Management Audit of the Department of Education's Storeroom

A Report to the Governor and the Legislature of the State of Hawaii

Report No. 02-02
January 2002

THE AUDITOR
STATE OF HAWAII

Office of the Auditor

The missions of the Office of the Auditor are assigned by the Hawaii State Constitution (Article VII, Section 10). The primary mission is to conduct post audits of the transactions, accounts, programs, and performance of public agencies. A supplemental mission is to conduct such other investigations and prepare such additional reports as may be directed by the Legislature.

Under its assigned missions, the office conducts the following types of examinations:

1. *Financial audits* attest to the fairness of the financial statements of agencies. They examine the adequacy of the financial records and accounting and internal controls, and they determine the legality and propriety of expenditures.

2. *Management audits*, which are also referred to as *performance audits*, examine the effectiveness of programs or the efficiency of agencies or both. These audits are also called *program audits*, when they focus on whether programs are attaining the objectives and results expected of them, and *operations audits*, when they examine how well agencies are organized and managed and how efficiently they acquire and utilize resources.

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

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

5. *Health insurance analyses* examine bills that propose to mandate certain health insurance benefits. Such bills cannot be enacted unless they are referred to the Office of the Auditor for an assessment of the social and financial impact of the proposed measure.

6. *Analyses of proposed special funds* and existing *trust and revolving funds* determine if proposals to establish these funds are existing funds meet legislative criteria.

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

8. *Fiscal accountability reports* analyze expenditures by the state Department of Education in various areas.

9. *Special studies* respond to requests from both houses of the Legislature. The studies usually address specific problems for which the Legislature is seeking solutions.

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

THE AUDITOR
STATE OF HAWAII
Kekuanaoʻa Building
465 S. King Street, Room 500
Honolulu, Hawaii 96813

OVERVIEW

Management Audit of the Department of Education's Storeroom

Report No. 02-02, January 2002

Summary

To reduce costs for its 260 - plus public schools, the Department of Education created a central storeroom some 30 years ago to purchase educational, office, and custodial supplies in bulk. The storeroom then sells these supplies to public schools at cost plus an 8 percent markup for delivery charges.

The department's poor management of its storeroom has been a long recognized problem. In our 1996 *Financial Audit of the Public School System*, Report No. 96-8, we noted that the storeroom's practice of unwarranted, excessive ordering resulted in obsolete inventory costs. We found that the storeroom's inventory was sufficient for one to three years, and in a specific example, reported the purchase of 48,000 scissors without justification.

In our present audit, we found no appreciable improvement. Overall, we found that the storeroom increases the schools' workload, wastes taxpayers' money, and is no longer an efficient means to purchase and distribute school supplies. The lack of inventory management, an onerous procurement system, slow distribution of educational supplies, high operational costs, antiquated operations, and mismanagement have resulted in the squandering of state resources. These deficiencies underscore our belief that the central storeroom is a "dinosaur" that is no longer needed and should be eliminated.

More specifically, we found that inept inventory management has resulted in excessive inventory balances. We analyzed 35 supply items in the warehouse and found that based on their demand, the department was storing, on average, over two years' worth of supplies. In the case of three items, the storeroom had over five years' worth of inventory. Another supply item was last purchased in 1990 and the department has enough inventory to fill orders for 12 more years.

Internal controls over inventory are non-existent. The storeroom's inventory records are inaccurate. Our November 2001 test count of 18 items, about four months after the last physical inventory was conducted by storeroom staff, found that 212 water hoses and 19 cases of computer paper were unaccounted for. The storeroom simply displaces perpetual inventory records when physical inventory counts do not match.

Furthermore, the storeroom's practice of purchasing supplies in excessive quantities results in large amounts of inventory susceptible to damage, spoilage, theft, and obsolescence. We found about $10,000 worth of obsolete student progress report cards being shredded to make packing materials. We also found that 166 U.S. flags purchased in 1993 were disposed of in 2001 because they were eaten by termites and deemed worthless.

Supplies of poor quality are sold to the public schools. Our review of the storeroom's files and interviews with public school officials disclosed numerous complaints about the storeroom's sale of defective and spoiled supplies.

In addition, the department has more warehouse space than necessary, currently paying $250,000 a year for approximately 23,000 square feet. Besides storing excessive quantities of supplies and obsolete and damaged items, the department is storing its old files as well.

The delivery of educational supplies is inefficient and creates more work for the schools. The storeroom takes an average of four weeks to deliver supplies to schools on Oahu and six to eight weeks for neighbor island schools. Also, the storeroom requires schools to place a minimum order and to consolidate their orders by specific supply item. If the order does not meet the required minimum, there is an additional charge to the school. Supplies are unloaded within 25 feet of the truck's tailgate to avoid additional delivery charges. This means personnel at some schools must move as many as 12 pallets of supplies to the desired locations on the campus.

We also found that the appropriate skills, knowledge, and background of the key personnel responsible for managing the central storeroom are questionable. For example, the supervising storekeeper acknowledged (1) that the purchase of over 2,700 water hoses, of which 212 were missing, was a mistake and (2) that the storeroom would have difficulty in selling all the water hoses that were ordered. The storeroom personnel's limited experience and knowledge of proper storeroom functions may have contributed to poor storeroom operations and wasted taxpayers' money.

Finally, the department's storeroom revolving fund does not meet the intent and purpose of a revolving fund. Section 23-11, HRS, stipulates that a revolving fund must be self-sustaining. All costs, including personnel salaries and wages, employee fringe benefits, and lease payments, must be considered in determining the self-sustainability of a fund. For the storeroom revolving fund, if all costs are considered for the period July 1, 1997 to June 30, 2001, there was a net loss of approximately $1.6 million.

Recommendations and Response

We recommended that the Legislature repeal Section 302A-1304, HRS, which required the department to establish the central storeroom and created the storeroom revolving fund. We also recommended that the board and the department eliminate the central storeroom.

The department agreed with our findings and recommendations. The department noted that it is in the process of implementing our recommendations.

Marion M. Higa
State Auditor
State of Hawaii

Office of the Auditor
465 South King Street, Room 500
Honolulu, Hawaii 96813
(808) 587-0800
FAX (808) 587-0830

Management Audit of the Department of Education's Storeroom

A Report to the Governor and the Legislature of the State of Hawaii

Submitted by

THE AUDITOR
STATE OF HAWAII

Report No. 02-02
January 2002

Foreword

This is a report of our audit of the Department of Education's management of its central storeroom. The audit was conducted pursuant to Section 23-4, Hawaii Revised Statutes, which requires the State Auditor to conduct postaudits of all departments, offices, and agencies of the State and its political subdivisions.

We wish to express our appreciation for the cooperation and assistance extended to us by the Department of Education, the Board of Education, and others whom we contacted during the course of the audit.

Marion M. Higa
State Auditor

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Chapter 1
Introduction

The Department of Education is responsible for a statewide public school system offering educational programs and services to over 180,000 students in over 260 public schools. To reduce the cost of educational supplies for the public schools, the department created a central storeroom to purchase educational, office, and custodial supplies in bulk. The storeroom then sells these supplies to public schools at cost plus an eight percent markup for delivery charges.

