CHAPTER 4

Correctional Services Department

Procurement of goods and services for correctional institutions

Audit Commission Hong Kong 28 March 2012 This audit review was carried out under a set of guidelines tabled in the Provisional Legislative Council by the Chairman of the Public Accounts Committee on 11 February 1998. The guidelines were agreed between the Public Accounts Committee and the Director of Audit and accepted by the Government of the Hong Kong Special Administrative Region.

Report No. 58 of the Director of Audit contains 8 Chapters which are available on our website at http://www.aud.gov.hk.

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PROCUREMENT OF GOODS AND SERVICES FOR CORRECTIONAL INSTITUTIONS

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Paragraph



PART 1: INTRODUCTION

1.1 This PART describes the background to the audit and outlines the audit objectives and scope.

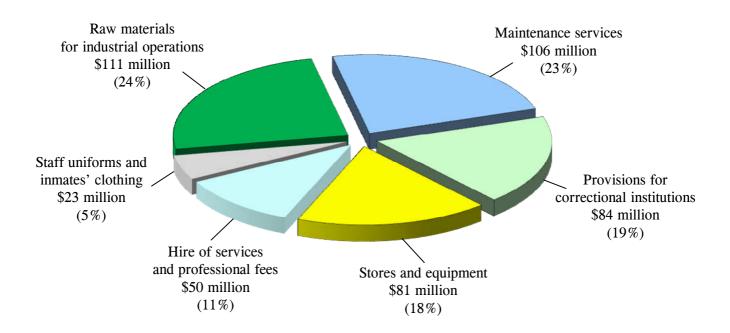
Background

- The Correctional Services Department (CSD) is responsible for the custody of persons committed or sentenced by the courts and those detained under the Immigration Ordinance (Cap. 115). As at 30 September 2011, there were 9,498 inmates in 27 correctional institutions (Note 1). The CSD manages the inmates in accordance with the Prisons Ordinance (Cap. 234). It provides them with food, basic necessities and a reasonable living environment. Appendix A shows the organisation chart of the CSD.
- 1.3 The CSD mainly adopts a centralised approach to procurement. The Central Supplies Unit of the Administration and Planning Division procures goods and services for the operation of all correctional institutions, including coordinating with the Operations Division to procure provisions through open tendering. The Industries Supplies Office of the Rehabilitation Division procures goods and services for the industrial operations managed by the Industries and Vocational Training Section (Note 2). As at 31 December 2011, the Central Supplies Unit and the Industries Supplies Office (each headed by a Senior Supplies Officer) had a total establishment of 27 staff.
- 1.4 Under the Stores and Procurement Regulations (SPRs Note 3), the CSD can make direct purchases of goods not exceeding \$1 million and services not exceeding \$1.43 million. It is required to purchase goods exceeding \$1 million but not exceeding \$1.43 million through the Government Logistics Department (GLD). For purchases of goods and services exceeding \$1.43 million, it is required to adopt tender procedures.
- **Note 1:** There were 14 prisons, 1 detention centre, 3 drug addiction treatment centres, 1 psychiatric centre, 3 half-way houses, and 4 rehabilitation centres and 1 training centre for young offenders.
- **Note 2:** The Section is responsible for managing the industrial operations in providing products to government departments and public sector organisations (e.g. the Hospital Authority) to sustain the gainful employment of inmates during their imprisonment.
- **Note 3:** The SPRs are made by the Financial Secretary/Secretary for Financial Services and the Treasury under the Public Finance Ordinance (Cap. 2).

1.5 In 2010-11, the CSD spent \$455 million on procuring goods and services. Figure 1 shows the breakdown of \$455 million by nature of goods and services procured.

Figure 1

Expenditure on procuring goods and services (2010-11)



Source: CSD records

Audit review

- 1.6 The Audit Commission (Audit) has recently conducted a review of the CSD's procurement of goods and services for correctional institutions to ascertain whether there is room for improvement. The audit review has focused on the following areas:
 - (a) procurement of provisions (PART 2);
 - (b) procurement of goods through direct purchases (PART 3); and
 - (c) procurement of services (PART 4).

Audit has found room for improvement in the above areas and has made a number of recommendations to address the issues.

General audit observations and recommendations

1.7 Procurement is an important process in a department's operation. Overall, this audit review has revealed instances where CSD officers did not strictly comply with the SPRs, particularly the financial limits for direct purchases, in procuring goods and services for correctional institutions. In Audit's view, the CSD needs to conduct an overall review of its procurement procedures and controls, and take effective measures to ensure that CSD officers always comply with the SPRs.

Audit recommendations

- 1.8 Audit has *recommended* that the Commissioner of Correctional Services should, in consultation with the Director of Government Logistics:
 - (a) conduct an overall review of the CSD procedures and controls on the procurement of goods and services for correctional institutions; and
 - (b) based on the review results in (a) above, take effective measures to ensure that CSD officers always comply with the SPRs on all procurement matters.

General response from the Administration

- 1.9 The **Commissioner of Correctional Services** agrees with the audit recommendations in paragraph 1.8. He has said that the CSD is conducting an overall review of the procedures and controls on the procurement of goods and services, and will take measures, where appropriate, to ensure compliance with the SPRs.
- 1.10 The **Secretary for Security** welcomes the audit recommendations in this report. He has said that the CSD will, in consultation with the relevant departments, conduct a review of the procedures and controls on the procurement of goods and services, and take appropriate measures to ensure compliance with the SPRs.
- 1.11 The Secretary for Financial Services and the Treasury agrees with the audit recommendations in this report. He has said that the Financial Services and the Treasury Bureau is prepared to assist the CSD in following up the recommendations in respect of its procurement strategies and compliance with the SPRs.
- 1.12 The **Director of Government Logistics** has said that the GLD stands ready to assist the CSD in the implementation of the audit recommendations in this report regarding procurement practices and adherence to the SPRs.

Acknowledgement

1.13 Audit would like to acknowledge with gratitude the full cooperation of the staff of the CSD during the course of the audit review.

PART 2: PROCUREMENT OF PROVISIONS

- 2.1 This PART examines the procurement of provisions for correctional institutions. The following issues are discussed:
 - (a) planning and monitoring of tendering tasks (paras. 2.5 to 2.10);
 - (b) mandatory requirements on delivery locations (paras. 2.11 to 2.16);
 - (c) mandatory requirements on vehicles, vessel and warehouse (paras. 2.17 to 2.26);
 - (d) mandatory experience requirement (paras. 2.27 to 2.32); and
 - (e) tendering strategy (paras. 2.33 to 2.43).

Provisions for correctional institutions

According to the Prisons Ordinance, the CSD shall provide each inmate with plain and wholesome food. Currently, correctional institutions provide four main and 11 subsidiary dietary scales for inmates, catering for their health, dietary and religious needs (Note 4). CSD contractors supply rice and food items to the institutions for cooking by designated inmates. In addition, a CSD contractor supplies canteen items (e.g. snacks, drinks and cigarettes) to the institutions for purchases by inmates using their earnings from work.

Tendering exercises

2.3 The CSD procures provisions for correctional institutions through open tenders. The last three tendering exercises were conducted in 2004, 2008 and 2011 respectively. In each exercise, the CSD awarded separate contracts for the supply of rice, food items and canteen items for a term of three years (Note 5). The key stages in each exercise are summarised as follows:

- **Note 4:** The dietary scales prescribe the variety and quantity of food. The four main dietary scales are Asian, Curry, Western and Vegetarian. The 11 subsidiary scales are minor variations to the four main scales.
- **Note 5:** For the 2011 tenders, the contract sums for the rice, food item and canteen item contracts were \$34 million, \$344 million and \$84 million, respectively.

