



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

Evaluation of Office of Insular Affairs Oversight of Capital Improvement Projects, Commonwealth of the Northern Mariana Islands



*Oversight of
Saipan Public
Health Facility
Raises Concerns*

Report No. P-GR-NMI-0004-2005

June 2007




United States Department of the Interior
Office of Inspector General
Washington, D.C. 20204

June 08, 2007

Memorandum

To: David B. Cohen
Deputy Assistant Secretary for Insular Affairs

From: Earl E. Devaney 
Inspector General

Subject: Evaluation of Office of Insular Affairs Oversight of Capital Improvement Projects, Commonwealth of the Northern Mariana Islands
(Report No. P-GR-NMI-0004-2005)

Our evaluation of the Commonwealth of the Northern Mariana Islands' (CNMI) Saipan Public Health Facility Project (Project) raises serious concerns about the quality of oversight exercised by your office over CNMI capital improvement projects (CIP) in general and this Project in particular. Our objective was to evaluate CNMI's management of the Project and to identify opportunities for improvement. Because of serious management deficiencies, however, we also evaluated your office's oversight of the Project.

We undertook our evaluation, in cooperation with the CNMI Office of the Public Auditor, at the request of the Legislature of CNMI, which was alarmed by the Project's cost overruns and delays. The attached report to the CNMI Governor and President of the CNMI Senate (Appendix 4) identifies the audit objective, scope, methodology, and management deficiencies, as well as opportunities to significantly improve CNMI's contracting performance and results. These opportunities may not be realized, however, without the active involvement of your office.

The Office of Insular Affairs (OIA) has stated that CIPs are the "building blocks for self-sufficiency in the insular areas," thereby creating a clear nexus between the success of a CIP and the success of your office in meeting the Secretary's mandate to establish sound financial practices, increase economic development, and demonstrate federal responsiveness in insular area communities. As one of the largest and most significant CIPs underway in CNMI, the Project merited your close oversight to help ensure its success. Instead of proactive oversight, however, your office failed to heed obvious red flags, which indicated serious Project management problems, and to use the tools at your disposal to keep the Project on target. Specifically:



Figure 1

► **Troubled Project History.** Since funding was initiated 10 years ago (see Figure 1), the \$17.6 million Project has experienced significant problems as it evolved from a hemodialysis center to a state-of-the-art health facility. From the outset, CNMI's Department of Public Works staff lacked the experience and expertise to contract for and manage a project of this size. Deficiencies included inadequate evaluations of contract proposals and price negotiations, unsupported sole source procurements, and unaddressed contractor nonperformance. The result:

➤ **Questionable contractor selection.** The best qualified firms may not have been selected at the most favorable prices. For example, the architectural and engineering (A&E) contracts were awarded absent any price or cost analysis.

➤ **Excessive costs and duplicative contracts.** CNMI issued contract modifications, without competition, for work that was not critical for a fully functioning facility. It also contracted with two, rather than one, A&E firms and with two construction management firms because in-house expertise was not available. When the first construction management firm failed to comply with its requirement to analyze contractor delay claims, CNMI took no action to recover costs for nonperformance, but instead issued a contract to another firm for this work.

➤ **Disruptions, unnecessary delays, contractor claims, and ultimately a Project that may not be operable because of the failure to plan for the \$5 million to \$8 million needed annually to operate and maintain the Project.**

► **U.S. Army Corps of Engineers (Corps) Reports.** Asked by CNMI to look at CNMI's contracting process, the Corps issued two reports,¹ one in 2003 and another in 2005, both of which identified serious deficiencies in CNMI's contract management. The 2003 report addressed weaknesses in CNMI's management of the CIP program, including the lack of a project team to efficiently administer the program and an experienced legal counsel to help resolve contractual issues. These weaknesses have yet to be corrected.

¹ U.S. Army Corps of Engineers, Honolulu District: *Review of the Operation and Management of the Capital Improvement Program for the Commonwealth of the Northern Mariana Islands*, March 2003. U.S. Army Corps of Engineers, Honolulu Engineer District: *Evaluation of the Design of the Public Health Building, Saipan, Commonwealth of the Northern Mariana Islands*, August 2005.

The 2005 report, which evaluated the design of the public health facility, concluded that the A&E contracts lacked critical provisions to ensure quality and timely deliverables, a condition that we determined was a significant factor in CNMI's inability to resolve design problems with the initial A&E firm. The report also recognized that CNMI lacked the necessary contracting expertise to manage large-scale CIPs and recommended that CNMI seek external assistance in the short term, while it developed long-term expertise.



**Saipan Public
Health Facility
Capital Improvement
Project**

Construction of new wing
(photo right) of the
Commonwealth Health
Center (photo above).
*Photos courtesy:
Office of Inspector General
(OIG)*



Figure 2

Warning signs, such as costly contract modifications, were clearly present throughout the life of the Project and should have prompted your office to step up its oversight to ensure that CNMI had the qualified and experienced officials necessary to administer large-scale CIPs. Although cognizant of the problems that surfaced throughout the Project's history, as evidenced by site visit reports by the two OIA staff located in the CNMI, your office took no action. In fact, your office continued to allocate funds (\$6.5 million to date) and reported the following in its fiscal year 2006 Budget Justification to the Interior and Related Agencies Appropriations Subcommittees:

CNMI has made great strides to strengthen the government's ability to effectively manage infrastructure grants and accelerate the spending of grant funds, and it has been especially diligent by assigning capable individuals to manage grant funds and by supporting project manager positions to monitor projects.

Contrary to OIA's assertions, our evaluation disclosed that CNMI mismanaged the Project to the extent that the new facility may not be fully operational and that OIA now needs to recover its portion of over \$1.2 million of questioned costs identified during our evaluation (see Table 1). Had OIA heeded the early warning signs that the Project

was in jeopardy, it could have mitigated the problems that surfaced and helped to ensure that CNMI had qualified and experienced officials administering the Project.

Table 1 Costs Questioned During Evaluation		
Finding Area	Costs*	Basis for Questioning
Installation of Air Conditioning	\$503,151	Unreasonable costs in excess of independent Government estimate.
Failure of SSFM International, Inc., to analyze contractor claims	45,000	Duplicative contract to Summit Consulting International.
Allocation of Project Management Contract Costs	103,680	Portion of construction management contract costs that did not benefit Project (Contractor was Stanley Good, P.E. dba Azuma Limited).
Construction Delay Claim	588,313	Unsupported contractor claim for delays, based on Summit report.
Total	\$1,240,144	

* Fifty percent of funding for the Project was provided by OIA and 50 percent by CNMI.

Necessity of Active OIA Oversight

Given CNMI's current economic downturn and its lack of contracting expertise, your office must actively oversee CNMI's CIP program to ensure the successful completion of projects. OIA is not using the tools it developed specifically to improve performance and accountability in the insular areas. Your competitive allocation system, implemented in fiscal year 2005, could provide the catalyst for helping CNMI develop a contracting office with highly skilled professionals capable of managing CIP grants. Under the system, any insular area not spending CIP funding effectively could receive less funding in the future. OIA's 2006 Budget Justification delineates the criteria for determining CIP allocations to insular area governments. Key criteria include:

- Reliability and timely completion of single audits, including resolution of findings.
- Prudent financial management.
- Compliance with grant reporting requirements.
- Extent to which CIP projects fulfill economic goals and meet community needs.
- Effective contract administration.

We found that OIA's initial CIP rating in December 2005 did not include "effective contract administration" in its scoring sheets for all four insular areas rated. CMNI, for example, received essentially the same level of CIP funding as the prior year, despite its highly ineffective contract administration of the Project. The problems we found are not unique to the health facility, as CNMI followed similar practices on other CIP projects.

Another management tool is imposing sanctions under Title 43 of the Code of Federal Regulations (43 CFR 12.52),² as appropriate, for a grantee that has a history of unsatisfactory performance. These sanctions include:

- Withholding approval to proceed from one project phase to another until receipt of acceptable evidence of contract performance.
- Additional project monitoring.
- Requiring the grantee to obtain technical or management assistance.

