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August 31, 2017

Mr. Darin Early, President
Rhode Island Commerce Corporation
315 Iron Horse Way, Suite 101
Providence, RI, 02908

Dear Mr. Early:

The Office of Internal Audit has completed its limited scope performance audit of the Rhode Island Commerce Corporation. The audit was conducted in accordance with Rhode Island General Laws (RIGL) §35-7.1-1 and with the International Standards for the Professional Practice of Internal Auditing. The recommendations included herein have been discussed with members of management, and we considered their comments in the preparation of this report.

RIGL §35-7.1-10(d), entitled *Annual and interim reports*, states that, "Within twenty (20) days following the date of issuance of the final audit report, the head of the department, agency or public body or private entity audited shall respond in writing to each recommendation made in the final audit report." Accordingly, management submitted its response to the audit findings and recommendations on August XX, 2017, and such response is included in this report. Pursuant to this statute, the Office of Internal Audit may follow up regarding recommendations included in this report within one year following the date of issuance.

We would like to express our sincere appreciation to the staff of the Rhode Island Commerce Corporation for the cooperation and courtesy extended to the members of our team during the course of this audit.

Respectfully yours,

Dorothy Z. Pascale, CPA
Chief

c—Jonathan Womer, Director, Office of Management and Budget, Department of Administration
Honorable William J. Conley, Chairperson, Senate Committee on Finance
Honorable Marvin Abney, Chairperson, House Finance Committee
Peter Keenan, State Controller, Office of Accounts and Control, Department of Administration

Audit Executive Summary

Why the Office of Internal Audit Did This Review

Rhode Island General Law §42-64-38, *Audit of the corporation*, requires the Office of Internal Audit to conduct a performance audit of the Rhode Island Commerce Corporation once every five years. The Office of Internal Audit established an initial five-year schedule; this audit was performed in compliance with the statute and the established schedule.

Background Information

The Rhode Island Commerce Corporation (RICC) is a quasi-public agency, established under Chapter 42-64 of the Rhode Island General Laws to be the State's lead agency for economic development, under the jurisdiction the Executive Office of Commerce. It is the responsible agency to carry out the policies and procedure as established by the Secretary, Governor and the Board of Directors. The agency's purpose is to promote the economic development of the State and general welfare of its citizens, encourage the preservation, expansion, and sound development of new and existing industry, business, commerce, agriculture, tourism, and recreational facilities in the state.

To Strengthen Controls, the Rhode Island Commerce Corporation should:

Incentive Programs

- Develop an integrated technology solution to facilitate internal/external program review.
- Develop a comprehensive written set of operating procedures to memorialize existing incentive program monitoring, application and processing procedures.

Transparency and Accountability

- Ensure transparency information is clearly posted on the Corporation website.
- Ensure adequate documentation exists to support employee requests for expense reimbursement prior to payment.

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Introduction

The Rhode Island Commerce Corporation (RICC) is a quasi-public agency, created under Chapter 42-64 of the Rhode Island General Laws to promote and encourage the preservation, expansion, and sound development of new and existing industry, business, commerce, agriculture, tourism and recreational facilities in the state.

Programs were created by State legislation in 2015 consisting of incentives, grants and tax credits to help grow businesses and create jobs in Rhode Island. The legislation gave RICC the authority and responsibility to create rules and regulations for the programs and to provide oversight. RICC responsibilities include the selection of awardees, executing of agreements, monitoring of compliance with agreements and reporting. Incentive award requests and recommendations are made by RICC staff to the Board of Directors who is responsible for final approval.

As part of this performance audit, the incentives listed in Appendix A and the program aspects were reviewed.

Recommendations and Management's Responses

Incentives Overview

Comprehensive rules and regulations have been created by RICC for the incentive programs based on the requirements of the applicable statutes; most of the programs were active during the audit period. Items observed during this performance audit, conducted during early May 2017 included:

- The need for an integrated technology solution for the Corporation monitoring activities to facilitate internal and external reviews to reduce the risk of recipient misappropriation of incentive funds.
- The need for written operating procedures memorializing the Corporation existing award monitoring, application and processing processes to reduce the risk of overreliance on a single resource.
- The need for of weighting system to support the selection processes for some programs to improve controls over the awarding of incentives or tax credits.

