Study of Printing Products and Services Utilized, Contracted, and Subcontracted by Hawaii State Government

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

Report No. 02-18
October 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
Kekuanao'a Building
465 S. King Street, Room 500
Honolulu, Hawaii 96813

OVERVIEW

Study of Printing Products and Services Utilized, Contracted, and Subcontracted by Hawaii State Government

Report No. 02-18, October 2002

Summary

Although printing is an integral part of the functioning of state government, there has been concern about the lack of information on state agency practices with respect to printing. Reflecting this concern, the Legislature, during the 2002 Regular Session, adopted House Concurrent Resolution 105, which requested the State Auditor to conduct a study of printing products and services utilized, contracted, and subcontracted by Hawaii state government.

We developed a two-pronged approach to the study, a questionnaire and a case study, in order to address the issues raised in the resolution. A questionnaire was developed and sent to state executive, judicial, and legislative agencies as well as the Office of Hawaiian Affairs. Utilizing the state procurement code's definition of printed materials, we asked agencies to estimate the cost, volume and number of print services performed in-house, with the Correctional Industries Program, or contracted out, either directly or through a subcontract. In addition, agencies were to identify whether contracted services were obtained in-state, in the U.S. but outside Hawaii, or outside the U.S.

We found that for FY2001-02 state agencies reported expending approximately $15 million for printing services statewide. Of this amount, approximately $13.5 million (90 percent) was expended in-state, with approximately $6.2 million expended with vendors in Hawaii by direct contract. In addition, of the $2.6 million for printing services expended through subcontract, approximately $1.66 million (64 percent) was also expended in-state. Agencies further reported expending approximately $3.6 million (24 percent) for in-house printing.

However, the reliability of this data, particularly the in-house printing expenditures, is questionable. Most state agencies do not formally assess in-house printing costs, resulting in incomplete and sometimes confusing information. While instructions were given to utilize the state procurement code's definition of printed materials as a guide, a number of agency responses did not fall within the definition. We found that especially in light of recent technological developments, the procurement code's printed materials definition may be insufficient to permit an accurate identification of state printing practices. For example, at least two agencies consider compact discs, which are not specified as printed materials in the procurement code, to be printed materials.

We also performed a case study to provide a more in-depth look at printing practices. We selected the Department of Business, Economic Development and Tourism and its administratively attached agencies – including the Hawaii Tourism Authority – as the focus of the case study. We found that state agencies generally appear to be in compliance with the state procurement code's printing

preference requirements, but that a lack of clarity about the requirements leads to inconsistent application. We also found in a limited number of contract procedures that the printing preference requirements were properly administered. However, in the majority of cases examined, the printing preference requirement did not apply. As a result, we are unable to substantiate the need for the printing preference requirement. Most contracted printing services are apparently awarded to in-state vendors regardless of the printing preference requirement.

Recommendations and Response

We recommended that all branches of state government consider the use of cost-benefit analyses to compare and evaluate alternatives when considering large volume printing, changing technology, or other similar situations. We also recommended that the Legislature review and assess the need for the printing preference requirement under Section 103D-1003, HRS. Finally, we recommended that if the Legislature intends that Chapter 103D, HRS, be followed at all contract and subcontract levels, it should consider revising the code to provide a clear statement of purpose and objectives.

The Department of Business, Economic Development and Tourism responded that it found the study to be professional and thorough and that "enterprise-wide" analyses of government operations were very beneficial. The department noted specifically that it believes that current state law does not require printing preference requirements to be stated in contracts when subcontracting is involved. The department also stated that since clearly written rules and regulations pertaining to the application of the printing preference requirements to subcontracting do not exist, compliance is not an issue. The department's statements support the report's finding on the need to review and clarify the intent of the state procurement code in this area.

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

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Submitted by

THE AUDITOR
STATE OF HAWAII

Report No. 02-18
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Foreword

This is a report of our study of printing products and services utilized, contracted, and subcontracted by Hawaii state government. The study was conducted pursuant to House Concurrent Resolution 105 of the 2002 Regular Session. We wish to express our appreciation for the cooperation and assistance extended by officials and staff of the Department Business, Economic Development and Tourism, the Hawaii Tourism Authority, and all state agencies we contacted during the course of this study.

Marion M. Higa
State Auditor

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Chapter 1
Introduction

House Concurrent Resolution No. 105 of the 2002 Regular Session requested the State Auditor to conduct a study of printing products and services utilized, contracted, and subcontracted by Hawaii's state government. The resolution notes that state agencies utilize both private companies within and beyond Hawaii as well as in-house printing services; however, the volume of and dollar amount spent on these printing products and services is unknown.

Specifically referencing the Department of Business, Economic Development and Tourism and the Hawaii Tourism Authority as examples, the resolution stated that some state agencies contract with independent non-governmental advertising and marketing agencies, which in turn subcontract with private companies that print large quantities of marketing and promotional material to promote Hawaii tourism, agriculture, and economic development. The resolution further noted that these subcontractors may use printing and binding vendors outside Hawaii without going through the formal bid process as required under the state's procurement code.

House Concurrent Resolution No. 105 specifically requested the Auditor to:

- Study all in-house and contracted print jobs, including contracts state agencies have awarded to private marketing or advertising firms that subcontract printing jobs;
- Identify the number of in-house and contracted print jobs and dollar amounts spent in Hawaii, out-of-state, and out-of-country; and
- Identify the number of employees and the direct and indirect costs of their labor, employee benefits, rent, equipment leasing, administrative supplies, and any other costs associated with state in-house printing operations.

The following report responds to the Legislature's request.

Background

Generally, printing is defined as any process that transfers to paper or another substrate (surface) an image from an original such as a film negative or positive, electronic memory, stencil, die, or plate. Printing is

an international industry with 155 countries purchasing printing paper supplies in 2002.

Printing is America's third largest manufacturing industry, employing over 1.2 million people in almost 46,000 establishments and selling over $160 billion worth of products through medium-sized businesses in 2001. General commercial printing holds the largest market segment, with 21,878 establishments, 403,228 employees, and nearly $54 billion in total revenue in 2000.

Printing is also a significant industry in Hawaii. The Printing Industries of America, Inc., the world's largest graphic art trade association, reported in its 1998 *Print Market Atlas* that Hawaii's commercial printing approximated $250 million, in sales, while out-of-state printing neared $200 million. At the time, there were 103 printing establishments in Hawaii, which employed nearly 1,850 people, and paid out almost $75 million in wages.