OIA's oversight failure, coupled with CNMI's poor management, has jeopardized the successful completion and operation of the Project. A project that is not complete or usable as planned not only negates your office's goal of helping CNMI develop an "economic backbone," but also endangers the quality of health care for CNMI citizens. Without a fully functioning facility, CNMI will not be able to improve the quality of care for its sick and most vulnerable patients, among them those patients requiring life-sustaining hemodialysis.

Recommendations

We recommend that you take actions to:

1. Participate with CNMI in developing a CIP planning process that ensures the completion of the health facility Project and the funding of both construction and operation and maintenance costs of future CIPs.
2. Initiate appropriate and timely sanctions, such as reducing CIP funding under the competitive allocation system, should CNMI fail to implement the corrective actions in response to our recommendations in the attached report *Evaluation of Saipan Public Health Facility Project: Oversight of Capital Improvement Projects, Commonwealth of the Northern Mariana Islands* (Appendix 4).
3. Take an active role in helping CNMI develop a contracting office with professionals who have the experience and expertise to effectively manage large-scale CIPs. This could include modeling the contracting office along the lines of federal acquisition education, training, and experience requirements.
4. Recover OIA's portion of the questioned costs identified in Table 1 and Appendix 1 of this report.

OIA Response and OIG Reply

Based on your January 22, 2007 response (Appendix 2) and subsequent discussions with OIA staff, we consider Recommendations 1, 2, and 4 to be resolved but

² 43 CFR 12.52 specifies that a grantee may be considered high risk if the federal awarding agency determines that the grantee has a history of unsatisfactory performance, is not financially stable, has a management system that does not meet standards, has not conformed to terms and conditions of previous awards, or is otherwise not responsible.

not implemented and Recommendation 3 to be unresolved. The status of audit recommendations is shown in Appendix 3.

Recommendation 1

In your response you stated that the CNMI health facility is “substantially complete” and that “OIA will continue to work closely with the CNMI Government to ensure satisfactory completion of the Project.” You also stated that OIA, CNMI Government, and Office of the Solicitor have discussed possible solutions to develop the resources necessary to operate and maintain all CIPs on a long-term basis, including developing “a maintenance account funded by a percentage of the CNMI Government’s annual CIP allocation” to cover operation and maintenance (O&M) costs of CIPs and “allocating building space for private-sector use to help generate revenues to cover operating costs.” In subsequent communications with your office, staff identified the OIA official responsible for implementing the recommendation, but stated that determining a completion date would be unrealistic, as the authority to ensure funding of CIP O&M costs may ultimately rest with the Office of the Solicitor or Congress.

OIG Reply. We are pleased to learn of ongoing discussions to address the important issue of ensuring long-term O&M for CIPs, particularly in the case of the health facility, which is essential to improving the quality of health care available to the residents of CNMI. While OIA may not have the final decision-making authority to determine how to cover long-term O&M for CIPs, it is the agency charged with carrying out the Secretary’s mandate to assist in the economic development of the insular areas and to be responsive to their needs. As such, OIA is the logical agency to pursue resolution of the issue of O&M funding for CIPs. Moreover, regardless of who makes the final decision, OIA will be a vital player in that decision, given its special relationship with and knowledge of the insular areas. Finally, we believe that the urgency of addressing long-term O&M costs requires a timetable, particularly when considering the near disastrous effect of the failure to consider these costs on CNMI’s public health facility, which was not completed in October 2006 as scheduled and which has not yet been opened. We therefore request that you provide us with the target date for resolving the issue with the Office of the Solicitor and determining final decision authority.

Recommendation 2

In your response, you stated that your funding allocation process is based, in part, on a grantee’s timely resolution of audit recommendations and that OIA would “incorporate” our “report’s recommendations, as applicable, into the process of allocating OIA funding.” You also stated that over the past several fiscal years, OIA “has reduced the CNMI Government’s CIP funding levels” and that “an initial preparation of the budget for FY 2008 indicates a similar reduction.”

OIG Reply. We commend OIA’s current use of the allocation process to encourage accountability in funding CIPs and request that you provide a target date for incorporating our report’s recommendations into your process for allocating CNMI funding.

Recommendation 3

In your response, you “respectfully assert[ed] that OIA has provided appropriate and effective oversight of the Project” and identified a number of actions taken “to help the CNMI Government to more effectively perform its contract management responsibilities.” In addition, during subsequent communication with your office, staff indicated that OIA cannot mandate a contracting office.

OIG Reply. We disagree on the effectiveness of OIA’s oversight and point to the troubled history of the Project itself as proof of the failure of your office to heed obvious warning signs, such as the 2003 and 2005 Corps’ reports, and step up your oversight to keep the Project on target. The oversight actions cited in your response primarily addressed your assistance in helping CNMI develop project and construction management expertise. While project and construction managers, engineers, and architects may have highly developed technical skills, they generally do not possess the highly specialized contracting expertise needed to effectively manage large-scale CIPs. Recommendation 3 reflects our findings, as well as the conclusions of both Corps’ reports, which identified serious contracting deficiencies and spoke to an urgent need to develop contracting expertise. Without this expertise, the deficiencies identified in both our report and the Corps’ reports will continue to undermine your goal of using CIPs as the “building blocks for self-sufficiency in the insular areas.” While your office may not be able to mandate a contracting office, it can hold CNMI accountable for implementing our audit recommendation and thereby take a proactive role in helping CNMI effectively manage large-scale CIPs. We are therefore requesting that you reconsider the recommendation (see Appendix 3).

Recommendation 4

In your response, you stated that OIA did “not agree with the recommendation” and identified actions that had been taken to address the cost issues. You also asked us to provide you with any additional information on the costs regarding the installation of air conditioning.

OIG Reply. As requested, we provided supporting documents for the air conditioning costs in January 2007. Based on your response and subsequent communications with your staff, we consider Recommendation 4 to be resolved, but not implemented (see Appendix 3).

The legislation, as amended, creating the Office of Inspector General requires that we report to Congress semiannually on all audit reports issued, the monetary effect of audit findings, actions taken to implement our audit recommendations, and recommendations that have not been implemented. The monetary effect of the findings is shown in Table 1 and Appendix 1 of this report.

Please provide a written response to this report by July 13, 2007. The response should supply the information requested in Appendix 3. We appreciate the cooperation shown by your office during our evaluation. If you have any questions regarding this report, please call me at (202) 208-5745.

Appendix 1

Monetary Impact

Finding Areas	Questioned Costs
Installation of Air Conditioning	\$ 503,151
SSFM Deduction for Nonperformance	45,000
Allocation of Project Management Contract Costs	103,680
Construction Delay Claim	588,313
Total	<u>\$1,240,144</u>

Appendix 2

OIA Response



Deputy Assistant Secretary

United States Department of the Interior

OFFICE OF INSULAR AFFAIRS

1849 C Street, NW

Washington, DC 20240

January 22, 2007



Memorandum

To: Earl E. Devaney
Inspector General

From: David B. Cohen
Deputy Secretary for Insular Affairs

Subject: Office of the Inspector General, Draft Report: Evaluation of Saipan Public Health Facility Project Raises Concerns About Oversight of Capital Improvement Projects, Commonwealth of the Northern Mariana Islands Assignment No. P-GR-NMI-0004-2005

The Office of Insular Affairs (OIA) has completed its review of the above-referenced draft report (Draft Report) regarding the Saipan Public Health Facility extension (Project) that has been constructed with OIA Capital Improvement Project (CIP) funds. We appreciate the opportunity to respond to the Draft Report, and respectfully assert that OIA has provided appropriate and effective oversight of the Project.

OIA has worked closely with the Government of the Commonwealth of the Northern Marianas (CNMI) on the Project since its approval by OIA in June 2000. Before processing any payment requests, OIA ensured that initial grant requirements were met. OIA performed reviews as necessary and restricted funding whenever it was determined that such action would help to ensure successful completion of the Project. For example, when design deficiencies were made apparent during the initial course of the construction phase, OIA suspended payments until the issues were resolved. OIA also performed reviews of the costs incurred on the Project and has taken corrective action as necessary. For example, OIA restricted \$170,000 of the grant due to architectural and engineering (A&E) design costs that have been determined ineligible.