- (a) *Planning tendering tasks*. The Administration and Planning Division and the Operations Division jointly draw up a work plan, setting target commencement and completion dates for major tendering tasks;
- (b) **Preparing tender specifications.** The Operations Division prepares the tender specifications (including setting mandatory requirements) as part of the tender documents. For the rice and food item tenders, it needs to review the dietary scales and take account of any revisions to ascertain the variety and quantity of food required. For the food item tender, it also needs to review the marking scheme (introduced in the 2008 tender Note 6) and seek the approval of the Central Tender Board (Note 7) for any revisions;
- (c) **Preparing other tender documents and estimate contract sums.** The Central Supplies Unit prepares other tender documents (e.g. specific tender terms and contract conditions to reflect the CSD's operational requirements). It also estimates the contract sums. It then submits tender requisitions to the GLD for inviting tenders; and
- (d) Evaluating tender offers and prepare tender reports. The CSD forms a tender assessment panel to examine whether the tender offers conform to the specifications, terms and conditions, and to rank them according to the tender prices or overall scores (for the food item tender). A tender report stating the recommendation on the tender to be accepted is submitted to the Central Tender Board for consideration.

Appendix B shows a flowchart of the tendering procedures.

Note 6: The marking scheme gives separate scores for price and non-price assessments, with weightings of 70% and 30% respectively.

Note 7: The Central Tender Board, chaired by the Permanent Secretary for Financial Services and the Treasury (Treasury), is appointed by the Financial Secretary to consider and decide, among others, on the acceptance of tenders for goods and general services exceeding \$10 million. The Board also advises or decides on matters concerning tenders (e.g. approving the use of a marking scheme in tender evaluation).

Audit has examined the 2004, 2008 and 2011 tendering exercises to ascertain whether there is room for improvement in procuring provisions for correctional institutions. The examination has highlighted several issues that warrant the CSD's attention. The issues, namely planning and monitoring of tendering tasks, setting mandatory requirements and reviewing tendering strategy, are discussed in paragraphs 2.5 to 2.43.

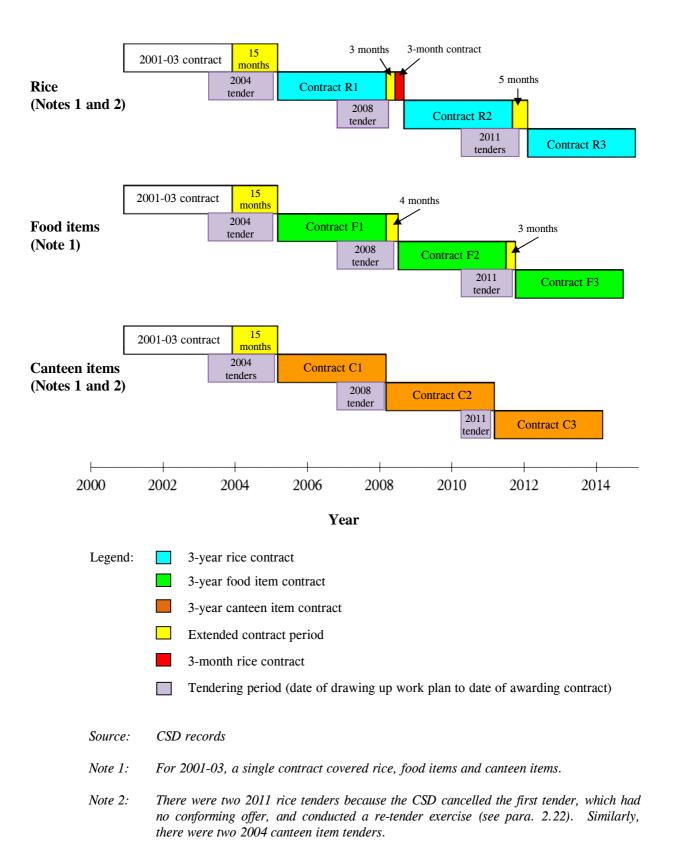
Planning and monitoring of tendering tasks

Tenders not completed in good time

2.5 In the three tendering exercises, the CSD's original work plans were to commence the new contracts immediately after the expiry of the old ones. It transpired that most of the tenders were not completed in good time. Figure 2 shows a time analysis of the three exercises, including the contracts awarded.

Figure 2

Time analysis of 2004, 2008 and 2011 tendering exercises



- 2.6 As shown in Figure 2, for all tenders (except the 2008 and 2011 canteen item tenders), the new contracts could not be awarded before the original contract periods of the old contracts expired. To maintain the supply of provisions to correctional institutions, the CSD extended the old contracts for 3 to 15 months. Details are as follows:
 - (a) **2004 tenders.** The CSD extended the old 2001-03 contract (Note 8) for 15 months as Contracts R1, F1 and C1 could not be awarded in good time;
 - (b) **2008** tenders. The CSD extended Contract R1 for three months and then entered into a three-month contract with the contractor of Contract R1 (Note 9) before it could commence Contract R2. It also extended Contract F1 for four months as Contract F2 could not be awarded in good time; and
 - (c) **2011 tenders.** Similarly, the CSD needed to extend Contract R2 for five months and Contract F2 for three months.

Audit analysis of tendering tasks

2.7 For the 2004, 2008 and 2011 tendering exercises, counting from the date of drawing up a work plan, it took 16 to 24 months to award all the contracts. Audit analysed the various tendering tasks to see whether there were common causes of the delays in completing the exercises. Audit found that the CSD took 3 to 9 months to review the dietary scales and another 3 to 11 months to set or review the marking scheme for evaluating food item tenders, resulting in delays in finalising the tender specifications. Table 1 shows the details.

Note 8: For 2001-03, one single contract covered all provisions. This was because the CSD accepted the offers from the same tenderer for rice, food items and canteen items (see para. 2.33(c) for details).

Note 9: The contractor of Contract R1 was also awarded Contract R2. After approving his request for deferring the commencement date of Contract R2, the CSD entered into a three-month contract with him to maintain the supply of rice.

Table 1

Time taken to review dietary scales and to set or review marking scheme (2004, 2008 and 2011 tenders)

	2004 tender (Month)	2008 tender (Month)	2011 tender (Month)
Reviewing dietary scales (Note 1)	9	3	8
Setting or reviewing marking scheme (Note 2)	_	11	3

Source: CSD records

Note 1: A review of dietary scales includes proposing revisions to dietary scales, calculating the potential cost implications, consolidating comments from individual correctional institutions on the probable inmates' reactions, seeking the endorsement of the Director of Health and obtaining approval from the Security Bureau.

Note 2: The CSD set the marking scheme for evaluating food item tenders in the 2008 tendering exercise and reviewed it in the 2011 exercise. In both exercises, it submitted the proposed schemes to the Central Tender Board and obtained the Board's approval.

Audit observations and recommendation

Audit is concerned that in the 2004, 2008 and 2011 tendering exercises, the CSD did not complete most of the tenders in good time and used contract extensions to maintain the supply of provisions to correctional institutions. Such contract extensions, without open and fair competition, did not provide assurance that best value for money had been achieved. As stated in SPR 520(c), contract extensions should be avoided as far as possible. In Audit's view, the CSD needs to improve its planning and monitoring of tendering tasks to ensure their timely completion, particularly the tasks of reviewing the dietary scales and the marking scheme for the food item tender.