To assess the management and use of the central storeroom in fulfilling its purpose, the State Auditor initiated this audit pursuant to Section 23-4, Hawaii Revised Statutes (HRS). This section requires the Office of the Auditor to conduct postaudits of the transactions, accounts, programs, and performance of all departments, offices, and agencies of the State and its political subdivisions.

Background of the Department of Education's Central Storeroom

The department's storeroom has been operating as the public school system's central purchasing center for approximately 30 years. According to Section 302A-1304, HRS, the Department of Education is required to establish a storeroom to provide schools with a source for commonly used educational, office, and custodial supplies. Prior to 1990, the department operated the storeroom with general fund moneys. Act 93, Session Laws of Hawaii (SLH) 1990, created the storeroom revolving fund and required the department to establish a central storeroom. Since then, the Legislature has authorized $2 million a year to the storeroom revolving fund for educational supplies.

In 1993, the department relocated the central storeroom from Honolulu's Mapunapuna area to its current location at the Waipahu Industrial Park. The storeroom leases approximately 23,000 square feet of warehouse space for about $250,000 a year.

The storeroom's mission and organizational structure

Within the Department of Education, the Procurement & Distribution Section under the Business Services Branch oversees the central storeroom, which procures and warehouses commonly used office, art, audio-visual, and custodial supplies, as well as paper, educational forms, and sports supplies. The section is responsible for the procurement of educational supplies, receipt, storage, and shipment of goods, inventory control, invoicing, receipt of payments, and follow-up of outstanding accounts receivable. A procurement and distribution specialist manages the Procurement & Distribution Section and is responsible for directing

the staff on storeroom operations, reviewing and approving any changes in storeroom supplies, and overseeing expenditures of storeroom funds.

The supervising storekeeper reports to the procurement and distribution specialist and is responsible for overseeing the day-to-day storeroom operations. The supervising storekeeper's responsibilities include determining order requirements, inventory management, maintaining the inventory database and records, maintaining the accounts receivable file, supervising the annual physical inventory and the receipt of goods, and planning deliveries to schools.

Four full-time workers (one storekeeper, two store clerks, one warehouse worker) and two part-time student helpers assist the supervising storekeeper. The storeroom also receives assistance from cafeteria workers and additional student helpers during the summer months to help fill the supply orders for the next school year. Exhibit 1.1 shows the organizational structure of the central storeroom.

Purchasing of educational supplies

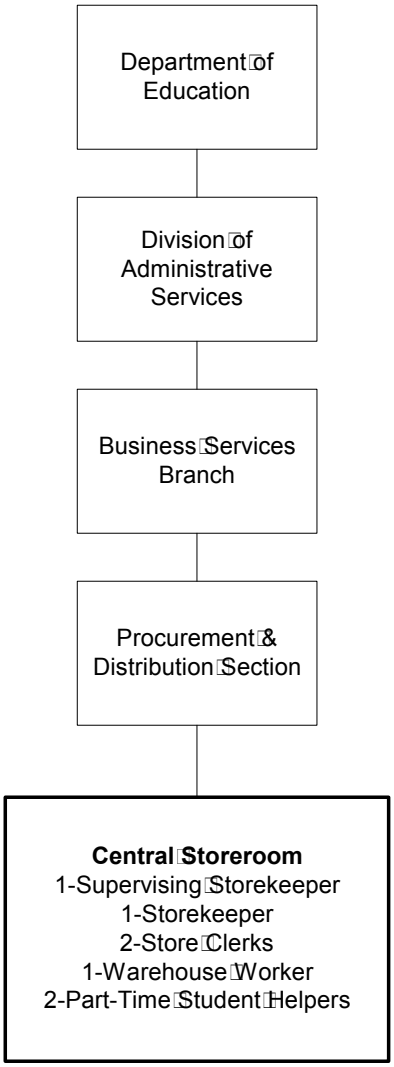
The storeroom is one of three methods for schools to purchase educational supplies. The other two are the State's mandatory price lists and commercial vendors. If the educational supply item is on the storeroom price list, the schools are required to purchase the item from the storeroom. If the supply item is not on the storeroom price list, the schools then check the mandatory price lists. If the item is on one of the mandatory price lists, the schools must purchase the supply from this list. If the item is not on any list, the schools can purchase the supply directly from any commercial vendor. The schools pay for all supplies through purchase orders that are electronically processed through the department's Financial Management System (FMS).

The storeroom revolving fund and its financial activities

A *revolving fund*, as defined in Section 37-62, HRS, is a fund that recognizes revenues and expenditures for goods and services provided by the fund. A revolving fund should exist for a specific purpose, and there should be a clear link between the benefits sought and charges made to the users or beneficiaries of the program. All costs should be included, such as personnel salaries and wages, employee fringe benefits, lease payments, supplies, materials, equipment, and motor vehicles.

The charges that schools pay for storeroom supplies are revenues to the storeroom revolving fund, created by Section 302A-1304, HRS. The expenditures of the storeroom revolving fund include supplies and the equipment and services needed to operate the storeroom. Any balance in excess of $400,000 at the end of the fiscal year must be lapsed to the State's general fund.

Exhibit 1.1
Organizational Chart of the Central Storeroom



Source: Department of Education

Our *Review of Revolving and Trust Funds of the Office of the Governor, Office of Hawaiian Affairs, and the Department of Education*, Report No. 96-21, as required by Section 23-12, HRS, found that the storeroom revolving fund was not self-sustaining. Although the storeroom revolving fund met most of the criteria of a revolving fund, we reported that general fund moneys paid for personnel salaries and all operating costs of the storeroom. Therefore, the fund was not self-sustaining and did not meet this criterion of a revolving fund.

In our *Financial Audit of the Public School System*, Report No. 96-8, we noted that the department's purchase commitments at fiscal year-end substantially reduced the ending fund balance, thereby decreasing the amount subject to lapse into the general fund. The report further stated that with smaller year-end purchase commitments, the department could have lapsed more moneys into the general fund. In fact, the department may have circumvented lapsing requirements by ordering more supplies than needed.

Our previous audit found flaws in storeroom practices

We also noted in our 1996 *Financial Audit of the Public School System*, Report No. 96-8, that the storeroom's practice of unwarranted, excessive ordering resulted in obsolete inventory costs. As a result of purchases and future commitments, the storeroom's inventory was sufficient for one to three years.

An example of excessive ordering was the purchase of approximately 48,000 scissors without any needs survey or justification of demand. Another example of the storeroom's practice of "loading up" on its inventory resulted in obsolescence costs of about $35,600 for 6,467 packages of thermal facsimile paper. We also reported that the lease cost for an unreasonably large warehouse to house excess and obsolete inventory was a waste of public funds.

We recommended that the department reduce its storeroom inventory, maintain inventory levels sufficient to meet a few months' demand, and consider leasing a smaller warehouse. In response to our recommendations, the department reported that it generally defended its inventory practices, but would re-evaluate inventory levels to determine if they could be reduced.

The findings from our past audits, in addition to teachers' complaints regarding the poor quality of supplies and service from the central storeroom, prompted the Office of the Auditor to initiate this audit.

Objectives of the Audit

1. Assess the efficiency and effectiveness of the management of the Department of Education's central storeroom in meeting the needs of the schools.