Certain programs where these observations should be implemented are identified and discussed in the following sections of this report.

Program Integrity

Most of the incentives have a "Program Integrity" section within their statutes that reads as follow:

Program integrity being of paramount importance, the commerce corporation shall establish procedures to ensure ongoing compliance with terms and conditions of the program established herein, including procedures to safeguard the expenditure of public funds and to ensure that the funds further the objectives of the program.

At the time of our review, RICC did have manual monitoring procedures in place to ensure continued safeguarding of the expenditure of public funds and compliance with the terms and conditions of each active program. RICC did not have a comprehensive technology solution in place to monitor these programs.

Recommendation:

- 1) Develop written operating procedures to memorialize existing staff actions and undertake a technology solution to monitor incentive programs.

Management's Response:

In 2016, Commerce established a set of rigorous processes that have ensured the appropriate use of economic development funds in a manner that best serves Rhode Island taxpayers. As the Audit correctly notes, Commerce is required by statute to “establish procedures to ensure ongoing compliance with terms and conditions of the [various incentive programs].” Commerce recognizes the “paramount importance” of safeguarding public funds and, subject to these “Program Integrity” provisions as well as other similar mandates (see R.I.G.L. § 42-64-36), has designed and implemented a system that minimizes risks and provides robust accountability.

Prior to awarding incentives under core economic development programs such as the Rebuild Rhode Island tax credit and the Qualified Jobs incentive act, Commerce follows a multi-step risk management process that includes: adopting rules and regulations; releasing and receiving applications; evaluating applications pursuant to Board adopted policies; recommending awards for first-level board review by the Commerce Investment Committee; and recommending awards for second-level review by the full Commerce Board of Directors.

The Audit correctly notes that Commerce has finalized rules and regulations for eleven (11) incentive programs and these codified procedures form the basis of Commerce’s broader risk management and accountability framework. A review of these regulations reveals that they contain numerous written procedures designed to safeguard public funds. For instance, the Rules and Regulations for the Rhode Island Qualified Jobs Incentive Act of 2015 detail a lengthy staff “Review Process” for ensuring that applications comply with both the program’s enabling legislation as well as the Rules and Regulations.

These Rules and Regulations also prescribe the framework for developing incentive agreements; key, formal mechanisms that further govern each award of taxpayer funds. For example, every incentive agreement entered into by Commerce and successful Qualified Jobs Incentive Act applicants includes, among other procedures, the “method for the applicant to annually certify that it has met the unemployment requirements of the Act for each year of the Commitment Period.” Furthermore, the Rules and Regulations spell out formal procedures for Commerce to evaluate whether the applicant has complied with the relevant laws, rules, and regulations—both for the applicant’s initial certification and for future annual certifications. Commerce regularly

evaluates its operating procedures and will continue to codify any procedures that are necessary for the organization's ongoing safeguarding of public funds.

Importantly, no taxpayer funds have been disbursed to successful applicants under key Commerce incentive programs such as the Qualified Jobs incentive act or the Rebuild Rhode Island tax credit. According to plan, Commerce has developed and will continue to develop robust monitoring mechanisms to ensure that projects remain in compliance with statutory and regulatory parameters once funds are disbursed pursuant to these incentive programs. These monitoring mechanisms include a comprehensive technology solution that will manage, collect, track, and report on the incentive programs and investments. Following a request for proposals, on July 24, 2017, the Commerce Board of Directors authorized the organization to contract with Brave River Solutions, LLC for the development of this technology solution. The development of this solution and corresponding written operating procedures is currently underway.

Responsible Party: Chief Financial Officer; Managing Director – Head of Investments
Anticipated Completion Date: December 2017; Ongoing

Program Incentives

Innovation Voucher Program

Rhode Island enterprises with fewer than 500 employees can receive grants up to \$50,000 for research and development assistance from a Rhode Island university or other provider. Thirty-four applications were received, and eleven were awarded for a total of \$451,897. Four of the thirty-four (three approved and one rejected) applications were reviewed; it was noted that while the applications were complete, a scoring section in the template used to summarize each reviewer's analysis was left blank on all review forms. There was no weighted scoring methodology to assign a point value to rank applicants. In addition, the name of the reviewer was missing from one of the four scoring sheets reviewed. Consistent and complete scoring and ranking of applicants based on program requirements is one of the important control components in the selection process. This methodology improves controls and reduces the risks of conflicts of interest and waste or abuse of funds.

