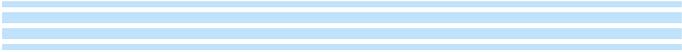




Office of the Public Auditor
Commonwealth of the Northern Mariana Islands

Marianas Visitors Authority
(Formerly Marianas Visitors Bureau)
Audit of Promotion and Advertising Services
Fiscal Years 1992 to 1998



Audit Report
AR-98-04

Contents

Executive Summary	i
Introduction	1
Background	1
Objectives, Scope, and Methodology	2
Prior Audit Coverage	3
Findings and Recommendations	4
Illegal Procurement of Promotion and Advertising Services	4
1. I & S Corporation	8
2. Prime Air System	16
3. New Visions Marketing Services, Ltd.	18
4. Dentsu Young & Rubicam, Inc.	20
5. Access Inc.	21
6. Ad Intelligence	22
7. JIC Corporation	22
8. Bozell CCAA	23
9. Ohta Publications	23
Appendices	33
A - Governor's Office Response dated May 20, 1998	33
B - MVA Managing Director Response dated June 18, 1998	34
C - Status of Recommendations	39

EXECUTIVE SUMMARY

Our audit showed that the Marianas Visitors Authority (MVA) procured promotion and advertising services in violation of the CNMI Procurement Regulations (CNMI-PR). At various dates from fiscal year 1992 to 1996, MVA (1) procured services from 9 foreign advertising companies amounting to more than \$7.34 million without following competitive selection procedures, (2) paid the companies without valid government contracts, (3) entered into "open-ended" agreements with several companies instead of firm fixed price contracts, and (4) compensated several companies using the cost-plus-a-percentage-of-cost method specifically prohibited under the regulations, or the cost reimbursement method without justification. Of the 9 companies, 3 were awarded contracts during fiscal year 1997 without following competitive selection procedures and were paid more than \$4.16 million. When the 3 contracts expired at the beginning of fiscal year 1998, the companies were allowed to incur expenditures although no new contracts had been approved. Such expenditures totaled \$2.72 million as of February 1998. As a result, (1) public funds were illegally spent by MVA in violation of procurement regulations, and (2) there was no assurance that expenditures totaling more than \$14.22 million were necessary or were procured at a fair and reasonable price.

Background

On February 12, 1998, the Office of the Attorney General (AGO) formally requested the Office of the Public Auditor (OPA) to audit MVA's procurement of promotion and advertising services from the I&S Corporation (I&S), a foreign advertising company based in Japan. According to AGO, I&S had been providing services without a contract.

Based on our preliminary investigation, it appears that MVA has also been procuring promotion and advertising services from other companies without valid contracts in violation of the CNMI-PR. To obtain a complete picture of the violations, OPA decided to conduct an audit of companies which provided the majority of promotion and

advertising services to MVA from fiscal years 1992 to 1998. The audit included I&S Corporation and 8 other companies.

MVA's primary purpose is to attract tourists to visit the CNMI. Consequently, a substantial portion of MVA's expenditures was geared toward the promotion and development of the CNMI as a premiere tourist destination. MVA's expenditures for promotion and advertising services increased from \$874,000 for fiscal year 1992 to more than \$4.8 million in fiscal year 1997. As a proportion of total expenditures, promotion and advertising services represented 28% in fiscal year 1992. This percentage increased to more than 52% in fiscal year 1997.

The CNMI-PR were promulgated under the authority of 1 CMC §2553 (j)

There was no assurance that expenditures totaling more than \$14.22 million were necessary or were procured at a fair and reasonable price.

which gives the Secretary of Finance the duty to be in control and be responsible for procurement and supply in the Commonwealth. The regulations apply to every expenditure of public funds irrespective of source, including federal assistance monies and Covenant funds. All government agencies are required to follow the CNMI-PR unless excepted by law. Procurement authority, however, may be delegated by the Secretary of Finance with certification of the Director of Procurement and Supply (P&S).

and advertising services. Our audit showed, however, that MVA procured promotion and advertising services in violation of the regulations. At various dates from fiscal years 1992 to 1996, MVA (1) procured services from 9 foreign advertising companies amounting to more than \$7.34 million without following competitive selection procedures, (2) paid the companies without valid government contracts, (3) entered into "open-ended" agreements with several companies instead of firm fixed price contracts, and (4) compensated several companies using the cost-plus-a-percentage-of-cost method specifically prohibited under the regulations, or the cost reimbursement method without justification. Of the 9 companies, 3 were awarded contracts during fiscal year 1997 without following competitive selection procedures and were paid more than \$4.16 million. When the 3 contracts expired at the beginning of fiscal year 1998, the companies were allowed to incur expenditures although no new contracts had been approved. Such expenditures totaled \$2.72 million as of February 1998. This occurred because MVA officials were not familiar with the procurement regulations. As a result, (1) public funds were illegally spent by MVA in violation of procurement regulations, and (2) there was no assurance that expenditures totaling more than \$14.22 million (Table 1) were

Objectives and Scope

The objectives of the audit were to determine whether MVA's procurement of promotion and advertising services complied with the CNMI-PR and other applicable laws and regulations.

The scope of our audit focused on MVA's procurement of promotion and advertising services from fiscal year 1992 to 1998. To accomplish our objectives, we selected 9 advertising companies which provided seventy three percent (73%) of promotion and advertising services to MVA during the period under audit.

Illegal Procurement of Promotion and Advertising Services

MVA is required to follow the CNMI-PR in the procurement of promotion

Advertising Companies	FY 1992-96	FY 1997	FY 1998	Total
1. I & S Corporation	\$ 4,236,062	\$ 3,914,924	\$ 2,659,230	\$10,810,216
2. Prime Air System	196,513	123,768	31,736	352,017
3. New Visions Marketing	154,617	124,080	27,992	306,689
4. Dentsu Young & Rubicam	1,116,229	-	-	1,116,229
5. Access, Inc.	525,638	-	-	525,638
6. Ad Intelligence	480,475	-	-	480,475
7. JIC Corporation	227,905	-	-	227,905
8. Bozell CCAA	223,994	-	-	223,994
9. Otha Publication	180,737	-	-	180,737
	\$ 7,342,170	\$ 4,162,772	\$ 2,718,958	\$14,223,900

Table 1

necessary or were procured at a fair and reasonable price.

Remedies Against Violation of Procurement Regulations

MVA procured promotion and advertising services from 9 advertising companies in violation of the CNMI-PR. The following is a discussion of possible remedies against violation of the regulation.

Past Contractors

Six of the 9 advertising companies were no longer providing services to MVA at the time of our audit. Consequently, the available remedies against these contractors may be limited because they have been fully paid. A contractor who violates the procurement regulations shall be subjected to a warning or reprimand, termination of the contract or suspension from being a contractor under a government contract, in addition to other penalties prescribed by law [CNMI-PR Section 6-211 (2)]. In these cases, however, the billings have been paid and the only possible action in this instance would be to suspend the contractors from being awarded government contracts in the future. The government could still seek damages but it would have to prove that the contractors acted in bad faith, among other considerations. Government employees, however, found to be responsible for the violations should be subject to adverse actions in accordance with CNMI-PR Section 6-211 (1).

Current Contractors

At the time of the audit (February 1998), MVA had allowed at least 3 advertising companies to incur expenses amounting

to more than \$2.7 million although no new contracts had been approved by the Governor. The companies had prior contracts with MVA which expired in fiscal year 1997. The companies were originally procured without following competitive selection procedures and had, in the past, conducted business with MVA without valid contracts. The AGO and Deputy Managing Director had already informed the companies to stop providing services explaining that MVA could not be held liable without a valid contract. However, top MVA officials, including the Board Chairman and the Managing Director, have failed to issue a similar statement to the other companies.

The decision to approve or disapprove a contract ultimately rests with the Governor since he is the last signatory in a government contract. However, if a contract is approved and is still found to be in violation of the regulations, which is likely the case with MVA, the contractor is still subject to the remedies under CNMI-PR Section 6-211 (2) which include the termination of the contract. If the contractor acted in good faith, he may be entitled to the actual costs incurred prior to termination. If the proposed award of the contract is canceled, the contractor has the option to protest the cancellation to the P&S Director, and subsequently appeal to the Public Auditor. The contractor will then be subject to the remedies prior to award provided under CNMI-PR Section 5-103 (1) of the regulations.

If the remedies are followed, there are two possible actions that could be taken if the solicitation of the contract is found to be in violation of the procurement regulations. One is to cancel the solicita-

tion, and the second is to make revisions to comply with the regulations. It is questionable, however, if the 3 proposed contracts can still be revised to comply with the procurement regulations. The selection of vendors violated competitive selection procedures and the contractors have already rendered services. MVA cannot solicit new proposals for past services. At any rate, there is no guarantee that the contractors will be selected again under open competitive procedures. Therefore, the only choice may be cancellation. If the contractor asserts any liability against MVA, the government should consider whether such liability can be assessed against the employee(s) who permitted the contractors to violate the procurement regulations (CNMI-PR Section 1-108).

Accordingly, we recommend that:

1. The Governor and the Attorney General's Office consider taking appropriate action against current and previous MVA officials, including the MVA Board Chairman and Managing Director, for violation of the CNMI-PR. Such action includes but is not limited to reprimand, suspension without pay, termination of employment, civil injunction, civil suit for damages or return of government money, or criminal prosecution [CNMI-PR Section 6-211 (1)]. At the least, reprimand letters should be issued and permanently filed in their personnel files.
 2. The Governor instruct MVA to cancel the proposed contracts with the 3 advertising companies for violation of the CNMI-PR. This recommendation is based on the
- fact that even if these proposed contracts were to be approved, they would still be in violation of the regulations. In such case, the contractor would be subject to the remedies under CNMI-PR Section 6-211(2) which include termination of the contract. If the contractors assert any liability against MVA, we recommend that the Attorney General's Office consider whether it is appropriate to file a cross claim against MVA officials and employees who were responsible for the violations discussed in this report.
3. P&S Director suspend the 9 advertising companies from becoming contractors or subcontractors on future government contracts for at least a year or such other period of time as deemed sufficient by the Director. The suspensions should be communicated to the companies to emphasize that they need to comply with the CNMI-PR when dealing with government agencies.
 4. The Board Chairman and the Managing Director ensure that all procurement of promotion and advertising services be procured competitively, in accordance with the CNMI-PR. To this end, both officials should ensure that all procurement conducted through the RFP process be awarded based on price and other evaluation factors stated in the RFP and not through appointment or majority vote of the Board.
 5. The Managing Director take steps for MVA to adopt the CNMI-PR. Identical regulations need to be adopted to enable MVA to continue

to conduct its own procurement functions.

6. The Managing Director, MVA Board members, and procurement officials should familiarize themselves with the CNMI-PR. They should both review the CNMI-PR and request the P&S Director to provide explanation to parts they don't understand. MVA employees involved in the procurement of goods and services should be required to be familiar with the details of the regulations.
7. The Managing Director establish a filing system that can provide a complete history of the transactions with each individual contractor. Contract files generally consist of (1) contracting files which document the basis for acquisition and the award of the contracts, (2) contract administration files which document actions taken to monitor contractor performance and compliance with the scope of work, and (3) payment contract files which document actions substantiating and reflecting contract payments.

Governor's Office Response

The Governor's letter response dated May 20, 1998 did not address Recommendations 1 and 2. The Governor explained that it is premature to make any decisions on the recommendations. He added that it is important that the response of MVA be obtained and be considered before any actions are taken (See Appendix A).

AGO Response

The Acting Attorney General did not respond to Recommendations 1 and 2.

P&S Response

The P&S Director did not respond to Recommendation 3.

MVA Response

The Managing Director was requested to respond only to Recommendations 4, 5, 6, and 7. Her letter dated June 18, 1998, however, responded to all recommendations (See Appendix B). The responses did not address the recommendations.