2. Assess whether the storeroom revolving fund meets statutory and other applicable criteria.

3. Make recommendations as appropriate.

Scope and Methodology

This audit focused primarily on the management practices of the central storeroom of the Department of Education for FY2000-01, including an assessment of the efficiency and effectiveness of overall storeroom operations and inventory and warehouse management. We also evaluated the storeroom revolving fund's ability to meet established statutory criteria.

We collected information through interviews, observations, document review, and testing at the storeroom. We also obtained input from schools on the quality of supplies and services received. We visited and contacted commercial vendors of storeroom supplies to obtain their feedback on the storeroom's operations.

We assessed whether the storeroom's delivery of educational supplies to the schools is timely and whether the supplies delivered are of a high quality at the lowest possible costs. We also examined the types of inventory items carried by the storeroom, price list violations, and price list exceptions to determine the quality of products and services offered by the storeroom. We reviewed the physical inventory procedures and reviewed inventory records to determine whether the storeroom has established sufficient internal controls to ensure that its inventory is properly safeguarded and accurately accounted for.

Sound management techniques and applicable laws and regulations issued by the United States General Accounting Office were used to determine the cost effectiveness of the storeroom. We also evaluated the storeroom's performance against national and Hawaii vendors' standards by using such measurements as inventory turnover rate. Finally, we followed up on the excess and/or obsolete inventory items identified by our 1996 audit to determine whether the department has improved the storeroom operations.

Our work was performed from May 2001 to December 2001 in accordance with generally accepted government auditing standards.

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Chapter 2

The Department of Education Storeroom Is a Dinosaur Wasting State Resources

This chapter presents the findings and recommendations of our assessment of the Department of Education's storeroom in meeting the needs of the public school system. The central storeroom purchases approximately $2 million of educational supplies annually. For about 30 years, the storeroom has purchased these supplies in bulk at discounted prices and sold them to the public schools for purposes of reducing the costs of education. To achieve cost savings, the department must apply sound management practices to ensure that public resources are efficiently and effectively used.

However, we found that the central storeroom increases the public schools' workload, wastes taxpayers' money, and is no longer an efficient means to purchase and distribute school supplies. The lack of inventory management, an onerous procurement system, slow distribution of educational supplies, high operational costs, antiquated operations, and mismanagement have resulted in the squandering of state resources. These deficiencies underscore our belief that the outmoded central storeroom is no longer needed and should be closed.

Summary of Findings

1. The Department of Education's storeroom wastes schools' time and taxpayers' money.

2. The storeroom revolving fund does not operate as a true revolving fund and instead merely serves to perpetuate an obsolete operation.

The Department of Education's Storeroom Wastes Schools' Time and Taxpayers' Money

The Department of Education's storeroom is obsolete, mismanaged, costly, unnecessary, and a burden to the public schools. Poor inventory management, an untimely distribution system, onerous procurement procedures, and antiquated operating techniques all contribute to the inefficient and ineffective operations of the storeroom. As a result of these problems, the central storeroom creates more work for the department and schools, wastes the department's money, and provides supplies of poor quality to the department and schools. We also found the sales of educational supplies to non-public schools and the qualifications of the storeroom personnel were questionable. Unable to compete with commercial vendors' superior services, the storeroom's operations are no longer cost efficient.

Inept inventory management wastes taxpayer money

Department officials report that their experience and judgment suffice to determine the type and amount of supplies that are needed to support the public schools. This outmoded method of inventory planning results in thousands of dollars of wasted taxpayers' money due to excessive purchasing of educational supplies. The excessive inventory has led to obsolete, damaged, missing, and spoiled supplies. Inventory records are not properly maintained; physical inventory counts are not reconciled to the perpetual inventory; and inventory counts are inaccurate when compared to the perpetual inventory. The lack of inventory controls provides no assurance that supplies are properly safeguarded and accounted for. We also found that the leased warehouse for storage of educational supplies is larger than necessary. These inept inventory practices have resulted in educational supplies of poor quality being delivered to the public schools.

Inadequate planning results in overstocked inventory

Our review of the storeroom's supply records found that the department failed to apply sound inventory planning techniques, resulting in more supplies than needed. Proper inventory planning is essential to ensure that the appropriate types and quantities of inventory are readily available. We found that storeroom personnel relied upon their past experiences and judgment to determine the amount and type of supplies needed for public schools. This subjective, non-systematic method of determining what supplies to order and how much to order has resulted in excess inventory that is susceptible to obsolescence, damage, shrinkage, and spoilage.

The department does not use analytical tools for inventory planning. One such tool is the *inventory turnover ratio*, by which the department could have determined whether excessive inventory was present. *Inventory turnover* is commonly used to measure how quickly inventory is sold. Generally, the higher the inventory turnover rate, the better the organization is performing. In Hawaii, the storeroom's own major vendors of educational supplies reported an average inventory turnover of about six to seven times per year. The storeroom's 35 supply items we evaluated fell far short of this mark. The turnover rate was only 0.87 times per year.

The department has excessive inventory on hand. We analyzed 35 supply items stored in the storeroom's warehouse at the end of FY2000-01 and found that based on their demand, the department was storing, on the average, over two years' worth of supplies. In the case of three items, the storeroom had over five years' worth of inventory.

In another assessment, we found a supply item that was last purchased in 1990. Based on the demand for that item in FY2000-01, the department still has available inventory to fill orders for 12 more years, which seems

to be excessive. The department should have reasonably estimated the low demand as well as determined the inventory turnover ratio for this item and purchased only a few months' worth of supplies. The moneys spent on this purchase should have remained in the revolving fund earning interest revenue rather than spent on bulk purchasing in excessive quantities that then sit in storage.

Internal controls over inventory are non-existent

The department lacks internal controls over its inventory. Internal controls ensure that assets are safeguarded against waste, loss, unauthorized use, and theft. A well-maintained perpetual inventory system is a type of internal control. A perpetual inventory system keeps track of the quantity of goods on hand at all times and provides essential information for purchasing and selling goods, including the quantity of goods received and disbursed. The accuracy of these records is periodically tested with a physical inventory count. Without a well-maintained perpetual inventory system and sound record keeping, the department cannot detect waste or theft or insure that assets are protected and moneys are expended properly.

We found that the storeroom's inventory records are inaccurate. In November 2001, about four months after the last physical inventory was conducted by storeroom staff, we performed test counts of 18 items in the storeroom. Balances for the department's perpetual inventory for 13 items or 72.2 percent were either overstated or understated. The test count also found that 212 water hoses and 19 cases of computer paper were unaccounted for. The missing water hoses were packed in over 35 cases and would be impossible to miscount or bypass during a physical inventory. In order to verify that the hoses were actually missing, the count was taken three times with the same results. A comparison of the differences noted between the perpetual inventory records and the physical inventory counts is shown in Exhibit 2.1.

In addition, we found that the department does not reconcile the perpetual inventory records to the physical inventory counts. A sound perpetual inventory system requires periodic verification of stock through a physical counting of the inventory. The reconciliation of these counts can identify errors, waste, loss, or theft of inventory. However, the procurement and distribution specialist and the supervising storekeeper reported that such a reconciliation is not performed. After the physical inventory on June 30, 2001, the storeroom's perpetual inventory records were replaced with the new physical inventory counts. The perpetual inventory counts for the previous fiscal year were eliminated. In response to our inquiry for these eliminated records, the department official reported that they could not be retrieved. The department has no way of knowing whether supplies were properly or improperly accounted for or if supplies were stolen.

