



OFFICE OF
INSPECTOR GENERAL
U.S. DEPARTMENT OF THE INTERIOR

CAPITAL IMPROVEMENT PROJECTS ADMINISTRATIVE FUNCTIONS

Procurement Deficiencies Plague the Virgin Islands
Port Authority





**OFFICE OF
INSPECTOR GENERAL**
U.S. DEPARTMENT OF THE INTERIOR

SEP 08 2010

Memorandum

To: Anthony M. Babauta
Assistant Secretary for Insular Affairs

From: Mary L. Kendall *Mary L. Kendall*
Acting Inspector General

Subject: Final Audit Report "Capital Improvement Projects Administrative Functions:
Procurement Deficiencies Plague the Virgin Islands Port Authority"
(Report No. VI-IN-OIA-0004-2010)

Our recent audit of the Virgin Islands Port Authority's (Authority) administration of capital improvement projects (see attachment) revealed program weaknesses that leave the Authority vulnerable to fraud, waste, and mismanagement. Specifically, the Authority's procurement and financial reporting deficiencies have resulted in inefficient and opaque operations, as well as loss of Virgin Island Government (Government) revenues. The problems we observed are not new, having been identified and reported on 5 years ago. We provided recommendations then that have gone unheeded.

Specifically, we found that the Authority regularly circumvented or inadequately documented the procurement process in the issuance of its capital improvement projects. We had, therefore, little or no assurance that contracts were issued to the most qualified, responsive, and deserving contractors. Further, capital improvement files were generally disorganized and incomplete. The files were in such disarray that we could not determine if the Authority followed basic procurement procedures. The disorganization so impeded our audit that we were forced to meet with the Authority's Executive Director and the Engineering Director in an attempt to obtain missing documents. Despite our best efforts at this meeting, the Authority still could not produce the documents that we requested. We therefore questioned over \$5.5 million in project costs.

In addition, we found a myriad of deficiencies in the Authority's financial reporting, such as inaccurate records of payments to contractors and service providers, unreported payments, and non-issued tax forms. Those deficiencies resulted in \$84.3 million in unreported income to contractors and \$12.6 million in taxes lost to the Virgin Islands Government.

In his response to our draft report, the Governor of the Virgin Islands (Governor) agreed that the lack of timely tracking of documentation impeded the Authority's ability to prove its compliance with basic procurement best practices. The response included input by the Authority's Executive Director, who agreed with four of the five recommendations, but took exception to certain findings and conclusions in the report. Based on these responses, which are included in the subject report, three recommendations to the Governor are considered resolved

and implemented, one remains unresolved, and one is resolved but not implemented. The status of all recommendations is shown in appendix 6 of the attachment.

One of the two recommendations to the Governor that require further action concerns initiation and completion of projects without benefit of contracts. The Executive Director maintains that the Authority used competitive contract procedures in all contracts recommended by the Engineering Division; that formal contracts were issued for all work related to capital improvement projects; and that the selection process related to the Crown Bay Dock and Retail Development Project was documented. We are referring the implementation of this recommendation to you for oversight. The Executive Director must provide evidence to the Office of Insular Affairs (OIA) that the procurement process was followed.

The unimplemented recommendation to the Governor concerns non-issuance of Internal Revenue Service (IRS) Forms 1099. The Executive Director and Director of Administration and Finance must provide copies of IRS Forms 1099 for contracts issued during the third quarter of fiscal year 2010. Continuing compliance with Federal requirements regarding issuance of IRS Forms 1099 and their submission to the Bureau of Internal Revenue is required.

Due to the long-standing, pervasive nature of the deficiencies described in the subject report, resolution and implementation of recommendations to the Governor may be in question. We recommend, therefore, that OIA:

1. Ensures that the Virgin Islands Government obtains from the Authority documentation that may demonstrate adherence to required procurement processes; determines whether such documentation supports the Executive Director's non-concurrence; takes appropriate action in the absence of documentary proof (see report recommendation number 1); and that the Government obtains copies of IRS 1099s for contracts issued, as appropriate by quarter (see report recommendation number 5).

Please provide us with your written response to this report, number VI-IN-OIA-0004-2010, within 30 days. The OIA response should provide information on actions taken or planned to address Authority provision of documentation that demonstrates that the required procurement process was followed and of IRS 1099s for contracts issued during the third quarter of fiscal year 2010, target dates, and titles of the officials responsible for implementation. Please address your response to:

Ms. Kimberly Elmore
Assistant Inspector General for Audits, Inspections and Evaluations
U.S. Department of the Interior
Office of Inspector General
1849 C Street, NW., MS 4428
Washington, DC 20240

If you have any questions regarding this memorandum or the subject report, please do not hesitate to contact me at (202) 208-5745.