Audit recommendation

2.9 Audit has *recommended* that the Commissioner of Correctional Services should, in future tendering for the supply of provisions to correctional institutions, improve the CSD planning and monitoring of tendering tasks, with a view to completing all the tenders in a timely manner.

Response from the Administration

2.10 The **Commissioner of Correctional Services** agrees with the audit recommendation. He has said that the CSD will take into account the recommendation with a view to completing the tenders in good time.

Mandatory requirements on delivery locations

2.11 The CSD has included mandatory requirements in the tender specifications. If any mandatory requirement is not complied with, a tender will be invalid and will not be considered further. A mandatory requirement set in all the 2004, 2008 and 2011 tenders was that tenderers should confirm that the required goods would be delivered to the designated unloading zone within the specified correctional institutions. Table 2 shows the number of mandatory delivery locations specified in the 2011 tenders.

Table 2

Mandatory delivery locations (2011 tenders)

	Number of delivery locations			
Type of correctional institution	Rice tender	Food item tender	Canteen item tender	
By motor vehicle				
Prison	13	13	13	
Rehabilitation centre (Note 1)	4	4	4	
Half-way house (Note 2)	3	3	_	
Training centre	1	1	1	
Psychiatric centre	1	1	1	
Detention centre	1	1	1	
Sub-total	23	23	20	
By marine vessel (Note 3)	By marine vessel (Note 3)			
Drug addiction treatment centre	3	3	3	
Prison	1	1	1	
Sub-total	4	4	4	
Total	27	27	24	

Source: CSD records

Note 1: Rehabilitation centres provide accommodation to young offenders (aged between 14 and 21) ordered by the court to be detained for receiving disciplinary training. As at 30 November 2011, there were 109 residents in such centres.

Note 2: Half-way houses provide accommodation to persons released under supervision from other correctional institutions for a period of transitional adjustment. As at 30 November 2011, there were 48 residents in such houses.

Note 3: Goods are required to be delivered by vessel to the pier at Hei Ling Chau (an outlying island) for onward delivery to the four institutions located on the island.

- 2.12 As shown in Table 2, both the 2011 rice and food item tenders specified 27 mandatory delivery locations. These included four rehabilitation centres and three half-way houses. However, for three of the four rehabilitation centres and all the three half-way houses, Audit has found that the meals for their residents are cooked and delivered to them by nearby correctional institutions. As such, no routine deliveries of rice or food items are required to be made to these six institutions (Note 10).
- 2.13 Similarly, Audit has found that although the 2011 canteen item tender specified 24 mandatory delivery locations, actually no deliveries of canteen items are required to be made to the four rehabilitation centres included therein. This is because their residents are not required to work and thus do not have earnings to buy canteen items.

Audit observations and recommendations

2.14 Specifying more mandatory delivery locations than actually needed in the tender documents may lead to unnecessarily high contract prices because tenderers would factor in a higher delivery cost in their quotations. In Audit's view, the CSD needs to ensure that the mandatory delivery locations specified in the tender documents properly reflect the actual need.

Audit recommendations

- 2.15 Audit has *recommended* that the Commissioner of Correctional Services should:
 - (a) critically review the mandatory service requirements in the tender documents to ensure that they conform to actual service needs; and
 - (b) in future tendering for the supply of provisions to correctional institutions, ascertain the locations where deliveries are actually needed before incorporating them as a mandatory requirement in the tender documents.

Note 10: According to the CSD, the rehabilitation centres and half-way houses share two emergency rice stores. Rice is delivered to the stores once a month.

Response from the Administration

2.16 The **Commissioner of Correctional Services** agrees with the audit recommendations. He has said that a review is expected to be completed by mid-2012. The CSD will take improvement measures as appropriate based on the review results.

Mandatory requirements on vehicles, vessel and warehouse

2.17 Since the 2008 tenders, the CSD has specified mandatory requirements on motor vehicles, marine vessel and warehouse. Table 3 shows the details of the requirements included in both the 2008 and 2011 tender specifications.

Table 3

Mandatory requirements on vehicles, vessel and warehouse (2008 and 2011 tenders)

	Minimum number required		
	Rice tender	Food item tender	Canteen item tender
Vehicle	6	12	12
Vessel	1	1	1
Warehouse (Note)	_	1	_

Source: CSD records

Note: The warehouse was required to have a storage capacity of not less than 25,000 cubic

metres.

Remarks: Tenderers were required to own or rent the vehicles, vessel and warehouse. If a

tenderer intended to rent them, he was required to produce documentary evidence

(e.g. a rental contract or a copy of letter of intent from the owner).

- Limited number of offers. In its consideration of the CSD's tenders for the supply of provisions to correctional institutions, the Central Tender Board has provided the CSD with advice and comments on the tendering strategy and requirements. In May 2008, in response to the Board's concern that only a limited number of offers had been received for the 2008 canteen item tender, the CSD agreed to review the tender requirements. In respect of the 2011 food item tender, Audit has found that:
 - (a) in January 2011, in seeking the Central Tender Board's approval for the revised marking scheme, the CSD expressed the view that a contractor with his own vehicles, vessel and warehouse would be more capable in maintaining a consistent level of service and in mobilising his resources during emergencies (e.g. inclement weather);
 - (b) later in January 2011, the Central Tender Board deferred considering the revised marking scheme. The Board suggested that the CSD should further consider the possibility of breaking down the contract into smaller ones. It also suggested the CSD to remove the mandatory requirements on vehicles, vessel and warehouse and to only set out clearly the service level requirements in the tender documents:
 - (c) in February 2011, the CSD undertook to conduct a review on its tendering strategy and requirements, and proposed that the 2011 food item tender should not be held up as the review would take a fairly long time; and
 - (d) in March 2011, noting the CSD's undertaking to conduct a review, the Central Tender Board approved the revised marking scheme for the 2011 food item tender.
- 2.19 Audit has identified other issues relating to the requirements on vehicles, vessel and warehouse. Details are set out in paragraphs 2.20 to 2.22.
- 2.20 *Inconsistent vehicle requirements among tenders.* Table 4 shows the delivery requirements for the 2011 tenders as compared with the vehicle requirements.

Table 4

Comparison of delivery and vehicle requirements (2011 tenders)

	Rice tender	Food item tender	Canteen item tender
Number of required deliveries by vehicle	Once a week to 22 locations (twice a week to one location)	Six times a week to 23 locations	Twice a month to 20 locations
Number of vehicles required	6	12	12

Source: CSD records

It can be seen from Table 4 that, as compared to canteen items, rice was required to be delivered more frequently and to more locations. However, 12 vehicles were required for the canteen item tender, doubling the 6 vehicles for the rice tender.

2.21 **Vehicle requirements more than actual need.** Audit examination of the vehicle records of all correctional institutions concerned for November 2011 (Note 11) has revealed that the vehicle requirements in the tender documents were more than the actual need. Table 5 shows the details.

Note 11: The correctional institutions recorded the plate numbers of all vehicles delivering goods to them.

Table 5

Comparison of number of vehicles required and used
(November 2011)

	Rice contract	Food item contract	Canteen item contract
Number of vehicles required in the tender and contract documents	6	12	12
Number of vehicles actually used by contractors per day for deliveries (Note)	3 or less	11 or less	4 or less

Source: CSD records and Audit analysis

Note: In November 2011, the rice, food item and canteen item contractors used a total of 5, 11

and 10 different vehicles, respectively.