Exhibit 2.1
Perpetual Inventory Records Versus Physical Count

Item	Stock #	Perpetual Inventory	Physical Count	Difference
Railroad Board	A755	222	268	46
Scissors, 6"	C621	326	321	-5
Release and Enroll Form	F045	211	211	0
Water Hose	J250	2,279	2,067	-212
Computer Paper	P110	233	214	-19
Laminating Film	C410	1,310	1,846	536
Laminating Film	C413	344	348	4
Laminator	C412	214	214	0
Punch, Paper	C580	116	357	241
Tape, Dispenser	C7151	65	65	0
Can, Rubbish	J020	421	421	0
Pliers	J350	28	27	-1
Wrench, 6"	J410	31	30	-1
Wrench, 8"	J420	8	0	-8
Football	S080	969	968	-1
Ball, Soccer	S035	230	325	95
Ball, Playground	S120	225	224	-1
Ball, Volleyball	S200	202	202	0

The storeroom's perpetual inventory records are inadequate. The department fails to keep records of items written off due to damage, spoilage, shrinkage, or obsolescence. For example, when an educational supply item has been deemed damaged, spoiled, or obsolete and is considered unusable, the storeroom personnel dispose of it by simply discarding the item. However, the number of items that have been discarded and the description of the item are not recorded. Therefore, the storeroom personnel have no knowledge or record of the number or value of supply items that have been disposed. Without these records and inventory reconciliation, it is impossible to determine whether educational supplies are properly safeguarded and not misplaced, improperly disposed, or pilfered.

Resources are squandered on obsolete, damaged, and spoiled inventory

The storeroom's practice of purchasing supplies in excessive quantities results in large amounts of inventory susceptible to damage, spoilage, theft, and obsolescence while in storage. In our previous report, *Financial Audit of the Public School System,* Report No. 96-8, we reported the storeroom's practice of "loading up" on its inventory, resulting in obsolescence costs. Specifically, we reported 6,467 packages of obsolete thermal facsimile paper, costing taxpayers $35,000. We recommended that the department reduce its inventory to a few

months' supply. Although the thermal facsimile paper has since been disposed, our current review of the storeroom's warehouse again found inventory that was obsolete, damaged, or spoiled.

For example, we found about $10,000 worth of obsolete Student Progress Report Cards that were being shredded to make packing materials for the storeroom. These report cards are official documents used solely for elementary schools bearing the signature of the superintendent of education, whereas middle and high schools use an automated system, which does not require the superintendent's signature.

Student Progress Report Cards are sold by the storeroom to the elementary schools in packets of 100 cards at an approximate cost of $8.30 per packet. In November 2001, we found about 1,200 packets of report cards bearing the signatures of the past two superintendents. Exhibit 2.2 shows two of the three pallets of report cards that were stored in the warehouse waiting to be shredded into packing material.

Exhibit 2.2
Obsolete Student Progress Report Cards Pending Shredding Into Packing Material

We also found other instances of spoiled and damaged supplies. During our audit, spoiled and unusable finger paints were being disposed. Although the finger paints had been stored for several years, it was during our audit that department personnel took appropriate action to determine that the paint was, in fact, spoiled and unusable. We also found that 166 U.S. flags purchased in 1993 were disposed of in 2001. These flags, eaten by termites and deemed worthless, had remained on the storeroom's shelves for over eight years. These examples of waste could have been prevented if the department had reduced its inventory. The probability that supplies would become obsolete, damaged, or spoiled could have been reduced, if not eliminated.

Educational supplies of poor quality are sold to public schools

Lack of inventory management has resulted in schools receiving educational supplies of poor quality. In addition, considering only the lowest prices when purchasing supplies can result in poor quality goods. Our review of the storeroom's files and interviews with public school officials disclosed numerous complaints related to the storeroom's sale of defective and spoiled supplies. Exhibit 2.3 lists some of the comments received from schools.

Moneys are wasted on unneeded warehouse storage space

The department has more warehouse space than necessary to store educational supplies required for a school year. Utility, building, and personnel costs for warehouses increase when an excessive amount of inventory is held for a long period of time and/or the warehouse is larger than necessary. Using warehouse space for other than its intended purpose also increases warehouse costs. In our examination of the warehouse, we found large amounts of unused and misused warehouse space.

As previously mentioned in this report, the department's practice of purchasing educational supplies in excessive quantities has resulted in maintaining an inventory that can fill orders for two to three years. The exorbitant purchasing of supplies requires more warehouse space and increases warehouse costs. The department should purchase supplies to fill orders for only a few months' demand and consider leasing a smaller space to reduce costs. Storing obsolete, damaged, and spoiled supplies adds to warehouse costs. Also, the size of the storeroom is much greater than necessary.

The warehouse is being used for other than its intended purpose. Because the central storeroom has excess, unused space, the department's old files are being stored in the warehouse. During our initial tour of the storeroom in June 2001, department officials acknowledged that the space was not being used for its intended purpose

Exhibit 2.3
Comments on the Quality of Educational Supplies

Date	Comments
July 2000	*Watercolor set leaking.*
August 2000	*Punch, paper, multiple hole item is broken.*
August 2000	*We have only 2 reams of* (writing paper)…*which we are asking to be replaced because of very light lines.*
October 2000	*The plug where air is put into the ball came out when the needle was retracted after pumping air into the ball. Plug will not stay in.*
November 2000	*Sharpener, pencil w/adj holes. Sharpener handle will not turn.*
January 2001	*The low fire clay is very poor quality. My students have become frustrated because it cracks so easily. The high fire clay has MOLD all over it. It must be old clay they* (storeroom) *are sending us. I will not use this clay again. It has been a disaster.*
January 2001	*The clay is dated 2/99 and has mold covering each slab of clay in the case. This clay will be used by kindergarten students. Washing the slab does not remove the mold and is not satisfactory for use with kindergarten children.*
January 2001	*She* (teacher) *says 2 out of the twelve* (markers) *wrote dark, the rest were a light pink and hard to see from the back of the classroom. She needs markers that write red, not pink.*
February 2001	*We got 4 staplers but only 1 was broken. Enclosed is the broken stapler for replacement.*
March 2001	*Mop wringer (cracked) to be replaced at next order shipment.*
March 2001	*I only used this* (stapler) *once and it doesn't work! I can't believe it!*
April 2001	*The balls were received damaged, one having a big hole from its creases and the other starting to thin out from the crease.*
August 2001	*Missing air valve, soccer ball.*
August 2001	*Specifically asked for Crayola Watercolors. Prang watercolors tend to be watery with almost no color. Crayola watercolors are more vibrant.*
August 2001	*5 of 6 Marker set rec'd ink dried out after constant writing.*

and that the old files would be transferred back to the respective sections of the department. However, as of November 2001, the department's old files are still being stored in the warehouse.

The department's utilization of warehouse space is inefficient. During our visits to major commercial vendors of educational supplies, we found in contrast that they maximized the use of their warehouse storage space. Unlike the storeroom's many empty shelves, the commercial vendors' shelves were fully utilized and well stocked with merchandise. Exhibit 2.4 shows the storeroom's empty shelves.

