legal services. The Authority used the attorney's proposal letter, which included an offer of services, as a contract. Although the Executive Director stated that he interviewed two

attorneys, we found no documentation of competition or analysis of the attorneys' proposals in the Authority's files. The Authority paid all invoices submitted by the attorney, totaling \$6,846, without a formal contract.

**Financial Consulting Services - \$200,655.** A 2-year contract for financial consulting services to the Authority expired on September 14, 1996. During the subsequent 6-year period, the consulting firm continued to provide services to the Authority without a contract. Then, on April 1, 2003, the Executive Director awarded a 1-year contract to the same firm for services related to the development of the Crown Bay commercial center on St. Thomas. We found no documentation to indicate the method used to select the firm for any of the services provided. Also, our review of paid invoices disclosed that the Authority paid the firm a total of \$200,655 from October 1999 to March 2003, but records were not available for us to determine the amount of payments made prior to October 1999. We further found that the Authority paid the firm \$1,536 for out-of-pocket expenses without supporting receipts or other documentation and \$2,700 for lodging costs at an unidentified local hotel.

**Investigative Services - \$5,000.** On July 29, 2003, the Authority awarded a contract for \$2,500 for investigative services. The Authority paid a retainer fee of \$1,250 on August 20, 2003, and the balance due of \$1,250 on October 15, 2003. The original contract stated that if additional investigative services were needed, a new contract would have to be approved and signed by both parties. However, on November 14, 2003, the Authority paid the contractor another \$2,500 for additional investigative work without preparing a follow-up contract. In addition, we could not determine if the investigative work was satisfactorily completed because we did not find an investigative report or other evidence of successful completion of the contracted work. Finally, we found that the Authority did not ensure that the contractor had a valid license to do business in the Virgin Islands, as required by the Virgin Islands Code.

**Water Quality Monitoring Services - \$453,797.** The Authority did not use competition to award three projects to a firm that provided water quality monitoring and related services to the Authority. The firm submitted statements of qualifications and proposals for projects at Crown Bay and the Charlotte Amalie Harbor on St. Thomas and at Gallows Bay on St. Croix. Contracts for these three projects were not prepared until June 27, 2003, after the proposed work had already started. Specifically, the Charlotte

Amalie Harbor project started in June 2000 or 35 months before the contract, the Gallows Bay project started in July 2001 or 23 months before the contract, and the Crown Bay project started in April 2003 or about 2 months before the contract. The Authority paid the contractor a total of \$453,797 before issuance of the contracts.

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## **PURCHASE ORDERS**

### **Competitive Procedures Were Not Always Followed**

The Authority did not always follow requirements for competition and file maintenance for purchase orders.

According to Section XI of the procurement manual, the Authority's Purchasing Division is to either fill requisitions from items in stock or follow the competitive bidding procedures to fill requisitions from an outside vendor. The purchasing manual requires that for purchases of \$2,500 or less, the Authority obtain at least two competing price quotations and issue the purchase order to the lowest cost vendor. Although this requisition/purchase order process is intended for the routine purchase of materials and supplies, we found that the Authority also used this process for large, one-time purchases of goods and services.

We reviewed a sample of 50 purchase orders (25 each from 2002 and 2003) totaling \$881,954, out of 2,158 issued totaling \$3.9 million. All 50 purchase orders were in the range of \$3,000 to \$61,000. We were unable to determine if all requisitions were completed as required because 26 of the originating requisitions (13 from each year) could not be located. The Authority also did not comply with the price quote requirement for purchases of \$2,500 or more for 34 of the 50 purchases. We could not determine why price quotations were not obtained in all required cases because of a lack of documentation.

We also noted a case (not part of our sample of 50 purchases) in which purchases from a vendor totaled about \$23,000 in 2002 and \$34,000 in 2003, but the Authority did not enter into a standing supply contract with the vendor and did not solicit competitive price quotations from other similar vendors in order to try to reduce the overall cost of the items being purchased.