OPA Comments

The Managing Director's response did not contain any additional information that could revise our recommendations. The Governor, AGO, P&S Director, and Managing Director should reconsider and implement the recommendations.

Status of Recommendations

Based on the responses we received, we consider all recommendations open. In light of the recent passage of Public Law 11-15 on June 17, 1998, however, we are revising Recommendation 5 which provides that MVA adopt the CNMI-PR. Instead, we recommend that MVA adopt its own procurement regulations consistent with the CNMI-PR as authorized under the new law. The additional information or action required to close the recommendations is presented in Appendix C.

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Introduction

Background

On February 12, 1998, the Office of the Attorney General (AGO) formally requested the Office of the Public Auditor (OPA) to audit the Marianas Visitors Authority's (formerly Marianas Visitors Bureau) procurement of promotion and advertising services from the I&S Corporation (I&S), a foreign advertising company based in Japan. According to AGO, I&S had been providing services without a contract.

Based on our preliminary investigation, it appears that the Marianas Visitors Authority (MVA) has also been procuring promotion and advertising services from other companies without valid contracts in violation of the CNMI Procurement Regulations (CNMI-PR). To obtain a complete picture of the violations, OPA decided to conduct an audit of companies which provided the majority of promotion and advertising services to MVA from fiscal years 1992 to 1998. The audit included I&S Corporation and 8 other companies.

Marianas Visitors Authority



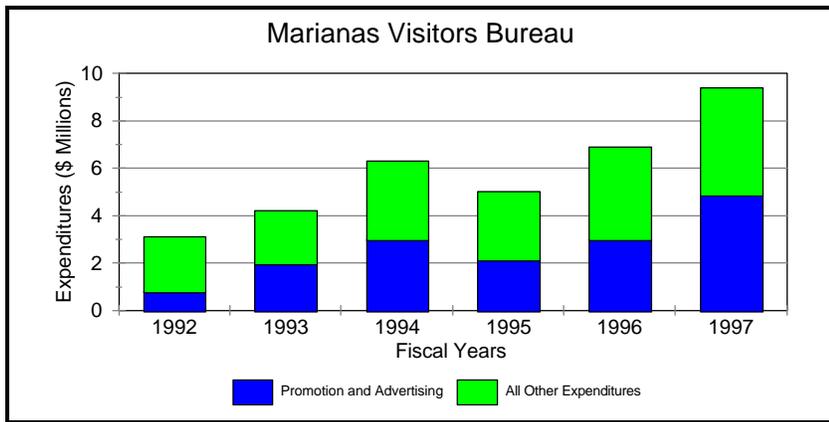
MVA was originally established pursuant to District Law 4-145 (4 CMC §2101) on February 11, 1976 as the Marianas Visitors Bureau (MVB), a non-profit organization for the promotion and development of the tourism industry in the CNMI. On August 22, 1994, the Governor's Executive Order 94-3 (E.O.), the "Second Reorganization Plan of 1994" became effective. Section 302(b) of the E.O. allocated MVB to the Department of Commerce for purposes of administration and coordination. The E.O. also increased the number of directors from nine to fourteen; allowed the Governor to appoint nine of the fourteen Board members with the advice and consent of the Senate; and required that two of the Governor's nine appointed members be from Rota and two from Tinian. The other five Board members are to come from the (1) hotel industry, (2) airline industry, (3) retail industry, (4) any small business that is a member of MVB, and (5) travel agency industry.

On June 17, 1998, Public Law 11-15, "Marianas Visitors Authority Act of 1998" took effect upon approval by the Governor. The new law vacated Section 302(b) of Executive Order 94-3, abolished the existing MVB and established a new public corporation named as the Marianas Visitors Authority or MVA. The new law reduced the number of directors from fourteen to nine, five of which will be appointed by the Governor with the advice and consent of the Senate. The remaining four

members will be chosen by private sector organizations, companies, or any other entities who are paying members accredited by MVA.¹

In accordance with its enabling legislation and subsequent amendments, MVA receives 70% of the hotel room occupancy taxes and 25% of the alcoholic container taxes collected by the CNMI Government. Revenues from these sources increased from about \$5.2 million in fiscal year 1992 to more than \$8.3 million in fiscal year 1997.

Promotion and Advertising Services



Graph 1

MVA’s primary purpose is to attract tourists to visit the CNMI. Consequently, a substantial portion of MVA’s expenditures was geared toward the promotion and development of the CNMI as a premiere tourist destination. MVA’s expenditures for promotion and advertising services increased from \$874,000 for fiscal year 1992 to more than \$4.8 million in fiscal year 1997 (see Graph 1). As a proportion of total

expenditures, promotion and advertising services represented 28% in fiscal year 1992. This percentage increased to more than 52% in fiscal year 1997.

CNMI Procurement Regulations

The CNMI-PR were promulgated under the authority of 1 CMC §2553 (j) which gives the Secretary of Finance the duty to control and be responsible for procurement and supply in the Commonwealth. The regulations apply to every expenditure of public funds irrespective of source, including federal assistance monies and Covenant funds. All government agencies are required to follow the CNMI-PR unless excepted by law. Procurement authority, however, may be delegated by the Secretary of Finance with certification of the Director of Procurement and Supply (P&S).

Objectives,
Scope, and
Methodology

The objectives of the audit were to determine whether MVA's procurement of promotion and advertising services complied with the CNMI-PR and other applicable laws and regulations.

¹The initial four members shall be chosen by the paying members within thirty days of the effective date of the law. The MVB Board Chairman shall also transfer all MVB assets and liabilities to MVA within the same period.

The scope of our audit focused on MVA's procurement of promotion and advertising services from fiscal year 1992 to 1998. To accomplish our objectives, we selected 9 advertising companies which provided seventy three percent (73%)² of promotion and advertising services to MVA during the period under audit. We reviewed and evaluated procurement and disbursement documents and vendor correspondence, and interviewed knowledgeable MVA officials and employees to determine compliance with the CNMI-PR.

This performance audit was conducted at the MVA Office in Saipan from February 16, to March 25, 1998. The audit was made, where applicable, in accordance with "Government Auditing Standards" issued by the Comptroller General of the United States. Accordingly, we included such tests of records and other auditing procedures as were considered necessary under the circumstances. We completed our field work on March 25, 1998. As part of our audit, we evaluated internal controls over procurement and payment of promotion and advertising services to the extent necessary to accomplish the audit objectives. We found internal control weaknesses in these areas, which are discussed in the Findings and Recommendations section of this report. Our recommendations, if implemented, should improve internal controls in these areas.

Prior Audit Coverage

During the past five years, several audit reports regarding MVA were issued by OPA and other independent auditing firms. For example, OPA issued an audit report dated December 11, 1994 on the settlement agreement between the former Managing Director and MVA's Executive Committee members. The report found that the settlement agreement should be considered invalid and payments made to the former Managing Director should be recovered.

At least three independent auditing firms issued annual audit reports relating to the financial statements of MVA for fiscal years 1991 to 1996. The firms reported several violations of the CNMI Procurement Regulations by MVA.

²Based on Fiscal Years 1992 to 1997 expenditures.

Findings and Recommendations

Illegal Procurement of Promotion and Advertising Services

There was No Assurance that MVA Expenditures Totalling More than \$14.22 Million were Necessary or were Procured at a Fair and Reasonable Price.

The Marianas Visitors Authority (MVA) is required to follow the CNMI Procurement Regulations in the procurement of promotion and advertising services. Our audit showed, however, that MVA procured promotion and advertising services in violation of the regulations. At various dates from fiscal years 1992 to 1996, MVA (1) procured services from 9 foreign advertising companies amounting to more than \$7.34 million without following competitive selection procedures, (2) paid the companies without valid government contracts, (3) entered into "open-ended" agreements with several companies instead of firm fixed price contracts, and (4) compensated several companies using the cost-plus-a-percentage-of-cost method specifically prohibited under the regulations, or the cost reimbursement method without justification. Of the 9 companies, 3 were awarded contracts during fiscal year 1997 without following competitive selection procedures and were paid more than \$4.16 million. When the 3 contracts expired at the beginning of fiscal year 1998, the companies were allowed to incur expenditures although no new contracts had been approved. Such expenditures totaled \$2.72 million as of February 1998. This occurred because MVA officials were not familiar with the procurement regulations. As a result, (1) public funds were illegally spent by MVA in violation of procurement regulations, and (2) there was no assurance that expenditures totaling more than \$14.22 million were necessary or were procured at a fair and reasonable price.

CNMI Procurement Regulations

No government contract shall be valid unless it complies with the CNMI-PR (CNMI-PR Section 1-107). All government agencies are required to follow the CNMI-PR unless excepted by law. Procurement authority, however, may be delegated by the Secretary of Finance with certification of the Director of P&S. Under the regulations, government contracts should generally be procured competitively unless the requirements for using other methods are met. All contracts should also utilize a firm fixed price unless cost reimbursement is justified in writing. The cost-plus-a-percentage-of-cost method of contracting is also specifically prohibited. In addition, no contract shall be effective and no funds may be obligated or expended until all necessary government signatures have been obtained.

Procurement Authority

The CNMI-PR were promulgated under the authority of 1 CMC §2553 (j) which directs the Secretary of Finance to control and be responsible for procurement and supply in the Commonwealth. The regulations apply to every expenditure of public funds irrespective of source, including federal assistance monies and Covenant funds.

CNMI-PR Section 1-105 provides that the regulations shall apply to all agencies, departments, branches of the government, political subdivisions, public corporations and agencies of local government of the Commonwealth. Any government entity which adopts the CNMI-PR or identical regulations may be authorized by the Secretary of Finance to administer procurement functions pursuant to CNMI-PR Section 2-201 (Decentralized Procurement). Under this section, the Director of P&S may delegate in writing other procurement functions and responsibilities to other agencies (except for purchases under the sole source, emergency, and expedited procurement methods which are required to be centralized through P&S) upon satisfying the following requirements:

- a) The CNMI Procurement Regulations have been duly adopted pursuant to the procedures required for adopting official business of such agencies.
- b) The agency has adequate staff capability necessary to carry out the functions of the Director of Procurement and Supply.
- c) The agency shall certify to the Director of Procurement and Supply that it is in compliance with (a) and (b) above.

CNMI-PR Section 2-201(2) also provides that:

Where the Director of Procurement and Supply has delegated his authority under this section, the official with expenditure authority may conduct bidding, procurement, negotiation and the administration of contracts involving funds appropriated to their own office, department, agency or branch. All such activity must be shown to the reasonable satisfaction of the Director to be in compliance with the regulations.

Applicability of Regulations to MVA

The law which established MVA in 1976 granted the agency the power to "adopt rules and regulations as may be necessary" to carry out its responsibilities (1 CMC §2106 (q)). The law, however, did not specifically grant MVA the authority to conduct its own procurement functions. As such, it cannot supersede the grant of authority to the Secretary of Finance who was designated to be "responsible for procurement and supply in the Commonwealth" (1 CMC §2553 (j)). Therefore, MVA is required to follow the CNMI-PR.

On June 5, 1996, MVA certified to the Secretary of Finance that it had adopted its own procurement regulations which were purportedly to be in substantial compliance with the CNMI-PR, and that it had adequate staff necessary to conduct its own procurement functions. On July 10, 1996, the Secretary of Finance authorized the

P&S Director to delegate procurement functions to MVA. On July 26, 1996, the P&S Director informed MVA that it had been authorized to administer its own procurement functions in accordance with its procurement regulations.

The Secretary of Finance's grant of authority to administer procurement functions, however, does not relieve MVA from complying with the provisions of the CNMI-PR. A proper delegation cannot be made unless an agency receiving the delegation has adopted identical regulations (CNMI-PR Section 1-105). Substantially similar regulations, therefore, cannot be used as a substitute for the CNMI-PR. When a delegation is made, only the procurement functions being performed by the P&S Director are handed over to the agency. Compliance with the regulations, however, is still required. If there are any differences between CNMI-PR and MVA Procurement Regulations (MVA-PR), CNMI-PR regulations prevail and MVA is required to follow the CNMI-PR.