As shown in Table 5, the number of vehicles required in the rice tender doubled those actually used for deliveries. For canteen items, the required number tripled the actual number.

2.22 **Rigid vessel specifications.** In 2011, the CSD conducted two rice tenders because a re-tender was required after cancelling the first tender, which had no conforming offers. In the re-tender, the CSD revised the rigid technical specifications for the lifting equipment of the vessel (Note 12) and awarded the contract to the lower of the two conforming bidders. For the 2011 food item and canteen item tenders, the CSD used the same rigid technical specifications as those included in the 2011 cancelled rice tender, and received only one conforming offer (from the incumbent contractor). As such, similar revisions to the vessel specifications may be required in future food item and canteen item tenders (Note 13).

- **Note 12:** In the re-tender, instead of requiring the lifting equipment to conform strictly to the technical specifications, the CSD allowed any lifting equipment meeting the service level requirements.
- Note 13: According to the SPRs, the use of technical specifications at the outset might limit the provision of innovative solutions or new technologies or products which suppliers might be able to offer, and restrict competition. In preparing tender specifications, departments should use functional and performance specifications, supplementing them by a technical specification only if absolutely necessary.

Audit observations and recommendations

- According to SPR 350, departments shall ensure that tender specifications are drawn up in a manner which meets the Government procurement principle of maintaining open and fair competition. Like the Central Tender Board, Audit is concerned about the limited number of tender offers received by the CSD (see para. 2.18), particularly that there was only one conforming offer (from the incumbent contractor) for the 2008 and 2011 food item and canteen item tenders (see para. 2.34). The audit findings in paragraphs 2.20 to 2.22 (including that the vehicle requirements were more than the actual need) suggest that the mandatory requirements on vehicles, vessel and warehouse might have been overly demanding. Besides limiting competition, the requirements may lead to unnecessarily high contract prices because tenderers would factor in a higher compliance cost in their quotations.
- Audit has found that, for similar tenders conducted by the Social Welfare Department and the Hospital Authority (Note 14), the tender specifications did not include similar vehicle, vessel or warehouse requirements. Regarding the CSD's concern about a contractor's capability in maintaining a consistent level of service and in mobilising his resources during emergencies (see para. 2.18(a)), Audit notes that the rice and food item contractors have already been required to maintain emergency stock in individual correctional institutions. In Audit's view, the CSD should critically review its mandatory requirements on vehicles, vessel and warehouse to determine whether they should be removed or revised to enhance competition.

Audit recommendations

- 2.25 Audit has *recommended* that the Commissioner of Correctional Services should:
 - (a) in the light of the limited number of tender offers received and the actual operational need, critically review the mandatory requirements on vehicles, vessel and warehouse; and
 - (b) based on the review results in (a) above, remove or revise the mandatory requirements in future tendering for the supply of provisions to correctional institutions, with a view to enhancing competition and achieving best value for money.

Note 14: The tenders concerned were the Social Welfare Department's 2010 tender for the supply of food to its hostels and the Hospital Authority's 2011 tender for the supply of food items to its hospitals.

Response from the Administration

2.26 The Commissioner of Correctional Services agrees with the audit recommendations. He has said that a review is expected to be completed by mid-2012. The CSD will take improvement measures as appropriate based on the review results.

Mandatory experience requirement

- 2.27 **2008** tenders. For all the 2008 tenders, as a new mandatory requirement, tenderers were required to possess at least three years relevant experience. According to the CSD, the new requirement would ensure the selection of suppliers capable of providing provisions to correctional institutions for the three-year contract period. In February 2008, noting that only one offer in the canteen item tender (from the incumbent contractor) met the minimum experience requirement, the Central Tender Board advised that the CSD should review whether the requirement could be relaxed in order to enhance competition.
- 2.28 **2011 food item and canteen item tenders.** For food items and canteen items, the 2011 tender specifications included the same three-year minimum experience requirement as for 2008. Both tenders had only one conforming offer (from the incumbent contractor).
- 2.29 **2011 rice tenders.** For the first 2011 rice tender, the tender specifications included the same three-year minimum experience requirement as for 2008. Only one offer (from the incumbent contractor) complied with the requirement. However, since the offer did not comply with the vessel specifications, the CSD cancelled the tender (see para. 2.22). In accordance with the Central Tender Board's advice, in the re-tender, the CSD (in addition to revising the vessel specifications) reduced the minimum experience requirement to two years. It awarded the contract to the lower of the two conforming bidders.

Audit observations and recommendations

2.30 As discussed in paragraph 2.23, Audit is concerned about the limited number of tender offers received by the CSD. In Audit's view, like the mandatory requirements on vehicles, vessel and warehouse, the mandatory experience requirement (particularly the three-year requirement for the food item and canteen item tenders) needs to be critically reviewed to determine whether it should be removed or revised to enhance competition.

Audit recommendations

- 2.31 Audit has *recommended* that the Commissioner of Correctional Services should:
 - (a) critically review the mandatory experience requirement, particularly the three-year requirement for the food item and canteen item tenders; and
 - (b) based on the review results in (a) above, remove or revise the requirement in future tendering for the supply of provisions to correctional institutions, with a view to enhancing competition and achieving best value for money.

Response from the Administration

2.32 The Commissioner of Correctional Services agrees with the audit recommendations. He has said that a review is expected to be completed by mid-2012. The CSD will take improvement measures as appropriate based on the review results.

Tendering strategy

Use of three-contract approach

- 2.33 Over the years, the CSD had made a number of changes in its tendering strategy for procuring provisions for correctional institutions, before using the current three-contract approach. Details are as follows:
 - (a) **Before 1997.** The CSD issued one set of tender documents in each tendering exercise. It divided the required provisions into two groups (dietary requirements and canteen items). Tenderers could bid for one or both of the groups. According to CSD records, the contracts from the 1980's to 1997 were awarded to the same contractor as no complete offer was received from other tenderers:
 - (b) **1997** tender. For the 1997 tender, with a view to engendering competition, the CSD further divided each group of provisions by regions for bidding by tenderers (Note 15). It received four offers. The incumbent contractor submitted the lowest offers for all regions and therefore won the tender;

Note 15: There were four regions, namely Hong Kong Island, Kowloon, the New Territories and the outlying islands.

- (c) **2000 tender.** For the 2000 tender (whereby the 2001-03 contract was awarded), the CSD divided the required provisions into three groups (rice, food items and canteen items) for bidding by tenderers. For this tender (and subsequent ones), it did not further divide the three groups by regions. There were four conforming offers for both the rice and canteen item groups and three for the food item group. As the incumbent contractor won all the three groups, he was awarded a contract covering all provisions; and
- (d) **2004 onwards.** In each exercise, the CSD awarded separate contracts for the supply of rice, food items and canteen items for a term of three years (see para. 2.3). Table 6 summarises the results of the 2004, 2008 and 2011 tenders.

Table 6

Results of using three-contract approach (2004, 2008 and 2011 tenders)

	2004 tenders	2008 tenders	2011 tenders
Rice			
Number of offers	4	2	4
Number of conforming offers	4	1	2
— Contractor	В	В	С
Food items — Number of offers	3	2	4
Number of conforming offers	1	1	1
— Contractor	A	A	A
Canteen items			
Number of offers	3	1	2
Number of conforming offers	1	1	1
— Contractor	A	A	A

Source: CSD records

Remarks: 1. For rice, only the results of the 2011 re-tender are shown. Similarly, for canteen items, the results of the 2004 re-tender are shown.