Recommendation:

- 2) Convert evaluation sheets to numerically-based scoring sheets to strengthen controls over the evaluation of the application selection process.

Management's Response:

As noted in Commerce's response to the "Program Integrity" section of the Audit, Commerce has developed a set of rigorous processes that have promoted economic development while ensuring the appropriate use of public funds in a manner that best serves Rhode Island taxpayers. The Innovation Voucher Program is designed to spur commercial research and development activity and technology transfer in Rhode Island by prioritizing applicants with the "greatest commercial potential," along with additional criteria that may be considered. See Rules and Regulations for the Innovation Initiative Voucher Program. The program aims to fund "Innovation Projects" across Commerce's targeted industries and awards funds on a rolling basis so that commercially viable

research is not delayed. As the Audit correctly notes, the program utilizes evaluation sheets developed to systematically evaluate the strength of a project’s “commercial potential” across a variety of sectors with a focus on the Corporation’s targeted industry investment strategy, as well as its performance on the factors outlined in the Rules and Regulations. This evaluation approach is in-line with national best practices for innovation-focused initiatives and is the result of a Commerce effort to adopt successful practices identified through a review of evaluation policies employed in other states.

Contrary to the implication in the Audit, the current approach is not without firm controls nor does it increase risks of conflicts, waste, or abuse. Like other key programs such as the Qualified Jobs Incentive Act or the Rebuild Rhode Island Tax Credit, applications are evaluated pursuant to Board adopted policies before awards are recommended by staff for review by the full Commerce Board of Directors. The framework provided in the regulations allows for prioritizing and considering nine factors when deciding which projects are worthy of awards. To address the requirements of the regulations and provide objectivity, evaluators are provided detailed instructions for reviewing applications. Evaluators assess systematically whether each application meets the following standards relative to the nine criteria established in the regulations:

- (1) Weak: Fails to demonstrate competency in the criterion or barely meets requirement of criteria
- (2) Adequate: Meets requirement of the criterion but is not exceptional. Is lacking.
- (3) Exceptional: Exceeds requirements of this criteria. Highly competitive.

Commerce staff use a checklist to document that evaluation sheets are complete and prepare a summary documenting the evaluators’ decisions to recommend, defer, or deny applications. Further, similar to the Qualified Jobs and Rebuild Rhode Island incentive programs noted above, Innovation Voucher recipients enter into an Incentive Agreement with Commerce that details, among other procedures, the performance and milestone reporting requirements needed for recipients to draw each stage of committed funds. If these milestones are not met, funding is withheld.

Commerce does not share the view that numerically-based scoring sheets or a weighted scoring process would strengthen the existing controls in place to ensure applications are fairly and consistently evaluated in accordance with the statute and regulations.

Responsible Party: N/A

Anticipated Completion Date: N/A

Innovation Network Matching Grants

Grants are made to intermediary organizations for projects that offer technical assistance or access to capital to Rhode Island small businesses in key industries. There were seven applications and four awards granted, totaling \$372,996. Our testing sample included two approved and three denied applications. As noted above, the best practice to promote greater transparency and equality is to use a scoring sheet to document the weighing of factors required in the application.

Recommendation:

- 3) Convert evaluation sheets to numerically-based scoring sheets for evaluation and documentation of the application selection process.

Management's Response:

As noted above, Commerce has developed a set of rigorous processes that have promoted economic development while ensuring the appropriate use of public funds in a manner that best serves Rhode Island taxpayers. The Innovation Network Matching Grant program employs an evaluation, award, and implementation process similar to that of the Innovation Voucher program where applications are evaluated pursuant to Board-adopted policies before awards are recommended by staff for review by the full Commerce Board of Directors and an agreement is consummated. The program's design promotes economic development while ensuring the appropriate use of public funds in a manner that best serves Rhode Island taxpayers.