Printing encompasses many different media

Printing is a part of the larger field of graphic communications, which is represented by processes and industries that create, develop, produce, and disseminate products utilizing or incorporating words or pictorial images to convey information, ideas, and feelings. Graphic communication processes include all printing methods, from offset lithography to specialty image reproduction methods. Short-run, offset printing or prepress and document photocopying services exemplify the most common quick-printing activities.

Commercial printers turn out products on a custom basis–-from annual reports to business cards, stock certificates, voting ballots, menus, brochures, catalogs, and more. However, the printer's traditional role of transforming raw information into a finished product on paper has changed. Today's printers not only produce ink-on-paper products but also include compact disc production, software file management, and Internet services.

Procurement code's definition of printed material

While national definitions of printing tend to be comprehensive, the *Hawaii Public Procurement Code's* (procurement code) definition takes a fairly restricted view of "printed material." Section 103D-1001, Hawaii Revised Statutes (HRS), defines printed material as:

"business forms, stationery, business cards, brochures, reports, publications, advertising and promotional collateral, and other related materials commissioned as part of any professional services contract."

This definition excludes printing that is part of normal daily activities (e.g., photocopies of correspondence or other material for record-keeping purposes), and specialized printing such as newspaper, package, or "quick" printing (i.e., copying and duplicating). For the purposes of our study, we refer to quick printing as "photocopying."

Procurement Code Specifies Printing Preferences

The state's procurement code is intended to ensure that the best products and services are obtained for government at the lowest prices and that all persons in the procurement system are treated fairly and equitably. The procurement code's purpose is to promote economy, efficiency, and effectiveness in the procurement of goods and services, and the construction of public works for the State and its counties. Preferences are a part of the code's requirements and are established in law to benefit certain classes or types of businesses that compete for state government work. Printing is one of eight preferences specified in the procurement code.

The procurement code's printing preference promotes in-state printing. Section 103D-1003, HRS, states that every printing, binding, or stationery contract bid for work to be performed in-state (including preparatory work, presswork, bindery work, other production-related work, storage costs, and shipping costs) will receive a *15 percent preference* in the bid evaluation. This preference applies to all bids or proposals unless it is established that the required work cannot be performed in-state.

Section 103D-1003, HRS, is implemented through Subchapter 2, Section 3-124 of the Hawaii Administrative Rules (HAR). The rules specify that a printing services contract shall be awarded to an in-state bidder if it is the lowest bid. If an in-state bidder is not the lowest bid, an increase of 15 percent shall be applied to each out-of-state bidder's proposal before determining the lowest bid proposal. The rules also state that additional preferences may apply to the extent permitted by law.

Previous Audits Identified Concerns With State Government Printing Practices

Two of our previous audits have already highlighted concerns with state government printing practices. Our *Audit of the Annual Report Costs of State Agencies*, Report No. 95-20, was initiated as a result of concerns about the costs of producing annual reports and whether these costs divert government resources from more pressing public needs. In it, we found that agencies could save money by producing their annual reports in-house rather than by contracting them out. We also concluded in our *Procurement Audit of the Correctional Industries Program*, Report No. 96-16—which was initiated to determine whether procurement statutes,

rules, exemptions, and practices of the Correctional Industries Program resulted in cost-effective procurement for state government—that the Correctional Industries Program's printing practices were inefficient and impracticable.

Annual reports audit emphasized guidelines to control costs

Our *Audit of the Annual Report Costs of State Agencies*, Report No. 95-20, sought to establish the costs of state agencies' annual reports, assess the reasonableness of those costs, and identify areas where savings could be realized. Although the amount of money spent on printing annual reports was minor compared to the total costs of state government, we noted that the State should look for ways to reduce unnecessary expenditures and diminish any public perception of waste and inefficiency. We warned that agencies choosing to contract out for printing services should follow applicable procurement requirements.

We suggested instituting flexible state guidelines in order to bring about cost savings, since a lack of guidelines had led to questionable costs. The report further recommended that the governor consider issuing annual report guidelines on how to produce and distribute annual reports at reasonable costs. Those guidelines should cover the purpose and content of the report; the importance of weighing the costs of in-house production and distribution versus contracting out; the need to consider use of the Correctional Industries Program's print shop; cost-effective graphic design, layout, colors, photos, number of pages, and paper stock; and a way to save on distribution costs.

Mandatory use of Correctional Industries Program for printing services found inefficient

In our *Procurement Audit of the Correctional Industries Program*, Report No. 96-16, we found that forcing state agencies to procure printing services from the Correctional Industries Program of the Department of Public Safety is both inefficient and unnecessary. Our report recommended that the director of public safety remove printing services from goods and services that must be purchased from the Correctional Industries Program.

At the time, Section 354D-6(d), HRS, required state agencies to send all their print jobs to the Correctional Industries Program. If the program could not perform the work, or if the agency needed the work done more quickly or believed it could acquire the printing at a better price from another vendor, the agency could submit a written waiver request. The Department of Accounting and General Services would not pay for printing done by vendors other than the Correctional Industries Program unless a waiver was provided with the payment request. Our report ascertained that it took the equivalent of one full-time person working three and a half months each year to process such waivers.

Responding to our recommendation and addressing concerns of the state's printing industry, the Legislature passed Act 140, Session Laws of Hawaii 1998, which amended Section 354D-6(d), HRS, by removing state agencies' requirement to purchase goods and services from the correctional industries print shop unless they obtained a waiver. Although the State Procurement Office administrator must still provide agencies with a list of services that the Correctional Industries Program provides, agencies may now choose whether or not to purchase those services from the program.

Objectives

1. Assess the cost of printing for Hawaii state government.

2. Determine whether selected state agencies are in compliance with the *Hawaii Public Procurement Code's* requirements for printing services.

3. Make recommendations as appropriate.

Scope and Methodology

We addressed the issues raised in House Concurrent Resolution No. 105 by first developing a questionnaire regarding state printing practices, during FY2001-02. Questionnaires were sent to state executive, judicial, and legislative agencies and to the Office of Hawaiian Affairs with instructions to forward the questionnaire to their administratively attached agencies for completion.

The questionnaire focused on the procurement code's definition of "printed materials." It did not ask agencies to provide information about photocopying (e.g., normal daily activities including routine copying and duplicating of correspondence for record-keeping purposes), specialized printing (such as newspaper or package printing) or seek to identify the source of printing funds. The questionnaire requested that agencies estimate the cost, volume and number of printing services performed in-house, with the Correctional Industries Program, or contracted out, either directly or through subcontract.