Attachment



OFFICE OF
INSPECTOR GENERAL
U.S. DEPARTMENT OF THE INTERIOR

CAPITAL IMPROVEMENT PROJECTS ADMINISTRATIVE FUNCTIONS

Procurement Deficiencies Plague the Virgin Islands
Port Authority





**OFFICE OF
INSPECTOR GENERAL**
U.S. DEPARTMENT OF THE INTERIOR

SEP 08 2010

The Honorable John P. deJongh, Jr.
Governor of the Virgin Islands
No. 21 Kongens Gade
St. Thomas, VI 00802

Re: Final Audit Report, "Capital Improvement Projects Administrative Functions —
Procurement Deficiencies Plague the Virgin Islands Port Authority"
(Report No. VI-IN-VIS-0003-2009)

Dear Governor deJongh:

This final report presents the results of our audit of administrative functions related to capital improvement projects initiated by the Virgin Islands Port Authority (Authority). We found procurement and financial reporting deficiencies much like those cited 5 years ago in our Report No. V-IN-VIS-0001-2004, "Procurement Practices, Virgin Islands Port Authority, Government of the Virgin Islands." Such longstanding deficiencies have led to an operation so inefficient that transparency cannot exist and have resulted in lost Virgin Islands Government revenues.

We received your May 19, 2010 letter regarding the draft of this report, with its enclosed response from the auditee (see appendix 1). We are pleased that you concur with the fact that the lack of timely tracking of documentation impeded the Authority's ability to substantiate compliance with basic procurement best practices. We also understand your hope that we would be able to revise our draft report. Upon careful review of the auditee's input, however, we found assertions in lieu of any new or exculpatory data (see appendix 2 for our response to the auditee).

We offer, therefore, five recommendations designed to improve the performance of administrative functions related to capital improvement projects in the Virgin Islands. Based on your response to our draft report, we consider recommendation 1 unresolved; recommendations 2, 3, and 4 resolved and implemented; and recommendation 5 resolved but unimplemented.

Please provide a response to this report by October 5, 2010 to our Caribbean Field Office, Ron deLugo Federal Building — Room 207, St. Thomas, VI 00802. The response should provide information on actions taken or planned to address findings related to recommendations 1 and 5. The response should also include target dates and titles of the officials responsible for implementation.

If you have any questions concerning this report, you may contact me at (202) 208-5745 or Mr. Hannibal M. Ware, Assistant Regional Manager, at (340) 774-8300.

Sincerely,

A handwritten signature in dark ink, appearing to read "Mary L. Kendall". The signature is fluid and cursive, with the first name "Mary" and last name "Kendall" clearly distinguishable.

Mary L. Kendall
Acting Inspector General

Table of Contents

Why We Performed This Audit 1

 Overview of the Virgin Islands Port Authority 1

What We Found 2

 Procurement Deficiencies 2

 Financial Reporting Deficiencies 4

Conclusion and Recommendations 6

 Conclusion 6

 Recommendations 6

Appendix 1: Governor of the Virgin Islands Response 7

Appendix 2: Office of Inspector General Reply to Auditee Response 19

Appendix 3: Scope and Methodology and Prior Coverage 21

 Scope and Methodology 21

 Prior Coverage 21

Appendix 4: Capital Improvement Projects Renewed 22

Appendix 5: Monetary Impact 24

Appendix 6: Status of Audit Recommendations 25

Why We Performed This Audit

We conducted this audit as part of our annual work plan, which requires assessment of performance of administrative functions related to the initiation and completion of Virgin Islands Port Authority (Authority) capital improvement projects (see appendix 3 for scope, methodology, and prior coverage).

Overview of the Virgin Islands Port Authority

The Authority is an instrumentality of the Virgin Islands Government that manages all airports and seaports, with the exception of the West Indian Company Dock. The Authority's Engineering Department manages all capital improvement projects and related contracts for architectural, engineering, and construction services. The Authority's Director of Engineering is the custodian of contract files for these projects, which are funded by federal and local grants, bond issuances, and a variety of fees.

Between 1998 and 2008, the Authority recorded initiation of 109 capital improvement projects, each of which required the hiring of various contractors and service providers. These 109 projects totaled \$211.7 million.

What We Found

The Authority's administration of multi-million dollar capital improvement projects leaves the Virgin Islands Government vulnerable to fraud, waste, and mismanagement — as it has for many years. In particular, its failure to address longstanding procurement and financial reporting deficiencies related to capital improvement projects has precluded efficient operations and hampers the ability to collect all Virgin Islands Government revenues.

Five years ago, we cited many of the same deficiencies identified in this audit. The recommendations for corrective actions that we made then have been ignored. The Authority continues to disregard its own internal rules and regulations in the selection of contractors and the award of contracts for capital improvement projects.