Competitive Selection

As a general rule, all government contracts are to be awarded by competitive sealed bids unless the procurement meets the criteria for other methods of source selection provided in the regulations (CNMI-PR Section 3-101). For example, if the use of competitive sealed bidding is neither practical nor advantageous to the government, a contract may be entered into by competitive sealed proposals (CNMI-PR Section 3-106).

Under the competitive sealed bidding method, bids are solicited through an Invitation For Bids (IFB) and award is made to the lowest responsive bid by a responsible bidder whose bid fully meets the requirements of the IFB. Under the competitive sealed proposal method, proposals are solicited through a Request For Proposals (RFP), and award is made to the responsible offeror whose proposal is most advantageous to the government. The difference between competitive sealed bidding and competitive sealed proposals is that, in competitive sealed bids, detailed specifications for the goods or services being procured are specifically provided in the IFB and vendors are required to strictly adhere to specifications, while in competitive sealed proposals, only general requirements for the goods or services being procured are provided in the RFP and vendors may submit proposals that substantially meet or exceed those requirements.

For procurement of promotion and advertising services where bidding is impractical, the preferred method should be competitive sealed proposals. To ensure competition, however, MVA must fully comply with the requirements for competitive sealed proposals. These include (1) written determination that competitive sealed bidding is not applicable, (2) adequate public notice of the RFP, and (3) award of contract in writing to the best qualified offeror based on evaluation factors set forth in the RFP and negotiation of compensation determined to be fair and reasonable.

Other Procurement Methods

A contract may also be procured using other methods if it meets the criteria for such methods. For example, procurement of services of accountants, physicians, and lawyers qualifies under the professional services method (CNMI-PR Section 3-107). The same services, however, may be procured using the sole source method (CNMI-PR Section 3-104) if the procurement meets the following criteria: (1) the P&S Director determines in writing that there is only one source for the required service, and (2) the official with expenditure authority provides a written justification explaining the (a) unique capabilities required, (b) why they are required, and (c) consideration given to alternative sources.

Government Contracts

CNMI-PR Section 3-401 requires that government contracts utilize a firm fixed price unless the P&S Director determines in writing that the use of a cost reimbursement contract is appropriate and advantageous to the government. The use of either a cost-plus-a-percentage-of-cost or percentage of construction cost method of contracting is specifically prohibited. Procurement made by government agencies is also required to comply with the "Contract Review, Processing, and Oversight" provisions under CNMI-PR Section 2-104. Under these provisions, all government contracts are required to be reviewed and approved by authorized government signatories. It is the responsibility of the Contracting Officer to ensure that no expenditures are incurred by the contractor prior to approval of the contract. No contract is effective against the CNMI Government until all necessary government signatures have been obtained.

Promotion and Advertising Services Procured Without Competition And Valid Government Contracts

We selected 9 advertising companies which provided approximately seventy three (73%) of promotion and advertising services to MVA and reviewed the related

Advertising Companies	FY 1992-96	FY 1997	FY 1998	Total
1. I & S Corporation	\$ 4,236,062	\$ 3,914,924	\$ 2,659,230	\$10,810,216
2. Prime Air System	196,513	123,768	31,736	352,017
3. New Visions Marketing	154,617	124,080	27,992	306,689
4. Dentsu Young & Rubicam	1,116,229	-	-	1,116,229
5. Access, Inc.	525,638	-	-	525,638
6. Ad Intelligence	480,475	-	-	480,475
7. JIC Corporation	227,905	-	-	227,905
8. Bozell CCAA	223,994	-	-	223,994
9. Otha Publication	180,737	-	-	180,737
	\$ 7,342,170	\$ 4,162,772	\$ 2,718,958	\$14,223,900

Table 1

procurement transactions from fiscal years 1992 to 1998. Our review showed that MVA procured services amounting to \$14.22 million from the 9 companies in violation of procurement regulations (See Table 1).

On various dates from fiscal years 1992 to 1996, MVA (1) procured services from 9 foreign advertising companies amounting to more than \$7.34 million without following competitive selection procedures, (2) paid the companies without valid government contracts, (3) entered into "open-ended" agreements with several companies instead of firm fixed price contracts, and (4) compensated several companies using the cost-plus-a-percentage-of-cost method specifically prohibited under the regulations or the cost reimbursement method without justification. Of the 9 companies, 3 were awarded contracts during fiscal year 1997 without following competitive selection procedures and were paid more than \$4.16 million. When the 3 contracts expired at the beginning of fiscal year 1998, the companies were allowed to incur expenditures although no new contracts had been approved. Such expenditures totaled \$2.72 million as of February 1998.

The following sections discuss the procurement violations committed by MVA in the procurement of each advertising company listed in Table 1. To minimize repetition, the specific provisions violated are cited and referred to only in the discussion relating to I&S Corporation below.

1. *I & S Corporation (\$10.81 Million)*

At the time of our audit, I&S Corporation (I&S), a foreign advertising service corporation, was providing promotion and advertising services for MVA in Japan. I&S services have included placement of advertisements in various media (newspapers, magazines, and trade periodicals), and production and purchase of advertising materials (photography, printing, television, and radio commercials). Our review of MVA's procurement transactions with I&S showed the following:

Fiscal Years 1992 to 1994

MVA's relationship with I&S began in fiscal year 1992 when MVA sent letters to 13 advertising companies in Japan soliciting proposals for promotion and advertising services.

- *MVA did not follow competitive selection procedures.* I&S was selected by MVA officials based on interviews of advertising companies in Japan. MVA, however, did not follow the requirements for competitive sealed proposals. Among other things, we found no evidence that (1) a written determination was prepared to justify solicitation of proposals instead of bidding, (2) an RFP was prepared and adequately published, and (3) a written determination was prepared supporting the selection of I&S based on price and other evaluation factors. MVA was unable to provide us documentation of the interviews conducted by MVA officials or copies of the proposals submitted by other advertising companies.

Under the regulations, competitive sealed proposals may be used only if the official with expenditure authority determines in writing that the use of competitive sealed bidding is neither practical nor advantageous to the government [CNMI-PR Section 3-106 (1)]. Proposals shall also be solicited

through RFPs, and adequate public notice of the RFP shall be made through newspapers of general circulation for at least thirty days [CNMI-PR Section 3-106 (2)-(3)]. Award shall be made to the responsible offeror whose proposal is determined in writing to be the most advantageous to the government taking into consideration price and other evaluation factors. No other factors or criteria shall be used in the evaluation, and the contract file shall contain the basis on which the award is made [CNMI-PR Section 3-106 (7)].

- *I&S was paid without a valid government contract.* From fiscal years 1992 to 1994, MVA compensated I&S based on submission of invoices or billing statements. The Managing Director and the Marketing Director confirmed to us that there was no contract or written agreement with I&S on file during this period.

Under the regulations, a contract must first be prepared by the official with expenditure authority for review and approval by authorized government signatories [CNMI-PR Section 2-104 (1)-(8)]. No contract is effective against the Commonwealth until all parties whose signatures are required on the contract form have signed the contract [CNMI-PR Section 2-104(10)]. The only instance where a contract is not required is when the procurement qualifies as a small purchase valued at \$10,000 or less. Under the small purchase procurement method, a purchase order may be prepared in lieu of a contract (CNMI-PR Section 3-103).

Besides violating procurement regulations, the lack of a written contract is likely to result in misunderstandings and disagreements with the contractor. For example, in fiscal year 1994, MVA disputed the costs charged by I&S in connection with the promotion of beach volleyball contests in Saipan and Japan. MVA subsequently settled the dispute by agreeing to pay an additional \$22,000 despite claiming that the charges were not in accordance with previous arrangements made with the company.

Fiscal Years 1995 to 1996

In January 1994, the previous MVA administration abruptly terminated the services of I&S for "dissatisfactory (sic) performance and insubordination" and appointed another advertising company to handle MVA promotions. A year later, the new MVA administration terminated the other company in January 1995 to "start out fresh." In April 1995, MVA issued an RFP for promotion and advertising services and I&S was selected again on May 18, 1995.

- *MVA did not follow competitive selection procedures.* Despite the issuance of an RFP, procurement regulations were still not followed by MVA. The RFP disclosed MVA's budget ceiling for the project (\$2,065,000). Consequently, there was no competition at all with respect to price. Further, I&S was selected based on a majority vote of board members. This was not in accordance with regulations which provide that selection be based on evaluation factors set forth in the RFP. In fact, MVA's Promotion and Advertising (PR & AD) Committee had

recommended another advertising agency, but was overruled by the majority vote of board members. According to the Managing Director, this occurred because it was the first time that promotion and advertising services were procured using the RFP method and MVA was not familiar with the requirements. However, in June 1995, MVA certified to DOF that it had the capability and staff to carry out its own procurement.

Under the regulations, a request for proposal shall state the relative importance of price and other evaluation factors [CNMI-PR Section 3-106 (5)]. Award shall be made to the responsible offeror whose proposal is determined in writing to be the most advantageous to the government taking into consideration price and other evaluation factors. No other factors or criteria shall be used in the evaluation, and the contract file shall contain the basis on which the award is made [CNMI-PR Section 3-106 (7)].

- *MVA entered into an agreement with I&S which did not utilize a firm fixed price. Instead, MVA compensated I&S using the cost-plus-a-percentage-of-cost method specifically prohibited under the regulations. MVA entered into an "advertisement and promotion development services" agreement with I&S for a period of sixteen months from June 1, 1995 to September 30, 1996. The agreement, however, did not specify a fixed contract amount. Instead, I&S was compensated for the costs of placing media advertisements plus 15% commission, and the costs of production and purchase of advertising materials plus 17.65% commission. The cost-plus-a-percentage-of-cost method of compensation used to pay I&S is specifically prohibited by procurement regulations [CNMI-PR Section 3-401 (1)]. The use of such method provides no incentive for the contractor to control costs and is a virtual invitation for overcharging because the more costs incurred, the higher are the contractor's commissions.*

Under the regulations, government contracts shall utilize a firm fixed price unless a cost reimbursement contract is justified [CNMI-PR Section 3-401 (2)]. The regulations effectively allow only two types of contracts: firm fixed price and cost reimbursement contracts. Similarly, the Federal Acquisition Regulations (FAR) used by all federal executive agencies classify contract types into two broad categories: fixed price contracts and cost reimbursement contracts. The FAR also prohibits the use of cost-plus-a-percentage-of-cost contracts (FAR Subpart 16.102). Cost reimbursement contracts may only be used in unusual circumstances and must be justified in writing.

- *The I&S agreement was not a valid government contract because it was not signed by all necessary government signatories. The agreement also did not include several contract clauses required under the regulations. The I&S agreement was signed sometime in August 1995 (no specific date was indicated) by only the Board Chairman, MVA Legal Counsel, and the contractor. Standard government contract clauses prohibiting gratuities, kickbacks, and contingent fees were also not included in the agreement.*

Under the regulations, the official with expenditure authority prepares the contract and certifies that it complies with procurement regulations. The P&S Director then reviews and approves the contract for compliance with the regulations. The contract is next approved by the Secretary of Finance certifying availability of funds. Then the Attorney General is to certify the contract as to form and legal capacity, after which the contract must be approved by the Governor. No contract is effective against the Commonwealth until all of the parties whose signatures are required have signed the contract (See Contract Review, Processing and Oversight, CNMI-PR Section 2-104). The regulations also require that prohibitions against gratuities, kickbacks, and contingent fees shall be conspicuously set forth in every contract (CNMI-PR Section 6-207).