### **File Maintenance Requirements Were Not Always Followed**

Section XVII-A to E of the procurement manual state that the Purchasing Office should maintain separate files for requisitions, purchase orders, contracts, receiving reports, and vendors. However, only the requisition and purchase order files were being maintained and, even then, these files were incomplete. For example, we could not locate 26 requisitions related to purchase orders in our sample. In addition, a contract file was not maintained because the Purchasing Office normally did not issue contracts to vendors from which day-to-day purchases of materials and supplies were made. In those cases where supply contracts were issued, they were maintained by either the Maintenance Division or the Accounting Office. Purchasing Office personnel further stated that, in their opinion, there was no need for a separate vendor file, and that receiving reports were not maintained because they were sent to the Accounting Office to be filed with the vendor payment documents. The Authority should either enforce the filing requirements contained in its purchasing manual or revise the manual based on the specific documentation needs of the Authority, consistent with good internal controls.

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### **PAYMENT PRACTICES**

The Authority did not always deduct gross receipt taxes from payments to contractors and service providers, as required by law. The Virgin Islands Code (33 VIC § 44) was amended on September 16, 1997, to require that Government of the Virgin Islands agencies deduct the 4 percent gross receipt tax from any single payment made to contractors in the amount of \$30,000 or more and from any payments made pursuant to a contract in the total amount of \$120,000 or more.

### **Gross Receipt Taxes of \$846,653 Were Not Deducted From Paid Invoices**

Authority officials stated that they were not aware of the new requirement until the Authority received a December 22, 2000 memorandum on the subject from the Bureau of Internal Revenue. The Authority began deducting the gross receipt tax in February 2001. However, it did not deduct the tax from all applicable payments to contractors and service providers. We identified gross receipt taxes totaling at least \$846,653 that were not deducted from payments to nine contractors and service providers for subsequent remittance to the Bureau of Internal Revenue. Specifically:

- Gross receipt taxes estimated at \$700,277 were not deducted from payments made to the construction contractor that worked on the Rohlsen Airport terminal building on St. Croix. Each invoice submitted by the contractor included the gross receipts tax as a separate line item to be reimbursed by the Authority.



However, the Authority did not begin deducting the tax from payments made to the contractor until February 2001.

Similarly, we estimated that gross receipt taxes of \$103,327 were not deducted from payments made to the Rohlsen Airport project management consultant. We were unable to determine, because of the lack of documentation, if these two off-island firms ever paid the gross receipt taxes, totaling \$803,604, to the Bureau of Internal Revenue.

- At least five payments made to the Authority's independent audit firm during fiscal years 2000 to 2004 (through January 2004) met the \$30,000 threshold for withholding gross receipts taxes. We estimated that gross receipts taxes totaling \$6,600 should have been deducted from payments on these invoices but were not. An Authority official said that she "thinks" the audit firm had a tax waiver, but we found that the tax waiver was for taxes in the Commonwealth of Puerto Rico. We also noted that the firm may have avoided the requirement for automatic deduction of gross receipts taxes by splitting invoices that would have totaled more than \$30,000. For example:
  - The audit firm issued four invoices to bill \$57,000 for audit services related to a marine bond issuance. Two of these invoices, which totaled \$37,000 (\$28,000 and \$9,000), were dated 10 days apart: November 8 and 18, 2002.
  - The audit firm also issued four invoices to bill \$95,000 for the fiscal year 2002 financial statement audit. Two of these invoices, which totaled \$50,000 (\$25,000 each), were dated 4 days apart: December 27 and 31, 2002.
- The Authority paid the computer consulting firm \$208,011 in four payments of more than \$30,000 each, but did not deduct gross receipts taxes totaling \$8,320.
- The Authority paid a financial consulting firm \$115,291 in three payments of more than \$30,000 each, but did not deduct gross receipts taxes totaling \$4,612.
- The Authority also did not deduct gross receipt taxes totaling \$16,074 from invoices totaling \$351,156 paid to the firm hired for many marine related projects.

- The Authority did not deduct gross receipt taxes totaling \$7,443 from payments totaling \$186,080 made to four vendors for goods or services procured through purchase orders.

A responsible Authority official could not explain why the taxes were not deducted from these invoice payments. We have provided a list of the contractors and service providers discussed above to the Bureau of Internal Revenue for followup review to determine whether the firms paid all applicable gross receipts taxes.