For printing services contracted to private vendors, agencies were also asked to identify whether the vendors were located in-state, in the U.S. but outside Hawaii, or outside the U.S. For in-house printing, agencies were asked to separately identify the costs of labor, equipment, materials, and facilities. We then conducted follow-up interviews to clarify agency responses and compiled and summarized the data.

Although follow-up interviews were conducted, time restrictions and the scope of responses to the questionnaire made it impractical to independently verify these answers. Therefore, we rely primarily upon the responses provided by the agencies. Our discussion and conclusions take into consideration these limitations.

In addition to the questionnaire, we performed a case study to provide a more in-depth look at printing practices. We selected the Department of Business, Economic Development and Tourism and its administratively attached agencies based on the concerns expressed in House Concurrent Resolution No. 105 about the department's contractual relationships. We reviewed management controls at the departmental, divisional, office, and administratively attached agency levels to evaluate whether procurement code requirements are followed for printing service contracts. Although this was a study and not an audit, we reviewed the department and its administratively attached agencies' printing practices for compliance with laws, regulations, and other compliance requirements significant to the study's objectives.

Based on a review of questionnaire responses, we judgmentally selected a sample of the Department of Business, Economic Development and Tourism's administratively attached agencies in order to review and assess their printing practices for compliance with the procurement code. We reviewed a sample of contracts, contract procedures, and other departmental processes from the selected administratively attached agencies to assess whether procurement code requirements were being followed for printing service contracts.

We interviewed designated contact persons for each selected office or agency as well as other departmental officials to understand practices related to printing services. We also interviewed State Procurement Office personnel to gain an understanding of the application of procurement code procedures.

Our work was performed from June 2002 through August 2002 in accordance with generally accepted government auditing standards.

Chapter 2

State Government Printing Practices and Policies Are Inconsistent and Unclear, Making the Assessment of Total Cost Difficult

This study was conducted largely in response to concerns about the lack of information on state government printing practices. Although printing is an integral part of the functioning of state government, agencies' practices and the costs incurred for printing services are areas that have not received much scrutiny or attention. State agencies do not routinely account for printing expenditures, and what constitutes "printing" varies across agencies.

Our study found that, generally, state agencies meet their printing needs in-state. The study also shows that, at least for directly contracted printing services, state agencies observe the *Hawaii Public Procurement Code* (procurement code) requirements. However, when attempting to identify costs for printing services, particularly in-house (meaning within state government) printing, we found the reliability of information provided to be questionable. This is due in part to the lack of clarity among agencies as to what constitutes "printing." In addition, state agencies' efforts to separately identify costs associated with in-house printing varied widely.

We also found that the applicability of the procurement code is not always clear when printing services are secured through subcontracts. Finally, we found that given the reported printing practices of state agencies, a review of the procurement code's printing preference requirement is warranted.

Summary of Findings

1. The cost of printing in Hawaii state government is difficult to assess. The *Hawaii Public Procurement Code's* definition of printed materials does not capture all state printing practices and many agencies do not routinely attribute costs to in-house printing. These factors hinder agencies from accurately determining the most efficient and effective printing alternatives.

2. State agencies appear to be in compliance with the requirements of the procurement code for printing services, but clarity in the code is warranted. The basis and need for the printing preference is not evident. Additionally, oversight responsibilities for printing

subcontracts are unclear. The procurement code lacks specificity in regard to monitoring responsibilities at the subcontract level and below.

The Cost of Printing in Hawaii State Government Is Difficult to Assess

Agencies reported that approximately $15 million was expended on printing services statewide during FY2001-02. Of this amount, approximately 90 percent was expended in-state. Agencies further reported that approximately $3.6 million, or 24 percent, was attributed to in-house printing. Notwithstanding the results of our questionnaire, agencies' responses revealed that given a definition of printed materials, their responses pertaining to in-house printing were inconsistent and therefore affect the credibility of the data.

State government lacks a clear definition of "printing"

State agencies gave varying responses to what was considered printing. This might be attributed to a failure to apply the procurement code's "printed materials" definition, or to shortcomings in the definition itself. The procurement code applies to state agencies that contract out print work; however, after reviewing state statutes, we could not identify any suitable alternative to the procurement code's legal definition of printed materials. Therefore, to foster consistent responses to our questionnaire, we used the code's definition to guide agency responses.

Since the decision to report certain activities as printing is somewhat arbitrary, it is possible that agencies neglected to identify or list some printing activities that could have qualified under the code's definition. On the other hand, agencies may have included materials that would be considered printing in a wider definition but which are not covered by the procurement code definition.

Some agencies included the purchase of pre-printed publications in their responses. While these may be examples of printing, pre-printed publications are not in the procurement code's definition of printed materials.

In other instances, agencies included such items as pens, lanyards, decals, plastic bags, banners, and compact discs as printed materials. These items are considered printing materials within the scope of printing as defined by the printing industry, but fall outside the state procurement code's definition.

One agency listed 15 copies of an instructional manual as printing, while another included one appeal record as printing. Given the description each agency provided, it appears that these are more likely examples of photocopying and not printing. The differentiation between

photocopying and printing appears to be somewhat subjective. As a result, some of the in-house printing jobs reported in our questionnaire could be viewed as photocopying, while others are not.

Technological developments emphasize the need to clarify the definition of printing

In light of recent technological developments in printing, the procurement code definition of "printed materials" is problematic, particularly with regard to in-house printing. At least two agencies noted that they now consider compact discs printed materials. Industry professionals note that with technological advances in office automation, and usage patterns such as on-demand printing, what constitutes "printed materials" may need to be better defined. Office automation can lead to a blurring in the differentiation of printing versus photocopying. Reports, business forms, and items such as stationery, which in the past were sent to printers can now be printed on-demand from an office copy machine.

With a range of alternative media now more readily available, the procurement code definition of printed materials may be insufficient to permit an accurate identification of state printing practices. As noted earlier, the reliability of information on in-house printing is particularly questionable.

In-house printing costs are inaccurate

The costs that agencies attributed to in-house printing services varied widely. As shown in Exhibit 2.1, questionnaire responses indicated that approximately $3.5 million worth of printing services were performed in-house, with individual agencies reporting anywhere from $0 to $1.8 million as the cost for their in-house printing during FY2001-02. The questionnaire asked that agencies attribute in-house printing costs by the expense categories of labor, equipment, materials, and overhead. A number of agencies were unable to separately attribute in-house printing costs by these categories. One agency responded that "they have no way" to compute the cost of in-house printing. Several other agencies were unable to attribute the cost of labor and materials associated with in-house printing, or provided incomplete or confusing responses. For example, one agency reported that one full-time position was involved with in-house printing, but reported the cost of that full-time position as "not applicable."