2. Contractor A was the contractor for all the contracts from the 1980's to 2003 (see para. 2.33(a) to (c)).

Limited number of tender offers

As shown in Table 6, for the 2008 and 2011 food item and canteen item tenders, only the incumbent contractor submitted a conforming bid. For rice, there were only one conforming offer for the 2008 tender and two for 2011. In considering the relevant tenders, the Central Tender Board has expressed concerns about the limited number of tender offers (see para. 2.18). It has suggested that the CSD should make attempts to explore more sources of supply and enhance competition, including conducting market research and reviewing the tendering strategy and requirements.

- 2.35 In response to the Central Tender Board's suggestions, the CSD has expressed the following concerns:
 - (a) **Standard of food items.** The disparity in the quality and standard of the food items among regions with different suppliers would become excuses for inmates and might create disruption to the operation of the correctional institutions;
 - (b) Security of institutions. The increase in number of suppliers entering the delivery locations, some of which are restricted areas, is undesirable from the security point of view; and
 - (c) *Increase in workload.* The increase in delivery frequency caused by the larger number of suppliers would increase the workload of correctional institutions.
- 2.36 The Central Tender Board has expressed the following views:
 - (a) the quality of food items to be provided by different suppliers would not be materially different as the specifications of the food items have been set out clearly in the tender and contract documents; and
 - (b) by engaging more than one supplier, the CSD can enhance its bargaining power and secure a fall-back position in the case of a disruption in supply from one of the suppliers.

As mentioned in paragraph 2.18(c) and (d), the Board has noted the CSD's undertaking to conduct a review of the tendering strategy and requirements.

Market research

2.37 **2007** *market research*. In October 2007, in seeking approval for introducing certain new mandatory requirements (see paras. 2.17 and 2.27) and a marking scheme in the 2008 food item tender, the CSD informed the Central Tender Board that according to its market research, at least four potential tenderers could meet the mandatory requirements. In the event, there were only two offers meeting such requirements (Note 16). On enquiry, the CSD could not produce the records of the market research for Audit examination.

Note 16: As one of the two offers failed to meet certain passing mark requirements in the marking scheme, the other offer (from the incumbent contractor) was the only conforming offer.

2.38 2010 market research. In early 2010, in response to the Central Tender Board's suggestion to explore more sources of supply, the CSD conducted another market research. According to the CSD, the research aimed to find out how many suppliers might submit tenders if the tendering strategy and requirements were not changed. The CSD provided suppliers with the critical terms and conditions of the existing contracts, and invited them to quote prices for the supply of the required rice, food items and canteen items (without requiring them to confirm or provide documents to support that they could meet the mandatory requirements). Table 7 shows the research results. In late 2010, in seeking the Board's approval for the revised marking scheme for the 2011 food item tender, the CSD informed the Board that three suppliers could "meet the mandatory tender requirements and specifications", which did not tally with the research results (Note 17). It transpired that there was, again, only one conforming offer (from the incumbent contractor).

Table 7

Results of 2010 market research

	Rice	Food items	Canteen items
Number of suppliers invited	100	88	85
Number of suppliers quoting prices for all required items (Note)	5	3	2
Number of suppliers quoting prices for some required items only	_	2	1

Source: CSD records

Note: The numbers include the incumbent contractor.

Note 17: As shown in Table 7, the research results only indicated that three suppliers had quoted prices for all required food items. There were no confirmations or supporting documents indicating that they could "meet the mandatory tender requirements and specifications".

Tender prices

Table 8 shows that, for the 2004, 2008 and 2011 food item tenders, the tender sums were significantly higher than the CSD's pre-tender estimates. Also, the 2011 tender sum of \$344 million represents a 95% increase from the 2004 tender sum of \$176 million. From 2004 to 2011, the index for food in the Consumer Price Index (A) increased by 52% only (Note 18), while the average daily number of inmates actually decreased by 22%.

Table 8

Comparison of tender sums and pre-tender estimates (2004, 2008 and 2011 food item tenders)

	2004 tender (\$ million)	2008 tender (\$ million)	2011 tender (\$ million)
Tender sum	176	244	344
Pre-tender estimate	135 (100%)	185 (100%)	303 (100%)
Difference	41 (30%)	59 (32%)	41 (14%)

Source: CSD records

Audit observations and recommendations

Audit shares the Central Tender Board's concern about the limited number of tender offers received by the CSD (see para. 2.23). Audit also agrees with the Board's suggestions that the CSD should make attempts to explore more sources of supply and enhance competition (see para. 2.34). Given that the contract prices for food items obtained under the current three-contract approach have been consistently higher than the pre-tender estimates by significant margins and have been on a steep increase (see Table 8), Audit considers that the CSD particularly needs to review its tendering strategy to determine what revisions are required to obtain more competitive tenders.

Note 18: In February 2012, upon Audit enquiry, the GLD indicated that: (a) while the index for food in the Consumer Price Index (A) was one of the indicators reflecting the price trend of the food item tenders, the increases in prices for some basic food items of the dietary scales were much more than that of the index; and (b) as most of the food items were from the Mainland and the contractor was required to deliver to various correctional institutions, the appreciation of the Renminbi against the Hong Kong Dollar and the rise in fuel cost would also have pressures on the prices.

- 2.41 As regards market research, Audit considers that there is room for improvement, as follows:
 - (a) **Record keeping.** As mentioned in paragraph 2.37, the CSD could not produce the records of the 2007 market research for Audit examination. In Audit's view, the CSD needs to keep proper records of market research for meeting operational needs and providing accountability;
 - (b) **Research methodology.** The CSD conducted the 2010 market research by inviting suppliers to give quotations based on the existing tendering strategy and requirements (see para. 2.38). The methodology cannot effectively gauge the market response under different contract arrangements (e.g. splitting the contracts into smaller ones in different ways). In Audit's view, the CSD needs to use a research methodology that can test out different tendering and contracting strategies, with a view to exploring more sources of supply; and
 - (c) **Research findings.** The CSD's conclusion of the 2010 market research in paragraph 2.38 did not tally with the research results. In Audit's view, the CSD needs to draw proper conclusion from research results to support decision making.

Audit recommendations

- 2.42 Audit has *recommended* that the Commissioner of Correctional Services should:
 - (a) in view of the limited number of tender offers received, review the current three-contract approach for procuring provisions for correctional institutions;
 - (b) based on the review results in (a) above, revise the tendering strategy where appropriate, with a view to maintaining open and fair competition and achieving best value for money;
 - (c) keep proper records of market research for meeting operational needs and providing accountability;
 - (d) use a research methodology that can test out different tendering and contracting strategies, with a view to exploring more sources of supply; and
 - (e) ensure that the conclusion of a market research tallies with the research results.

Response from the Administration

2.43 The Commissioner of Correctional Services agrees with the audit recommendations. He has said that a review is expected to be completed by mid-2012. The CSD will take improvement measures as appropriate based on the review results.

PART 3: PROCUREMENT OF GOODS THROUGH DIRECT PURCHASES

- 3.1 This PART examines the following issues relating to the procurement of goods through direct purchases:
 - (a) repeated same-day direct purchases from same supplier (paras. 3.6 to 3.12);
 - (b) repeated direct purchases of goods used regularly (paras. 3.13 to 3.17); and
 - (c) authorisation of direct purchases (paras. 3.18 to 3.21).