During this audit, we reviewed 12 capital improvements projects (see appendix 4). These projects totaled \$86.2 million and included 118 contractors and service providers. In terms of procurement deficiencies, we found that some projects were initiated and completed without contracts in place to protect the Authority's best interest. In other projects, contract files were haphazardly maintained without evidence to support actions taken. In terms of financial reporting deficiencies, project costs were not accurately recorded. Further, IRS Forms 1099 were not issued to ensure all payments to service providers were reported to the Internal Revenue Bureau.

Procurement Deficiencies

Although the Authority has policies and procedures in place that require it to competitively select contractors and service providers, we found that it does not comply with those requirements. For example, the Engineering Department routinely ignores the Authority's detailed, 14-step process for ensuring accountability and transparency (see Figure 1). Further, we found the Authority's procurement filing system to be pervasively disorganized and its individual project files to be incomplete. This failure of proper performance of administrative functions permits inefficient operations, jeopardizes the Authority's financial interest, and increases the potential for fraud, waste, and mismanagement.

Of the 12 capital improvement projects that we reviewed, nine evidence procurement deficiencies. In those nine projects, worth \$75 million, the Authority either circumvented or inadequately documented the procurement process. We were, therefore, unable to find any evidence that the required documents exist and have no assurance that the Authority issued contracts to the most qualified, responsive, and deserving contractors.

The most egregious example of circumvention concerns the Lindbergh Bay Park. By classifying the project as “in-house,” the Authority avoided the normal contracting process and retained control over \$900,000 in project funds. The Authority then used \$443,300 of those funds to hire the “casual labor” of private citizens. In other words, none of the casual laborers who worked on this project was an Authority employee. Further, none provided services under a formal contract. Finally, upon project completion, the former Executive Director of the Authority (who also planned and managed the project) hired three of these private citizens to work for the Authority. The three had received \$394,400 of the \$443,300.



Figure I.

In terms of documentation, we found disorganization and incomplete files. Many files had been strewn across all areas of the Engineering Department, including empty cubicles and offices (see below). Overall, the majority of project files were in such disarray that we could not determine if the Authority followed proper procurement procedures.

This disorganization so impeded our audit that we were forced to meet with the Authority’s Executive Director and the Engineering Director in an attempt to obtain missing documents. Despite our best efforts at this meeting, the Authority still could not produce the documents that we requested.



Figure 2. Project files strewn across cubicles.

In addition, many project procurement files are incomplete. We were forced to work with copies of contracts because the Authority was unable to provide the originals. Further, many files fail to document how contractors were selected or whether they met basic requirements for conducting business in the Virgin Islands. We provide two examples below of projects with incomplete files.

- Crown Bay Dock and Retail Development Project, worth \$39 million. Of the 35 contracts involved in the development project, the Authority could not locate procurement files for 32, which were valued at \$4.2 million.
- Crown Bay Dredging Project, worth \$966,060. The procurement file for the primary contractor, which was paid \$897,000, could not be located. Also, the Authority included contract wording that indicated the existence of two bidders rather than to document the selection process.

Financial Reporting Deficiencies

Our review of the Authority's financial reporting revealed a myriad of deficiencies, such as inaccurate records of payments to contractors and service providers of \$1.3 million, unreported payments, and non-issued tax forms. In the case of the Enighed Pond Marine Terminal Project, the Authority reported that \$15.5 million was expended. In fact, we discovered that project costs of \$16.5 million were expended — \$1 million over the reported amount. Absent the accurate recording of project costs, the Authority cannot have a true financial picture, because it cannot properly capitalize its assets.

Moreover, during the past 10 years, the Authority has failed to:

- Prepare and issue required IRS Forms 1099 for any contractors and service providers who received payments over \$600; and
- Report \$84.3 million in payments made to contractors and other service providers.

This failure to follow financial reporting requirements hinders the Government of the Virgin Islands from collecting all its taxes. Utilizing a conservative tax rate of

15 percent, the Virgin Islands Government potentially lost \$12.6 million in much needed tax revenues (see appendix 5) over this period.

Conclusion and Recommendations

Conclusion

Procurement best practices require that a properly documented procurement file provide an audit trail from the initiation of the acquisition process to the beginning of the contract. The file should provide a complete background, including the basis for the decisions made at each step in the acquisition process. A well-documented file should:

- Speak for itself, without need of interpretation;
- Support actions taken;
- Provide information for reviews and investigations; and
- Furnish essential facts in case of litigation.

The Authority fails to meet this standard even though it has rules and regulations in place that require it to competitively select contractors and service providers, ensure efficient operations, and protect its financial interests. The Authority does not even record project costs accurately or comply with financial reporting requirements. Its institutional inefficiency and poor procurement and financial reporting practices leave the Virgin Islands Government subject to fraud, waste, and mismanagement, as well as hinder the collection of all taxes owed.