Exhibit 2.4
Wasted Warehouse Storage Space

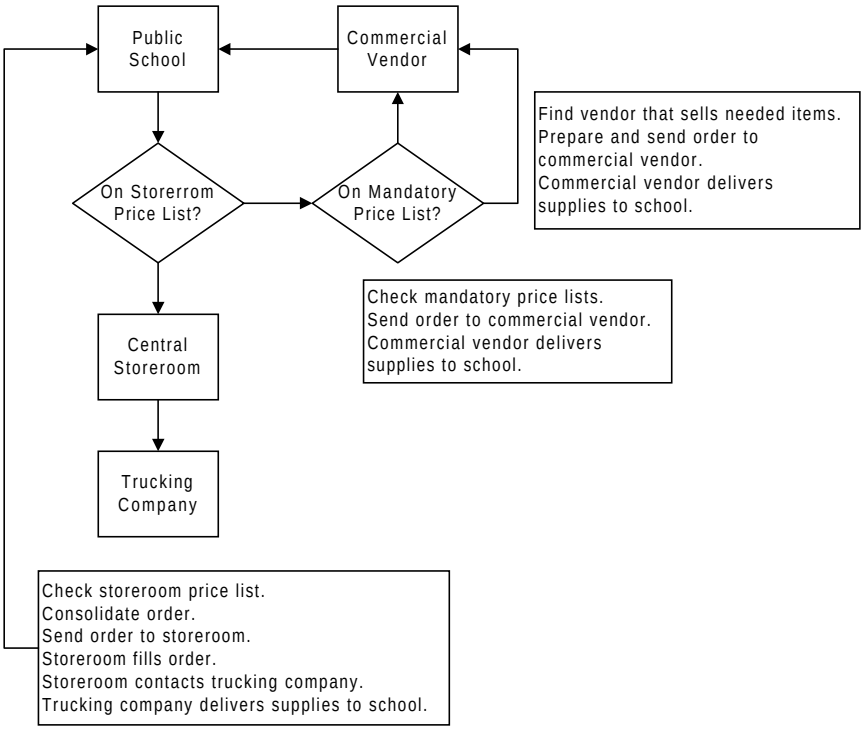
The department's onerous procurement system is inefficient

As previously described, to purchase educational supplies, public schools are required to first use the storeroom price list, then the mandatory state price lists, and finally a commercial vendor. Prior to the beginning of the school year, each school submits an opening order request, the largest purchase of supplies made by the schools for the entire school year. Teachers first submit purchase requests to their respective supervisor, who then consolidates the requests which are forwarded to the school's administration office. The administration office further consolidates the supervisor's requests and submits to the storeroom one purchase order for the entire school. The storeroom then fills the orders and contacts a trucking company to deliver the educational supplies to the schools. Additional supplies are ordered throughout the remaining school year in the same manner, but are generally smaller orders that may be consolidated.

If the storeroom does not have an item needed by a school, the school checks the mandatory price lists for the item. If the item is on a list, a purchase order is prepared and sent to the contracted vendor. The vendor is responsible for filling the order and delivering the supplies to the school.

If the supply is not on the storeroom or mandatory price lists, the school sends the purchase order to any commercial vendor that sells the item and the vendor then delivers the item to the schools. Exhibit 2.5 shows the process public schools must follow in purchasing educational supplies.

Exhibit 2.5
Process for Purchasing Educational Supplies



We found that the department's procurement system for storeroom purchases makes inefficient use of state resources. The *exception to purchase from the storeroom process* wastes time and adds little value to the procurement system. In addition, the *procurement violation process* for small purchases of educational supplies is so heavily bureaucratic that it unfairly increases schools' personnel workload. The state

procurement system for obtaining an *exception to purchase from a price list* and *procurement violation* process is a more practicable option for small purchases.

Obtaining exceptions to purchase from the storeroom is cumbersome

The State Procurement Code's Section 3-121, Hawaii Administrative Rules (HAR), requires the department to develop procedures for purchases from mandatory price lists. To comply with the State's administrative rules, the department also developed a specific procurement process for obtaining exceptions to purchase from the mandatory price lists and from the storeroom price list. Failure to obtain an approved exception results in a procurement violation.

Public schools are required to purchase educational supplies from the storeroom's price list as described previously. When the storeroom price list is not suitable, the schools must submit a Request Exception from Purchasing from Price List form to the Procurement & Distribution Section for approval. The process for requesting an exception to purchase involves the following steps:

- Schools complete the *Request Exception from Purchasing from Price List* form.
- The purchasing specialist at the department's Procurement & Distribution Section reviews the request and recommends approval or disapproval.
- The request is forwarded to the supervisor of the Procurement & Distribution Section for review and approval or disapproval.
- The request is returned to the purchasing specialist who returns the request to the originating school.
- If the request is approved, the school purchases the supplies from a commercial vendor.

However, we found that the procedures for obtaining an exception to purchase from the storeroom price list were ineffective, were burdensome for personnel, and had limited benefits. During FY2000-01, the department received approximately 220 requests for an exception to purchase from the storeroom price list of which we reviewed a sample of 95. The sample exception requests totaled about $9,800 or an average of about $100 for each exception. Of the 95 sampled requests, we found that 36 (37.9 percent) of the requests from the schools were for an amount less than $25. We also found that about 85 percent of the exception requests were approved. Because the majority of exception

requests are approved and the requests are for such small dollar amounts, the review and approval process does not appear to add any value to the procurement system and, in fact, unnecessarily taxes personnel time.

The procurement violation procedure is arduous and unnecessary

The department has developed a cumbersome bureaucratic procurement violation process. Violations, as defined in Section 3-131, HAR, are normally inadvertent and usually result from administrative error, lack of knowledge, or simple carelessness. The section further states that when a purchasing violation occurs, the department will determine whether corrective action is necessary. An example of a violation is a school's failure to purchase a supply that is available from the storeroom and on the storeroom price list.

The department developed an arduous process to address possible procurement violations as follows:

- The department's Vouchering Section of the Business Services Branch periodically audits invoices from commercial vendors for public school purchases of educational supplies.

- If any of the items on the invoices are included on the Storeroom Price List, a Possible Procurement Violation form is sent to the respective school for resolution.

- The school must respond to the following eight questions listed on the Possible Procurement Violation form.

1. What was not done that resulted in this procurement violation?

2. Why did this procurement violation occur?

3. To the administrator/principal: As the delegated authority who must approve all purchases, how would you explain this happening?

4. How can we assist you in preventing a reoccurrence?

5. What steps have you taken to prevent a reoccurrence?

6. Are there any options available to you in dealing with this situation, such as, returning the goods?

7. Are you requesting for (sic) after-the-fact approval (applies to pre/post-audit) and why?

8. Are there any other mitigating factors that you wish to provide for our consideration in this situation?

    - The administrator/principal signs the Possible Procurement Violation form and sends it to the department's Procurement & Distribution Section.

    - The supervisor of the Procurement & Distribution Section reviews the form and recommends approval or disapproval of the violation. The form is then forwarded to the Chief Procurement Officer for approval or disapproval.

    - The Chief Procurement Officer approves or disapproves the violation and returns the form to the Procurement & Distribution Section.

    - The violation form is sent back to the respective school.

    - If the violation is approved, the invoice is processed for payment.

    - The form is finally returned to the Vouchering Section of the department for payment to the vendor.