Responsible Party: N/A

Anticipated Completion Date: N/A

Transparency and Accountability

Meet All Transparency Requirements

RIGL 42-64-8.3 *Transparency requirements* state that quasi-public agencies subject to the Act make various documents available to the public by posting the information directly on the agency website. RICC did meet most of the requirements; however, we noted two areas for improvement:

Strategic Plan: RICC formally adopted and posted on the website the Brookings Institution, "*Rhode Island Innovates: A Competitive Strategy for the Ocean State*", January 2016. This report is the corporate strategic plan; however, the report is not clearly identified as such on the website.

Job Descriptions: RICC staff directory section of the website contains brief job descriptions summarizing the role, key functions and responsibilities each team member. However, the Corporation does not have comprehensive job descriptions posted to the website.

All transparency requirements should be clearly posted to the agency website. The agency should consider putting all transparency requirements in one location on the website.

Recommendation:

- 4) Ensure that all required transparency information is posted to the RICC website.

Management's Response:

Strategic Plan: The Audit correctly notes that Commerce's enabling legislation establishes transparency requirements for the organization. To ensure transparency, Commerce is obligated to post an extensive assortment of plans, reports, financial statements, and organizational documents on its website. R.I.G.L § 42-64-8.3. Of the fifteen specific requirements enumerated in

R.I.G.L. § 42-64-8.3, the Audit took issue with Commerce’s approach towards job descriptions of its executive director and management, and strategic plan(s). As the Audit notes, Commerce has posted these required materials on its website.

The Audit notes that R.I.G.L. § 42-64-8.3(6) deems Commerce’s “strategic plans” public records and directs the organization to post relevant records on its website. Commerce has posted this report and, as such, Commerce is in compliance with the statute. Commerce’s strategic plan, the Rhode Island Innovates report, was developed in 2015-2016 in collaboration with the Brookings Institute’s Metropolitan Policy Program, Battelle Technology Partnership Practice and Monitor Deloitte. The Report serves not only as Commerce’s strategic planning document but also as the state’s long-term economic development plan. In January 2016, the Council of Economic Advisors, an entity managed by Commerce, approved the Report as the state’s Long-term Economic Development Vision and Policy as described in R.I.G.L. § 42-64-17.1. The Report is posted to the Commerce website where viewers are prompted to “Review Rhode Island’s new economic strategy and download the report here,” which links to a copy of the Report.

Job Descriptions: The Audit notes that R.I.G.L. § 42-64-8.3(1) calls for the posting of “job descriptions of its executive director and management” on its website. Commerce has posted these descriptions and meets the statutory requirement. For instance, on the site’s “Staff Directory” page, Commerce describes the job of its President as “Overseeing the daily operations of the agency,” while “Play[ing] an integral part in growing the Rhode Island economy and implementing the budget, working with the Executive Office of Commerce and the Governor’s Office.” Similarly, the site describes the job of Commerce’s Managing Director of Financial Services as “Oversee[ing] the Rhode Island Industrial Facilities Corporation bond issuance (RIIFC), Rhode Island Industrial Recreation-Building Authority mortgage insurance (IRBA), Renewable Energy Fund (REF), State Small Business Credit Initiative and the Small Business Loan Fund (SBLF) programs,” in addition to “Manag[ing] the administration, business and policy decisions of the various financial services programs to assure compliance with board actions and policies.” Further job descriptions exist for Commerce’s entire management team including its Executive Vice President of Client Services, Executive Vice President for Business Development, Managing Director and Head of Investments, Chief Financial Officer, and Chief Marketing Officer, as well as for other non-management team members, which is not legislatively required.

Commerce shares the view expressed in the Audit that its significant accountability and transparency mandate is necessary to safeguard the expenditure of public funds, notes the Audit’s recommendation, and will continue to take steps to ensure public access to information.

Responsible Party: N/A

Anticipated Completion Date: N/A

Strengthen Controls Over Travel Expenses and Employee Reimbursements

RICC has adopted a set of employee expense and travel policies as required by RIGL 42-64 to ensure that all employees have clear and consistent requirements for business travel and related expense reimbursement requests.