Recommendations

To improve performance of administrative functions related to capital improvement projects at the Virgin Islands Port Authority, we recommend that the Governor of the Virgin Islands ensure that the Authority:

1. Comply with the requirements to use competitive contract procedures and to issue formal contracts for all work related to capital improvement projects.
2. Develop and implement a tracking system or checklist to make sure that procurement-related requirements are met for all contracts.
3. Follow existing internal policies regarding the documents that should be maintained in contract and other procurement files.
4. Record capital improvement project costs accurately.
5. Issue IRS Forms 1099 to contractors and service providers and forward copies to the Internal Revenue Bureau.

Appendix I: Governor of the Virgin Islands Response



THE UNITED STATES VIRGIN ISLANDS

OFFICE OF THE GOVERNOR
GOVERNMENT HOUSE

Charlotte Amalie, V.I. 00802
340-774-0001

May 19, 2010

Ms. Mary L. Kendall
Acting Inspector General
United States Department of the Interior
Office of the Inspector General
Caribbean Field Office
Ron deLugo Federal Building, Room 207
St. Thomas, Virgin Islands 00802

Re: Response by the Government of the Virgin Islands to United States Department of the Interior, Office of the Inspector General's (OIG) Draft Audit Report, Capital Improvement Projects Administration Functions, Virgin Islands Port Authority (Report No. VI-IN-VIS-0003-2009)

Dear Ms. Kendall:

I acknowledge receipt of the above-referenced draft audit report, which was transmitted with correspondence dated May 15, 2010. Since the beginning of my Administration, I have stressed the importance of Government accountability including the accountability of an autonomous governmental instrumentality such as the Virgin Islands Port Authority (VIPA or the Authority). I concur with the Office of Inspector General's conclusion that procurement best practices require proper documentation throughout the acquisition stage, and in the case of the VIPA, the lack of timely tracking such documentation impeded the VIPA ability to substantiate their compliance.

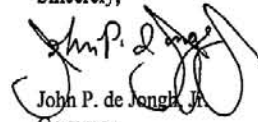
Pursuant to my request, Mr. Kenn Hobson, the Executive Director, on behalf of the VIPA provided responses along with supporting documentation to the OIG's draft Audit Report findings and recommendations. Enclosed you will find these responses to the draft audit report and the supporting documentation. It is my hope that the enclosed documents will provide

Ms. Mary L. Kendall
May 19, 2010
Page 2

additional information that address many of the concerns posed in the draft audit report, and therefore, the OIG can incorporate the appropriate revisions.

Thank you for affording the Government of the Virgin Islands an opportunity to comment on the OIG's draft audit report with respect to the issues concerning the Virgin Islands Port Authority.

Sincerely,



John P. de Jongh, Jr.
Governor

Enclosures

pc: Mr. Kenn Hobson, Executive Director, Virgin Islands Port Authority
Mr. Cassan Pancham, Chairperson, Virgin Islands Port Authority Governing Board

VIRGIN ISLANDS PORT AUTHORITY

Response to draft audit report, Capital Improvement Projects Administrative Functions – Procurement Deficiencies Plague the Virgin Islands Port Authority (VI-IN-VIS-0003-2009, March 2010)

FINDINGS #1: PROCUREMENT DEFICIENCIES

Although the Authority has policies and procedures in place that require competitive selection of contractors and service providers, the U. S. Department of the Interior's Office of the Inspector General (DOI-OIG) found that the Authority does not comply with those requirements. DOI-OIG also found the Authority's procurement filing system to be disturbingly and pervasively disorganized and its individual project files to be incomplete. The majority of project files were in such disarray that DOI-OIG could not determine if the Authority followed proper procurement procedures.

In addition, many project procurement files are incomplete. DOI-OIG was forced to work with copies of contracts because the Authority was unable to provide the originals. Many files fail to document how contractors were selected or whether they met basic requirements for conducting business in the Virgin Islands.

Recommendations

1. Ensure compliance with requirements to use competitive contract procedures and to issue formal contracts for all work related to capital improvement projects.
2. Ensure development and implementation of a tracking system or checklist to make sure that procurement related requirements are met for all contracts.
3. Ensure adherence to existing internal policies regarding the documents that should be maintained in contract and other procurement files.

Virgin Islands Port Authority's Response

The Virgin Islands Port Authority (VIPA or the Authority) does not concur with the finding, in general. More specifically, the Authority does not agree that it disregarded its own internal rules and regulations in the selection of contractors and in awarding contracts for capital improvement projects.

VIPA concurs, however, that the Engineering Division may not have kept all contract files in an organized manner as required by the Procurement Manual.

Further, original contracts were not generally maintained in the procurement files. Accordingly, in lieu of originals, copies of the (executed) contracts were provided.