    - If the violation is denied, the school is responsible for payment.

Through our review of the storeroom's files and interviews conducted with school staff, we noted the following comments from schools questioning the reasonableness of the current procurement violation system:

- *I really think that the time consumed explaining such an insignificant purchase really speaks loudly about our entire procurement and distribution system. But, again, I know we can all justify why we do the things we do.*

- *It takes three months before we get storeroom supplies. Is it possible to get supplies sooner than that. (sic) If we were to go to (sic) outside vendor, we get delivery as soon as they get the purchase order.*

- *DOE storeroom order took 4 months for delivery of supplies.*

- *DOE storeroom item # C2651 comes in packs of 12. Teacher needed only one steno pad.*

- *We ordered three items from a local vendor. Having a $50.00 minimum order is a hardship.*

- *I only needed one sharpie pen and one tape.*

- *DOE storeroom* (sic) *not able to deliver supplies when needed.*

The department's procurement violation procedures are onerous and add little value to the procurement system. When we reviewed a sample of 295 supply items from the Possible Procurement Violation forms for FY2000-01, the review showed that purchasing these items through the department storeroom would have reduced costs for supplies by only $436.87, or an average of $1.48 per item.

We also reviewed a sample of 31 of the 48 Possible Procurement Violation forms for FY2000-01, all of which the chief procurement officer had approved. Of the 16 schools involved in procurement violations, 15 schools identified the storeroom's untimely delivery as the primary reason for the violation.

In addition, we found that purchasing educational supplies through the storeroom can actually cost the public schools more money because the storeroom charges a separate fee for minimum handling and shipping costs. An administrative fee of $10 is assessed on all purchase orders totaling less than $50. In our review of the 31 procurement violations, 10 violations or 32 percent were for purchases of less than $50. If the schools purchased these supplies from the storeroom, they would have been assessed this $10 additional administrative fee. To illustrate: one procurement violation was for purchasing one roll of masking tape from a commercial vendor for $2.99 rather than from the storeroom. However, if the school had purchased the tape from the storeroom, it would have been assessed the $10 administrative fee and the cost for the tape would be $12.99 — over four times as much as the original purchase price.

The State's procurement system is a viable option for purchases

The State has developed a procurement system that is less cumbersome than the Department of Education's system. The State's system for procurement violations combines the procurement violation process with the exception to purchase from the mandatory price lists process. The same exception to purchase from the mandatory price lists process is used to prevent a procurement violation from occurring. This system reflects a more efficient use of personnel time than the department's procurement system.

The state procurement system follows these steps:

- The pre-audit branch of the Department of Accounting and General Service (DAGS) reviews invoices for price list violations.
- If a violation is discovered, a violation form is sent to the agency.
- The agency prepares a *Request for Authorization to Purchase Outside of State Procurement Office Price List* form that provides a justification for the exception request.
- The exception request is signed by the agency's approving authority and sent to the State Procurement Office (SPO).
- The purchasing specialist at SPO recommends approval or disapproval.
- The request form is sent to the assistant procurement officer for approval or disapproval.
- The exception request is sent back to the purchasing specialist.
- The exception request is returned to the agency where the invoice is processed for payment.
- The form is sent to the pre-audit branch for review and payment.

A state procurement official reported that a review was being conducted to determine the efficacy of allowing the agencies' purchasing representatives to approve requests for exception with the intent of further eliminating bureaucratic red tape. A comparison of both the department and state procurement systems for procurement violations is shown in Exhibit 2.6.

Delivery and distribution of supplies is untimely and increases schools' workload

The department's delivery of educational supplies is inefficient and creates more work for the public schools. The purpose of the storeroom is to save money for the department. However, the savings achieved from bulk purchasing does not justify the increased delivery time and personnel workload at the schools. The inability to deliver supplies to a school's storage area and the practice of consolidating purchase orders create more work for school personnel.

The department's delivery of supplies is not timely. It takes an average of one month for the storeroom to deliver supplies to schools on Oahu. For the neighbor islands, the average delivery time is between six weeks

Exhibit 2.6
Comparison of the Department of Education and State Procurement Systems

Category	Department	State
Number of different systems	Two Systems • Violations • Exceptions	One System • Violations integrated with exceptions
Organizations involved in the procurement process	Violations (Four Sections) • Vouchering Section • Public School • Procurement & Distribution Section • Business Services Branch (CPO) Exceptions (Three Sections) • Vouchering Section • Public School • Procurement & Distribution Section	Violations and Exceptions (Three Sections) • Pre-Audit Branch • Agency • State Procurement Office
Justification for violation	Eight Questions 1. What was not done that resulted in this procurement violation? 2. Why did this procurement violation occur? 3. The administrator/principal: As the delegated authority who must approve all purchases, how would you explain this happening? 4. How can we assist you in preventing a reoccurrence? 5. What steps have you taken to prevent a reoccurrence? 6. Are there any options available to you in dealing with this situation, such as, returning the goods? 7. Are you requesting for after-the-fact approval (applies to pre/post-audit) and why? 8. Are there any other mitigating factors that you wish to provide for our consideration in this situation?	One Justification Response • Justification for purchase outside of the price list

to two months. However, these problems are not encountered when schools purchase supplies from commercial vendors. The average delivery time of supplies to schools on Oahu and neighbor islands by commercial vendors is about one week.

For Oahu schools, the storeroom arranges with a trucking company to pick up and deliver pallets of supplies from the storeroom to the schools. Trucking companies' fees, which are regulated by the Public Utility Commission, include delivery costs if the delivery is unloaded within 25 feet of the truck's tailgate, referred to as "tailgate unloading." Therefore, the storeroom hires all delivery trucks to perform "tailgate unloading" to avoid additional charges. For some schools, this is not a problem because their loading and storage areas are within the 25 feet limitation. Unfortunately, this is not true for all schools so their personnel must move as many as 12 pallets of supplies to the proper locations, creating additional work.

In addition, the storeroom's requirement that schools consolidate their opening purchase order creates more work for the schools. Public schools consolidate purchases from the storeroom by specific supply item to reduce the workload of the storeroom personnel. By consolidating supply items for the storeroom, the storeroom has fewer purchase orders to fill; however, the responsibility for separating the delivered order is left with the school. For example, if five teachers order one box of pencils each, the school is required to request five boxes of pencils. The storeroom delivers one shipment of five boxes of pencils, which the school's administration must then physically separate by the respective requestors of the pencils. This creates more work at the school's level. The opening order for the next school year is the largest order placed and some schools receive many pallets of educational supplies in one shipment. School personnel reported that it takes weeks to complete the separation of supplies.

These problems do not exist for purchases from commercial vendors who provide better service to schools island-wide. Commercial vendors deliver supplies within one week, without delivery fees, to the preferred location of the respective school, and do not require schools to consolidate purchase requests by supply item. Thus, commercial vendors provide timely service and considerably reduce the workload of schools.

The storeroom's antiquated operations cannot compete with commercial vendors' services

The storeroom's outdated method of providing services to public schools cannot compete with island-wide commercial vendors who are more efficient. The storeroom was created about 30 years ago when fewer vendors of educational supplies were available. Commercial prices were higher due to the lack of competition. Today, a larger selection of available vendors results in greater competition, improved prices, and an

increased selection and availability of products. Commercial vendors perform the same functions as the department's storeroom, with competitive prices and timelier service.