Fiscal Year 1997

The original agreement with I&S expired on September 30, 1996. The Managing Director explained that MVA renewed the agreement for fiscal year 1997 based on a provision in the agreement which stated that the "contract may be extended up to an additional two years depending on performance and budget availability."

According to the Managing Director, the renewal was recommended by the PR & AD Committee which believed that MVA should develop a long term relationship with its advertising company just like in the private sector. MVA, however, was unable to provide us documentation of the PR & AD Committee's decision to renew the I&S agreement or approval by the MVA Board. The I&S contract was approved subsequent to May 5, 1997, more than 7 months after the original agreement had expired (no specific approval date was indicated by the Governor; however, the Attorney General's approval was dated May 5, 1997). According to the Managing Director, the processing of the contract was significantly delayed because of several changes recommended by the Attorney General which I&S also had to review. Our review of available documents showed, however, that MVA started discussion of a new contract with I&S only in January 1997, more than 3 months after the previous agreement expired in September 1996.

- *I&S was awarded a new contract without following competitive selection procedures.* MVA documented the renewal of the I&S agreement by preparing a new contract with a similar provision for a two year extension. There was no written documentation indicating what type of procurement method was used to award the contract to I&S. There was also no written justification why I&S was selected again by MVA.

Under the regulations, contracts should generally be procured competitively unless other methods apply. There are no provisions in the regulations which allow automatic renewal or extension of contracts. Therefore, renewal of a contract should be justified and documented using one of the procurement methods specified under the regulations. In our opinion, the only method which could allow a contract to continue without competition is through the use of

the sole source procurement method. However, if the procurement does not satisfy sole source requirements, the contract should be procured competitively.

- *MVA allowed I&S to incur expenditures before approval of the contract.* The contract with I&S was approved only in May 1997. The contract period, however, was retroactive, i.e., from October 1, 1996 to September 30, 1997. We reviewed I&S billings and confirmed that a substantial amount of work was performed by I&S before the actual approval date.

Under the regulations, it is the responsibility of the official with expenditure authority to ensure that the contractor does not sign the contract or incur any expenses under it until all necessary government signatures have been obtained [CNMI-PR Section 2-104 (9)].

- *MVA entered into a contract with I&S which did not utilize a firm fixed price. Instead, MVA used the cost-plus-a-percentage-of-cost method specifically prohibited under the regulations and the cost reimbursement method without any written justification.* Under the contract, I&S shall be compensated for costs of placing media advertisements plus 15% commission, and costs of production and purchase of advertising materials plus 17.65% commission (this compensation arrangement was similar to the previous agreement). The contract, however, limited the amount of compensation to a total amount of \$3.265 million. In addition, the contract allowed I&S to bill MVA for reimbursement of travel and communication expenses.

S *No basis for contract price.* Although the contract limited the amount of compensation, it cannot be considered a firm fixed price contract because the contract price could vary depending on the amount of costs incurred by the contractor. We also found no evidence of price negotiation or offer submitted by I&S which should have been the basis for a firm fixed price. There was also no list of projects or work to be performed by I&S and their corresponding cost breakdown. Apparently, the compensation limit was based on the amount of the available MVA budget for promotion and advertising expenses. Without a specific scope of work tied to a definite contract price, MVA (or anyone else) has no basis for determining the progress of the contractor's work and whether the work has been completed. Such practice is also susceptible to fraud and abuse. For example, agency officials could allow the contractor of a commission-based contract to continue incurring unnecessary costs.

Under the regulations, government contracts shall utilize a firm fixed price unless a cost reimbursement contract is justified [CNMI-PR Section 3-401 (2)]. Although the regulations do not provide a definition of a firm fixed price contract, the FAR (used by federal executive agencies) defines a firm fixed price contract as a contract which "provides for a price that is not subject to any adjustment on the basis of the contractor's cost experience in performing the contract. This contract type places upon the contractor

maximum risk and full responsibility for all costs and resulting profit or loss. It provides maximum incentive for the contractor to control costs and perform effectively and imposes a minimum administrative burden upon the contracting parties (FAR Subpart 16.202).”

- S *Use of cost-plus-a-percentage-of-cost method of contracting.* The I&S contract called for a payment scheme based on the cost-plus-a-percentage-of-cost method. Under such method, I&S was compensated for costs incurred plus a 15 or 17.65 percentage commission which was computed on that cost base.

Under the regulations, the cost-plus-a-percentage-of-cost method of contracting is specifically prohibited [CNMI-PR Section 3-401 (1)].

- S *The I&S contract allowed cost reimbursements.* The contract allowed I&S to bill MVA for reimbursement of various expenses. However, we found no written determination that cost reimbursement was appropriate.

Under the regulations, a cost reimbursement contract may be used only if the P&S Director determines in writing that (a) uncertainties in the work to be performed make the cost of performance too difficult to estimate with the degree of accuracy required for a firm fixed price contract; and (b) use of a cost reimbursement contract is likely to be less costly to the government than any other type due to the nature of the work to be performed under the contract [CNMI-PR Section 3-401 (3)].

Fiscal Year 1998

Discussions to renew the I&S contract for fiscal year 1998 began in August 1997 when I&S conducted a presentation before the MVA Board. In a subsequent meeting in September 1997, the MVA Board agreed to renew I&S's contract. The former governor, however, rejected the renewal of the contract on November 14, 1997. Despite the rejection, MVA officials continued to lobby for the renewal of the contract. The following violations were noted for fiscal year 1998:

- *MVA did not follow competitive selection procedures.* Initially, a new contract for \$3.55 million was prepared by MVA for approval by the former governor. However, the Attorney General questioned the contract because it did not undergo the RFP process. At the suggestion of the Attorney General, MVA then prepared a change order extending the term of the contract based on the renewal provision of the previous contract. The proposed change order, however, was questionable because it increased the contract price from the original \$3.265 million to \$6.815 million or a 109% increase. The \$3.55 million change order amount exceeded the original contract price by \$285,000. This effectively resulted in a new contract that was procured without undergoing the normal procurement process.

As previously discussed, contracts should generally be procured competitively unless other methods are appropriate. Allowing a change order that more than

doubles the amount of the original contract circumvents the procurement regulations. In our opinion, the only method which could allow a contract to continue without competition is through the use of the sole source procurement method. The use of this method, however, should comply with the requirements provided under the regulations.

- *No reasonable basis for contract price.* We found no evidence that the \$3.55 million contract price was negotiated or proposed by I&S. Documents showed that MVA established the price based on the available budget for promotion and advertising expenses (per October 2, 1997 memo of Managing Director to P&S Director).

The Assistant Attorney General assigned to MVA also noted that the contract price was being treated as a budget ceiling instead of a fixed contract amount. He pointed out that airfare and travel expenses of MVA staff and board members were included in the contract. In addition, we were informed by the MVA Comptroller that local vendors hired by I&S were paid directly by MVA. The budget for such payments was taken out of the I&S contract amount. This practice effectively circumvented procurement regulations because payments to the local vendors did not undergo the normal procurement process.

- *MVA allowed I&S to incur expenditures although no new contract had been approved.* At the time of the audit, the I&S contract had already expired and no new contract had been approved for fiscal year 1998. MVA officials, however, allowed I&S to incur expenditures in violation of procurement regulations.

S *Expenditures incurred without a valid contract.* As of February 1998, expenditures incurred by I&S totaled more than \$2.6 million in fiscal year 1998. These consisted of unpaid invoice billings of about \$1.0 million, unbilled expenditures of about \$1.6 million for services which had already been provided, and purchase orders charged to local vendors of about \$52,000 (of which around \$25,000 has already been paid by MVA). This did not include anticipated expenditures for March 1998 which could amount to more than \$258,000.

Under the regulations, it is the responsibility of the official with expenditure authority to ensure that the contractor does not incur any expenses until all necessary government signatures have been obtained. No contract is effective against the Commonwealth until all parties whose signatures are required on the contract form have signed the contract [CNMI-PR Section 2-104 (10)].

The Managing Director explained that promotion and advertising require long lead times. This requires weeks or months of advance preparations and planning before actual execution. According to her, the former governor assured MVA of the approval of the I&S contract. Thus, MVA allowed I&S to continue its promotional and advertising work despite the expiration of the previous contract. In several letters to the Acting Attorney General

and the Assistant Attorney General for MVA, I&S claimed that it relied on the representation by MVA officials that the contract would be approved. I&S also explained that several ongoing media projects could not be canceled because these were too far into development. I&S insisted that MVA would still be liable for the full amount in cancellation fees even if these projects were canceled.

- S** *MVA officials could be held personally liable for I&S expenditures.* Our review of available documents showed that top MVA officials had repeatedly assured I&S that the contract would be approved. The officials did not attempt to stop the advertising company's activities despite the absence of an existing contract. Such actions were in direct violation of procurement regulations. The following are examples of these actions:
- N** MVA and I&S correspondence and memos issued after September 30, 1997, showed that the Managing Director and other MVA officials continued coordination and planning of I&S promotion and advertising activities although no new contract had been approved.
 - N** On October 16, 1997, MVA entered into a 50,000,000 Yen (\$500,000) separate agreement with I&S to obtain the services of a Japanese actor. The agreement, which did not undergo the procurement process, was signed only by the Managing Director and Board Chairman.
 - N** On October 27, 1997, I&S notified MVA that it could not proceed with further assignments without a contract. On October 29, 1997, the MVA Board Chairman requested I&S to reconsider its plan to halt promotional activities. The Board Chairman assured I&S that the former Governor would sign the contract.
 - N** In a December 4, 1997 memorandum, the Assistant Attorney General (AAG) for MVA informed the Managing Director and Board members that it was not prudent to risk personal liability for expenses incurred by I&S prior to approval of its contract. The AAG also suggested that MVA send a letter to I&S directing the company to stop its activities and make no further commitments. Instead of following the AAG's suggestions, the Managing Director and Board Chairman wrote letters to the former Governor and the presiding officers of the Legislature on December 11, 1997 pleading for approval and funding of I&S contract.
 - N** On January 30, 1998, the Attorney General's Office (AGO) issued a letter to I&S to stop all work being performed for MVA. According to AGO, there was no guarantee that the Governor would approve the I&S contract. The Managing Director, however, issued two directives on February 20, 1998 defying the AGO's letter. The two directives in-

structed MVA staff to continue supporting present and upcoming media projects of I&S.

Under the regulations, any procurement action of an employee in violation of the procurement regulations is an action outside the scope of his or her employment. The government should seek to have any liability asserted against it by a contractor which directly results from these improper acts determined judicially to be the individual liability of the employee who committed the wrongful act (CNMI-PR Section 1-108). The regulations define "employee" to mean any individual receiving a salary from the government, including appointed and elected officials, and other non-salaried individuals performing personal services for the government [CNMI-PR Section 1-201 (8)].

2. *Prime Air System (\$352,017)*

Prime Air System (PAS) currently represents MVA in Korea. As MVA's representative in Korea, PAS duties are to make sales calls to travel agents and tour operators, respond to inquiries regarding the CNMI, and provide advice on the latest tourism related developments. Our review of MVA's procurement transactions with PAS showed the following:

- *PAS services were procured without competition.* MVA failed to comply with competitive selection procedures in the procurement of PAS services. MVA also did not follow the requirements for other procurement methods which may be applicable.
- S In fiscal year 1993, MVA entered into a "tourist and development services" agreement with PAS for \$50,000 from December 1, 1993 to November 30, 1994. Based on available documents, PAS was selected by the PR & AD Committee because of the endorsement of two airline companies (PAS was the general sales agent for the two airlines). This selection method was not in accordance with the regulations.
- S In November 1994, the PAS agreement was renewed by MVA for another year under the same terms and conditions as in the previous agreement. MVA was unable to provide evidence of board approval to renew the agreement. Further, the renewal letter was signed only by the president of PAS and not by any MVA official.
- S PAS continued providing services throughout fiscal year 1996 although its agreement supposedly expired in November 1995. MVA was unable to provide documents showing that PAS's services were renewed.
- S In fiscal year 1997, MVA awarded a contract for \$50,000 to PAS through the sole source procurement method. The contract, which was completely approved only on September 25, 1997, was made to apply retroactively from

November 29, 1996 to September 30, 1997. In addition, the sole source justification letter of the Managing Director failed to state the consideration given to alternative sources as required under the regulations.