With regard to each of the contracts referenced by the Audit, the Authority followed its own procurement rules and regulations and Virgin Islands law as set out in 29 VIC Section 541 *et seq.* (the Authority's enabling statute).

With regards to the following specific contracts referenced in the Audit, the Authority attaches hereto documents identified and described as supportive of the award of each contract. These documents may consist of such items as Board Committee minutes, Board Meeting minutes, actual contract documents, bid comparison documents, Notices of Award, Notices to Proceed, etc. In all cases there may not be a single form containing indication of all the steps followed in awarding the contract, but there is clearly ample documentation supporting compliance in each instance.

It should be noted that of the twelve (12) capital improvement projects reviewed, three (3) were specifically identified by name: Lindbergh Bay Park, Crown Bay Dock and Retail Development Project, and the Crown Bay Dredging Project. These three (3) projects will be covered by setting out the contracts related to each and the documents supporting each contract (see Appendices I and II attached). The documentation for the other nine (9) projects are available for review.

Recommendation 1: Comply with the requirements to use competitive contract procedures and to issue formal contracts for all work related to capital improvement projects.

VIPA Response - All contracts recommended by the Engineering Division meet these requirements. The Authority will continue this practice.

Recommendation 2: Develop and implement a tracking system or checklist to make sure that procurement-related requirements are met for all contracts.

VIPA Response - Engineering has developed a contract file checklist that will be completed for each contract and inserted in each contract file to ensure that the procurement requirements for each project are met. The Authority has also established a receipt for files (i.e. custody receipt) to monitor all files taken by the Legal Division and/or the auditors.

Recommendation 3: Follow existing internal policies regarding the documents that should be maintained in contract and other procurement files.

VIPA Response - The checklist that will be utilized to ensure compliance with procurement requirements identifies and enumerates the fourteen (14) items required to be in the project file, in accordance with the Procurement Manual.

Corrective Action Plan

VIPA will utilize the checklist developed and ensure that the contract files are maintained in accordance with the requirements stipulated in the Procurement Manual.

VIPA will commence simultaneously executing at least three (3) original contracts for any contractor with whom it is authorized to conduct business. One (1) original will be maintained in the procurement file in the Engineering Division, and one (1) original will be kept by the Legal Division.

Due Date: 3rd quarter – Fiscal Year 2010

Responsible Parties: Executive Director, VIPA and Director of Engineering, VIPA

FINDINGS #2: FINANCIAL REPORTING DEFICIENCIES

DOI-OIG's review of the Authority's financial reporting revealed a myriad of deficiencies, such as inaccurate records of payments to contractors and service providers of \$1.3 million, unreported payments, and non-issued tax forms. Absent the accurate recording of project costs, the Authority cannot have a true financial picture, because it cannot properly capitalize its assets.

During the past 10 years, the Authority failed to:

- prepare and issue required IRS Form 1099 for any contractors and service providers who received payments over \$600; and
- report \$84.3 million in payments made to contractors and other service providers.

This failure to follow financial reporting requirements hinders the Government of the Virgin Islands from collecting all its taxes.

Recommendations

4. Ensure accurate recording of capital improvement project costs.
5. Ensure issuance of IRS Form 1099 to contractors and service providers and submit copies to the Internal Revenue Bureau.

Virgin Islands Port Authority's Response

The VIPA concurs that it did not prepare IRS Form 1099 for contractors and its service providers, but does not concur that \$84,300,000 was unreported income to the Virgin Islands Government. Also, through the normal course of processing payments, assets are normally recorded accurately. This instance of underreported asset was an unusual occurrence where the contractor was not paid directly by VIPA, but VIPA was the inheritor of the asset.

During the years audited, the Virgin Islands Port Authority paid Gross Receipt Taxes to the Government of the Virgin Islands, on any contract over \$120,000 and any single payment for services rendered over \$30,000; for a total of \$4,243,563.86. Total revenues reported through the Gross Receipt reporting process to the Internal Revenue Bureau paid by VIPA to the providers were \$106,089,096.50.

Recommendation 4: Record capital improvement project costs accurately.

VIPA Response - The Authority's assets are normally recorded accurately. Through the normal process, the correct value of the asset would be recorded because it flows through the system from accounts payable when the contractor is paid. However, if there is another circumstance where there is a third party involvement, the normal procedure will be enforced to ensure that final documents are received to close out the asset.

Recommendation 5: Issue IRS Form 1099 to contractors and service providers and forward copies to the Internal Revenue Bureau.

VIPA Response - The Authority concurs that it has lapsed in the issuance of 1099's. As was stated during the audit, a plan is already in place to meet that requirement for calendar year 2010. The Authority in implementing this compliance is also working on issuing Form 1099's for 2009 aggregating to approximately \$3 million during the 3rd quarter of FY 2010. This process will continue to ensure issuance of Form 1099's to VIPA's major contractors. Some 2009 Form 1099's have already been issued to-date for roughly \$70,000.