Financial limits

3.2 According to the Guide to Procurement issued by the Financial Services and the Treasury Bureau, achieving best value for money and maintaining open and fair competition are the twin policy objectives for government procurement. The SPRs require departments to adopt different types of procedures for procuring goods within different financial limits. Table 9 shows the requirements applicable to the CSD.

Table 9

Types of procedures for procuring goods

SPR	Financial limits	Procurement procedures
220	Over \$1.43 million	Tender
240	Over \$1 million to \$1.43 million	Procurement through GLD (invite at least five quotations)
260(b)	Over \$50,000 to \$1 million	Direct purchases (invite at least five quotations)
260(a)	Over \$5,000 to \$50,000	Direct purchases through purchasing cards (invite more than one quotation)
265(a)	\$5,000 or less	Direct purchases through purchasing cards or in cash (obtain reasonable rates)

Source: SPRs

Remarks: All departments are delegated the authority to make direct purchases of goods not exceeding \$500,000. This financial limit is raised to \$750,000 for departments with Supplies Officers, \$1 million for departments with Senior Supplies Officers (e.g. the CSD) and \$1.43 million for departments with Chief Supplies Officers or above.

- 3.3 *Compliance with financial limits.* The SPRs have the following provisions on the compliance with the financial limits:
 - (a) Interpret financial limits strictly. SPR 205 provides that the financial limits refer to the total value of stores or services of a similar nature which, in normal practice, are obtained in a single purchase. Controlling Officers shall ensure that officers responsible for procurement matters interpret these limits strictly, and that they do not evade the limits by dividing procurement requirements into instalments or by reducing the usual duration of contracts; and
 - (b) Not to make repeated purchases exceeding financial limits. SPR 246 provides that departments may only make repeated direct purchases of the same items within 12 months if the cumulative value of the purchases does not exceed the direct purchase authority limits (i.e. \$1 million for the CSD). If departments have to use a particular item regularly in quantities with a value in excess of the respective direct purchase authority limits, they shall purchase it through the GLD.

Procedures for making direct purchases

3.4 The Central Supplies Unit invites suppliers' quotations after receiving procurement requests from correctional institutions, and normally selects the lowest conforming offer. After obtaining the approval of the approving officer, the Unit places an order with the selected supplier or makes the purchase through purchasing card or in cash, as required. The Industries Supplies Office adopts similar procedures in making direct purchases for the industrial operations managed by the Industries and Vocational Training Section.

Audit examination of direct purchases

Audit has sample checked the CSD's direct purchases of goods made between 2009 and 2011. Audit has found issues requiring the CSD's attention. The issues are discussed in paragraphs 3.6 to 3.21.

Repeated same-day direct purchases from same supplier

3.6 Audit has found nine cases (Cases A to I) of repeated same-day direct purchases of items of a similar nature from the same supplier. The nine cases involved a total of 24 purchases (Purchases 1 to 24). Details are at Appendix C. The audit findings are set out in paragraphs 3.7 to 3.9.

- 3.7 **Procurement requests.** Upon enquiry, the CSD could not produce for Audit examination the procurement requests for six purchases in two cases (Purchases 3 and 4 in Case B and Purchases 13 to 16 in Case F). Audit examination of the procurement requests in the other seven cases has revealed that:
 - (a) for each of six cases (Cases A, C, E and G to I), there were two or three procurement requests, but all were initiated by the same institution. For each such request, the CSD obtained the required goods by making a separate purchase; and
 - (b) for the remaining case (Case D), there was only one procurement request. The CSD obtained the required goods by making three purchases.

3.8 *Cases A to F.* For each case:

- (a) the total procurement requirements exceeded \$50,000, ranging from \$58,575 to \$247,567;
- (b) according to SPRs 205 (see para. 3.3(a)) and 260(b) (see Table 9 in para. 3.2), the CSD should have obtained the goods in a single direct purchase, by inviting at least five quotations. This was particular so for Case D, which had only one procurement request; and
- (c) however, instead of making one direct purchase, the CSD used purchasing cards to make two to five direct purchases of less than \$50,000 each from the same supplier on the same day (after inviting two or three quotations for each purchase).

3.9 *Cases G to I.* For each case:

- (a) the total procurement requirements exceeded \$1.43 million;
- (b) according to SPRs 205 and 220 (see Table 9 in para. 3.2), the CSD should have adopted tender procedures to procure the goods; and
- (c) however, instead of tendering, the CSD made two or three direct purchases of less than \$1 million each from the same supplier on the same day (after inviting 10 to 14 quotations for each purchase).

Audit observations and recommendations

3.10 SPR 205 requires Controlling Officers to ensure that their officers interpret the financial limits strictly and do not evade them by dividing procurement requirements. In mid-January 2012, in response to Audit enquiry, the CSD said that its officers had arranged bulk purchases to meet procurement requests received since August 2011, inviting at least five quotations in each case. While Audit welcomes the CSD's initiative, Audit considers that the CSD still needs to look into the nine cases of repeated same-day direct purchases from the same supplier (i.e. Cases A to I) and further improve its procedures and controls on the procurement of goods. In particular, the top management of the CSD should impress on all officers concerned the importance of compliance with the SPRs.

Audit recommendations

- 3.11 Audit has *recommended* that the Commissioner of Correctional Services should:
 - (a) look into Cases A to I to ascertain why the CSD officers concerned did not comply with the SPRs, and take appropriate follow-up actions;
 - (b) improve the procedures and controls on the procurement of goods through direct purchases to ensure that CSD officers always comply with the SPRs and do not evade financial limits by dividing procurement requirements;
 - (c) regularly remind all CSD officers concerned about the department's commitment to strictly comply with the SPRs; and
 - (d) remind CSD officers to maintain proper records of procurement requests.

Response from the Administration

- 3.12 The **Commissioner of Correctional Services** agrees with the audit recommendations. He has said that:
 - (a) for the Central Supplies Unit, an upgrading of its existing Procurement Information System is underway to strengthen the controls. The upgraded system will include, among other enhancement measures, regular production of management information reports on all direct purchases of goods with similar description. Based on the reports, timely information about direct purchases will be available for viewing and inspection before arranging direct purchases. It is expected that the system will be ready for live run in the latter part of 2012; and

(b) for the Industries and Vocational Training Section, a computerised Contract Monitoring Scheme is being developed to maintain its purchase records to ensure that all purchases are made in accordance with SPR 205. The system will be implemented in September 2012.

Repeated direct purchases of goods used regularly

- 3.13 Audit has also found other repeated direct purchases of less than \$50,000 each for goods used regularly by correctional institutions, as follows:
 - (a) *Inmates' sandals*. In 2010-11, by 28 repeated direct purchases, the CSD procured a total of 42,900 pairs of sandals from the same supplier with a cumulative value of \$1.01 million, exceeding the limit of \$1 million specified in SPR 246 (see para. 3.3(b)). Between April and November 2011, by 24 repeated direct purchases, it procured a total of 43,830 pairs of sandals from the same supplier with a cumulative value of \$1.03 million, also contrary to SPR 246;
 - (b) *Inmates' canvas shoes.* In 2010-11, by 14 repeated direct purchases, the CSD procured a total of 42,750 pairs of canvas shoes from the same supplier with a cumulative value of \$590,000; and
 - (c) *Inmates' vests.* In 2010-11, by 15 repeated purchases, the CSD procured a total of 11,936 vests from the same supplier with a cumulative value of \$742,000.