- S In fiscal year 1998, MVA prepared a change order for \$50,000 to extend the sole source contract with PAS for another year. At the time of the audit, however, the change order had not yet been approved by the Governor. The change order would have been effective October 1, 1997 to September 30, 1998. The Managing Director explained that MVA solicited proposals and interviewed several offerors in Korea, including PAS. The Board voted to retain PAS upon the recommendation of a committee that evaluated the proposals.

The use of a change order to award a contract procured through RFP was not in accordance with regulations. Instead of a change order, MVA should award a new contract to PAS if its proposal was evaluated as the best. Based on available documents, however, MVA officials interviewed all offerors and supposedly based their selection on the results of the interviews. However, we did not find any basis for the selection because MVA did not rank each offeror based on price and other evaluation factors (such as the contractor's experience, financial capability, manpower, etc...). Instead, MVA officials who conducted the interview prepared a memo summarizing the information they obtained from each offeror. The memo, however, did not measure or rank each offeror's responsiveness to the requirements of the RFP. Without a measurement basis, two persons reviewing the results of the interview could come up with different conclusions. For example, we found at least two offerors who submitted a lower price than PAS. We could have chose these two if price was considered the most important factor. Another example, a board member who participated in the interview indicated in his trip report that at least two offerors were more capable and able to meet the RFP requirements compared to PAS. We could not understand why PAS was considered the "best value" by MVA.

Under the RFP method (CNMI-PR Section 3-106), MVA should first review the responsiveness of proposals based on price and other evaluation factors set forth in the RFP (e.g., by providing points for each evaluation factor and ranking offerors based on the most number of points accumulated). If clarification is needed and to insure full understanding of proposals, MVA may conduct discussions and negotiate with the responsible offerors found to be in the competitive range to determine their best and final offer (only those offerors who are reasonably susceptible of being selected for award need to be interviewed). Award should then be made to the responsible offeror whose proposal is determined in writing to be most advantageous to the government taking into consideration price and other evaluation factors set forth in the RFP. No other factors or criteria shall be used in the evaluation.

- *PAS agreement was not a valid government contract.* The initial PAS agreement and subsequent renewals were not valid government contracts because they were not signed by all necessary government signatories (including the Attorney General and the Governor). The agreement was signed only by the Board Chairman, MVA Legal Counsel, and the contractor. The renewal was signed only by the contractor.
- *PAS was compensated using the cost reimbursement method without written justification.* Both the PAS agreement and sole source contract called for the payment of \$50,000 per year plus reimbursement of extraordinary out-of-pocket expenses. However, there was no written document justifying that cost reimbursement was appropriate. Under the regulations, cost reimbursement may be allowed only if the P&S Director determines in writing that cost reimbursement will be advantageous and likely to be less costly to the government. We noted, however, that actual payments to PAS significantly exceeded \$50,000 because of cost reimbursements. For example, in fiscal year 1997 alone, PAS was paid more than \$123,000.
- *PAS was allowed to incur expenses without a new contract.* At the time of the audit, MVA's change order to renew the PAS contract for fiscal year 1998 was still in process. MVA, however, allowed PAS to perform work and incur expenses totaling more than \$31,700 without a valid government contract. Under the regulations, no expenditures should be incurred by the contractor until the contract has been signed by all necessary government signatories.

On February 23, 1998, the Acting Managing Director issued a letter informing PAS to stop all promotional activities for MVA until such time as a signed contract is in place.

3. *New Visions Marketing Services, Ltd. (\$306,689).*

New Visions Marketing Services, Ltd. (NVMS) currently provides promotional services as MVA's Representative in Taiwan. Our review of MVA's procurement transactions with NVMS showed the following:

- *NVMS services were procured without competition.* NVMS services were procured by MVA using the sole source procurement method. However, the justifications given by MVA did not warrant the use of the sole source method.
- S On January 27, 1995, MVA entered into a sole source "tourist and development services" agreement with NVMS for \$60,000 from February 1, 1995 to January 31, 1996. The reasons given by the Managing Director for sole sourcing the agreement were (1) MVA wanted to maximize the opportunity by opening a representative office as quickly as possible because of the opening of direct flights to Taiwan, and (2) the contractor was familiar with the promotion and marketing program of CNMI competitors in the tourist industry.

The sole source justifications of the Managing Director, however, did not warrant the awarding of a sole source contract. First, the urgency of obtaining promotional services was not a sufficient reason to forego the benefits of competitive procurement. No emergency existed because there was no threat as to public health, safety, or welfare. Second, there was no indication that MVA attempted to obtain information from other companies in Taiwan. Based on available documents, the Board Chairman pushed for the approval of NVMS as MVA representative because it was highly recommended by a top official of a hotel in Saipan. Under the regulations, consideration should be given to alternative sources. Lastly, there was no written determination by the P&S Director that there was only one source for promotional services in Taiwan.

- S NVMS continued providing services throughout fiscal year 1996 although its agreement supposedly expired on January 31, 1996. MVA was unable to provide us documents showing that the NVMS agreement was renewed.
- S In fiscal year 1997, MVA awarded a contract for \$60,000 to NVMS through the sole source procurement method. The contract, which was approved by the former Governor only on September 4, 1997, was made to apply retroactively from February 1, 1997 to September 30, 1997. In addition, the sole source justification letter of the Managing Director failed to state the consideration given to alternative sources as required under the regulations.
- S In fiscal year 1998, MVA prepared a change order for \$25,000 to extend the sole source contract with NVMS. The extension was for a six-month period from October 1, 1997 to March 31, 1998. At the time of the audit, however, the change order had not yet been approved by the Governor. The Managing Director explained that MVA solicited proposals and interviewed several offerors in Taiwan, including NVMS. The Board, however, was unimpressed with any of the offerors and voted to retain NVMS on a month-to-month basis.

As previously discussed, the use of a change order to award a contract procured through an RFP was not in accordance with regulations. Instead of a change order, MVA should award a new contract to the best offeror. Based on available documents, however, MVA officials interviewed all offerors and supposedly based their selection on the results of the interviews. However, we did not find any basis for the selection because MVA did not rank each offeror based on price and other evaluation factors (such as the contractor's experience, financial capability, manpower, etc...).

- *The original NVMS agreement was not a valid government contract.* The NVMS agreement signed on January 31, 1995 was not a valid government contract because it was not signed by all necessary government signatories (including the Attorney General and the Governor). The agreement was signed only by the Board Chairman and the contractor.
- *NVMS was compensated using the cost reimbursement method without written justification.* Both the original 1995 NVMS agreement and the subsequent 1997 sole source contract called for the payment of \$60,000 per year plus reimbursement of extraordinary out-of-pocket expenses. However, there was no written document justifying that cost reimbursement was appropriate. Under the regulations, cost reimbursement may be allowed only if the P&S Director determines in writing that cost reimbursement will be advantageous and likely to be less costly to the government. We noted, however, that actual payments to NVMS significantly exceeded \$60,000 because of cost reimbursements. For example, in fiscal year 1997 alone, NVMS was paid more than \$124,000.
- *NVMS was allowed to incur expenses without a new contract.* At the time of the audit, MVA's change order to renew the NVMS contract for the six months ending March 31, 1998 was still in process. MVA, however, allowed NVMS to perform work and incur expenses totaling \$27,990 without a valid government contract. Under the regulations, no expenditures should be incurred by the contractor until the contract has been signed by all necessary government signatories.

On February 23, 1998, the Acting Managing Director issued a letter directing NVMS to stop all promotional activities for MVA until such time as a signed contract is in place.

4. *Dentsu Young & Rubicam, Inc. (\$1.116 Million)*

Dentsu Young & Rubicam (DYR) provided advertising services for MVA in Japan, Hongkong, and Korea for about ten months from April 1994 until January 1995. Our review of MVA's procurement transactions with DYR showed the following:

- *MVA procured the services of DYR without following competitive selection procedures.* In March 1994, the previous MVA administration appointed DYR to handle MVA promotions as the replacement for I&S which had been terminated earlier by the Board in January 1994. DYR was selected because it was supposedly the second choice when I&S was first selected in 1992 from among other advertising agencies. The procurement of DYR through direct appointment by the Board was not in accordance with procurement regulations. In addition, MVA was unable to provide documentation showing the results of evaluation of proposals in 1992.
- *MVA's agreement with DYR did not utilize a firm fixed price. DYR was also compensated using the cost-plus-a-percentage-of-cost method specifically prohibited under the regulations.* MVA entered into an agreement with DYR to provide promotion and advertising

services commencing April 1, 1994. The open-ended agreement did not specify a firm fixed price as recommended under the regulations. DYR was also compensated for costs of placing media advertisements plus 15% commission, and costs of production and purchase of advertising materials plus 17.65% commission. This cost-plus-a-percentage-of-cost method of compensation used to pay DYR is specifically prohibited by procurement regulations.

- *The DYR agreement was not a valid government contract.* The agreement was not a valid government contract because it was not signed by all necessary government signatories (including the Attorney General and the Governor). The agreement was signed only by the Board Chairman, MVA Legal Counsel and the contractor. The standard government contract clauses (e.g. prohibition against kickbacks and gratuities) required under the regulations were also not included in the agreement.

DYR was terminated in January 1995 by the current MVA administration which wanted to “start out fresh” in promoting the CNMI. Its replacement, I&S continues to provide services to MVA at the time of the audit.

5. *Access Inc. (\$525,638)*

Access Inc. (Access) served as MVA representative in Japan from fiscal year 1990 to fiscal year 1995. Access' duties were to make sales calls to travel agents and tour operators in Japan, respond to inquiries regarding the CNMI, and provide advice on the latest tourism related developments. Our review of MVA's procurement transactions with Access showed the following:

- *MVA selected Access without following competitive selection procedures.* In May 1990, Access was chosen by the Board to represent MVA in Japan upon the advice of the MVA consultant (who was the former managing director). There was no documentation showing that other proposals were obtained and evaluated by the Board. The MVA Consultant subsequently became a Board member of MVA (he later resigned when the current MVA administration came on board). His wife established a local company with the president of Access while he was an MVA Consultant.
- *Access was paid without a valid government contract.* From 1990 until the latter part of 1993, Access was paid a monthly fee of 800,000 Yen, or about \$8,000, plus reimbursement of expenses. MVA, however, had no contract or agreement with Access. According to the former deputy director, MVA's relationship with Access was based on a "gentlemen's agreement" which was practiced in Japan.
- *MVA entered into an agreement with Access without setting a firm fixed price. Access was compensated using the cost reimbursement method without any justification.* In September 1993, the Board agreed to increase the monthly fees charged by Access from 800,000 to 1,000,000 Yen. We found no documentation, however, that the increase was requested by Access. MVA documented the increase by entering

into a "Tourist and Investment Development Service" agreement with Access which was signed only by the Board Chairman, MVA Legal Counsel, and contractor. The agreement was for a period of two years from October 1, 1993 to September 30, 1995. Apart from the monthly fees, the agreement allowed Access reimbursement for "extraordinary expenses." These expenses totaled more than \$85,000. However, there was no written determination by the P&S Director that cost reimbursement was appropriate and advantageous, as required by the regulations. There was also no definition of extraordinary expenses. Consequently, Access was reimbursed for expenses, some of which were not related to MVA's representation in Japan. For example, Access was reimbursed for sending funeral flowers to its own president as condolence for the death of a relative. Access was also reimbursed for personal expenses (conference fees) of the wife of a former MVA board member.