The technological changes of recent years have revolutionized the commercial retail and distribution industry. In today's marketplace, the concept of *just-in-time inventory* prevails. Just-in-time inventory calls for an organization to purchase supplies at the precise moment when needed with the goal of maintaining a *zero inventory*. The benefits from using just-in-time inventory are: moneys are not tied up in stored inventory and are available for other purposes; the risk of shrinkage, obsolescence, and spoilage is reduced; less storage space is needed; and less money is spent on personnel to maintain unmoving inventory. Supplies gathering dust on warehouse shelves do not constitute zero inventory. When these supplies are so overstocked that they spoil or become damaged or obsolete, they are indications of wasted resources and wasted taxpayers' money. Such inventory does not add value.

Sale of educational supplies to non-public schools is questionable

The Legislature appropriates approximately $2 million of general fund moneys to the storeroom revolving fund with the intention of purchasing educational supplies to support the State's *public* school system each year. However, the department's central storeroom also sells educational supplies to *non-public* schools.

Act 93, SLH 1990, established the storeroom revolving fund, ostensibly to reduce the costs of supplies for the public school system. The department's testimony specifically stated that the purpose of the storeroom revolving fund was to purchase supplies for the *public school* system. However, Section 302A-1304, HRS, says "*schools*" and not "*public schools.*" Despite the generic term, "*schools,*" the legislative intent and purpose refers to public schools. Therefore, the storeroom's sales of educational supplies to non-public schools appear questionable.

We found the following questionable sales to non-public schools:

- The department sells educational forms, art supplies, paper products, and other items to private schools. Private schools are charged an additional fee, equal to 15 percent of the total purchase amount, to reimburse the storeroom for administrative and operating costs.

- The storeroom sold 36 basketballs affixed with Pepsi Cola logos to Pepsi Cola Hawaii. As the storeroom cannot endorse a commercial enterprise by issuing the basketballs to schools, and the company that manufactured and sold the basketballs to the storeroom had gone bankrupt, the storeroom chose to sell the balls to Pepsi Cola Hawaii.

- Educational supplies were sold to the Hawaii Youth Challenge Academy, a Department of Defense school operated by the National Guard. However, costs were handled as though it were a state public school.

These storeroom sales appear to circumvent legislative intent. When we questioned department personnel about the authorization for these sales, they could not provide any justification for their approval. As a result, state moneys intended for public schools are being used to support non-public entities.

Qualifications of storeroom personnel are questionable

The appropriate skills, knowledge, and background of the key personnel responsible for managing the central storeroom are questionable. Effective human resource management requires that job descriptions and classifications be established to identify the education and training needed to perform a particular job. Job requirements delineate the experience, education, training, skills, and abilities needed. Knowledge and background provide the information related to a particular job, while skill is a person's observable capability to perform the job. In selecting personnel for key management positions, the person's skills, knowledge, and background should correspond to the requirements of the job description. However, we found that the selection of individuals for key management positions for the central storeroom is questionable in meeting the above described criteria.

The individual in the procurement and distribution specialist position does not fully meet the requirements of the job description for that position. The major duties and responsibilities of the procurement and distribution specialist include overseeing storeroom operations and serving as the agency's purchasing head. The specialist is required to spend 60 percent of his time on procurement, 20 percent on storeroom operations, and 20 percent on other duties. In addition, the specialist should have knowledge of inventory management and control, supply determination and purchasing, receiving and stocking of inventory, customer needs, delivery of orders, invoicing, and bill collection.

The current procurement and distribution specialist, previously a high school principal and district business specialist, reported that his past job qualifications and skills on procurement and distribution functions included the monitoring of contracts, writing contract specifications, and evaluating requests for proposals. The specialist also reported a lack of experience and training on storeroom operations. During the audit, we noted the following instances that indicated a lack of knowledge, skills, and background on storeroom operations that probably contributed to the ineffectiveness and inefficiency of the department's storeroom.

- When the specialist was asked if any inventory turnover or other analysis was performed, the response was to ask the Office of the Auditor staff to perform the analysis.

- Specialist did not know how deliveries to schools were handled.

- Specialist did not know what the physical inventory procedures were.

- On numerous occasions, specialist gave erroneous or contradictory information regarding policies and procedures followed by storeroom personnel.

The qualifications of the supervising storekeeper are also questionable. The supervising storekeeper is required to have work experience that involves performance of clerical work, with demonstrated knowledge of storekeeping practices, methods and procedures, and inventory record-keeping procedures. The job description also requires supervisory experience. The current supervising storekeeper, previously a custodian with the department, worked as a stock clerk at a grocery store and has minimal prior supervisory experience. The supervising storekeeper is also involved in determining the amount of supplies to be ordered and inventory procedures, but has limited training in inventory management. For example, the supervising storekeeper acknowledged that the purchase of over 2,700 water hoses, of which 212 we previously reported were missing, was a mistake and admitted that the storeroom would have difficulty in selling all the water hoses that were ordered.

The storeroom personnel's limited experience and knowledge of proper storeroom functions may have contributed to poor storeroom operations and wasted taxpayer's money in damaged, spoiled, obsolete, and potentially stolen supplies.

The Storeroom Revolving Fund Does Not Operate as a True Revolving Fund and Instead Merely Serves to Perpetuate an Obsolete Operation

The department's storeroom revolving fund does not meet the intent and purpose of a revolving fund. Section 23-11, HRS, stipulates that a revolving fund must be self-sustaining. In our Report No. 96-21, we noted that the storeroom revolving fund was not self-sustaining because personnel and some operating costs were not included in the fund expenses. General funds are used for these costs. When including these costs, we found that the storeroom revolving fund actually loses money. As we have shown in this report, the central storeroom is plagued with mismanagement, provides poor service, and wastes taxpayer's money; however, its existence is preserved in the statutes.

Section 302A-1304, HRS, requires the department to operate a central storeroom and establishes the storeroom revolving fund. To eliminate

the central storeroom and revolving fund requires repealing or rewording Section 302A-1304.

The department failed to meet the intent of a revolving fund by ignoring significant costs

The Department of Education's central storeroom does not meet the intent of a revolving fund as the fund is not self-sustaining. Section 37-62, HRS, provides the following definitions for a revolving fund and its operating costs:

- "Revolving fund means a fund from which is paid the cost of goods and services rendered or furnished to or by a state agency and which is replenished through charges made for the goods and services or through transfers from other accounts or funds."

- "Operating costs means recurring costs of operating, supporting and maintaining authorized programs, including costs for *personnel salaries and wages, employee fringe benefits, lease payments*, supplies, materials, equipment and motor vehicles."

Therefore, to fully comply with the requirements of a revolving fund, all costs, including personnel salaries and wages, employee fringe benefits, and lease payments, must be considered in determining the self-sustainability of the fund.

We obtained financial data from the department to determine the total cost of operating the storeroom, including all personnel salaries and operating costs. The department has not recognized some personnel and operating costs for the storeroom revolving fund. If all costs were considered, the storeroom has had significant losses for the past few years. For the period of July 1, 1997 to June 30, 2001, the storeroom had a net loss of approximately $1.6 million. Exhibit 2.7 shows the total revenues generated and costs of the storeroom for the past four fiscal years.