During the course of the Project, it became apparent to OIA that the CNMI Government required additional expertise to effectively manage the Project. To help provide technical advice, OIA approved the CNMI Government's request to enlist the aid of the U.S. Army Corps of Engineers. The Army Corps identified deficiencies in the CNMI Government's contract management practices. To help the CNMI Government address the deficiencies, OIA funded a Project Manager Program that enabled the CNMI Government to obtain additional expertise. Project managers were hired by the CNMI Government through the program for each of the CNMI's main islands of Saipan, Tinian and Rota. The Saipan-based project manager was instrumental in identifying problems related to the Project and

ensuring that they were corrected. The Project is now substantially complete with only the installation of furniture, fixtures and equipment remaining. I personally toured the Project earlier this month. It is quite an impressive facility, and will significantly improve the quality of health care that is available to the residents of the CNMI.

The following are OIA's responses to specific recommendations made in the Draft Report:

1. Participate with CNMI in developing a CIP planning process that ensures the completion of the health facility project and the funding of both construction and operation and maintenance costs of future CIPs.

OIA will continue to work closely with the CNMI Government to ensure satisfactory completion of the Project. The Project is substantially complete with only furniture, fixtures, and equipment remaining to be procured.

Although the CNMI Government has committed funding for the Project in its FY 2007 budget, OIA believes that the development of resources available for continued operations and maintenance of all CIPs on a long-term basis is needed, and OIA has been working to identify a solution. In October 2006, OIA discussed its concerns with both the CNMI Government and the Department of the Interior's Office of the Solicitor. Several possible solutions were discussed, including:

- The development of a maintenance account funded by a percentage of the CNMI Government's annual CIP allocation to be used by the CNMI Government on all completed CIPs on an as-needed basis, and
- Allocating building space for private-sector use to help generate revenues to cover operating costs.

2. Initiate appropriate and timely sanctions, such as reducing CIP funding under the competitive allocation system, should CNMI fail to implement the corrective actions in response to our recommendations in the attached report: Evaluation of Saipan Public Health Facility Project: Oversight of Capital Improvement Projects.

OIA's process of allocating funding incorporates a grantee's responses to inquiries and program recommendations made by OIA, compliance with Federal grant requirements, timely resolution of all compliance audit recommendations and resolution of other recommendations as applicable. The information used in the process is compiled by OIA's Accountability Policy Specialist and analyzed in partnership with OIA's grant analysts. OIA is reviewing the report identified above and will incorporate the report's recommendations, as applicable, into the process of allocating OIA funding.

OIA has reduced the CNMI Government's CIP funding levels over the past several years based upon the results of the allocation process. Levels of CIP funding to the CNMI Government totaled \$12.4 million in FY 2005, \$11.2 million in FY 2006 and \$10.6

million in FY2007. An initial preparation of the budget for FY 2008 indicates a similar reduction.

3. Take an active role in helping the CNMI develop a contracting office with professionals who have the experience and expertise to effectively manage large-scale CIPs. This could include modeling the contracting office along the lines of federal acquisition education, training and experience requirements.

OIA takes an active role to help the CNMI Government to more effectively perform its contract management responsibilities. For example:

- As noted above, OIA implemented the CIP-funded Project Manager Program to increase oversight of CIPs with well qualified and experienced technical staff. In October 2006, OIA worked with the CNMI Government to help revise the scopes of work of the project managers. For example, each program manager now has the authority to hire an administrative assistant and construction inspectors as needed. The revisions serve to increase the capacity of the offices of the program managers and, therefore, increase the CNMI Government's contract management capabilities.
- OIA provided funding to the CNMI Government to create a "Special Assistant for CIP" position. The Special Assistant reported directly to the Governor and oversaw the planning, management and technical aspects of the CIP Program in the CNMI. This position was not continued by the current administration.
- OIA supported the CNMI Government's requests for a review of the initial A&E design and a change order audit and analysis of contractor delay claims. OIA also evaluated the Project for possible disallowed costs and will continue to do so periodically.
- As noted above, OIA initiated and funded the Project Manager Program. We are considering expanding it.
- OIA's CIP grant terms and conditions include a provision allowing the grantee to charge costs associated with the administration of CIPs to the grant as well as to procure outside expertise, including engineering expertise, if approved by OIA. This provision is intended to allow the grantee to hire qualified and competent staff for its projects.
- OIA's process of allocating OIA grant funds includes a grantee's resolution of issues of concern raised by OIA. The issues may include concerns over noncompliance with Federal grant regulations related to contract management.
- OIA provides direct funding for training and sponsors conferences and workshops within which topics related to contract management are presented.

4. Recover OIA's portion of the questioned costs identified in Table 1 and Appendix 1 of this report.

OIA does not agree with the recommendation and have addressed each of the cost issues below.

Installation of Air Conditioning - \$503,151

The Draft Report references a CNMI Government's estimate that indicates an overpayment of \$503,151 for the installation costs of the air conditioner. However, the CNMI Government's Saipan-based project manager has stated that he is not familiar with the estimate referenced in the Draft Report, and that he is not aware of any issues regarding the installation costs. Please provide us with any additional information that you may have that might enable us to further evaluate this recommendation.

SSFM Deduction for Nonperformance - \$45,000

According to the CNMI Government's representative, a final payment of approximately \$50,000 to SSFM has been withheld pending further review. The CNMI Government has not completed its analysis of the matter. OIA will work with the CNMI Government and determine the appropriate action to resolve this issue.

Allocation of Project Management Contract Costs - \$103,680

These questioned costs cover a three-year period throughout which the CNMI Government inadvertently charged 100% of the project manager's costs to the Project rather than allocating the costs to the various CIPs for which the project manager was responsible. OIA will work with the CNMI Government to ensure that costs are correctly transferred to the appropriate CIPs. All of the projects are funded by OIA, and no recovery is therefore necessary.

Construction Delay Claims - \$588,313

The CNMI Government has negotiated with construction contractors AIC Marianas and Spectrum to offset claims of approximately \$250,000 and \$67,000, respectively through deductive change orders. Both of the parties have agreed that the negotiated amounts will resolve all of the identified concerns regarding construction delays. It is therefore not necessary for OIA to recover any funds related to this matter.

OIA has performed reviews and identified questioned costs related to the A&E design of the Project. An analysis conducted in FY 2005 determined that only 78% of the design documents prepared by the initial A&E firm were adequate because the structural design did not fully meet the building code standards for this earthquake prone area of the

Pacific. As a result, 22% of the \$775,000 initial design costs, or \$170,500, is to be recovered. No recoupment is necessary at this time as the amount will be held against the final payment on the project. Also, a reduction in the overall grant will be processed prior to the expiration of the grant. OIA does not believe it is prudent to reduce the grant at this time as final costs are not yet known. OIA will continue to perform reviews and take corrective action as necessary.

Thank you again for the opportunity to respond to the Draft Report. My staff is prepared to meet with your office and the CNMI's Office of the Public Auditor at your request. If you have any questions or require additional information, please do not hesitate to contact me directly at 202-208-4736. You or your staff may also contact Mr. Nikolao Pula, Director of Insular Affairs, at 202-208-6816, or Mr. Tom Bussanich, Division Director of Budget and Grant Management, at 202-208-6971.

cc: Roy Kime, OIA Liaison, OIG

Appendix 3

Status of Recommendations

Recommendations	Status	Action Required
1 and 2	Resolved; Not Implemented	Provide target dates for completion of implementation.
3	Unresolved	Reconsider the recommendation and provide a plan identifying actions to be taken, target dates for completion, and titles of officials responsible for implementation
4	Resolved; Not Implemented	Provide (1) documentation showing target dates for resolution of questioned costs related to installation of air conditioning and SSFM's deduction for nonperformance and (2) copies of change orders showing deductions for \$250,000 and \$67,000 for construction delay claims.