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## OTHER MATTERS

Although not a part of our overall audit objective, we noted that the Port Authority did not have a formal information technology disaster recovery plan and had not developed user access and security policies. This left the Authority vulnerable to security breaches of its accounting and other automated systems. Additionally, the Authority relied almost exclusively on an off-island computer consultant for work related to its computer systems and accounting software. This also left the Authority vulnerable to the failure of these critical systems without access to immediate, on-site service.

We believe that the Authority should assess its information technology (1) disaster recovery, (2) user access and security, and (3) system maintenance policies and practices, and develop comprehensive guidelines for securing this critical operation. Failure of its computer systems could cripple the Authority's day-to-day operations.

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# RECOMMENDATIONS

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## TO THE EXECUTIVE DIRECTOR OF THE VIRGIN ISLANDS PORT AUTHORITY

We recommend that the Executive Director of the Virgin Islands Port Authority:

1. Provide all employees with responsibilities related to the procurement process with a copy of the Port Authority's Procurement Policy and Procedures Manual, and hold meetings with these employees to familiarize and discuss with them the specific requirements of their positions as related to the procurement process.
2. Develop and implement a tracking system or checklist to ensure that procurement-related requirements are followed for all contracts.
3. Exercise due care during the planning for future capital improvement projects to provide prospective contractors with as detailed and complete project specifications as possible so as to minimize the need for contract change orders and/or amendments.
4. Implement procedures to ensure that contract change orders for Federally-funded capital projects are approved in advance as required by Federal Aviation Administration regulations. Also ensure that future Federally-funded contracts contain the "audit access" clause and any other clauses required by Federal grant requirements.
5. Enforce compliance with the requirements that competitive procedures be used and formal contracts be issued for all contracts related to capital improvement projects and for other types of professional services.
6. Either enforce compliance with the existing internal policies regarding the types of documents that should be maintained in contract and other procurement files, or revise the policies based on the specific documentation needs of the Authority, consistent with good internal controls.
7. Establish and implement record control procedures to ensure the security of procurement files, including the use of file sign-out procedures.

8. Enforce existing policies that require at least two price quotations and the issuance of contracts for purchases of goods and service of \$2,500 or more.

9. Make all contractors aware of the Virgin Islands Code requirement that gross receipts taxes be deducted from payments made by the Port Authority, and implement procedures to ensure that such taxes are withheld and paid over to the Virgin Islands Bureau of Internal Revenue as required by law.

10. Cooperate with the Virgin Islands Bureau of Internal Revenue in ensuring that the contractors and service providers discussed in this report have paid the \$846,653 in gross receipts taxes that wasn't deducted from payments they received from the Port Authority.

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## **AUDITEE RESPONSE**

We received a March 9, 2005, response from the Port Authority's Executive Director. The Executive Director stated that, although he took exception to certain findings and conclusions in the report, he "acknowledges the fact that there is a need for significant improvement." The Executive Director further stated that the Port Authority would take action to (1) revise the Procurement Policy and Procedures Manual for clarity and consistency, (2) establish proper files and maintain appropriate records, particularly for construction contracts, and (3) ensure compliance with Federal rules and regulations pertaining to grants for capital projects and programs, to include monitoring by the Authority's Internal Audit unit. These three actions generally correspond to Recommendations 1, 6, and 4, respectively. However, the response did not address the other seven recommendations. Accordingly, we consider Recommendations 2, 3, 5, 7, 8, 9, and 10 to be unresolved and request additional information for Recommendations 1, 4, and 6 (see Appendix 4).

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## **OFFICE OF INSPECTOR GENERAL REPLY**

An attachment to the Executive Director's response included lengthy comments on specific sections of the draft audit report. For the most part, those comments either (1) took issue with the wording used in the report, rather than addressing the substance of the problem areas noted, or (2) provided generalized statements to the effect that the Port Authority followed appropriate steps during the procurement process, without providing support for such statements. Specific comments included in the response and our replies follow:

- The response stated that the Background section referred to payments made to professional service contractors over a 6-year period, but the Objective and Scope section only referred to audit steps carried out with regard to transactions during fiscal years 2002 and 2003 and, to the extent necessary, during 2004. This is an incorrect interpretation of the audit scope. We performed audit steps for transactions during fiscal years 2002 and 2003, and also extended the steps to “other periods as appropriate” for contracts that were active in fiscal years 2003 and 2004. Therefore, we performed audit steps for periods prior to fiscal year 2002 for contracts that were active in fiscal years 2003 or 2004.
- The response stated that we should not have relied upon the two prior audit reports issued by the Port Authority’s Internal Auditor, stating that those reports were not final reports. We did not rely on the Port Authority’s internal audit reports to either determine our audit tests or reach any of our audit conclusions. We based our audit findings and recommendations on our independently performed audit tests and independently derived audit conclusions. The Executive Director told us about the two reports at the time of our entrance conference for this audit and suggested that we obtain copies from the Internal Auditor, which we did. Furthermore, we cited these reports simply for historical purposes to show that problems similar to those we found had been previously identified by the Internal Auditor.
- The response stated that our conclusion was “misleading and unfounded.” We disagree. Our finding that the Port Authority did not have adequate control over its procurement function is accurate, clearly supported by the details presented in the report, and substantiated by our audit working papers. Further, we noted that the response presented the Port Authority’s procedures to demonstrate that it adequately controlled procurement. However, in virtually every case, the conditions we found during the audit clearly showed that the established procedures were not always followed. This was true with regard to the (1) documentation of procedures used to select contractors; (2) maintenance of complete contract files; (3) justification for contract change orders; (4) documentation of the use of either competitive bidding or competitive negotiation, as appropriate; (5) issuance of formal contracts to professional service providers; (6) solicitation of price quotations for purchases under \$2,500 and issuance of contracts for purchases over \$2,500; and (7) deduction of gross

receipts taxes from payments to contractors. The response glossed over most of the specific examples contained in the body of the report as though they did not exist.

- In responding to our finding on the lack of competition for the award of professional services contracts, the response stressed that such contracts do not have to be advertised but are subject to competitive negotiation. We agree. However, competitive negotiation does not mean no competition. It means the issuance of a request for proposals from potential contractors and the selection of the successful proposal based on qualifications and on the relative quality of the proposal. The Virgin Islands Code allows the Port Authority to use either “competitive bidding” or “competitive negotiation,” as appropriate. But the underlying requirement is that procurement should be based on the principle of competition.
- The response made blanket statements that certain professional service contracts had been approved by the Authority’s Governing Board, but did provide documentation to support these statements.
- The response questioned our conclusion that formal contracts either were not issued or were issued untimely for certain professional services acquired by the Authority, stating that “a mutual agreement between two parties is a bidding (sic) contract.” Lack of written contracts is bad business. The Port Authority should, at a minimum, use a standardized written contract agreement that contains certain clauses to define the goods or services to be acquired, state the cost of such goods or services, define the procedures for dispute resolution, provide for audit access to related contractor records, and otherwise protect the Authority’s interests. This was not done for the professional service contracts cited in this report.
- Lastly, the response states that, contrary to statements in the report, the Port Authority “has taken out gross receipts taxes from all applicable contracts in question from the effective date [December 22, 2000] informed by the [V.I.] Bureau of Internal Revenue.” In that regard, the response included correspondence from one contractor requesting the Port Authority’s assistance in securing a tax clearance letter<sup>3</sup> from

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<sup>3</sup> A tax clearance letter is a form issued by the Bureau of Internal Revenue to certify that a taxpayer is current on payment of all applicable taxes (including gross receipts taxes) as a pre-condition for being allowed to renew its business license.

the Bureau of Internal Revenue so that it could renew its business license. However, the response also included a letter the Bureau of Internal Revenue had issued to the contractor on May 10, 2001, stating that there was no record on file showing that the contractor had paid gross receipts taxes for 1999, 2000, and the first few months of 2001. The Port Authority's response did not include any documentation to demonstrate that this contractor or the other nine contractors/vendors cited in the report had paid applicable gross receipts taxes.