Audit observations and recommendations

- As shown in Table 9 in paragraph 3.2, SPR 260(a) only requires inviting more than one quotation for direct purchases not exceeding \$50,000 each through purchasing cards. It is inappropriate to repeatedly use such procedures for purchasing regularly used goods (of a larger total value) as the limited competition cannot assure that best value for money is achieved. In Audit's view, the CSD needs to procure such goods in bulk using tender or other more competitive procedures, with a view to obtaining more competitive prices from suppliers.
- 3.15 In addition, the non-compliance with SPR 246 for two consecutive years (i.e. the CSD's repeated direct purchases of sandals see para. 3.13(a)) suggests that the CSD has not established effective controls to ensure compliance. In Audit's view, the CSD needs to rectify the situation. It should purchase regularly used goods through the GLD in accordance with SPR 246 when their values exceed its direct purchase authority limit of \$1 million.

Audit recommendations

- 3.16 Audit has *recommended* that the Commissioner of Correctional Services should:
 - (a) procure goods regularly used by correctional institutions in bulk using tender or other more competitive procedures, instead of making repeated direct purchases of less than \$50,000 through purchasing cards;
 - (b) establish effective controls to ensure compliance with the financial limit for repeated direct purchases specified in SPR 246; and
 - (c) purchase regularly used goods through the GLD when their values exceed the CSD's direct purchase authority limit.

Response from the Administration

3.17 The **Commissioner of Correctional Services** agrees with the audit recommendations. He has said that appropriate action will be taken to implement them.

Authorisation of direct purchases

- 3.18 The SPRs specify detailed requirements on approving acceptance of offer before making a direct purchase. Audit sample check of the CSD's direct purchases has revealed instances of non-compliance with the requirements, as follows:
 - (a) **Purchase without approval.** In a direct purchase of sandals in 2009, the CSD received four offers (ranging from \$285,000 to \$705,000). The highest offer of \$705,000 was accepted without documented justifications. Up to 31 December 2011, no approval of acceptance of offer had been given for this purchase; and
 - (b) **Purchases without prior approval.** In a direct purchase of leather gloves at \$350,000 in 2010, approval of acceptance of offer was given only 133 days after the order was placed. Similarly, for 10 direct purchases not exceeding \$50,000 each between April and June 2011, approvals of acceptance of offer were given only 6 days to 2.5 months after the goods were delivered to the correctional institutions (Note 19).

Note 19: In mid-January 2012, the CSD informed Audit that the user sections had arranged and approved the 10 purchases before submitting their procurement requests to the Central Supplies Unit. The CSD had asked the user sections to follow proper procedures since August 2011.

Audit observations and recommendations

3.19 Audit is concerned that the direct purchases mentioned in paragraph 3.18 had been made before approvals of acceptance of offer were given, particularly for the higher-value ones. In Audit's view, the CSD needs to look into the cases and take measures to prevent recurrence.

Audit recommendations

- 3.20 Audit has *recommended* that the Commissioner of Correctional Services should:
 - (a) find out the control weaknesses that have resulted in CSD officers making direct purchases before obtaining approval of acceptance of offer; and
 - (b) take measures to rectify the control weaknesses.

Response from the Administration

- 3.21 The **Commissioner of Correctional Services** agrees with the audit recommendations. He has said that:
 - (a) to ensure that proper approval is obtained before placing an order, standard forms have been adopted for making direct purchases and all staff responsible for arranging direct purchases have been briefed on the proper procedures to be followed in future; and
 - (b) regarding the direct purchase without approval mentioned in paragraph 3.18(a), despite the fact that the detailed evaluation report has not been properly filed, the then Head of the Central Supplies Unit confirmed in March 2012 that the highest offer of \$705,000 was the only conforming offer. Covering approval of acceptance of the offer was given in March 2012.

PART 4: PROCUREMENT OF SERVICES

- 4.1 This PART examines issues relating to the procurement of the following services:
 - (a) maintenance services (paras. 4.3 to 4.15); and
 - (b) cleaning services (paras. 4.16 to 4.28).

Financial limits

4.2 As mentioned in paragraph 3.2, achieving best value for money and maintaining open and fair competition are the twin policy objectives for government procurement. Table 10 shows the different types of procurement procedures which departments are required by the SPRs to adopt when procuring services within different financial limits.

Table 10

Types of procedures for procuring services

SPR	Financial limits	Procurement procedures
220	Over \$1.43 million	Tender
280(c)	Over \$50,000 to \$1.43 million	Direct procurement (invite at least five quotations)
280(b)	Over \$5,000 to \$50,000	Direct procurement through purchasing cards (invite more than one quotation)
290	\$5,000 or less	Direct procurement through purchasing cards or in cash (obtain reasonable rates)

Source: SPRs

Maintenance services

Service level agreement

- 4.3 According to Financial Circular No. 6/2001 issued in August 2001, a Controlling Officer can choose to enter into a service level agreement with a trading fund direct, without recourse to competitive bidding, if he is clearly satisfied that:
 - (a) the trading fund is fully capable of delivering in a cost-effective manner specific services that his department needs; and
 - (b) having regard to the circumstances of the case (such as the urgency or the special circumstances of the services required), inviting competitive bidding for the delivery of such services is not appropriate.

The Controlling Officer will be accountable for the decision on why competitive bidding is not appropriate.

- 4.4 The CSD has been using the maintenance services of the Electrical and Mechanical Services Trading Fund (EMSTF) direct, without recourse to competitive bidding. The current service level agreement has a term of 10 years (from 2008-09 to 2017-18), with an option to terminate it after the first five years. Under the agreement, the EMSTF provides maintenance services to ensure that the CSD's systems and equipment (e.g. closed circuit television systems and radio communication systems) and vehicle fleet are in a safe and efficient condition, and in compliance with relevant statutory requirements.
- 4.5 The CSD pays an annual basic fee to the EMSTF, which is subject to the following adjustments:
 - (a) Variation in quantities of systems and equipment. The amount of adjustment is calculated by applying unit charging rates to the number of systems and equipment concerned;
 - (b) *Variation in number of vehicles.* Adjustment is made according to the changes in fleet size, service scope and performance level; and
 - (c) *Variation in cost of labour and materials.* The adjustment is based on a factor derived from the EMSTF's cost structure.

In addition, the CSD pays additional charges for corrective maintenance exceeding the cost limits specified in the service level agreement.

4.6 Table 11 shows the maintenance charges for 2008-09 to 2010-11.

Table 11

Maintenance charges (2008-09 to 2010-11)

	2008-09 (\$ million)	2009-10 (\$ million)	2010-11 (\$ million)
Systems and equipment			
Annual basic fee	76.2	80.1	83.1
Other maintenance charges	2.8	3.6	7.6
Sub-total	79.0	83.7	90.7
Vehicle fleet			
Annual basic fee	5.6	5.5	5.7
Other maintenance charges	0.7	0.9	1.2
Sub-total	6.3	6.4	6.9
Total	85.3	90.1	97.6

Source: Audit analysis of CSD records

Performance targets

4.7 The service level agreement specifies a service availability target of 92% for all vehicles. Table 12 shows the performance targets for systems and equipment.