Appendix 4

**OIG Report: *Evaluation of Saipan Public Health Facility*
Project: Oversight of Capital Improvement Projects,
*Commonwealth of the Northern Mariana Islands***



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

Office of the Public Auditor
Commonwealth of the Northern
Mariana Islands



Evaluation of Saipan Public Health Facility
Project: Oversight of Capital Improvement
Projects, Commonwealth of the Northern Mariana
Islands

Report No. P-GR-NMI-0003-2005

June 2007



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

Office of the Public Auditor
Commonwealth of the Northern
Mariana Islands



EVALUATION REPORT

June 8, 2007

The Honorable Benigno R. Fitial
Governor of the Commonwealth
of the Northern Mariana Islands
Juan S. Atalig Memorial Building
Isa Drive, Capitol Hill
Saipan, MP 96950

The Honorable Joseph M. Mendiola
Senate President
15th Commonwealth Legislature
P.O. Box 500129
Saipan, MP 96950

Dear Governor Fitial and Mr. Mendiola:

The enclosed report presents the results of our evaluation of the Saipan Public Health Facility Project (Project) by the Office of Inspector General (OIG) and the Office of the Public Auditor for the Commonwealth of the Northern Mariana Islands (CNMI). We conducted the evaluation in response to a request by the CNMI Legislature to recommend appropriate action to ensure Project funds are expended in compliance with applicable laws and regulations. In line with this request, we evaluated CNMI's management of the Project and identified opportunities for improved performance and results. Because of serious management deficiencies, we also evaluated the Office of Insular Affairs' oversight of the Project and are issuing a separate report to the Deputy Assistant Secretary for Insular Affairs. We did not, however, evaluate the claims filed by Project construction contractors because Summit Consulting International (Summit), under contract with CNMI, has reviewed these claims. CNMI is currently using the Summit report in negotiations with Project contractors to settle contractor claims. The scope and methodology of our review are detailed in Appendix 1 of the report.

At \$17.6 million, the Project is one of CNMI's largest capital improvement projects (CIP). Since its inception 6 years ago, the Project's magnitude and scope have changed significantly as it evolved from a hemodialysis center to a state-of-the-art health facility. The construction contract alone increased from \$5.6 million to \$12.5 million, over double the initial contract amount, and Project completion has been delayed to the point that as of the date of this report, it has yet to be completed. Changes in the scope of the Project are only partially responsible for the contract modifications and time delays. Serious deficiencies in the contracting process, including the failure to adhere to established procurement regulations and the lack of qualified and experienced officials to administer the CIP program, significantly affected construction costs and time frames. Some of these issues were noted in U. S. Army Corps of Engineers (Corps) reports,

issued in 2003 and 2005 (Appendix 1), but CNMI failed to use this information to improve its contracting operations. Had CNMI used the 2003 report, for example, it might have mitigated the problems that surfaced on the Project by establishing a strong contracting office and using attorneys trained in procurement regulations to provide critical guidance

The recent downturn in CNMI's economy has heightened our concern, as CNMI has not identified a funding source for the estimated \$5 million to \$8 million needed annually to operate the new facility. CNMI will not be able to improve the quality of care for its sick and most vulnerable patients, including those requiring life-sustaining hemodialysis, without a fully functioning facility. We made four recommendations to help CNMI better manage the contracting process. We believe that implementation of these recommendations can help CNMI minimize contract costs and delays on future CIPs.

In your March 6, 2007 response to our draft report (Appendix 4), you concurred with Recommendations 1, 2, and 3 and directed the Office of the Attorney General, in conjunction with the Secretary of Finance, to take the lead and implement our recommendations within 120 days. Based on the response, we consider these recommendations to be resolved but not implemented. Your response did not address Recommendation 4, and, as such, we consider this recommendation to be unresolved. The status of our recommendations is shown in Appendix 5.

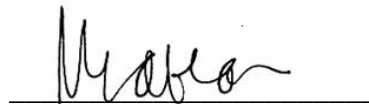
The legislation, as amended, creating the OIG requires that we report to Congress semiannually on all audit reports issued, the monetary effect of audit findings, actions taken to implement audit recommendations, and recommendations that have not been implemented. See Appendix 2 for the monetary impact of the findings in this report.

Please provide a response to Recommendation 4 by July 13, 2007. Your response should state concurrence or nonconcurrence with the recommendation and provide the information requested in Appendix 5. Please address your response to Mr. Kevin Graves, Acting Field Supervisor, Honolulu Field Office, 2800 Cottage Way, Suite E-2712, Sacramento, California 95825. We appreciate the cooperation shown by the CNMI government during our evaluation. If you have any questions regarding this report, please call me at (202) 208-5745 or Mr. Sablan at (670) 322-6481.

Sincerely,



Earl E. Devaney
Inspector General



Michael S. Sablan
Public Auditor, CNMI

Enclosure

cc: David B. Cohen, Deputy Assistant Secretary for Insular Affairs
Nikolao Pula, Director, Office of Insular Affairs
Marina Tinitali, Audit Liaison Officer, Office of Insular Affairs

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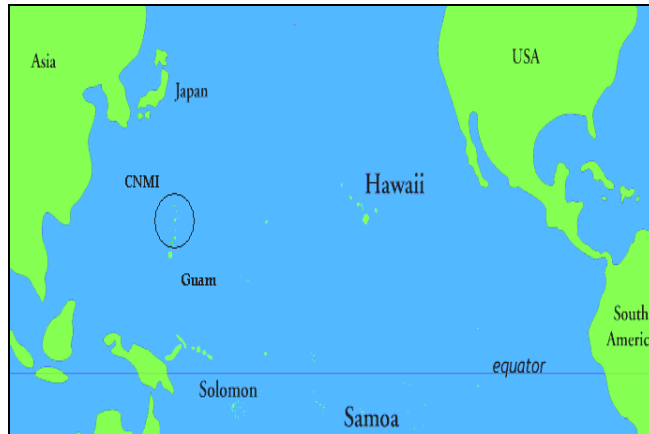
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Acronyms

A&E	Architectural and Engineering
AIC.....	AIC Marianas, Inc.
CIP	Capital Improvement Project
CNMI	Commonwealth of the Northern Mariana Islands
COTR.....	Contracting Officer’s Technical Representative
DPW.....	Department of Public Works, CNMI
IGE.....	Independent Government Estimate
OIA	Office of Insular Affairs, Department of the Interior
OIG	Office of Inspector General, Department of the Interior
SSFM	SSFM International, Inc.

Project History

The Commonwealth of the Northern Mariana Islands (CNMI) is a self-governing Commonwealth of the United States located about 3,300 miles west of Hawaii. CNMI consists of 14 islands, with a total land area of 183.5 square miles and a population of about 70,000. The principal inhabited islands are Saipan, Rota, and Tinian.



Map of Pacific Islands

Figure 1

Source: www.maps-pacific.com
(CNMI reference added by OIG)

The Secretary of the Department of Finance, who is responsible for procurement and supply functions for the CNMI Government, has delegated procurement authority for capital improvement projects (CIP) to the Secretary of the Department of Public Works (DPW). To ensure the efficient functioning of the CIP contracting process, DPW is responsible for (1) reviewing specifications and statements of work to ensure compliance with procurement principles, (2) incorporating required provisions in contracts, (3) negotiating a fair and reasonable contract price, (4) modifying contracts to incorporate changes, and (5) enforcing contract provisions.

At \$17.6 million, the Saipan Public Health Facility Project is one of CNMI's largest CIPs, with 50 percent of the funding (\$8.8 million) provided by the Office of Insular Affairs (OIA) and 50 percent by CNMI. The Project is the first expansion of the Commonwealth Health Center (Center) in about 18 years. Constructed in the mid-1980s on the island of Saipan, the Center was geared for a population of 35,000. Population on the island today is about 62,000.

Based on funding available at the time, the Project was initially conceived as a hemodialysis center.¹ DPW awarded an architectural and engineering (A&E) contract to Leo A. Daly Company to design the Project in October 2000 and a firm, fixed-price construction contract for \$5.6 million to AIC Marianas, Inc. (AIC), in June 2002. Project completion was scheduled for August 2004. To help oversee the Project, CNMI awarded contracts to N. Stanley Good, P.E. dba Azuma Limited (Azuma) and SSFM International, Inc. (SSFM), for construction management services. Project offices, organizations, and responsibilities are shown in Appendix 3.