In several instances, agencies provided only fractional costs. For example, one division within an agency provided supply costs because it was required to reimburse another division for use of its printer. However, that division was unable to identify any other cost associated with what was reported as in-house printing.

Exhibit 2.1
Summary of Direct State Expenditures for Printing Services

Agencies	In-House Services	Correctional Industries	Contracted - Hawaii	Contracted - Mainland/ International	
OFFICE OF THE GOVERNOR	$711	$7,428	$58,254	$0	
OFFICE OF THE LIEUTENANT GOVERNOR	$3,783	$22,923	$269,104	$0	
ACCOUNTING & GENERAL SERVICES	$778	$19,012	$614,662	$52,141	M
AGRICULTURE	$7,871	$19,299	$16,931	$0	
ATTORNEY GENERAL	$3,858	$62,188	$127,974	$22,832	M
BUDGET & FINANCE	$152,261	$24,983	$555,713	$0	
BUSINESS, ECONOMIC DEVELOPMENT, & TOURISM	$21,882	$16,388	$109,098	$84,021	M & I
Housing & Community Development Corporation of Hawaii	$2,291	$8,998	$0	$0	
Office of Planning	$265	$1,926	$32,344	$360	M
Natural Energy Laboratory of Hawaii Authority	$2,283	$412	$0	$0	
Land Use Commission	$0	$616	$0	$0	
Aloha Tower Development Corporation	$0	$55	$0	$0	
Barbers Point Naval Air Station Redevelopment Commission	$305	$0	$0	$0	
Hawaii Strategic Development Corporation	$0	$0	$0	$485	M
Hawaii Community Development Authority	$2,519	$497	$9,828	$0	
High Technology Development Corporation	$0	$240	$15,458	$2,100	M & I
Hawaii Tourism Authority	$0	$615	$12,822	$0	
COMMERCE & CONSUMER AFFAIRS	$54,616	$16,530	$44,746	$0	
DEFENSE	$0	$16,420	$38,437	$0	
EDUCATION	$483,049	$0	$245,480	$0	
HAWAIIAN HOME LANDS	$0	$10,352	$109,818	$0	
HEALTH	$51,919	$214,123	$511,005	$206,851	M
HUMAN RESOURCES DEVELOPMENT	$21,949	$10,846	$2,038	$0	
HUMAN SERVICES	$136,425	$95,957	$358,995	$865	M
LABOR & INDUSTRIAL RELATIONS	$7,776	$57,788	$245,305	$2,359	M
LAND & NATURAL RESOURCES	$7,713	$19,785	$162,545	$48,320	M
PUBLIC SAFETY	$43,864	$72,432	$12,217	$0	
TAXATION	$297,700	$444,313	$404,536	$32,879	M
TRANSPORTATION	$161,206	$21,759	$66,478	$184,007	M
UNIVERSITY OF HAWAII	$1,785,227	$73,331	$1,612,615	$104,781	M & I
THE JUDICIARY	$258,173	$5,667	$150,387	$245,184	M
OFFICE OF HAWAIIAN AFFAIRS	$0	$796	$160,044	$0	
STATE OF HAWAII - LEGISLATURE					
Senate	$3,217	$260	$81,663	$0	
House of Representatives	$71,000	$2,800	$69,000	$0	
LEGISLATIVE SERVICE AGENCIES					
Legislative Reference Bureau	$0	$17,118	$0	$305,734	M
Office of the Auditor	$10,486	$15	$10,892	$0	
Office of the Ombudsman	$343	$420	$3,158	$0	
State Ethics Commission	$447	$1,082	$9,511	$0	
Grand Total	**$3,593,917**	**$1,267,373**	**$6,121,057**	**$1,292,919**	

M = Mainland
I = International

Note: Does not include expenditures for sub-contracted printwork.
Slight differences may be due to rounding.

Some agency reprographic centers do track costs

Agencies that maintain separate reprographic centers, such as the Department of Education, the University of Hawaii, and the Judiciary, maintained more detailed in-house printing cost records. A reprographic center is a unit within an agency that provides printing services to the agency. Since reprographic centers generally charge costs to the entity requesting the printing services, there is likely to be substantiation for these costs. Approximately $2.8 million, or 79 percent, of the state's total reported in-house printing expenditures were from agencies with reprographic centers. One agency's reprographic center was able to provide a breakdown of each cost element for in-house printing based upon a per impression (copy) cost.

Most agencies do not formally assess in-house printing costs

While a few reprographic centers may track printing costs, the majority of state agencies do not formally assess in-house printing costs. Of the 28 primary agencies we surveyed, eight agencies reported having a reprographic center, but only two of these agencies had used cost-benefit techniques to determine in-house cost-effectiveness. The Judiciary provided documentation to substantiate that a cost-analysis had actually been conducted, while the other agency indicated that it had provided its best guess. Of the nine agencies that reported substantial in-house printing on "fancy" copiers, only the Departments of Business, Economic Development and Tourism, and Land and Natural Resources have recently conducted cost-benefit analyses.

In fact, agencies often rely on institutional knowledge rather than any analytical cost-benefit review to justify in-house printing practices versus contracting out for printing jobs. For example, during our follow-up interviews, several agencies commented that they contracted out certain printing jobs because "that's how they've always done it." Other justifications included timesavings, on-demand printing, size or complexity of the print job, need for a quick turnaround, lack of equipment capability, and manpower. All of these may be valid reasons for an agency's printing practices' decisions, but few decisions actually have documented support.

Available cost-benefit analyses yield mixed results

Two agencies' cost-benefit analyses pointed toward cost savings by printing in-house, while one concluded that contracting out was preferable. Only two of the agencies we surveyed were able to produce documentation of the cost-benefit analyses they conducted.

The Judiciary's Reprographics Center provided a detailed accounting of costs for personnel, operations, graphics and negatives, cost per square

foot of the reprographic center, and projected cost for outside vendors to have provided the same services. The center concluded that the cost of printing in-house totaled $338,970, versus $492,165 if the work had been contracted out. Based on the comparison, the reprographics center contends that it saved the Judiciary and the State approximately $153,195 during FY2001-02 and that it was more cost-effective in providing all in-house printing and related services than outside vendors would have been.