Corrective Action Plan

VIPA will reinforce the procedure of having accounting sign off on all capital projects before payment is processed, even on capital improvement project costs for projects with third party involvement.

The Authority will comply with the Federal requirements and issue Form 1099s annually, as applicable. The required copy of the Form 1099 will also be forwarded to the Bureau of Internal Revenue (aka Internal Revenue Bureau).

VIPA will comply with requirements for issuance of IRS Form 1099s and will continue to issue those for 2009 in order to report payments to its major contractors on Form 1099 to the Bureau of Internal Revenue.

Implementation Date: 2nd quarter – Fiscal 2010

Due Date: 3rd quarter – Fiscal 2010 & on-going

Responsible Parties: Executive Director, VIPA and Director of Administration & Finance, VIPA

APPENDIX I

VIPA Responses to specific paragraph(s) in the Draft OIG Audit (VI-IN-VIS-0003-2009)

Page 3, paragraph 2: *"the Authority either circumvented or inadequately documented the procurement process. We were, therefore, unable to find any evidence that the required documents exist and have no assurance that the Authority issued contracts to the most qualified, responsive, and deserving contractors."*

Yes, the Engineering Division may not keep all contract files in an organized manner as required by the Procurement Manual, but nevertheless, a review of the projects reviewed by the Auditors found that the Authority's policies were followed as set out in the Procurement Manual or as directed by the Authority's Board of Directors. Before a contract is prepared or reviewed for legal sufficiency, all documents relating to how the contractor was selected, along with the Governing Board's approval, are provided to the Legal Division. Each capital project contractor selection follows the process outlined in the Procurement Manual.

First, bids or proposals are solicited in accordance with VIPA's Procurement Manual. Then, a review of the bids or proposal received is conducted and a recommendation is made to the Executive Director. The recommendation is then presented to the Projects and Operations Committee of VIPA's Governing Board, stipulating that the contractor recommended is the lowest, responsive, and responsible bidder. The Committee's recommendation is forwarded to the full Board and, if approved, a contract award is made.

In evaluating bids from contractors, there are specific documents that must be submitted in order for a bid to be considered responsive. A spreadsheet is prepared in reviewing the documents submitted against the bid requirements.

APPENDIX II

VIPA Response re: Three Capital Improvement Projects specifically identified

LINDBERGH BAY PARK

"The most egregious example of circumvention concerns the Lindbergh Bay Park. By classifying the project as "in-house," the Authority avoided the normal contracting process and retained control over \$900,000 in project funds."

To state that the park project is the most egregious is a matter of opinion. The VIPA erected the Lindbergh Bay Park project in two phases over a four year period. The project was referred to as "in-house" because it was a VIPA team project where staff members of the Authority got together and used their creativity to provide a public facility for the enjoyment of the residents of St. Thomas and its visitors. The work entailed rip-rap, excavation, construction, and installation of fixtures and equipment. The Authority could not utilize its maintenance staff for major construction work due to limitations in the union contract. The maintenance staff can only be used for preventative maintenance, minor and major repairs, equipment installation and other limited construction projects. Casual labor with the assistance of the Port Authority maintenance staff was utilized to facilitate the build out of the entire project. The project involved contribution of time and talent by members of the Authority's staff at no additional cost to the Authority. The project was done in two phases:

Phase I

1. Place fill material to meet requirements for flooding (casual labor & staff)
2. Place rock boulders for shore protection (revetment) a \$150,000 value, materials donated by Darlan Brin
3. Construct restroom (casual labor)
4. Build platform for Gazebo - concrete base (casual labor)
5. Build platform slab for play system - poured concrete base (casual labor)
6. Build four (4) concrete tables (for cooking and grilling) (casual labor)
7. Repair surface for volleyball court (casual labor)
8. Build two (2) concrete planters (casual labor)
9. Build concrete platform for kid's basketball court (casual labor)
10. Fence the park (casual labor)
11. Install bollards using timber from the old Frederiksted Pier in parking area to secure property (casual labor)
12. Install purchased Gazebo (casual labor & staff)
13. Install play system (casual labor & staff)

14. Install basketball funnel (casual labor & staff)
15. Build system for swings and install (casual labor & staff)

Phase II

1. Site preparation (installation of plumbing to include intake pipe from the ocean and discharge to the gut) (casual labor)
2. Build concrete platform (casual labor)
3. Install turnstiles (casual labor & staff)
4. Install shoreline protection (casual labor)
5. Build a pump & control house (store stainless steel pumps) (casual labor)
6. Build an energy house (casual labor)
7. Bridge access across gut (casual labor)
8. Build a tower "lighthouse" (casual labor)
9. Install water systems to include Fun Fountain Umbrella, Lemon Drops, Fire Hose, and Bucket System (casual labor & staff)
10. Signage (casual labor & staff)
11. Installation of rubber tiles (casual labor & vendor)

The detail of the work involved is listed and all the evidence is available to be seen publicly. The facility was a welcome addition to St. Thomas and continues to be a facility enjoyed by the general public. Three (3) of the seven (7) casual laborers were hired on a temporary basis at the end of the project by former Executive Director, Gordon Finch. This resulted from their excellent skills shown in the construction of the park. These three (3) temporary employees eventually became permanent employees through the employment process of the Authority. The labor cost over the four (4) year period for the casual labor employed was \$378,717.00. Previously, at the time of the Audit the personnel files could not be found. The files have since been located and are available for review.