As funding increased, the Project evolved into a two-tiered, state-of-the-art health facility, with the hemodialysis center on the upper level and executive and administrative offices, bio-terrorism center, and a 10,000 square-foot medical warehouse room on the lower level. A key benefit of the expanded facility was a larger hemodialysis unit. With 29 stations, more than double the stations now available at the Center, hemodialysis patients can receive life-sustaining treatment at reasonable hours of the day. To accommodate its patient workload, the existing hemodialysis center operates 24 hours a day, 7 days a week. In January 2004, a second A&E contract was awarded to Taniguchi Ruth Architects (Taniguchi) to re-design the expanded Project.

As construction began, CNMI encountered design problems which were not resolved by the initial design firm. CNMI modified the Taniguchi contract to re-work portions of the design. The re-work resulted in alleged Project delays and in \$855,535 in claims filed by AIC and its subcontractor for design delays, changes and disruptions. Summit Consulting International (Summit), under contract with CNMI, reviewed these claims, recommended payment of \$267,222, and questioned \$588,313. CNMI is currently using the Summit report in negotiations with Project contractors.

In November 2004, the CNMI Legislature, concerned about cost overruns and delays, asked us to evaluate the Project, a review that we undertook in cooperation with CNMI's Office of the Public Auditor.

¹ Hemodialysis, the most frequently prescribed type of dialysis treatment for patients suffering from kidney failure, involves use of a special filter called a dialyzer or artificial kidney to clean the blood. Most hemodialysis patients require treatment three times a week and an average of 3 hours per dialysis "run."

Results of Evaluation:

Strong Contracting Office Needed to Manage All Capital Improvement Projects

The lack of a strong contracting office impeded construction of the Project from the start. As CNMI's CIP Contracting Office, DPW lacked the contracting expertise, such as a qualified and experienced contracting officer and cost-price analyst, to plan and administer the Project. The costly modifications and delays experienced by the Project as it evolved increased initial contract awards by over \$7 million and delayed Project completion. As shown on Figure 2, the construction contract alone increased from \$5.6 million to \$12.5 million.

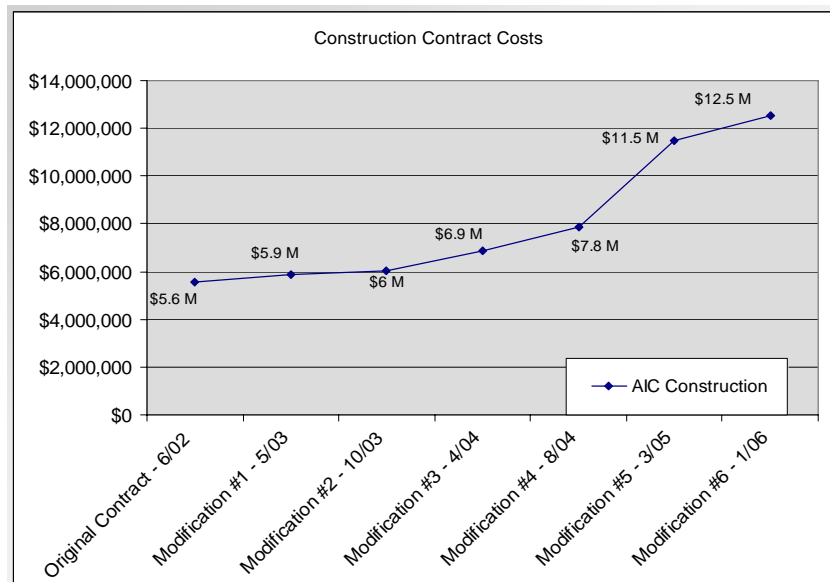


Figure 2

CNMI Failed in Key Areas of Contracting Process

We believe strong contracting office planning and administration could have mitigated the cost overrun and delay problems that surfaced on this Project and ensured compliance with CNMI's procurement regulations. Our evaluation identified significant weaknesses in CNMI's contracting process. Specifically, CNMI officials failed to ensure that (1) contractor proposals were properly evaluated and negotiated, (2) A&E contracts included key provisions to protect government interests, (3) contract modifications were justified and reasonably priced, (4) contractor nonperformance was documented and appropriate corrective

action taken, and (5) costs were properly allocated to the Project.

Evaluation and Negotiation of Contractor Proposals Were Inadequate

The failure of CNMI contracting officials to comply with procurement regulations seriously compromised the evaluation and negotiation of Project contractor proposals. It is CNMI's policy to negotiate contracts for a fair and reasonable price based on demonstrated contractor competence and qualifications. The general process for negotiated contracts is outlined in Figure 3 on page 5.

Deficient Proposal Evaluations. CNMI did not adhere to its procurement regulations involving contractor selection for the two A&E contracts and the Summit contract. To ensure selection of the best contractor, the evaluation process requires (1) qualified evaluators, (2) written evaluation instructions, (3) independent government estimates (IGEs), and (4) oversight by an experienced contracting officer. We found CNMI lacking in all these areas.

Under CNMI regulations, the evaluation team documents the selection decision by assessing the comparative strengths, weaknesses, and risks of each offeror's proposal in terms of the evaluation factors in the solicitation. Our analysis showed that the evaluation team included only numerical scores with minimal comments to support the scores. The scoring system used by the Summit evaluation team was inconsistent; one evaluator, for example, used a one to five scoring system, while a second evaluator used a zero to one scoring system. As a result of deficiencies in proposal evaluations, the contractors selected for the A&E and delayed claim contracts may not have been the best qualified firm.

❖ Develop contract requirement.

❖ Prepare IGE to determine what the contract should cost. The IGE is developed independently without contractor influence, based on the proposed scope of work and historical costs.

❖ Ensure sufficient funds are available.

❖ Conduct market research to determine best method of acquiring goods and services.

❖ Develop acquisition plan to identify key milestones in the acquisition process and address significant technical, management, or other considerations.

❖ Develop source selection plan.

❖ Issue solicitation.

❖ Conduct contractor site visits.

❖ Convene selection team of qualified personnel and provide team with an evaluation plan that includes, at a minimum, (1) statement of evaluation factors and their relative importance, (2) evaluation process methodology and techniques to be used, and (3) documentation requirements.

❖ Evaluate proposals.

❖ Conduct discussions and negotiations.

❖ Prepare post-negotiation memorandum to document the rationale for selecting and awarding the contract and determining reasonability of price.

❖ Award Contract.

❖ Monitor contractor performance.

❖ Close out contract.

General Process for Negotiated Contracts
Figure 3

Poor Negotiation Practices. CNMI did not ensure that contracts, including modifications, were negotiated for a reasonable price, as required by regulations. Specifically, the regulations outline the following types of information that must be reviewed and evaluated when determining price reasonability: (1) the IGE, (2) cost information in sufficient detail to support and justify the contract, and (3) cost information for similar services. CNMI officials stated that A&E contracts were awarded based solely on the contractor's proposed price absent any price or cost analysis or negotiations. CNMI did not develop an IGE or require the contractors to submit a detailed proposal that included a cost breakdown by labor category, labor hours, labor rates, overhead, and profit. Without an IGE and contractor cost breakdown, CNMI could not compare labor hours with labor hours of similar projects, labor rates with labor rate surveys and contractor payroll records, and overhead rates with contractor financial records to determine the reasonability of proposed rates and negotiate a reasonable contract price.

Design Contracts Deficient

As Project construction began, DPW officials and the initial design firm worked to resolve design issues. However, DPW officials said that as the Project moved further along, the firm failed to respond to DPW's numerous requests for information and a key principal of the design team was no longer involved with the Project. Alleged design problems began to surface, and the second A&E firm's scope of work was modified to correct design problems. At the same time, CNMI hired the U.S. Army Corps of Engineers (Corps) to independently assess the Project's design. The Corps' report included an exhaustive list of technical comments on the initial Project design. For example:

- ❖ New site work items, such as roads and parking, were incomplete or not shown.
- ❖ Building finished floor was shown with no possible way for adjacent areas to connect to it.
- ❖ Grading was incorrect.

According to a Corps' official, the absence of key provisions was instrumental in CNMI's inability to resolve alleged design deficiencies with the initial A&E firm. Our evaluation, confirmed by the Corps' report, revealed that

CNMI's A&E contracts lacked key standard provisions usually found in federal government contracts to ensure the professional quality of designs, drawings, specifications, and other services furnished by a contractor. Unfortunately, CNMI uses the same A&E template for all of its CIPs. As a result of CNMI's failure to involve attorneys experienced in procurement, provisions such as those shown in Figure 4 were not included in the contract.