The Department of Business, Economic Development and Tourism provided cost comparison estimates for use of "electronic printing" with compact discs to replace traditional printing. A representative of the department indicated that the department could compile annual reports for more than ten administratively attached agencies onto one $0.11 compact disc. This results in less storage cost requirements and reduces the usage of paper and printing supplies. The department also claims timesavings with the "electronic printing" process. For example, in the past, the department printed reams of departmental letterhead. However, whenever the department's director changed, the remaining unused letterhead was wasted. Now, the department uses a letterhead template stored on its intranet system to print letterhead on demand using regular paper. There is no longer a need to contract for printed letterhead paper, and the department reduces the problem of outdated stationery.

The department also states that less time is spent scheduling and proofing the print work and hard copy. The department notes that in a five-month period starting in February 2002 when it began producing compact discs, more than 700 compact discs were distributed at trade shows, business meetings, and foreign trade missions. The department estimates saving $177 per compact disc, which translates into a savings of $123,655.

The Department of Land and Natural Resources' Aquatic Resources Division also provided a rough breakdown of costs for in-house printing of the division's newsletter using its new copier. The division kept track of the personnel hours used, as well as the special paper required. Repair costs for the newly acquired machine, which overheated and broke down twice during the course of the copying were not included. In this case, the division found it cost over twice as much to print a newsletter in-house than by using the Correctional Industries Program, which would have cost only $700.

Assessment is essential for cost-effective printing

As illustrated above, and confirmed by some printing industry research, improvements to in-house printing capabilities do not always translate into cost savings. Although technological advances mean that more

printing can be carried out in-house, the product expenses may not result in agency cost-savings. Printers, copiers, multi-function products, and the services and supplies required to run them represent a significant annual expense to most agencies. The purchase of any of this equipment involves buying the device, supplies, and maintenance costs and can require significant initial up-front expenditures.

Leasing is a popular alternative to purchasing. Typically, leasing printing equipment is based on "buying the page" produced by the devices, as opposed to the actual devices—that is, a combination of a leasing fee and a per copy cost may be charged based on projected usage. Leasing can protect the agency from rapidly changing technology and therefore help control costs. However, for leasing to be effective an agency must be able to accurately estimate its in-house printing demands. Failure to make an accurate estimate can result in leasing equipment, which is under- or over-utilized. In either situation, the lack of an adequate evaluation of printing needs diminishes any cost-effectiveness efforts.

Use of cost-of-service techniques is recommended

The use of cost-of-service techniques (cost-benefit analyses) can help ensure that agencies accurately evaluate their printing needs when comparing alternatives such as in-house versus contracted vendors. Cost-of-service techniques can guide an agency to identify and evaluate both direct and indirect costs associated with in-house printing practices as well as contractor, administration, and other costs incurred when contracting out. However, since such efforts are time-consuming, agencies might consider using such analyses primarily for large volume printing, when changing technology, and in other similar situations.

State Agencies Appear To Be in Compliance With Requirements of the Procurement Code for Printing Services, But Clarity in the Code Is Warranted

The state's procurement code specifically identifies printing as one of the industries that should receive preferential treatment. "Preferential treatment" means that, as much as possible, for printing jobs contracted out by state agencies, Hawaii-based or in-state printing vendors would be favored over out-of-state vendors. This stipulation is known as the Printing, Binding and Stationery Work Preference or *printing preference* (Section 103D-1003, Hawaii Revised Statutes (HRS)).

To address this concern, our report utilizes a case study approach to examine state agencies' compliance with the code's printing preference requirements. We found that while state agencies generally appear to be in compliance with the printing preference, a lack of clarity in the application of the printing preference resulted in mixed responses. For

example, application of the printing preference requirement at the subcontractor level is not clear and leads to inconsistent implementation.

We also raise a more basic question of whether the printing preference requirement is truly necessary. Our questionnaire responses do not link the printing preference requirement to state agencies' printing practices. It appears that most state agencies' printing services are contracted in-state without having to apply the printing preference requirement. This makes it difficult to assess whether the printing preference is effective or warranted.

Printing preference requirements are reflected in the bid process

As part of our case study, we reviewed a sample of the Department of Business, Economic Development and Tourism's contracts for printed services. We also reviewed the printing practices questionnaire responses for ten agencies administratively attached to the department. Four of the ten agencies were then selected as part of our case study review. The other six agencies were not selected because their questionnaire responses indicated there were essentially no printing services contracts issued during FY2001-02. The department stated that it has limited oversight authority over the Office of Planning and the Natural Energy Laboratory of Hawaii Authority.

Preference requirements are specified in proposal requests

We reviewed three of the Department of Business, Economic Development and Tourism's printing related contracts executed in FY2001-02. We also reviewed the request for bid or proposal specifications for each contract and found that the printing preference requirement was properly listed in an addendum as a special condition or term of the proposal. Instructions were provided to the potential bidder on how to correctly claim credit for the printing preference. Bid/ proposal evaluation forms included the printing preference option among the factors to be considered.

We reviewed documentation received for each of the three printing contract proposals awarded through the bid/proposal process during FY2001-02. One set of bids included only in-state bidders, while another included only out-of-state bidders. In both situations, the printing preference requirement did not apply. In these cases, the contracts were awarded on the basis of the "lowest responsible bidder."

For the one printing services proposal that did include both in- and out-of-state bidders, the printing preference was applied and included as part of the bids evaluation. The contract was awarded to an in-state bidder based upon that bid being the lowest responsible bid when adjusted for the in-state printing preference.

Hawaii printing industry representatives contend that the printing preference accommodates Hawaii-based businesses' higher overhead costs, which consequently result in higher bids. A Hawaii-based company that provides printing services through subcontracts also stated that Hawaii-based printing businesses generally submit bids that are 15 to 40 percent higher than mainland-based companies, although the cost differential can be offset when shipping costs are taken into consideration. In the single example we reviewed, the Hawaii-based vendor's unadjusted bid was 5 percent higher than the lowest mainland vendor's bid, but 35 percent lower than the highest mainland vendor's bid. While this finding is limited to one example, it does not appear to strongly support the contention that bids from in-state vendors are categorically higher than mainland bids.

Administratively attached agencies also generally follow the procurement code

The administratively attached agencies we reviewed also generally follow the procurement code for printing services contracts, even though an agency may be technically exempt from the procurement code's requirements. However, since all of the contracts executed were small purchase and contracted to in-state vendors, the printing preference requirements were not applicable.