6. *Ad Intelligence (\$480,475)*

Ad Intelligence (AI), an advertising company based in Japan, was hired sometime in fiscal year 1994 for promotional activities dubbed as "International Friendship Year 1994." Our review showed the following procurement violations:

- *MVA procured AI's services without following competitive selection procedures.* The only supporting procurement documents on file were a proposal and schedule of activities submitted by AI to the Managing Director.
- *AI was paid without a valid government contract.* AI was compensated based only on invoices submitted to MVA.

AI's proposal included a design contest and production of a "Statue of Friendship" monument for approximately \$40,000. Based on our inquiries, the monument was never built, although this was included among the invoices paid by MVA.

7. *JIC Corporation (\$227,905)*

JIC Corporation (JIC) based in Japan provided promotion and advertising services to MVA from fiscal year 1992 to 1993. Its services were mainly for ad placements, and production and distribution of posters and accessories (such as vests, putters, and T-shirts).

- *MVA procured JIC's services without following competitive selection procedures.* MVA was unable to provide evidence of competitive procurement of JIC.
- *JIC was paid without a valid government contract.* MVA payments to JIC were supported only by invoices.

Except for invoices listing the general locations (e.g. Tokyo, Nagoya, etc...) where the posters or accessories were distributed, there were no supporting documents evidencing that the items were actually distributed. For example, pictures of posters

at the location, or acknowledgment receipts, or listing of persons or companies receiving the accessories, should have been required by MVA before payments were made.

8. *Bozell CCAA (\$223,994)*

Bozell CCAA (Bozell) provided promotion and advertising services in Taiwan during fiscal years 1992 to 1994.

- *Bozell's services were procured without competition.* MVA was unable to provide evidence of competitive procurement of Bozell.
- *Bozell was paid without a valid government contract.* MVA had no contract or agreement with Bozell on file. Payments were based solely on invoices.
- *MVA subsequently entered into an agreement with Bozell without setting a firm fixed price. The agreement also called for payment using the cost-plus-a-percentage-of-cost method specifically prohibited under the regulations.* In October 1993, the former MVA Managing Director signed an "advertiser/agency agreement" with Bozell for one year ending September 30, 1994. The agreement did not set a fixed contract amount, and called for payment of charges for placing advertisements and conducting promotions plus a 17.65% commission.

9. *Ohta Publication (\$180,737)*

Ohta Publication (Ohta), a company based in Japan, was responsible for publishing an advertising supplement (inserted in magazines or newspapers) called the 'Marianas Sales Guide,' and also published the MVA calendar. Ohta provided services to MVA for fiscal years 1990 to 1995.

- *Ohta's services were procured without following competitive selection procedures.* There was no evidence of competitive procurement for the publishing services which probably could have been obtained locally.
- *MVA paid Ohta without a valid government contract.* MVA had no contract or agreement with Ohta on file.

Ohta's advertising billings to several local hotels and tourist shops were paid by MVA. The advertisements were included in the Marianas Sales Guide. We did not find evidence of reimbursements or payments made by these hotels and shops to MVA.

Procurement Did Not Go Through P&S Division

Under the regulations, all procurement functions must be conducted by the P&S Director unless an agency has been granted specific authority by law or has been delegated the authority to conduct its own procurement by the Secretary of Finance and P&S Director. During fiscal years 1992 to 1996, however, all procurement of

promotion and advertising services by MVA did not go through the P&S Division, in violation of the CNMI-PR. MVA also did not route contracts and agreements to the Attorney General and the Governor for review and approval as required under the regulations.

In our discussion with the current Managing Director, she stated she did not know why the previous administration failed to follow the CNMI-PR. However, she explained that prior to 1994, the previous administration was following certain MVA marketing guidelines for procurement of promotion and advertising services. MVA subsequently prepared its own procurement regulations and began following them. However, MVA reverted back to the CNMI-PR after the former Governor issued an executive order (EO 94-3) reorganizing government agencies (the executive order placed MVA under the Department of Commerce). A short time later, however, the Attorney General's Office requested MVA to again comply with the CNMI-PR. The Managing Director said that MVA complied with the AGO's request, but she could not remember the reason behind the AGO's action.

Based on our subsequent inquiries and review of available documents, MVA published a draft of its own procurement regulations in the Commonwealth Register in December 1994. The regulations, however, were formally adopted by MVA only in April 1996 when the Managing Director requested the Secretary of Finance to allow MVA to conduct its own procurement. In July 1996, the Secretary of Finance authorized the P&S Director to delegate procurement functions to MVA and allow the agency to conduct its own procurement in accordance with the MVA-PR. Sometime in November 1996, MVA submitted several contracts to the Attorney General's Office (AGO) for review and comments. The AGO, however, returned the contracts because of non-compliance with the CNMI-PR. The AGO pointed out that MVA prepared sole source contracts without going through the P&S Division, and that some of the contracts did require the signature of the Governor. According to the AGO, it was aware that MVA had been delegated procurement authority by the Secretary of Finance. However, a proper delegation cannot be made unless the agency has adopted the CNMI-PR or identical regulations. Even under those regulations, procurement under the sole source method may not be delegated. The regulations also require that the Governor's approval be obtained.

Routing of Contracts

MVA's procurement practice was to process contracts internally. Sometime in 1997, MVA began routing contracts to the P&S Director, the Attorney General and the Governor for review and approval (apparently, as a result of the AGO's comments in November 1996). Since MVA was authorized to conduct procurement functions only in July 1996, MVA's failure to route contracts in the previous years violated the CNMI-PR.

At the present time, MVA should not be required to route all contracts to the P&S Director since it has already been delegated procurement authority. MVA, however, should still route contracts to the Attorney General and the Governor for approval.

Procurement under the sole source, emergency, and expedited methods must still be handled by the P&S Division, since these functions cannot be delegated under the CNMI-PR.

MVA-PR Not Identical With CNMI-PR

We compared the MVA-PR with the CNMI-PR. Although the MVA-PR appeared substantially similar, there were several major differences. For example, MVA-PR excluded professional, advisory, and technical services from the definition of services. The MVA-PR also added a separate section for procurement of marketing proposals (which gave the Managing Director the sole authority to procure proposals without competition). In addition, the approval of the Attorney General and the Governor was not required. Also, an MVA appeal committee was designated to handle bid protest appeals, instead of the Public Auditor.

As previously discussed, the Secretary of Finance's grant of authority to administer some procurement functions does not relieve MVA from complying with the provisions of the CNMI-PR. A proper delegation cannot be made unless an agency receiving the delegation has adopted identical regulations. MVA is therefore still required to follow the provisions of the CNMI-PR should there be differences with the MVA-PR. In any event, even if a proper delegation is made, only the procurement functions being performed by the P&S Director are handed over to the agency. The regulations remain the same and the duties and functions of other government officials or agencies mentioned in the regulations cannot be transferred or delegated.

MVA Officials Not Familiar With CNMI-PR

Based on our discussions, it appeared that MVA officials believed that in procuring advertising contracts, solicitation of proposals was enough, and the Board could choose among the proposers, either by majority vote or appointment. They were not aware of the specific requirements for the use of competitive sealed proposals or other procurement methods. For example, MVA supposedly solicited proposals for advertising services in Taiwan and Korea, but used sole source contracts or change orders instead of awarding the contracts under the RFP method. A contract file containing the basis for selection is also not maintained as required under the regulations. Most of the documents we gathered in reviewing a particular contract came from different sections of MVA. There was no systematic or centralized filing system for contract documents.

We asked the Managing Director if she was aware that MVA officials could be held personally liable for violation of the procurement regulations. She told us that she was not aware of the personal liability. She also said that she and other officials were only abiding by the decisions of the Board.

Remedies Against Violation of Procurement Regulations

As previously discussed in this report, MVA procured promotion and advertising services from 9 advertising companies in violation of the CNMI-PR. Consequently, public funds were illegally spent by MVA, and there was no assurance that expenditures valued at \$14.22 million were necessary or were procured at a fair and reasonable price.

Past Contractors

Six of the 9 advertising companies were no longer providing services to MVA at the time of our audit. Consequently, the available remedies against these contractors may be limited because they have been fully paid. A contractor who violates the procurement regulations shall be subjected to a warning or reprimand, termination of the contract or suspension from being a contractor under a government contract, in addition to other penalties prescribed by law [CNMI-PR Section 6-211 (2)]. In these cases, however, the billings have been paid and the only possible action in this instance would be to suspend the contractors from being awarded government contracts in the future. The government could still seek damages but it would have to prove that the contractors acted in bad faith, among other considerations. Government employees, however, found to be responsible for the violations should be subject to adverse actions in accordance with CNMI-PR Section 6-211 (1).

Current Contractors

At the time of the audit (February 1998), MVA had allowed at least 3 advertising companies to incur expenses amounting to more than \$2.7 million although no new contracts had been approved by the Governor. The companies had prior contracts with MVA which expired in fiscal year 1997. The companies were originally procured without following competitive selection procedures and had, in the past, conducted business with MVA without valid contracts. The AGO and Deputy Managing Director had already informed the companies to stop providing services explaining that MVA could not be held liable without a valid contract. However, top MVA officials, including the Board Chairman and the Managing Director, have failed to issue a similar statement to the other companies.

The decision to approve or disapprove a contract ultimately rests with the Governor since he is the last signatory in a government contract. However, if a contract is approved and is still found to be in violation of the regulations, which is likely the case with MVA, the contractor is still subject to the remedies under CNMI-PR Section 6-211 (2) which include the termination of the contract. If the contractor acted in good faith, he may be entitled to the actual costs incurred prior to termination. If the proposed award of the contract is canceled, the contractor has the option to protest the cancellation to the P&S Director, and subsequently appeal to the Public Auditor. The contractor will then be subject to the remedies prior to award provided under CNMI-PR Section 5-103 (1) of the regulations. If the remedies are followed, there are two possible actions that could be taken if the

solicitation of the contract is found to be in violation of the procurement regulations. One is to cancel the solicitation, and the second is to make revisions to comply with the regulations. It is questionable, however, if the 3 proposed contracts can still be revised to comply with the procurement regulations. The selection of vendors violated competitive selection procedures and the contractors have already rendered services. MVA cannot solicit new proposals for past services. At any rate, there is no guarantee that the contractors will be selected again under open competitive procedures. Therefore, the only choice may be cancellation. If the contractor asserts any liability against MVA, the government should consider whether such liability can be assessed against the employee(s) who permitted the contractors to violate the procurement regulations (CNMI-PR Section 1-108).

Conclusion and Recommendations

MVA violated CNMI-PR in the procurement of promotions and advertising services. MVA should adopt measures to comply with these regulations and implement remedies against violations. Accordingly, we recommend that:

1. The Governor and the Attorney General's Office consider taking appropriate action against current and previous MVA officials, including the MVA Board Chairman and Managing Director, for violation of the CNMI-PR. Such action includes but is not limited to reprimand, suspension without pay, termination of employment, civil injunction, civil suit for damages or return of government money, or criminal prosecution [CNMI-PR Section 6-211 (1)]. At the least, reprimand letters should be issued and permanently filed in their personnel files.
2. The Governor instruct MVA to cancel the proposed contracts with the 3 advertising companies for violation of the CNMI-PR. This recommendation is based on the fact that even if these proposed contracts were to be approved, they would still be in violation of the regulations. In such case, the contractor would be subject to the remedies under CNMI-PR Section 6-211(2) which include termination of the contract. If the contractors assert any liability against MVA, we recommend that the Attorney General's Office consider whether it is appropriate to file a cross claim against MVA officials and employees who were responsible for the violations discussed in this report.
3. P&S Director suspend the 9 advertising companies from becoming contractors or subcontractors on future government contracts for at least a year or such other period of time as deemed sufficient by the Director. The suspensions should be communicated to the companies to emphasize that they need to comply with the CNMI-PR when dealing with government agencies.
4. The Board Chairman and the Managing Director ensure that all procurement of promotion and advertising services be procured competitively, in accordance with the CNMI-PR. To this end, both officials should ensure that all procurement conducted through the RFP process be awarded based on price

and other evaluation factors stated in the RFP and not through appointment or majority vote of the Board.