Responsibility of the Contractor
<p>The Contractor shall be responsible for the professional quality, technical accuracy, and coordination of all designs, drawings, specifications, and other services furnished by the Contractor under the contract. The Contractor shall, without additional compensation, correct or revise any errors or deficiencies in its designs, drawings, specifications, and other services (Federal Acquisition Regulation 52.236-23).*</p> <p><i>* To further protect its interest, CNMI should add a time frame to this provision for correcting deficiencies</i></p>
Substitutions of Key Personnel
<p>The Contractor shall provide complete resumes for proposed substitutes and any additional information requested by the Contracting Officer. Proposed substitutes should have comparable qualifications to those of the persons being replaced. The Contracting Officer will notify the Contractor within 15 days after receipt of the required information of the consent of the substitutes. No change in fixed prices may occur as a result of key personnel substitution (Naval Facilities Command (NAVFAC) 52.52.237-9301).</p>

Figure 4

Contract Modifications Were Not Managed Effectively

CNMI management of contract modifications for the Project was also poor. For example, CNMI did not ensure modifications for sole source procurements were justified, reasonably priced, and processed timely, as required by procurement regulations. Effective management of contract modifications is critical, as modifications can significantly increase the cost and duration of a project.

Unsupported Sole Source Procurements. CNMI procurement regulations are designed to promote full and open competition to help ensure the best product or service is obtained at the lowest possible price. In line with these regulations, CNMI awarded the basic contracts for the Project competitively. However, it issued contract

modifications to an incumbent contractor without competition when it should have solicited new bids/contracts. The initial Project plans focused on a fully operational hemodialysis center on the upper level and did not include the completion of the lower level for executive offices and clinics. Examples of lower level items included:

- ❖ Architectural drawings for interior spaces (\$681,600).
- ❖ Additional elevator for lower level (\$110,700).
- ❖ Additional electrical work for lower level (\$398,500).

CNMI contract modifications for these requirements amounted to sole source procurement without a valid reason.

Inadequate Price or Cost Analysis. CNMI did not conduct price or cost analyses² to determine the reasonability of contract modifications and use the analyses in price negotiations. In our opinion, had CNMI conducted such analyses for the following modifications, it may have saved significant costs:

- ❖ Air-Conditioning Equipment - In developing the initial bid, AIC followed the standard contracting practice of soliciting quotes for air-conditioning installation from multiple vendors and selected the lowest priced responsible bidder. However, when CNMI revised the specifications prior to installation and requested AIC to submit a new price proposal, AIC requested only the selected vendor to submit a quote rather than seeking multiple quotes. CNMI eventually approved the modification for \$2,085,481 (\$503,151 more than its engineering estimate). A CNMI official could not provide a valid explanation or post-negotiation documents to explain this significant difference.
- ❖ Construction Management Services - The original management services contract was competitively bid and awarded to SSFM. However, CNMI did not conduct a price or cost analysis or develop an IGE to ensure that modifications to extend the contract were reasonably

² A price analysis evaluates and compares a contractor's proposed price with (1) the IGE, (2) other prices received in response to the solicitation, (3) commercial prices, or (4) previous prices proposed for the same or similar items. A cost analysis analyzes each element of cost in the contractor's proposal and is usually required if a price analysis alone is insufficient to determine reasonability of a proposed price.

priced. CNMI approved a modification for \$186,840 to extend services for 1 year and was in the process of approving a second modification for \$186,840 for an additional 1-year extension at the time of our review. The modification prices were based upon SSFM's initial award. Although CNMI could have negotiated a substantially reduced cost for these modifications based on (1) the expected decline of SSFM's involvement in the Project as it neared completion³ and (2) SSFM's noncompliance with the provisions of the contract, as discussed in the following section, it did not do so. In addition, despite CNMI procurement regulations prohibiting agencies from allowing contractors to work with an expired contract, SSFM was allowed to do so from August 2005 until at least December 2005.

Action Was Not Taken to Address Contractor Nonperformance

CNMI failed to adequately monitor SSFM's performance to ensure compliance with contract terms. CNMI awarded a firm, fixed-price contract to SSFM for project construction management based on SSFM's technical proposal that it had qualified and experienced staff to perform the required tasks and deliverables. These tasks and deliverables included development of IGEs for contract modifications and analyses of contractor delay claims. Despite SSFM's failure to comply with these requirements, CNMI took no action to recover costs from SSFM. CNMI's only reaction to SSFM's nonperformance was to award a \$45,000 fixed-price contract to Summit to analyze construction delay claims that were within the scope of the SSFM contract. As of November 2005, CNMI had not taken any action against SSFM to recoup monies for nonperformance.

Evaluating and documenting contractor performance is a critical contracting best practice. Documentation of deficiencies is vital in seeking corrective actions, including contract deductions and termination. In addition, a contractor's past performance is a key factor in the contractor evaluation process. Federal agencies are required to maintain a contractor performance database that includes the contractor's track record in conforming to contract requirements, schedules, budgets, and standards of good workmanship and demonstrating a commitment to customer

³ SSFM had only one inspector at the construction site on a periodic basis.

satisfaction. CNMI does not have such a database, even though the Corps' 2003 report recommended that CNMI establish one. A contractor performance database would better enable CNMI to evaluate future contract proposals.

Contract Costs Were Improperly Allocated

CNMI did not establish procedures to ensure that project management contract costs were properly allocated to projects. The Project was funded by an OIA-administered grant and is subject to Office of Management and Budget Circular A-87 "Cost Principles for State, Local, and Indian Tribal Governments," which states that costs are allocable to a grant or contract in line with the relative benefits received. CNMI failed to comply with this provision. The Azuma contractor was responsible for managing several projects for CNMI. However CNMI improperly charged the entire \$273,600 to the Project instead of allocating the costs to all benefiting projects proportionate to the benefits received and, as a result, overcharged the Project by about \$103,680⁴ over the 2-year period ending June 2005 (see Figure 5).

PROJECT MANAGEMENT COSTS		
Item	Claimed	Questioned
Original Contract	\$86,400	\$34,560
Modification 1, 2 and 3	\$187,200	\$69,120
Totals	\$273,600	\$103,680

Figure 5

Proprietary Information Was Not Safeguarded

CNMI did not ensure that contractor proprietary information was adequately safeguarded against unauthorized use and disclosure. During the evaluation process, government employees analyze contractor proposals, which include privileged or confidential information, such as cost breakdown; direct labor rates; overhead rates; profit margins; trade secrets; and manufacturing processes, operations, and techniques. Release of this information could result in competitive harm to the contractor or impair the government's ability to obtain like information in the future. The importance of safeguarding proprietary information is such that the federal government enacted government-wide legislation stipulating civil and criminal penalties for

⁴ Based on time estimates spent on the respective projects, as provided by an Azuma official.

**Strong
Contracting
Office Essential**

unauthorized disclosure and use of such information. Although we did not find instances of unauthorized disclosure and use, CNMI did not have adequate control over contractor proposals and was, in fact, unable to locate all contractor proposals submitted for the Project.

The lack of a strong contracting office is the root cause for deficiencies identified in CNMI's contract management. The federal government has long recognized the importance of developing a highly skilled professional acquisition workforce. Studies conducted in the 1970s resulted in improved management of the acquisition workforce and the passage of key legislation. In 1990, for example, the Defense Acquisition Workforce Improvement Act established education, training, and experience requirements for the Department of Defense. The 1996 Clinger-Cohen Act established comparable requirements for civilian agencies. As a result, contracting officials in federal agencies today are required to meet education and experience requirements and undergo a rigorous and extensive training program, including continuing education requirements to maintain or enhance their skills. For example, requirements for a Level II⁵ Contracting Officer are listed in Figure 6.