We reviewed the questionnaire responses for ten agencies administratively attached to the Department of Business, Economic Development and Tourism. Four of the ten agencies were selected as part of our case study review of printing services contracts. The other six agencies were not selected because their questionnaire responses indicated that there were essentially no printing services contracts issued during FY2001-02.

The Natural Energy Laboratory of Hawaii Authority reported that during FY2001-02, all its printing services were either performed in–house or through the Correctional Industries Program. There were no instances where the procurement code's printing preference requirements were applicable. For the same period, the Office of Planning reported that nine of its 22 printing services contracts were executed with in-state vendors, while 13 contracts were with the Correctional Industries Program. We reviewed the nine in-state contracts and found that all were small purchase contracts, executed in accordance with the low-bid, minimum number of written quotations requirement of the procurement code. The printing preference requirements were also not applicable.

The Housing and Community Development Corporation of Hawaii (HCDCH) reported that all its printing services were provided in-state, either through in-house means, the Correctional Industries Program, or

in-state vendors. We reviewed HCDCH's printing services contracts with in-state vendors and found that they were small purchase contracts executed in accordance with the procurement code's guidelines. The printing preference requirements did not apply.

The Hawaii Tourism Authority is by statute exempt from the provisions of the procurement code, but the authority's contracts and program manager states that the authority follows the intent and spirit of the code to the extent possible, as long as it does not interfere with fulfillment of the authority's mission.

The tourism authority's questionnaire response indicated that a total of seven direct printing services contracts totaling $12,500 were issued during FY2001-02—two with the Correctional Industries Program and five with in-state vendors. The authority noted that the five jobs contracted in-state followed small purchase guidelines of the procurement code.

The tourism authority had by far the largest reported expenditures for printing services through subcontracts, with approximately $2.5 million expended during FY2001-02. Of this amount, about $400,000 was awarded to mainland United States vendors and approximately $486,000 was awarded to vendors outside of the United States. Thus, approximately $1.5 million, or 64 percent, of the authority's reported expenditures for subcontracted printing services were in-state.

In follow-up discussions, authority personnel opined that out-of-state printing services contracts are often a function of location—that is, products are printed in proximity to their intended destination. For example, promotional materials intended for Japan are printed in Japan. Materials for a mainland United States promotional campaign are printed on the mainland near the campaign's fulfillment center. Hawaii printing industry representatives generally agreed that it was impractical to expect printing services in these situations to be performed in-state.

Oversight responsibilities for printing subcontracts are unclear

While state agencies appear to observe the printing preference requirements when directly contracting for printing services, these requirements are not as clear when subcontracting is involved. This is due in part to a lack of clarity concerning application of the procurement code printing preferences to subcontracts and also to a belief that the printing preferences should not necessarily apply in a subcontracting situation.

Subcontracting for printing services is not widely used by state agencies. Only eight agencies reported using this practice. Of these, six agencies reported expending approximately $30,000 for printing services

subcontracts during FY2001-02. The Hawaii Tourism Authority expended the largest amount for printing service subcontracts with $2.5 million (96 percent) of the total $2.6 million total reported expenditures. Most of these expenditures were actually reported as sub-subcontracts. The Department of Business, Economic Development and Tourism, which reported $108,000 in printing service subcontracts incurred by two divisions, ranked a distant second in expenditures behind the tourism authority.

Printing subcontract specifications vary widely

The level of detail for printing services varies widely in subcontract specifications. Generally, when subcontracted, printing services represent an ancillary function to the primary contract. As a result, the level of detail and specificity of requirements varies. For example, as part of an effort to measure visitor satisfaction, a contract might be issued for printed surveys, which are distributed to visitors and later tabulated through an optical character reader. The content and format of the survey may be very specific in the contract in order that the optical reader requirements can be met.

In other instances, a primary contract may specify only that promotional brochures are to be printed and distributed. The design and content are left to the primary contractor and no further detailed specifications are developed. We found this to be particularly prevalent among the sub-subcontracts at the Hawaii Tourism Authority. These differences in product expectations and specifications may also affect the degree to which procurement code printing preferences and monitoring are applied to subcontracts.

Monitoring responsibility for subcontracts differs

The Department of Business, Economic Development and Tourism's monitoring practices for compliance with the procurement code printing preference are inconsistent. The State Procurement Office contends that even when printing services are incidental to a contract and are subcontracted to another vendor, the procurement code's printing preference requirements should be applied. The State Procurement Office noted that requirements such as pricing of the brochure and identification of whether the printing will be performed in-state or not, should be specified in the proposal. In addition, bidders should be aware that the printing preference would be applied to all bids.

Our review of the department's printing services subcontracts showed generally that these stipulations are not specified in the special conditions and terms of the bid/proposals. This would be counter to the

procurement office's contention that the printing preference requirement should be included.

However, in one series of contracts that we reviewed, the primary contractor stated that all printing would be done in-state. In this situation, the printing preference would not apply as long as the terms of the primary contract are observed. In the other contract/subcontract awards reviewed, all printing subcontracts were awarded by the primary contractor to in-state vendors, although the printing preference requirement was not explicitly identified. In this situation, the printing preference would also not apply because no out-of-state vendors were involved.

Despite these factors, the department still did not comply with the State Procurement Office's interpretation of the applicability of the printing preference requirement in the contract specifications. The noncompliance may be due to the lack of specificity in the procurement code pertaining to expectations of subcontractors. Although the State Procurement Office contends that printing preference requirements should be specified in the subcontracts, the office also acknowledges that the procurement code is generally silent regarding specific expectations for subcontracting other than the ability to monitor, inspect, and audit subcontracts.

The Hawaii Tourism Authority does not monitor printing sub-subcontracts for printing preference compliance

The Hawaii Tourism Authority also generally does not impose the procurement code's printing preference requirement in its subcontracting and sub-subcontracting practices. The authority, technically exempt from the requirements of the procurement code, states that it follows the procurement to the extent feasible. The authority is tasked with the responsibility of promoting tourism for the State of Hawaii. The approach taken by the authority is to contract with various entities including counties and private companies to develop promotional strategies for tourism. The authority maintains that each of its primary contractors is charged with the responsibility for development of specific activities that will support the tourism goals of the State.