5. The Managing Director take steps for MVA to adopt the CNMI-PR. Identical regulations need to be adopted to enable MVA to continue to conduct its own procurement functions.
6. The Managing Director, MVA Board members, and procurement officials should familiarize themselves with the CNMI-PR. They should both review the CNMI-PR and request the P&S Director to provide explanation to parts they don't understand. MVA employees involved in the procurement of goods and services should be required to be familiar with the details of the regulations.
7. The Managing Director establish a filing system that can provide a complete history of the transactions with each individual contractor. Contract files generally consist of (1) contracting files which document the basis for acquisition and the award of the contracts, (2) contract administration files which document actions taken to monitor contractor performance and compliance with the scope of work, and (3) payment contract files which document actions substantiating and reflecting contract payments.

Governor's Office Response

The Governor's letter response dated May 20, 1998 did not address Recommendations 1 and 2. According to the Governor, his office has reviewed the report and recognize that it raises serious concerns. The Governor believes that it is premature to make any decisions on the OPA recommendations regarding actions that should be taken by his office. He also stated that it is important that the response of MVA be obtained as provided in 1 CMC § 7823(a) [the Auditing Act], and considered by OPA before a decision is made whether to take disciplinary action against officials or contractors and what the nature of any such action should be. He further stated that such decisions should only be based upon OPA's final analysis after consideration of MVA's response.

AGO Response

The Acting Attorney General did not respond to Recommendations 1 and 2.

P&S Response

The P&S Director did not respond to Recommendation 3.

MVA Response

The Managing Director was requested to respond only to Recommendations 4, 5, 6, and 7. Her letter dated May 20, 1998 responded to all recommendations. Her responses, however, did not address the recommendations as discussed below:

Recommendation 1

The Managing Director stated that the present management and MVA Board cannot offer recommendation or actions relative to decisions made by the previous management and Board of Directors of MVA. The MVA would leave this discretion to the OPA and the AGO's office. The Managing Director pointed out, however, that in the controversial I&S case, the MVA board chose to renew the contract of I&S. The contract was signed by all parties except for the former Governor despite his verbal promise that the contract will be signed after the election. The Managing Director claimed that it is universally acceptable in societies that when the head of State and similar titular persons make commitments verbal or otherwise, their word of assurance and promise is almost as good as the full faith and credit guarantee of the government towards a public debt. The Managing Director further contended that the management and the Board acted in good faith in following prescribed procedures in the renewal of I&S contract.

OPA Comments

Modern societies are governed by laws and regulations. Among other things, the CNMI-PR was promulgated to provide for increased public confidence in the procedures followed in public procurement, to foster broad-based competition within the free enterprise system, to insure the fair and equitable treatment of persons who deal with the procurement system of the Commonwealth, and to provide safeguards for the maintenance of a procurement system of quality and integrity. MVA officials, however, completely disregarded the CNMI-PR when they spent public funds without following competitive selection procedures, paid contractors without valid contracts, and entered into agreements prohibited under the regulations. Consequently, MVA had no assurance that expenditures totaling more than \$14.22 million were necessary or were procured at a fair and reasonable price. Taking appropriate actions against the responsible MVB officials is not only in accordance with CNMI-PR Section 6-211 (1) but also will go a long way in maintaining public confidence in government procurement and discouraging abuse of public funds.

Recommendation 2

The Managing Director stated that the contracts (to represent MVA in Korea and Taiwan) for the two companies were bid out and an award was made for one contract. The Managing Director also stated that the other contract was allowed to operate on a monthly basis until a qualified contractor is selected. Furthermore, the idea to allow the two advertising companies to operate pending an approved 12 month contract was to provide continuity of promotion and marketing activities without interruption.

OPA Comments

In another example of CNMI-PR violations, MVA interviewed offerors and supposedly based their selection on the results of the interview. However, there was

no basis for the selection because MVA did not measure or rank each offeror's responsiveness to the requirements of the RFP (i.e. price, experience and other evaluation factors). For example, at least two offerors submitted a lower price than the contractor who was awarded the contract. The board member who participated in the interview indicated in his trip report that other offerors were more capable and able to meet the RFP requirements compared to the selected contractor. In the case of the other contractor, the MVA Board "voted" to retain the company on a "month-to-month" basis. Under the CNMI-PR, selection should be based on the responsiveness of the proposals to the RFP requirements. The practice of awarding contracts by appointment or majority vote of the Board is not only illegal but defeats the purpose of competitive procurement.

Recommendation 3

The Managing Director stated that the recommendation to suspend the 9 advertising companies from participating in future government contracts should be reconsidered. According to her, the foreign companies should not be penalized for "violation of the CNMI-PR" because they committed their services to MVA based on accepted practices in their countries. She recommended that they be allowed to be familiar with the CNMI-PR. The Managing Director added that MVA should (not) write the RFP specifications so detailed that these alone might cause companies to "self exclude" themselves from the process.

OPA Comments

All companies transacting with CNMI government agencies should be familiar with the CNMI-PR. MVA should require all companies, foreign or not, to comply with the CNMI-PR instead of accommodating "accepted practices" in their countries. Suspension of the 9 companies (for a limited period as determined by the P&S Director) will put them on notice that the CNMI-PR should be observed and followed in their dealings with the government. With regards to RFP specifications, these should be detailed enough to avoid any misunderstanding by the offerors and MVA.

Recommendation 4

In response to our recommendation that MVB procure promotion and advertising contracts in accordance with the CNMI-PR and not through appointment or majority vote of the Board, the MVA Managing Director stated that there are existing criteria for selecting a contractor for facility, equipment purchase and service projects. These criteria, however, does not include the services of an advertising company although price and qualification is always a consideration. The Managing Director further stated that, in the future, a standard written criteria must be established for selecting advertising and promotion contractors that will be in general compliance with the CNMI-PR. According to her, OPA should be included in drafting the criteria.

OPA Comments

As discussed in the report, for procurement of promotion and advertising services where bidding is impractical, the preferred method should be “competitive sealed proposals” under CNMI-PR Section 3-106. Under this section, award of the contract should be made in writing to the best qualified offeror based on evaluation factors set forth in the RFP and based on negotiation of compensation determined to be fair and reasonable. The Managing Director should reconsider and implement the recommendation.

Recommendation 5

In response to our recommendation that MVA adopt the CNMI-PR, the Managing Director stated that under the new legislation, MVA will devise its own procurement regulations which will be in general compliance with the CNMI-PR. The Managing Director also stated that the existing CNMI-PR needs revision to include provisions important to MVA in order to compliment the procurement requirements of foreign countries. The Managing Director further stated that it appears that the CNMI-PR was tailored to accommodate procurement practices within and among U.S. states and territories only and does not provide flexibility to accommodate foreign procurement practices and standards. According to her, the MVA has a unique situation different from other government agencies because it deals regularly with foreign countries in terms of money exchange, office leases, representation, marketing and promotional activities.

OPA Comments

Under the new legislation (Public Law 11-15), MVA was authorized to adopt its own procurement and supply regulations “consistent” with the CNMI-PR. This means that MVA can adopt its own procurement regulations as long as these are **similar or identical** to the CNMI-PR. Therefore, the provisions of the regulations cannot be revised or changed to reflect different or additional methods of procurement. There is no significant “difference” between adopting the CNMI-PR and adopting regulations “consistent” with the CNMI-PR except that in the latter, designated MVB officials will handle all procurement functions previously handled by the P&S Division. The procurement methods stated in the CNMI-PR, however, should be retained.

As previously discussed, promotion and advertising contracts can be procured under the competitive sealed proposal method (CNMI-PR Section 3-106). There is no need for new procurement methods that will accommodate questionable foreign procurement practices. In light of the new legislation, however, we are revising our recommendation that MVA adopt the CNMI-PR. Instead, we recommend that MVA adopt its own procurement regulations consistent with the CNMI-PR.

Recommendation 6

The Managing Director stated that MVA will arrange with the P&S Division to conduct future CNMI-PR familiarization workshop to the MVA Board and management.

OPA Comments

MVA should provide a time frame for completing the workshop and provide copies of written requests or arrangements made with the P&S Division.

Recommendation 7

The Managing Director stated that presently, MVA has a paper trail which can trace the execution of a contract, performance monitoring, and payments to the contracts. However, this paper trail can be further improved with a file system as recommended.

OPA Comments

MVA should provide a time frame for improving the filing system. Once completed, a copy of written policies and procedures describing the agency's filing system should be submitted to OPA. As discussed in the audit, there was no systematic or centralized filing system for contract documents. Most of the documents we gathered in reviewing a particular contract came from different sections of MVA.

Status of Recommendations

Based on the Governor and MVA responses, we consider all recommendations open. The additional information or actions required to close the recommendations are presented in Appendix C.



COMMONWEALTH OF THE NORTHERN MARIANA ISLANDS

Pedro P. Tenorio
Governor
Jesus R. Sablan
Lt. Governor

MAY 20 1998



Leo L. LaMotte
Public Auditor
P.O. Box 1399
Saipan, MP 96950

Dear Mr. LaMotte:

Re: Draft Audit Report on the Audit of Promotion and
Advertising Services Procured by Marianas Visitors Bureau (MVB)

Thank you for providing my office with a copy of the draft audit report referenced above. We have reviewed the report and recognize that it raises serious concerns.

I believe that it is premature, however, to make any decisions on the recommendations that you have made regarding action by this office. It is important that the response of MVB, the agency being audited, be obtained as provided in 1 CMC § 7823(a), and considered by your office, before a decision is made whether to take disciplinary action against officials or contractors and what the nature of any such action should be. Such decisions should only be based upon your final analysis after consideration of the agency response.

We have no additional knowledge to offer concerning the facts surrounding the MVB transactions that are the subject of the report. However, we appreciate your giving us the opportunity to comment.

Sincerely,

PEDRO P. TENORIO



June 18, 1998

664-3200
 664-3200-1
 664-3237
 664-3237

Mr. Leo Lawrence LaMotte
 Public Auditor
 Public Auditor's Office
 P.O. Box 1399
 Saipan, MP 96950
 Sent Via Fax: 234-7812

Pages: 5 total

RE: MVB's Response to Draft Audit of Promotion and Advertising Services Procured by the Marianas Visitors Bureau

Hafa Adai Mr. LaMotte:

Thank you for granting our request for extension in preparing our response to your draft audit report on our procurement of promotion and advertising services.

We are pleased to provide you with the attached response to the report. The response is drafted to address the seven recommendations and conclusions of the report. We hope that this information will help to clarify some of the findings of the report.

Thank you for your understanding. Please do not hesitate to contact me at 664-3240 if you should have any questions.