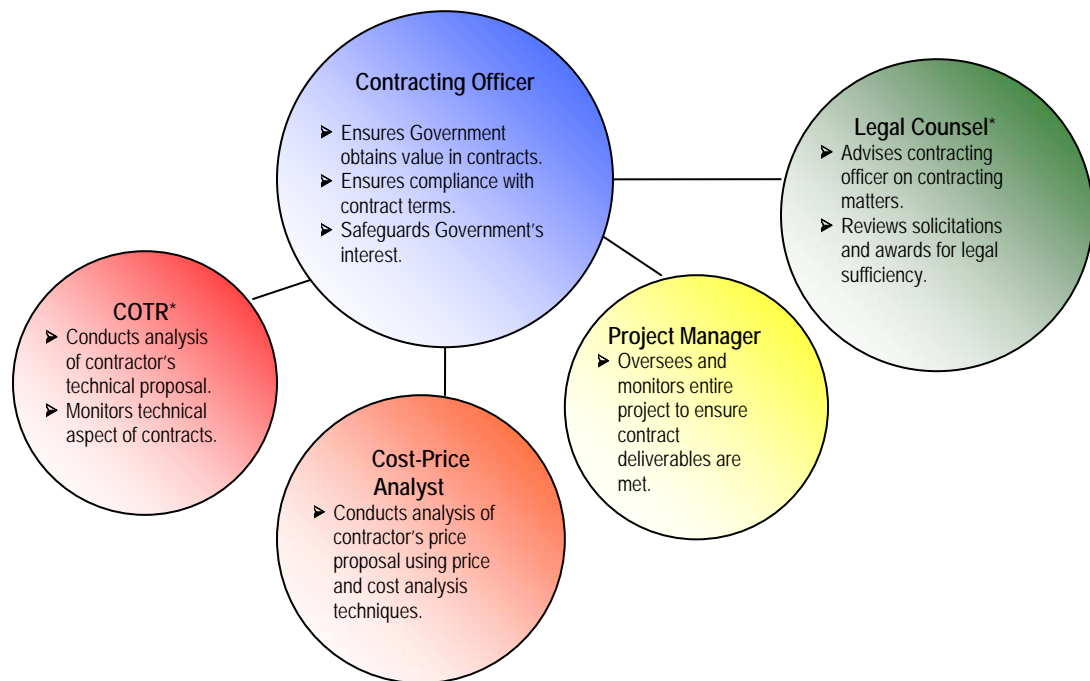
CONTRACTING OFFICER LEVEL II REQUIREMENTS		
Education	Experience	Training
Baccalaureate Degree Minimum of 24 semester hours including accounting, business, law, finance, contracts, purchasing, and industrial management	Two years of contracting experience	Contracting Contract Pricing Government Contract Law

Figure 6

Key contracting officials in CNMI, however, are political appointees and often lack the contracting expertise to plan and administer CIP projects. In this case, DPW did not have a qualified and experienced contracting officer or cost-price analyst to plan and administer the Project. The practice of using political appointees also results in the lack of continuity for complex long-term CIPs, such as this Project. In 2006,

⁵ Level II normally provides signature authority for acquisitions up to \$5 million.

for example, CNMI elected a new administration, and the Project's contracting officer and contracting officer's technical representative (COTR), both political appointees, subsequently resigned. Political appointments may also result in the selection of individuals who may not be the best qualified for the position. Both the contracting officer and COTR positions are critical in developing a strong contracting office and ideally should be filled by individuals who have permanent status and meet requirements comparable to their federal counterparts. In addition, the contracting officer should be assisted by an experienced cost-price analyst and other key advisors, as illustrated in Figure 7.



*Provided, as needed, from departmental offices.

Key Advisors to Contracting Officer
Figure 7

Although CNMI has launched initiatives to improve CIP management in the past, these initiatives were not enough. Like its federal counterparts, CNMI needs top-level commitment to develop a contracting office with highly skilled contracting professionals, capable of effectively managing large-scale CIPs if CNMI is to fulfill development goals and maintain financial support for infrastructure improvements.

Recommendations

We recommend that the Governor of the Commonwealth of the Northern Mariana Islands:

1. Develop a contracting office with highly skilled professionals, along the lines of federal requirements, who are capable of effectively managing large-scale CIPs.
2. Use the Federal Acquisition Regulation as the framework to identify best practices and the general framework for revising A&E contracts.
3. Direct contracting officials to comply with existing grant and procurement regulations, specifically, to:
 - Use full and open competition to the fullest extent possible.
 - Develop and use IGEs as a baseline for negotiating a fair and reasonable price for goods and services and ensuring contractors clearly understand contract requirements.
 - Document the contract and modification price reasonability determination.
 - Select the best qualified contractor by ensuring the evaluation team is 1) knowledgeable and qualified, 2) provided written evaluation instructions, and 3) under the supervision of an experienced contracting officer.
 - Allocate costs to projects based on benefits received.
 - Safeguard proprietary information.
4. Establish and maintain a CNMI-wide contractor performance evaluation database to assist with the evaluation process and document and take appropriate corrective actions for contractor nonperformance.

**Governor's
Response and
OIG Reply**

In his March 6, 2007 response to our draft report (Appendix 4), the Governor concurred with Recommendations 1, 2, and 3 and directed the Office of the Attorney General, in conjunction with the Secretary of Finance, to take the lead in implementing the recommendations within 120 days. The Governor stated that “full compliance will be contingent on the availability of funding required to establish the contracting official position,” but also stated that preliminary discussions with the Office of Insular Affairs “has indicated willingness to provide the necessary funding.” Based on the response, we consider these recommendations to be resolved but not implemented and will follow up with the Office of Attorney General after the 120-day implementation time frame.

The Governor’s response did not address Recommendation 4. As such, we request that the Governor respond to the recommendation and provide the information requested in Appendix 5.

Appendix 1

Objective, Scope, and Methodology

Our objective was to evaluate CNMI's management of the Project and identify opportunities for improved performance and results. Because of significant management deficiencies, we also evaluated OIA's oversight of the Project. We conducted the on-site (fieldwork) portion of our evaluation from November 2005 through March 2006. Our evaluation was conducted in accordance with the January 2005, *Quality Standards for Inspections*, issued by the President's Council on Integrity and Efficiency. To accomplish our objective, we:

- ❖ Reviewed CNMI procurement regulations, public laws, grant documents, contract documents, financial and progress reports, Corps' reports, and the Summit report.
- ❖ Interviewed CNMI officials, staff, and contractors.
- ❖ Reviewed the Department of the Interior's *Fiscal Year 2005 Performance and Accountability Report*, including information required by the Federal Manager's Financial Integrity Act. The Department reported the need to increase economic self-sufficiency for insular areas and address persistent management problems in these programs.
- ❖ Reviewed internal controls and identified weaknesses relating to Project management and identified opportunities for improved performance and results.

We did not evaluate the Project's initial A&E firm's compliance with contract terms because the Corps, under contract with CNMI, had conducted a comprehensive evaluation of the Project design that included coverage of this area. We also did not evaluate the claims filed by Project construction contractors because Summit, under contract with CNMI, had reviewed these claims. CNMI is currently using the Summit report in negotiations with Project contractors to settle the claims.

During the past 5 years, neither OIG nor the Government Accountability Office has issued any procurement reports on the CNMI Government. However, a 2003 OIG report on the

Commonwealth Ports Authority's Saipan Harbor Project⁶ identified significant weaknesses in project management. Specifically, the Authority (1) did not adequately analyze or justify contract change orders and incurred contract cost overruns totaling \$6.9 million, (2) entered into a noncompetitive contract for construction management services, and (3) improperly used liquidated damages of \$980,000 from the Saipan Harbor Project for a project on Rota.

A 2003 OIG report to the Office of Insular Affairs on grant administration⁷ addressed the need for improved monitoring of grants to insular areas. In addition, the following reviews conducted by other entities are relevant to the Project:

- ❖ U.S. Army Corps of Engineers, Honolulu District: *Review of the Operation and Management of the Capital Improvement Program for the Commonwealth of the Northern Mariana Islands*, March 2003. The report identified significant shortcomings that hindered efficient and effective management of projects. These shortcomings included (1) lack of a dedicated project team, (2) absence of a contractor performance evaluation database, and (3) conflicting procurement regulations.
- ❖ U.S. Army Corps of Engineers, Honolulu Engineer District: *Evaluation of the Design of the Public Health Building, Saipan, Commonwealth of the Northern Mariana Islands*, August 2005. The report identified serious deficiencies in A&E contracting procedures for the Project. It also identified the need for a strong contracting office.
- ❖ Summit Consulting International: *CNMI Public Health Center – Change Order Audit and Analysis*, June 2005. The report provided the results of Summit's analysis of the \$855,535 in delay claims submitted by AIC and its subcontractor for alleged Project design delays, disruptions, and changes. Summit questioned \$588,313 of the claimed amount.