Printing services in conjunction with the Hawaii Tourism Authority's tourism promotional efforts are often at the sub-subcontract level. The tourism authority's primary tourism promotion contract is with the Hawaii Visitors and Convention Bureau. The bureau in turn subcontracts with various private companies to develop specific targeted promotional efforts aimed at satisfying the state's overall tourism goals. As part of these subcontracts, additional sub-subcontracts may be awarded for printing services as part of each promotional campaign.

For example, the Hawaii Visitors and Convention Bureau may contract with a promotional agency to promote a major professional golfing tournament. Printed brochures distributed as part of publicity for the event are obtained through a sub-subcontractor from a printing vendor. The tourism authority notes that at this level it normally does not monitor the contracts. The authority contends that this level of detail would be beyond the expertise of authority personnel and essentially amounts to micromanagement of private vendors that are retained because of their background and knowledge in these areas.

The State Procurement Office states that regardless of the level of the contract there is a responsibility to monitor to ensure that contract requirements are met. Although contract monitoring is important, the level of monitoring needs to be at a "reasonable" level. The lack of specification as to what would be considered "reasonable" at the subcontract and sub-subcontract levels results in reliance upon each agency's own interpretation of what is sufficient monitoring.

We believe the intent of the procurement code's printing preference requirement is to ensure that, to the extent practicable, when state agencies contract for printing services from private vendors, in-state vendors are utilized. To meet this requirement, there should be reasonable efforts to make it clear to bidders that there is a preference for in-state printing services. However, this is not the same issue as contract monitoring or evaluation of the type, quality or choice of the printed product. Monitoring to ensure that the intent of the printing preference is observed does not mean micromanagement of the contracting process.

The majority of state printing needs are met in-state

As we noted earlier, based on agency responses to our questionnaire and our case study, we did not find strong evidence of linkage between the procurement code's printing preference and state agencies' actual printing practices. The basis for the printing preference in the procurement code is presumed to be based on the need to ensure that state government printing services are satisfied through the use of in-state printing options. We found that, in fact, most state government printing requirements are satisfied in-state. However, it does not appear that the procurement code's printing preference requirement plays a significant role in creating this practice. We found that most state agency printing practices do not trigger the printing preference requirement.

Most contracted printing work is performed in-state through small purchase awards

Most of the printing services contracted by state agencies to private vendors are through small purchase contracts awarded to in-state

vendors. Since the vendors are mostly in-state, the printing preference requirements of the procurement code are not applicable. As a result, it cannot be demonstrated in these situations whether the existence of the printing preference requirement would have had any effect upon the selection of a printing vendor.

State agencies we surveyed reported that approximately $6.2 million, or 50 percent, of their total direct printing expenditures are contracted with vendors in Hawaii. In addition, of the approximately $2.6 million in printing services contracted through subcontracts, $1.66 million (64 percent) was subcontracted to vendors in Hawaii. We found that the majority of state agencies' contracted printing services are small purchase contracts awarded in accordance with small purchase requirements in the state procurement code. Our case study review of small purchase contracts in the Department of Business, Economic Development and Tourism confirmed that this department generally followed the lowest bid requirement to award small purchase contracts. In addition, since vendors solicited were all in-state, the procurement code printing preference requirement did not apply.

In total, responses to our questionnaire indicate that approximately 90 percent of the total expenditures for state government printing services are awarded in-state through a combined use of in-house, the Correctional Industries Program, or in-state contracts (approximately $11.1 million of the reported $12.3 million in direct printing services expenditures). This means that only about $1.2 million (10 percent) of the FY2001-02 reported direct expenditures for printing services were subject to the procurement code's printing preference requirements.

Basis and need for printing preference is not evident

The state's procurement code stipulates a total of eight preferences. In order of subchapter in the Hawaii Administrative Rules, these are:

- Hawaii Products Preference;
- Printing, Binding, and Stationery Work Preference;
- Reciprocal Preference;
- Recycled Products Preference;
- Software Development Business Preference;
- Preference to In-State Contractors Bidding on State Agency Contracts for State Agency Contracts for Public Works Projects;

- Tax Preference; and
- Qualified Community Rehabilitation Programs Preference.

Based on our review of these preferences, we concluded that they can be classified into three basic categories:

- Benefit of a specific type of Hawaii-based business;
- Achievement of a specific social purpose; and
- Assurance of equity for Hawaii businesses that seek out-of-state contracts.

The Hawaii products; printing, binding, and stationery work; software development business; and in-state contractor preferences all appear intended to benefit a specific type of Hawaii business. Although the procurement code does not specifically list objectives or purposes for the preferences, the State Procurement Office interpreted objectives and purposes as part of its implementation of the code in the administrative rules. We conclude that implicit in the establishment of these preferences is the recognition that these businesses provide a benefit to the State that offsets the procurement code's basic premise of fairness and equity. Therefore, there is a *need* for the State to impose a preference requirement. For example, application of the Hawaii Products Preference is intended to promote use of products made in Hawaii by state agencies.

Similarly, establishment of a printing preference appears intended to ensure that printing services contracted by state agencies to outside bidders gives preference to local businesses. Advocates of the printing preference contend that the preference is needed to ensure support for the local printing industry. Application of the printing preference would thus help offset this differential for state printing services contracts. However, results of our questionnaire and our case study review of selected printing contracts appear to contravene the argument for this preference.

Conclusion

To our knowledge, the printing practices of Hawaii's state government have never been formally reviewed. State agencies do not routinely track costs related to printing, and any available information is inconsistently reported. Review of factors in determining whether it is more cost-effective to print in-house or contract out is sporadic. Additionally, when agencies do decide to contract out for services, procurement code requirements are not clear.

The prevalent nature of printing in state government's day-to-day activities demands that agencies take a closer look at not just the cost, but the most effective means of accomplishing printing tasks.

Recommendations

1. All branches of state government should consider the use of cost-of-service techniques (cost-benefit analyses) to compare and evaluate alternatives when considering large volume printing, when changing technology, and in other similar situations.

2. The Legislature should review and assess the need for the printing preference requirement under Section 103D-1003, HRS.

3. The Legislature should determine whether it is the intent that provisions of Chapter 103D, HRS, be followed at all contract and subcontract levels when state funds are involved. If the intent of the procurement code is oversight and monitoring at all contract levels, then the code should be revised to provide a clear statement of purpose and objectives.