We tested a sample of fourteen fiscal year 2016 travel reimbursements totaling \$11,757.28, and forty fiscal year 2016 employee mileage reimbursements totaling \$4,417.42 to determine if reimbursements complied with the RICC policies.

Results from selected testing follows:

- Four reimbursements for airfare had appropriate documentation detailing actual airfare costs incurred, but lacked two additional quotes as required by policy.
 - One airfare was reimbursed in full, despite the employee using personal airline points to pay for a portion of the cost.
- Two employee mileage reimbursements greater than 25-miles neglected to include Google map or map quest documentation as required by policy.
- Five employee mileage reimbursements neglected to deduct commuter miles.

To ensure compliance with policies it is important to maintain a strong internal control system over employee reimbursements.

Recommendation:

- 5) Ensure that there is adequate documentation to support the reimbursement of employee expenses prior to payment.

Management's Response:

The Audit notes that Commerce has adopted a specific set of employee expense and travel policies as required by RIGL 42-64 to ensure "employees have a consistent set of requirements for business travel and related expense reimbursement". This policy was adopted on April 3, 2000 and last modified September 7, 2012.

At the time of the policy's most recent modification on September 7, 2012, Commerce implemented a manual set of approval procedures that include the submittal by an employee of a paper based expense report or request for expense reimbursement using an Excel template with corresponding receipt attachments, and depending on the nature and amount of reimbursement request varying levels of manger, accounting and/or executive review.

In order to ensure continued rigor, pace and diligence in processing employee reimbursement expenses requests, Commerce is moving towards an automated solution for expense reporting and management. Commerce has selected a platform, Certify, based on the recommendation of our existing payroll service, CSC Paymaster. Certify is a mobile platform that will upload directly

into CSC Paymaster. This platform will strengthen internal controls over expenditures and improve the overall efficiency and ease of use of the employee reimbursement system.

Commerce shares the view expressed in the Audit that compliance with policies is important to maintain a strong internal control system over employee reimbursements. Commerce will continue to enforce and assess these policies to ensure they are appropriate, while implementing an automated solution for expense reporting and management.

Responsible Party: Chief Financial Officer; Comptroller; Accounting Department
Anticipated Completion Date: Completed; October 2017

Objectives and Scope

The objective of the activity under review was to assess whether RICC is achieving economy, efficiency and effectiveness in the employment of all available resources to achieve its mission and to determine compliance with RIGL §42-64-8., *Transparency requirements established.*

The primary areas that the audit focused on were:

- Transparency Requirements
- Incentive Programs
- Travel and Entertainment Expenses
- Advertising Expenses
- Procurement

Methodology

As part of our audit work, the Office of Internal Audit (OIA) gained an understanding of existing controls in place at the RIRRC for performance management. To address our audit objective, we performed the following:

- Reviewed, documented and gained an understanding of meeting minutes.
- Depicted work flows.
- Identified process control and mission centric risks.
- Assessed the risks.
- Reviewed the third-party vendor contracts.
- Assessed compliance with contractual terms and necessity of contract to mission achievement.
- Noted control or efficiency deficiencies.

The OIA used an external audit firm, Cayer Caccia, LLP (CC), to supplement its staff during the performance of this audit. CC performed the detailed audit work and was selected using a competitive bidding process.

Appendix A

Program Incentives Considered During this Audit

<u>Incentive</u>	<u>Enabling Statute</u>
Rebuild Rhode Island Tax Credit	RIGL §42-64.20
Tax Increment Financing	RIGL §42-64.21
Tax Stabilization Incentive Program	RIGL §42-64.22
First Wave Closing Fund	RIGL §42-64.23
Small Business Assistance	RIGL §42-64.25
Rhode Island Wavemaker Fellowship	RIGL §42-64.26
Main Street RI Streetscape Improvement Program	RIGL §42-64.27
Innovation Voucher Program and Network Matching Grant	RIGL §42-64.28
Industry Cluster Grants	RIGL §42-64.29
Anchor Institution Tax Credit	RIGL §42-64.30
Rhode Island Qualified Jobs Incentive Act	RIGL §44-48.3