⁶OIG: *Commonwealth Ports Authority - Saipan Harbor Improvement Project*, Report No. 2003-I-0073, September 2003.

⁷ OIG: *Report on Grants Administered by the Office of Insular Affairs*, Report No. 2003-I-0071, September 2003.

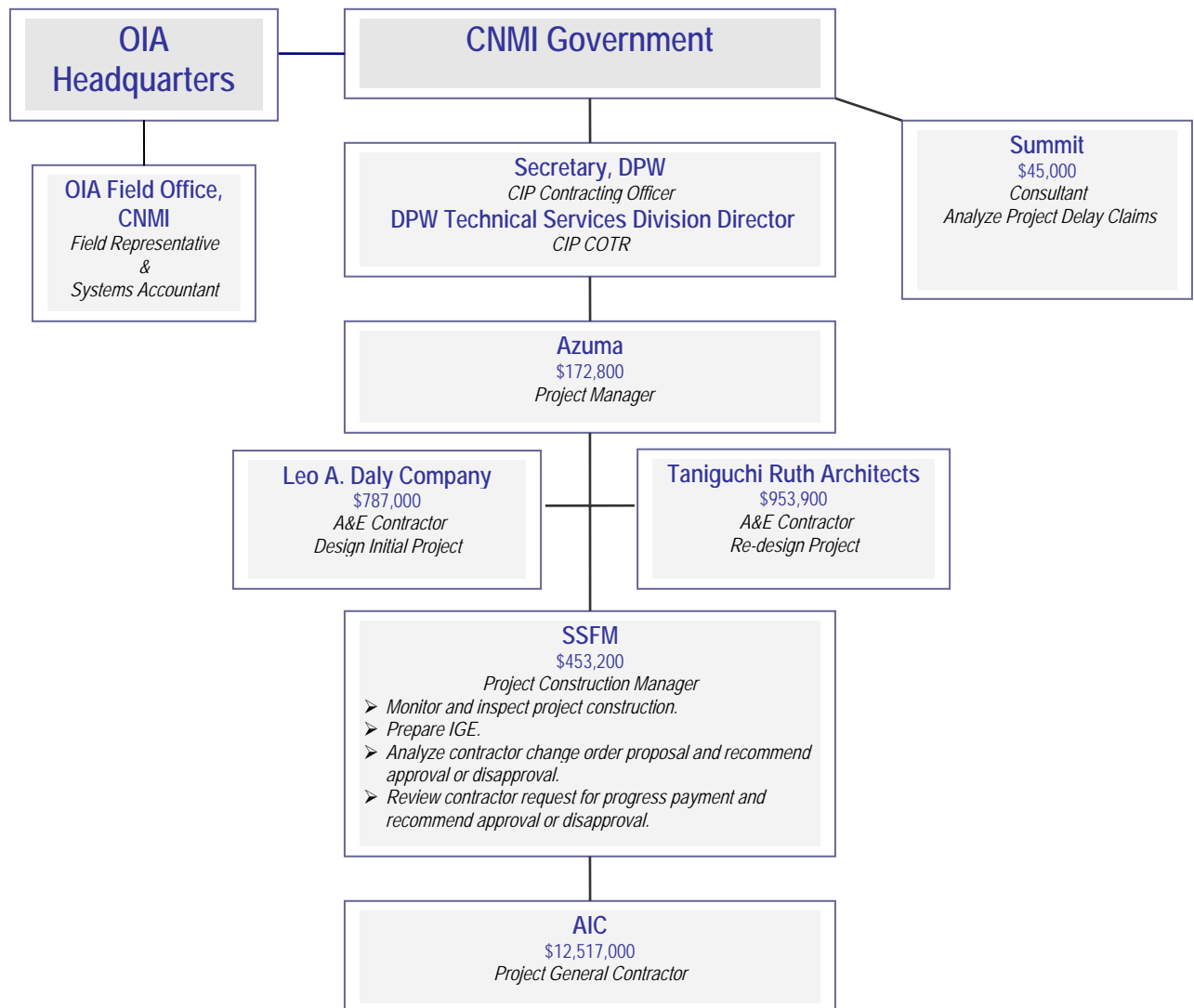
Appendix 2

Monetary Impact

Finding Areas	Questioned Costs
Installation of Air Conditioning	\$ 503,151
SSFM Deduction for Nonperformance	45,000
Allocation of Project Management Contract Costs	103,680
Construction Delay Claim	588,313
Total	<u>\$1,240,144</u>

Appendix 3

Project Offices, Organizations, and Responsibilities



Appendix 4

CNMI Government Response



COMMONWEALTH OF THE NORTHERN MARIANA ISLANDS

Benigno R. Fitial
Governor

Timothy P. Villagomez
Lieutenant Governor

MAR 06 2007

Ms. Anne L. Richards
Assistant Inspector General for Audit
U.S. Department of the Interior
1849 C Street, NW, MS 5341
Washington, D.C. 20240
Fax (808) 525-5322

Re: Evaluation of Saipan Public Health Project
Assignment No. P-GR-NMI-0003-2005 (November 2006)

Dear Ms. Richards:

Since our last communication regarding the audit of the Saipan Public Health Project (Assignment No. P-GR-NMI-0003-2005) ("Audit"), representatives of the Executive Office of the Commonwealth of the Northern Mariana Islands ("Commonwealth") have met with the Public Auditor and your staff to discuss our previously identified concerns.

As a result of these discussions, the Commonwealth has decided not to comment on the statement of facts contained in the Audit and to restrict our comments to the recommendations. Specifically, the Commonwealth endorses the three recommendations contained in the Audit, as are summarized below.

1. Development of a contracting office based on the federal model.
2. Establishment of standards for development and amendment of architect and engineering contracts based on the Federal Acquisition Regulation standards.
3. The establishment of requirements for compliance with existing grant and procurement regulations by contracting officials.

I have directed the Office of the Attorney General to take the lead in the implementation of these recommendations in conjunction with the Secretary of Finance. These changes should be implemented within 120 days of the date of this communication, however full compliance will be contingent on the availability of funding required to establish the contracting official position. Preliminary discussions with the Department of Interior Office of Insular Affairs has indicated willingness to provide the necessary funding.

Please allow this letter to supersede our earlier comments on the Audit. If you have any questions or comments on this matter, please contact me.

Respectfully,


TIMOTHY P. VILLAGOMEZ

c.c. Senate President Joseph M. Mendiola

Caller Box 10007 Saipan, MP 96950 Telephone: (670) 664-2200/2300 Facsimile: (670) 664-2211/2311

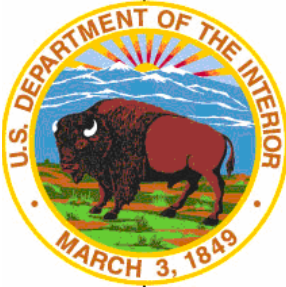
Appendix 5

Status of Recommendations

Recommendations	Status	Action Required
1, 2, and 3	Resolved Not Implemented	We will follow up with the Office of the Attorney General after the 120-day implementation time frame.
4	Unresolved	<p>If you concur with the recommendation, please provide a plan of action that includes target dates and the titles of the officials responsible for implementing corrective action.</p> <p>If you do not concur, please state the reason for nonconcurrence and provide a plan of action that includes alternative corrective action and target dates for addressing the underlying deficiencies.</p>

Report Fraud, Waste, Abuse and Mismanagement

Fraud, waste, and abuse in government concerns everyone: Office of Inspector General staff, Departmental employees, and the general public. We actively solicit allegations of any inefficient and wasteful practices, fraud, and abuse related to Departmental or Insular area programs and operations. You can report allegations to us in several ways.



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