Appendix A
List of Primary and Secondary Agencies Responding to Printing Questionnaire

PRIMARY AGENCY	SECONDARY AGENCY
Office of the Governor	
Office of the Lieutenant Governor	• Campaign Spending Commission • Office of Elections • Commission on the Status of Women • Office of Information Practices
Department of Accounting and General Services	• State Foundation on Culture and the Arts
Department of Agriculture	• Agribusiness Development Corporation
Department of the Attorney General	
Department of Budget and Finance	• Public Utilities Commission • Office of the Public Defender • Employees' Retirement System • Hawaii Employee-Union Health Benefits Trust Fund
Department of Business, Economic Development and Tourism	• Housing and Community Development Corporation of Hawaii • Office of Planning • Natural Energy Laboratory of Hawaii Authority • Land Use Commission • Aloha Tower Development Corporation • Barbers Point Navel Air Station Redevelopment Commission • Hawaii Strategic Development Corporation • Hawaii Community Development Authority • High Technology Development Corporation • Hawaii Tourism Authority
Department of Commerce and Consumer Affairs	
Department of Defense	
Department of Education	
Department of Hawaiian Home Lands	
Department of Health	• State Health Planning and Development Agency • Executive Office on Aging • Office of Environmental Quality Control • State Council on Developmental Disabilities
Department of Human Resources Development	
Department of Human Services	• Office of Youth Services
Department of Labor and Industrial Relations	• Hawaii Labor Relations Board • Hawaii Workforce Development Council
Department of Land and Natural Resources	
Department of Public Safety	
Department of Taxation	
Department of Transportation	• Oahu Metropolitan Planning Organization
University of Hawaii	• University of Hawaii Press • University of Hawaii Foundation • Research Corporation of the University of Hawaii
The Judiciary	
The Office of Hawaiian Affairs	
State of Hawaii Legislature	• Senate • House of Representatives • Office of the Ombudsman • Office of the Auditor • Legislative Reference Bureau • Hawaii State Ethics Commission

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Response of the Affected Agency

Comments on Agency Response

We transmitted a draft of this report to the Department of Business, Economic Development and Tourism. A copy of the transmittal letter to the department is included as Attachment 1. A copy of the department's response is included as Attachment 2.

The department noted that, in general, the study was very professional and thorough, and also stated that it finds "enterprise-wide" analyses of government operations very beneficial. The department's specific comments reflected its belief that the application of the printing preference to subcontractors was not part of current state law. Additionally, the department disagreed with our conclusion that the department was not in compliance with the State Procurement Office's interpretation of the printing preference requirements in contract specifications, pointing to the lack of clearly defined rules and regulations involving subcontractors.

We note that the department's comments reflect the concerns expressed in the report on the need to clarify the applicability of the state procurement code's printing preference requirements when subcontracting is involved.

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

October 18, 2002

COPY

The Honorable Seiji F. Naya
Director
Department of Business, Economic Development and Tourism
No. 1 Capitol District
250 South Hotel Street
Honolulu, Hawaii 96813

Dear Dr. Naya:

Enclosed for your information are three copies, numbered 6 to 8 of our confidential draft report, *Study of Printing Products and Services Utilized, Contracted, and Subcontracted by Hawaii State Government*. We ask that you telephone us by Tuesday, October 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 Monday, October 28, 2002.

The Governor, and presiding officers of the two houses of the Legislature have also been provided copies of this confidential 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

BENJAMIN J. CAYETANO
GOVERNOR
SEIJI F. NAYA, Ph.D.
DIRECTOR
SHARON S. NARIMATSU
DEPUTY DIRECTOR
DAVID W. BLANE
DIRECTOR, OFFICE OF PLANNING

DEPARTMENT OF BUSINESS, ECONOMIC DEVELOPMENT & TOURISM

No. 1 Capitol District Building, 250 South Hotel Street, 5th Floor, Honolulu, Hawaii 96813
Mailing Address: P.O. Box 2359, Honolulu, Hawaii 96804
Web site: www.hawaii.gov/dbedt

Telephone: (808) 586-2355
Fax: (808) 586-2377

October 28, 2002

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

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OFC. OF THE AUDITOR
STATE OF HAWAII

Dear Ms. Higa:

Thank you for your letter of October 18, 2002, regarding your confidential draft report, *Study of Printing Products and Services Utilized, Contracted, and Subcontracted by Hawaii State Government.* We welcome the opportunity to respond to the recommendations contained within the report. In general, we find the study very professional and thorough. I have found these "enterprise-wide" analyses of government operations very beneficial.

In the draft before us, however, there are a number of areas that we wish to directly respond to. The section "Monitoring responsibility for subcontracts differs" includes the following statements:

> *The Department of Business Economic Development and Tourism's monitoring practices for compliance with the procurement code printing preference are inconsistent... The State Procurement Office noted that requirements such as pricing of the brochure and identification of whether the printing will be performed in-state or not, should be specified in the proposal.*

This appears to be based upon an oral statement from the State Procurement Office that indicates that subcontracted printing requires the application of the printing preference. Without having the details concerning the specific contract, it is difficult to fully respond to observations regarding print jobs for the "brochures". DBEDT does not include language in its contracts instructing subcontractors of the necessity to have printing performed in-state, nor does DBEDT believe that this is the current state law. It should be noted that, as stated in the report, all DBEDT contracts involving subcontracted printing were in fact performed in-state.

This section also includes the following statements:

> *Despite these factors, the department still did not comply with the State Procurement Office's interpretation of the printing preference requirement in the contract specifications. The noncompliance may be due to the lack of specificity in the procurement code pertaining to the expectations of subcontractors.*

As there are no written clearly-defined State Procurement Office rules and regulations with regard to requirements for preferences involving subcontractors, nor rules on how to calculate these preferences "other than the ability to monitor, inspect, and audit subcontracts," DBEDT does not believe that this is a compliance issue.

When DBEDT enters into a contract, the Contractor is required to fulfill the terms and provisions of said contract. The majority of DBEDT contracts are fixed firm with all subcontractor costs included in the overall cost of the contract. DBEDT, in accordance with the Attorney General's *General Conditions,* is authorized to approve or disapprove any subcontractor the contractor intends to use.

DBEDT contracts include specific deliverables with corresponding payments being made upon the Contractor's satisfactory conveyance of these deliverables. If the product received is not satisfactory, the Contractor must provide a satisfactory product at its own expense. DBEDT deals with the Contractor and the Contractor works with the subcontractor. DBEDT has the right to approve or disapprove of any subcontractor. But in accordance with the terms of the contract, DBEDT works solely with the Contractor to ensure that the contract provisions are satisfactorily provided.

Sincerely,

Seiji Naya