CROWN BAY DOCK and RETAIL DEVELOPMENT PROJECT

Contracts Issued to subcontractors initially hired by American Bridge

At approximately 95% completion, the Authority terminated American Bridge as Contractor and entered into direct contracts with most of the subcontractors who had not completed their scope of work under the prime contract, so long as their work had been determined to be satisfactory. In each instance the new direct contract was at a cost reflecting what was left to be done under the prime contract. In no case did the cost of the direct contract exceed the cost for work remaining to be done at the time of termination. In the case of subcontractors

whose work was completed fully under the American Bridge contract, the Authority did not enter into contracts with them. In the case of subcontractors whose work was determined to be defective, the Authority opted to seek independent companies to do the repair and/or remaining work.

"Our review of the Authority's financial reporting revealed a myriad of deficiencies, such as inaccurate records of payments to contractors and service providers of \$1.3 million unreported payments, and non-issued tax forms. In the case of the Enighed Pond Marine Terminal Project, the Authority reported \$15.5 million was expended. In fact we discovered that project cost of \$16.5 million were expended - \$1 million over the reported amount. Absent the accurate recording of project costs, the Authority cannot have a true financial picture, because it cannot properly capitalize its assets."

The Authority concurs with the findings regarding the Enighed Pond Marine Terminal Project. The final cost is \$16.5 million. Through the audit it was revealed that the final two (2) payment records (Payment #27 & 28) were not channeled through the Finance/Accounting Office, rather the requests were sent directly to the Public Finance Authority (PFA) for processing. The normal feed was the Engineering Office certified the pay document for the work completed; the Accounting Office checked the documents for the mathematical accuracy and retained a copy of the pay documents to be added to the construction in progress. The documents were then forwarded to PFA for payment and PFA then sent back copies of paid vouchers to the Authority. Due to failure of the documents being sent to Accounting, the final payments were not recorded to the assets. Under normal circumstances, if the payments were made directly by the Authority rather than a third party source, the assets would not have been undercapitalized. The circumstances surrounding the project were not within the normal VIPA project process.

CROWN BAY DREDGING PROJECT

"Crown Bay Dredging Project, worth \$966,060.00. The procurement file for the primary contractor, which was paid \$897,000.00, could not be located. Also, the Authority chose to include contract wording that indicates the existence of two bidders rather than to document the selection process."

There was a file located in the Engineering Office that contained the contract and the payment files for the Crown Bay Dredging Project. In this particular case, the procurement process was handled by the Executive Director. After reviewing his files and that of the Legal Division, it was found that there were copies of correspondence showing that proposals were sought and that the Governing Board of the Authority was polled to select the particular contractor. Thus, the selection process was in fact documented. These correspondences are enclosed.



**Virgin Islands Port Authority
P.O. Box 301707
St. Thomas, VI 00803-1707**

Respectfully submitted, this 19th day of May 2010.

A handwritten signature in black ink, appearing to read "Kenn Hobson", written over a horizontal line.

Kenn Hobson
Executive Director
Virgin Islands Port Authority

Appendix 2: Office of Inspector General Reply to Auditee Response

The Governor of the Virgin Islands responded to this report in its draft form on May 19, 2010 (see appendix 1). The Governor agrees that the lack of timely tracking of documentation impeded the Authority's ability to prove its compliance with basic procurement best practices and encloses input by the Authority's Executive Director.

The Executive Director, while agreeing with four of the five recommendations, took exception to certain findings and conclusions in the report. Specifically, the Executive Director maintains that the Authority used competitive contract procedures in all contracts recommended by the Engineering Division and that formal contracts were issued for all work related to capital improvement projects. Moreover, he takes issue with our opinion that Lindbergh Bay Park is the "most egregious example of circumvention" of the procurement process that we found. Finally, the Executive Director states that the selection process related to the Crown Bay Dock and Retail Development Project was documented.

After conducting 8 months of reviews, we could not state that the policies and mandates of the Authority's Board of Directors have been followed. We are no more able to verify the Executive Director's contentions after receiving his response to the Draft Report.