In the private sector, businesses operate for the purpose of making a profit. These profits are realized only when revenues exceed the total costs to operate the business. A key measurement of success is the breakeven point when the business can cover all expenses but profits are not being realized. At the breakeven point, the business is deemed fully self-sustaining. This measurement of self-sustainment can be applied to the storeroom or any other revolving fund.

For the storeroom revolving fund to be fully self-sustaining, the selling price for educational supplies must be increased. Based on our breakeven analysis in Exhibit 2.7, the selling price for educational supplies must be increased by a minimum of 20.4 percent in order for the

Exhibit 2.7
Financial Data for FY1997-98 to FY2000-01 (in thousands)

Description	FY1997-98	FY1998-99	FY1999-2000	FY2000-01	Total
Revenues	2,276	1,808	1,849	1,987	7,920
Operating Costs	739	555	647	666	2,607
Educational Supply Costs	1,846	1,800	1,458	1,826	6,930
Total Storeroom Costs	2,585	2,355	2,105	2,492	9,537
Loss	($ 309)	($ 547)	($ 256)	($ 505)	($ 1,617)
Breakeven Analysis *	(13.6%)	(30.3%)	(13.8%)	(25.4%)	(20.4%)

* Represents loss over revenue

storeroom to breakeven. The additional cost incurred through an increased selling price of educational supplies would then be transferred to the public schools.

When considering the total mark-up of the department's educational supplies, commercial vendors may prove to be more cost effective for the public schools. The storeroom purchases supplies from commercial vendors at a discounted price. The storeroom then adds an additional 8 percent of the total invoice price for delivery costs. With a breakeven point of 20.4 percent, the total mark-up from the original purchase price should be 28.4 percent. For example, if the storeroom purchases a supply item for $1 each, the current selling price to the schools would be $1.08 ($1 x 8 percent = $.08). However, for the storeroom to be self-sustaining, the selling price should be $1.28 ($1 x 28.4 percent = $.284).

Savings can be achieved by using a price list procurement system similar to the State Procurement Office Price List. Commercial vendors of supplies to the central storeroom reported that the mark-up for supplies on the State Procurement Office Price List generally ranges from 5 to 12 percent and includes free delivery. By using a price list procurement system, the department could possibly save as much as $400,000 per year.

Section 302A-1304, HRS, preserves the storeroom

The central storeroom, as created about 30 years ago by the department, was funded with general fund moneys. At that time, the department was not required to operate a central storeroom. In 1990, Act 93, SLH, supported the department's request to establish a central storeroom and a revolving fund to operate the storeroom. Act 93 stipulated that, "there

shall be a storeroom established by the department to provide schools a source for commonly used educational, office, and custodial supplies." Act 93 not only created the storeroom revolving fund, but by requiring the department to operate a central storeroom the act preserved the existence of the storeroom. Without amending or repealing Section 302A-1304, HRS, the State will continue to support an obsolete and poorly run storeroom that provides no benefit to the public school system.

Conclusion

Our audit found that the department's central storeroom is obsolete, costly, poorly run, and a waste of state resources. It offers no benefit to the State or the public school system.

Section 302A-1304, HRS, requires the Department of Education to establish a central storeroom and the Legislature appropriates $2 million annually for the storeroom revolving fund's purchases of educational supplies to support the public school system. The storeroom's fundamental purpose to assist the public schools in purchasing educational, office, and custodial supplies at the lowest possible cost has been eclipsed by commercial vendors and the ineptitude of the storeroom's management. While the storeroom has purchased educational supplies in bulk, received discounted prices, and passed these savings on to the public schools for about 30 years, the storeroom's method of excessive bulk purchasing of educational supplies is not effective. Today, private industry is more efficient, economical, and competitive, and can better meet the needs of the public schools. Commercial vendors can provide quality educational supplies at reasonable and discounted prices with better service to the public schools.

Recommendations

1. The Legislature should repeal Section 302A-1304, HRS, which required the Department of Education to establish the central storeroom and created the storeroom revolving fund.

2. The Board and Department of Education should eliminate the central storeroom.

Responses of the Affected Agencies

Comments on Agency Response

We transmitted drafts of this report to the Department of Education and the Board of Education on January 17, 2002. A copy of the transmittal letter to the Department of Education is included as Attachment 1. The department's response is included as Attachment 2. The Board of Education did not respond.

The department stated that it agrees with our findings and concurs that the storeroom is not the most efficient means to provide educational, office, and custodial supplies to schools. The department noted that it will develop an alternative method, other than a storeroom, for schools to procure supplies. The department also reported that it has asked the Legislature to repeal Section 302A-1304, HRS, to begin the closure of the storeroom on a planned basis. We commend the department for its efforts to address the findings and for taking steps to implement our recommendations.

ATTACHMENT 1

STATE OF HAWAII
OFFICE OF THE AUDITOR
465 S. King Street, Room 500
Honolulu, Hawaii 96813-2917

MARION M. HIGA
State Auditor

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

January 17, 2002

COPY

The Honorable Patricia Hamamoto
Superintendent of Education
Department of Education
Queen Liliuokalani Building
1390 Miller Street
Honolulu, Hawaii 96813

Dear Ms. Hamamoto:

Enclosed for your information are three copies, numbered 6 to 8 of our draft report, *Management Audit of the Department of Education's Storeroom*. We ask that you telephone us by Tuesday, January 22, 2002, on whether or not you intend to comment on our recommendations. If you wish your comments to be included in the report, please submit them no later than Friday, January 25, 2002.

The Board of Education, Governor, and presiding officers of the two houses of the Legislature have also been provided copies of this draft report.

Since this report is not in final form and changes may be made to it, access to the report should be restricted to those assisting you in preparing your response. Public release of the report will be made solely by our office and only after the report is published in its final form.

Sincerely,

Marion M. Higa
State Auditor

Enclosures

ATTACHMENT 2

BENJAMIN J. CAYETANO
GOVERNOR

Patricia Hamamoto
Superintendent

STATE OF HAWAII
DEPARTMENT OF EDUCATION
P.O. BOX 2360
HONOLULU, HAWAII 96804

OFFICE OF THE SUPERINTENDENT

January 25, 2002

RECEIVED
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OFC. OF THE AUDITOR
STATE OF HAWAII

The Honorable Marion M. Higa
State Auditor
Office of the Auditor
465 South King Street, Room 500
Honolulu, Hawaii 96813-2917

Dear Ms. Higa:

This is in response to the "Management Audit of the Department of Education's Storeroom" draft report.

The Department of Education concurs that the Storeroom is not the most efficient means to provide educational supplies, office and custodial supplies to schools. We will develop an alternative method, other than a Storeroom, for schools to procure said supplies.

We have asked the legislature to repeal Sec. 302A-1304 HRS to begin the closure of the Storeroom on a planned basis.

We appreciate the efforts in your conducting the audit, as it serves as a basis to carry out this management decision.

If there are any questions, please call Chris Ito, Accounting Director, of the Business Services Branch at 586-3450.

Very truly yours,

Patricia Hamamoto
Superintendent

PH:am

cc: Mr. Herbert Watanabe, Board of Education

AN AFFIRMATIVE ACTION AND EQUAL OPPORTUNITY EMPLOYER