Olomwaay,

Anicia Q. Tomokane
 Managing Director

cc: Board of Directors
 File

MVB Response to Audit of Promotion and Advertising Services
By the Office of the Public Auditor

1. The present management and Board of Directors cannot offer recommendation action(s) relative to decisions made and actions taken in the past by the previous management and Board of Directors of Marianas Visitors Bureau. We would leave this discretion to the Office of the Public Auditor and the Attorney General's office. One particular matter, however, needs to be considered with respect to the controversial issue of the advertising agency (I &S) in Japan. The MVB board chose to renew the contract of I & S after preliminary reviews were made of its previous advertising performance for MVB and other evaluation means. A contract was prepared and signed by all parties with the exception of the former governor, Froilan C. Tenorio. The former governor, titular head of the CNMI, verbally assured the MVB board chairman, Antonio S. Guerrero and member, Frederico Dela Cruz months before the gubernatorial election in two official meetings, that he will sign the contract right after the election. Unfortunately, the promise was not kept and this led to the much publicized, controversial and sensationalized violation of procurement regulation. It is universally acceptable in societies that when the head of State and similar titular persons make commitments verbal or otherwise, their word of assurance and promise is almost as good as the full faith and credit guarantee of the government towards a public debt. In our local culture, the verbal assurance of a chief or a governor has a greater meaning than in most western societies. Because traditionally, our ancestors relied not on written documents to announce approval of decisions and transactions but through oral announcements. Tribal chiefs made oral proclamations and they became the law of the land. This tradition still lives within many of us and we rely to a great degree on the word of a titular head person. The fact that a contract was prepared only after the Board of Directors

contract was prepared only after the Board of Directors officially awarded I & S at a meeting via the renewal process and the document was declared legally sufficient and fund availability was certified gives it more reason to assume that management and the Board acted in good faith to follow prescribed procedures. This action showed that management has made significant efforts and sincere attempts towards improving the Bureau's selection and awarding process if one would compare this action with previous management and Board practices.

To further show support of the advertising agency's product, "Blue, Blue, Blue" the former governor asked that this advertisement be used to promote the CNMI in the CNN international news program. We believe that the MVB management made significant improvements in the selection and awarding of MVB projects. The prescribed processes have been adhered to in most cases and can be attested by the most current favorable financial audit report of MVB by Burger and Comer, P.C.

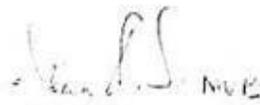
2. The contracts for Korea and Taiwan were bid out and an award was made for the Korea office. The Taiwan office was allowed (again by the Board of Directors) to operate on a month to month basis until a better qualified contractor is selected following a critical review of the first group of proposals received. An RFP process was done the second time. The idea to allow these two offices to operate pending an approved 12 month contract was to provide continuity of promotion and marketing activities without interruption. The intent is good. It served the interest of MVB's promotion efforts of our islands and benefitted the people of the CNMI.
3. To impose suspension of one year on the non-U.S. advertising companies should be reconsidered. If decisions by the

companies to commit their services to MVB were based on other forms than a standard executed contract/lease and such instruments are acceptable in Japan, Korea and Taiwan, then the advertising companies should not be penalized for “violation of the CNMI-PR.” As an alternative, these companies should, in the future, be allowed to be thoroughly familiar with the CNMI-PR before an award of a project is made following a competitive bidding process. We should write the RFP specifications so detailed that these alone might cause companies to “self exclude” themselves from the process.

4. There are existing written criteria for selecting a contractor for facility, equipment purchase and service projects. The latter, however, does not include the services of an advertising company although price is always a consideration and the qualifications of the company. In the future, a standard rating criteria (written) must be established for selecting advertising and promotion contractors. It will be in general compliance with the CNMI-PR. In addition, the Office of the Public Auditor should be included in helping draft the criteria so that it is fully aware of the needs of the Bureau.
5. MVB will, under the new legislation, devise its own procurement regulations which will be in general compliance with the CNMI-PR. The existing CNMI-PR needs revision however to include provisions that are critically important to MVB in order to compliment the procurement of services requirements of foreign countries which may not be in agreement with U.S. procurement laws. It appears that the CNMI-PR was tailored to accommodate procurement practices within and amongst U.S. states and territories only with applicable U.S. procurement restriction standards. It does not provide enough flexibility to accommodate foreign procurement practices and standards. The Bureau has a unique situation different from most government departments and agencies in

that it deals regularly with Japan, Korea, Taiwan and even Russia in terms of money exchange, office leases, CNMI representation, manpower recruitment, and marketing/promotion activities.

6. MVB will arrange with the Division of Procurement and Supply for the latter to conduct future CNMI-PR familiarization workshop for the Bureau's Board and management.
7. Presently, the Bureau has a paper trail which can trace the execution of a contract/lease, performance monitoring, and payments to the contracts. However, this paper trail can be further improved into a file system as recommended which provides easy access to the information for review.


6-18-75

Appendix C
Page 1 of 4

STATUS OF RECOMMENDATIONS

Recommendations	Agency to Act	Status	Agency Response/ Additional Information or Action Required
<p>1. The Governor and the Attorney General's Office consider taking appropriate action against current and previous MVA officials, including the MVA Board Chairman and Managing Director, for violation of the CNMI-PR. Such action includes but is not limited to reprimand, suspension without pay, termination of employment, civil injunction, civil suit for damages or return of government money, or criminal prosecution [CNMI-PR Section 6-211 (1)]. At the least, reprimand letters should be issued and permanently filed in their personnel folders.</p>	<p>GOV and AGO</p>	<p>Open</p>	<p>The Governor responded that it is premature to make any decisions on the recommendations. He added that it is important that the response of MVA be obtained and be considered before any actions are taken.</p> <p>No response was received from AGO.</p> <p>Although not required, the Managing Director responded that the present management and MVA Board cannot offer recommendations relative to decisions made by the previous management and board members.</p> <p>OPA Comment</p> <p>MVA's response, through the Managing Director, did not contain any additional information that could revise our recommendation. The Governor and AGO should reconsider and implement the recommendation.</p>
<p>2. The Governor instruct MVA to cancel the proposed contracts with the 3 advertising companies for violation of the CNMI-PR. This recommendation is based on the fact that even if these proposed contracts were to be approved, they would still be in violation of the regulations. In such case, the contractor would be subject to the remedies under CNMI-PR Section 6-211(2) which include termination of the contract. If the contractors assert any liability against MVA, we recommend that the Attorney General's Office consider whether it is appropriate to file a cross claim against MVA officials and employees who were responsible for the violations discussed in this report.</p>	<p>GOV and AGO</p>	<p>Open</p>	<p>See Governor's response on Recommendation 1.</p> <p>No response was received from AGO.</p> <p>Although not required, the Managing Director responded that 2 of the 3 contracts were bidded out. An award was made for one contract while the other contract was allowed by the Board to operate on a monthly basis until a qualified contractor is selected.</p> <p>OPA Comment</p> <p>Solicitation of proposals is not enough. Selection should be based on the responsiveness of the proposals to the RFP requirements. Awarding of contracts by appointment or majority vote of the Board is not only illegal but defeats the purpose of competitive procurement.</p> <p>MVA's response, through the Managing Director, did not contain any additional information that could revise our recommendation. The Governor and the AGO should reconsider and implement the recommendation.</p>

STATUS OF RECOMMENDATIONS

Recommendations	Agency to Act	Status	Agency Response/ Additional Information or Action Required
<p>3. P&S Director suspend the 9 advertising companies from becoming contractors or subcontractors on future government contracts for at least a year or such other period of time as deemed sufficient by the Director. The suspensions should be communicated to the companies to emphasize that they need to comply with the CNMI-PR when dealing with government agencies.</p>	<p>P&S</p>	<p>Open</p>	<p>No response was received from the P&S Director.</p> <p>Although not required, the Managing Director responded that the suspension should be reconsidered because the 9 advertising companies were not familiar with the CNMI-PR.</p> <p>OPA Comment</p> <p>All companies transacting with CNMI government agencies should be familiar with the CNMI-PR without exceptions. Suspension of the 9 companies (for a limited period as determined by the P&S Director) will put them on notice that the CNMI-PR should be observed and followed in their dealings with the government.</p> <p>The P&S Director should reconsider and implement the recommendations.</p>
<p>4. The Board Chairman and the Managing Director ensure that all procurement of promotion and advertising services be procured competitively, in accordance with the CNMI-PR. To this end, both officials should ensure that all procurement conducted through the RFP process be awarded based on price and other evaluation factors stated in the RFP and not through appointment or majority vote of the Board.</p>	<p>MVA</p>	<p>Open</p>	<p>The Managing Director responded that there are existing criteria for selecting a contractor for facility, equipment purchase and service projects. These criteria, however, does not include the services of an advertising company although price and qualification is always a consideration. The MVA Managing Director further stated that, in the future, a standard written criteria must be established for selecting advertising and promotion contractors that will be in general compliance with the CNMI-PR. According to her, OPA should be included in drafting the criteria.</p> <p>OPA Comment</p> <p>The Managing Director's response did not address the recommendation. As discussed in the report, for procurement of promotion and advertising services where bidding is impractical, the preferred method should be "competitive sealed proposals" under CNMI-PR Section 3-106.</p> <p>The Managing Director should reconsider and implement the recommendation.</p>

STATUS OF RECOMMENDATIONS

Recommendations	Agency to Act	Status	Agency Response/ Additional Information or Action Required
<p>5. The Managing Director take steps for MVA to adopt the CNMI-PR. Identical regulations need to be adopted to enable MVA to continue to conduct its own procurement functions.</p>	<p>MVA</p>	<p>Open</p>	<p>The Managing Director responded that, under the new legislation (Public Law 11-15), MVA will devise its own procurement regulations which will be in general compliance with the CNMI-PR. The MVA Managing Director also stated that the existing CNMI-PR needs revision to include provisions important to MVA in order to compliment the procurement requirements of foreign countries.</p> <p>OPA Comment</p> <p>Under the new legislation (Public Law 11-15), MVA was authorized to adopt its own procurement and supply regulations "consistent" with the CNMI-PR. This means that MVA can adopt its own procurement regulations as long as these are similar or identical to the CNMI-PR. There is no significant "difference" between adopting the CNMI-PR and adopting regulations "consistent" with the CNMI-PR except that in the latter, designated MVB officials will handle all procurement functions previously handled by the P&S Division. The procurement methods stated in the CNMI-PR, however, should be retained.</p> <p>As discussed in the report, promotion and advertising contracts from foreign companies can be procured under the competitive sealed proposal method (CNMI-PR Section 3-106). There is no need for new procurement methods that will accommodate questionable foreign procurement practices.</p> <p>In light of the new legislation, however, we are revising our recommendation that MVA adopt the CNMI-PR. Instead, we recommend that MVA adopt its own procurement regulations consistent with the CNMI-PR.</p>
<p>6. The Managing Director, MVA Board members and procurement officials should familiarize themselves with the CNMI-PR. They should both review the CNMI-PR and request the P&S Director to provide explanation to parts they don't understand. MVA employees involved in the procurement of goods and services</p>	<p>MVA</p>	<p>Open</p>	<p>The Managing Director stated that MVA will arrange with the P&S Division to conduct future CNMI-PR familiarization workshop to the MVA Board and management.</p> <p>OPA Comment</p>

STATUS OF RECOMMENDATIONS

Recommendations	Agency to Act	Status	Agency Response/ Additional Information or Action Required
<p>should be required to be familiar with the details of the regulations.</p>			<p>MVA should provide a time frame for completing the workshop and provide copies of written requests or arrangements made with the P&S Division.</p>
<p>7. The Managing Director establish a filing system that can provide a complete history of the transactions with each individual contractor. Contract files generally consist of (1) contracting files which document the basis for acquisition and the award of the contract, (2) contract administration files which document actions taken to monitor contractor performance and compliance with the scope of work, and (3) payment contract files which document actions substantiating and reflecting contract payments.</p>	<p>MVA</p>	<p>Open</p>	<p>The Managing Director stated that presently, MVA has a paper trail which can trace the execution of a contract, performance monitoring, and payments to the contracts. However, this paper trail can be further improved with a file system as recommended.</p> <p>OPA Comment</p> <p>MVA should provide a time frame for improving the filing system. Once completed, a copy of written policies and procedures describing the agency's filing system should be submitted to OPA. As discussed in the audit, there was no systematic or centralized filing system for contract documents. Most of the documents we gathered in reviewing a particular contract came from different sections of MVA.</p>