Selection of contractors: We recognize that the Authority may have, in many cases, followed procurement rules and regulations. In any given instance, however, we can have no assurance that the Authority issued contracts to the most qualified, responsive, and deserving contractors due to the lack of procurement process documentation. In fact, the contract documents provided as part of the Executive Director's response included: unsigned copies of contracts we already possess in signed form; a copy of a request for proposal that differs from the one in our files that it represents; and additional evidence that indicates that the Authority may have overpaid a contractor by \$215,000. None of these documents serve to refute our assessment.

Circumvention: No question can exist that the Lindbergh Bay Park project exemplifies circumvention of the procurement process. The Executive Director's contention is that this project was performed "in-house." We disagree. By the Executive Director's own admission, "casual labor . . . was utilized to facilitate . . . the entire project." Opinion applies only to our assessment of the project as the "most egregious" that we found.

We hope that the Authority will be able to overcome many of their long-standing deficiencies by implementing all the recommendations contained in this report.

Their full implementation will be required to ensure an efficient and transparent operation.

Appendix 3: Scope and Methodology and Prior Coverage

Scope and Methodology

This audit's objective was to assess Virgin Islands Port Authority performance of administrative functions related to capital improvement projects. We performed our work from March to October 2009 and interviewed officials, reviewed procurement and payment files, and visited project sites on St. Thomas, St. John, and St. Croix. We also studied procurement industry best practices and evaluated internal controls related to the management of capital improvement projects.

Our scope was limited by the Authority's inability to locate all procurement files and its inaccurate recording of project costs. We were, therefore, forced to determine actual costs based on a review of payment documents. We also reviewed payment documents obtained from the Public Finance Authority and studied procurement industry best practices.






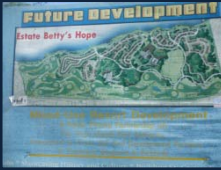

We conducted this audit in accordance with the "Government Auditing Standards" issued by the Comptroller General of the United States. Those standards require that we plan and perform an audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on the audit objectives. We tested the validity of records and conducted other auditing procedures as necessary under the circumstances. We believe that the work performed provides a reasonable basis for our conclusions and recommendations based on our audit objectives.


Prior Coverage

In March 2005, we issued Report No. V-IN-VIS-0001-2004, "Procurement Practices, Virgin Islands Port Authority, Government of the Virgin Islands." The report revealed that the Authority failed to:

1. Follow procurement related requirements for all contracts;
2. Exercise due care in planning capital improvement projects;
3. Establish record control procedures to ensure the security of procurement files; and
4. Comply with:
 - a) requirements for competition and the issuance of formal contracts related to capital improvement projects;
 - b) internal policies regarding types of documents that should be maintained in contract and procurement files; and
 - c) the Virgin Islands Code requirement that gross receipts be deducted from payments made to service providers and contractors.

Appendix 4: Capital Improvement Projects Renewed

Project Name		Number of Contractors/Service Providers	Total Project Cost (U.S. Dollars)
	Ann Abramson Pier	7	4,694,467.04
	CEK Airport Taxiway	3	9,403,735.11
	Crown Bay Marine Terminal	58	39,292,329.93
	Enighed Pond	6	16,588,505.35
	Phase I Security Fencing	1	202,442.10
	Commercial Business Park	1	315,000.00
	Lindbergh Bay Park	26	871,075.37

Project Name		Number of Contractors/Service Providers	Total Project Cost (U.S. Dollars)
	CEK Airport Renovation	5	2,851,579.23
	Crown Bay Dredging	7	966,060.33
	CEK Airport Taxiway Rehabilitation	2	12,064,679.60
	Cruz Bay Pier Expansion	1	46,568.75
	STT- Waterfront Plan	1	287,903.48
TOTALS:		118	87,584,346.29

Appendix 5: Monetary Impact

Questioned Costs
\$5,540,300
Virgin Islands Government — Unrealized Tax Income
UNREPORTED INCOME
\$84,300,000
Potential Taxes Lost
\$12,600,000

Appendix 6: Status of Audit Recommendations

Recommendation	Status	Action Required
1	Unresolved	We will be referring this issue to the Office of Insular Affairs for oversight and to ensure compliance. Please provide them with any requested documentation that demonstrates that the required procurement process was followed.
2	Resolved and Implemented	None
3	Resolved, and Implemented	None
4	Resolved and Implemented	None
5	Resolved, Not Implemented	Provide copies of 1099s for contracts issued during the third quarter of fiscal year 2010.

Report Fraud, Waste, and Mismanagement



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



By Mail:

U.S. Department of the Interior
Office of Inspector General
Mail Stop 4428 MIB
1849 C Street, NW
Washington, D.C. 20240

By Phone:

24-Hour Toll Free
Washington Metro Area

800-424-5081
703-487-5435

By Fax:

703-487-5402

By Internet:

www.doioig.gov