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## APPENDIX 1 - PRIOR AUDIT COVERAGE

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### PORT AUTHORITY INTERNAL AUDIT REPORTS

The August 2002 internal audit report “Review of Quality Builders, Inc.’s CM-At-Risk Services Contract” stated that the Port Authority did not: (1) hold the contractor responsible for gross receipt taxes, (2) hold the contractor accountable for all penalties and interests levied on gross receipts, (3) receive reimbursement for gross receipt taxes billed, (4) hold the contractor responsible for personnel expenses, and (5) ascertain that all invoices were substantiated by supporting documentation before issuing payments. None of the five recommendations related to these findings were implemented.

The December 2000 internal audit report “Discrepancies with Contract Between Birk Hillman Consultants, Inc. and the Port Authority” stated that the Port Authority did not: (1) hold the contractor liable for payment of gross receipts taxes and deduct taxes from payments in accordance with the Virgin Islands Code, (2) require the contractor to submit proof of gross receipts tax payments, (3) establish a tracking mechanism in the Accounting Department to ensure that payments were disbursed in accordance with the contract, (4) obtain receipts for travel expenditures and other out-of-pocket expenses paid to the consultant, (5) notify the consultant that the amount of \$964,020 had related taxes of \$38,560 included in the lump sum, and (6) prepare change orders for an additional \$95,472 that was paid without appropriate authorization. None of the six recommendations related to these findings were implemented.



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## APPENDIX 2 - MONETARY IMPACT

<b>FINDING SECTION</b>	<u>Unrealized Revenues</u>	<u>Unsupported Costs</u>	<u>Questioned Costs</u>
Unsupported Out of Pocket Expenses		\$4,236	
Gross Receipt Taxes Not Deducted from Payments	\$846,653		
Unreimbursed Gross Receipts Taxes	<u>                    </u>	<u>                    </u>	<u>\$1,124</u>
Totals	<u>\$846,653</u>	<u>\$4,236</u>	<u>\$1,124</u>

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All amounts represent local funds.

## APPENDIX 3 – RESPONSE TO DRAFT REPORT



### VIRGIN ISLANDS PORT AUTHORITY

OFFICE OF THE EXECUTIVE DIRECTOR

P.O. Box 301707

ST. THOMAS, USVI 00803-1707

March 9, 2005

Mr. Roger La Rouche  
Assistant Inspector General for Audits  
Office of Inspector General  
U.S. Department of Interior  
184999 C Street, NW (MS-5341)  
Washington, DC 20240

Dear Mr. La Rouche:

Attached you will find a response to the Draft Audit Report entitled  
"Procurement Practices, Virgin Islands Port Authority, Government of the Virgin  
Islands" (No. V-IN-VIS-0001-2004).

While this agency has taken exception to certain findings and conclusions, it  
acknowledges the fact that there is a need for significant improvement. As  
such, this agency will undertake the following:

1. Revise the Procurement Policy and Procedures (Manual) for clarity and consistency.
2. Establish proper files and maintain appropriate records, particularly for construction projects.
3. Ensure compliance with Federal Rules and Regulations pertaining to grants for capital projects and programs. The Internal Audit unit of this agency will provide monitoring services to this end.

This agency is prepared to respond to any further inquiry and to provide any  
additional information required prior to issuance of a final audit report by your  
office.

Sincerely,

Darlan Brin  
Executive Director

DB:bd

pc: Arnold E. van Beverhoudt Jr.  
Field Office Supervisor

[Attachments have been omitted by the Office of Inspector General.]

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## APPENDIX 4 – STATUS OF RECOMMENDATIONS

Finding/Recommendation Reference	Status	Action Required
1, 4, and 6	Management concurs; additional information requested.	Provide a plan of action that includes target dates and the titles of the officials responsible for implementing corrective action.
2, 3, 5, 7, 8, 9, and 10	Unresolved.	Consider the recommendations and provide a response that expresses concurrence or nonconcurrence with each recommendation. If concurrence is indicated, provide a plan of action that includes target dates and the titles of the officials responsible for implementing corrective action. If nonconcurrence is indicated, provide the reason for nonconcurrence and a plan of action that includes alternative corrective action and target dates for addressing the underlying deficiencies.

**If you wish to receive additional CDs of this report, please contact  
the Department of the Interior, Office of Inspector General, at  
202-208-5745**

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