Table 12
Performance targets for systems and equipment

		Compliance level	
Service item	Performance targets	(2008-09 to 2012-13)	(2013-14 to 2017-18)
Service availability of major systems (Note 1)	95% to 99%	Not applicable (Note 2)	Not applicable (Note 2)
Response time for system failure call (Note 3)	30 minutes to 5 days	75%	80%
Time to complete repair work (Note 4)	1 to 7 days	75% to 95%	80% to 95%

Source: CSD records

- Note 1: Service availability targets are set for electricity supply distribution, air-conditioning installation, fire service installation, lift and escalator installation, laundry equipment, steam and hot water supply and electronics systems.
- Note 2: The service level agreement states that compliance level is not applicable to service availability targets for major systems.
- Note 3: Target response times are set for building services, and urgent and non-urgent calls for electrical and mechanical engineering and electronics services.
- Note 4: Targets are set for urgent and non-urgent repair work.

Critical venues

- 4.8 The service level agreement specifies the following services for critical venues:
 - (a) *Emergency and contingency programme*. The EMSTF will develop contingency plans for critical venues of the CSD (e.g. Stanley Prison), and will review and update the plans biennially;
 - (b) Safety assessment. The EMSTF will provide advisory services to improve/enhance safety of some critical venues of the CSD such as workshop and major plant rooms; and

(c) *Maintenance charges*. The EMSTF will provide a charge breakdown for each critical venue so as to facilitate the CSD's in-house expenditure control and monitoring.

However, in response to enquiry, the CSD has informed Audit that "critical venues" are not defined in the agreement and it has not agreed with the EMSTF on what venues should be classified as critical venues for the purposes of the agreement. As a result, the EMSTF has yet to provide the specified services.

Audit observations and recommendations

Need to define critical venues

Audit considers that, at the outset, the service level agreement should have a definition of "critical venues" in order to stipulate clearly the scope of the specified services. While the Stanley Prison is cited in the agreement as an example of critical venues (see para. 4.8(a)), the EMSTF has not yet provided the specified services for the prison and the CSD has taken no follow-up action. In Audit's view, the CSD needs to take urgent action to agree with the EMSTF on what venues should be classified as critical venues and ensure that the EMSTF provides the specified services for all such venues as soon as possible. The CSD also needs to ensure that significant terms are clearly defined in future agreements.

Need to monitor performance

According to the service level agreement, on request of the CSD, the EMSTF is required to submit an annual report on its actual performance as compared with the specified performance targets (see para. 4.7). However, since the commencement of the agreement in April 2008 and up to October 2011, the CSD had not made such request. On Audit enquiry, the CSD obtained the 2010-11 annual report from the EMSTF. According to the report, the EMSTF achieved the service availability target for vehicles, the target response times for system failure calls and the target times for repairs. However, the report did not show the actual service availability for major systems as required by the agreement. In addition, as indicated in Note 2 to Table 12 in paragraph 4.7, the agreement does not set out clearly to what extent the EMSTF should achieve the service availability targets for major systems. On Audit enquiry, the CSD indicated that the EMSTF had yet to set the compliance levels for the major systems.

4.11 In Audit's view, the CSD needs to monitor the performance of the EMSTF's maintenance services, including reviewing the EMSTF's annual performance report, so as to take appropriate follow-up action where the performance is not satisfactory. In this connection, the CSD needs to ensure that the EMSTF's annual performance report shows the actual performance against all performance targets, including those for service availability of major systems. The CSD also needs to follow up with the EMSTF on setting the compliance levels for the service availability targets for major systems.

Need to review cost-effectiveness

4.12 As mentioned in paragraph 4.3, Financial Circular No. 6/2001 requires a Controlling Officer to be clearly satisfied with the cost-effectiveness of the services of a trading fund before entering into a service level agreement with the trading fund direct, without recourse to competitive bidding. The CSD had not conducted a review of the cost-effectiveness of the EMSTF's maintenance services before it entered into the current 10-year agreement direct. In Audit's view, such cost-effectiveness review helps ensure compliance with the requirements of Financial Circular No. 6/2001 and achieve value for money.

Audit recommendations

- 4.13 Audit has *recommended* that the Commissioner of Correctional Services should:
 - (a) agree with the EMSTF without delay on what venues should be classified as critical venues for the purposes of the service level agreement between the CSD and the EMSTF;
 - (b) for the critical venues in (a) above, ensure that the EMSTF provides the services as specified in the service level agreement as soon as possible;
 - (c) ensure that significant terms like "critical venues" are clearly defined in future service level agreements;
 - (d) monitor the performance of the EMSTF's maintenance services, including reviewing the EMSTF's annual performance report, and take appropriate follow-up action where the performance is not satisfactory;
 - (e) ensure that the EMSTF's annual performance report shows the actual performance against all performance targets, including those for service availability of major systems;

- (f) follow up with the EMSTF on setting out in the service level agreement clearly the compliance levels for the service availability targets for major systems; and
- (g) review the cost-effectiveness of the EMSTF's services before choosing to use the services direct.

Response from the Administration

- 4.14 The **Commissioner of Correctional Services** agrees with the audit recommendations. He has said that action is being taken to implement them.
- 4.15 The **Director of Electrical and Mechanical Services** has said that:
 - (a) the EMSTF will work together with the CSD to implement the audit recommendations; and
 - (b) regarding the compliance levels for the service availability targets for major systems, the term "Not applicable" stated in the service level agreement actually means that the EMSTF will fully comply with the targets (i.e. 100% compliance level). He agrees that the term has caused confusion and the EMSTF will confirm the compliance levels with the CSD accordingly.

Cleaning services

Direct procurement

4.16 The CSD uses direct procurement procedures to obtain cleaning services for common areas in the offices, quarters and compounds of correctional institutions. It adopts a set of standard contract terms for the cleaning service contracts. It also standardises the service requirements and incorporates them into the contracts in the form of schedules of duties, cleaning schedules and schedules of minimum labour force. Currently, there are 13 cleaning service contracts (Contracts 1 to 13). A list of the contracts is at Appendix D.

Contract values

4.17 The value of each cleaning service contract is between \$0.08 million and \$1.42 million, not exceeding \$1.43 million. Under SPR 220 (see Table 10 in para. 4.2), departments are required to adopt tender procedures when procuring services exceeding \$1.43 million.

Contract scopes

4.18 Each contract covers one to six correctional institutions. The CSD generally groups institutions under a contract when they are near to each other.

Contract durations

4.19 The duration of each contract is either 12, 18 or 24 months. There are no documented justifications for awarding contracts of different durations.

Audit comparison of current and old contracts

- 4.20 Awarding a contract of a smaller scope or a shorter duration generally results in a smaller contract value. Audit has compared the scopes and durations of the current and the old contracts (i.e. the immediately preceding ones). Four current contracts have smaller scopes or shorter durations as compared with the old ones. Details are discussed in paragraphs 4.21 and 4.22.
- 4.21 Awarding contracts of smaller scopes. After the expiry of the old contract covering both Correctional Institution A and the nearby Correctional Institution B, the CSD awarded a separate contract for each institution, without documented justifications. Table 13 shows the details.

Table 13

Awarding contracts of smaller scopes

	Correctional institutions covered	Duration (Month)	Value (\$ million)
Old contract	Correctional Institution A and Correctional Institution B	12	1.27
Current contracts	Correctional Institution A	12	0.96
Current contracts	Correctional Institution B	12	0.59

Source: Audit analysis of CSD records

Table 13 shows that if there had been only one current contract covering both institutions as for the old contract, its contract value would likely have exceeded \$1.43 million (i.e. tender procedures would have been required).

4.22 Awarding contracts of shorter durations. After the expiry of two 24-month contracts (for Correctional Institution C and Correctional Institution D respectively), the CSD awarded two 18-month contracts, without documented justifications. Table 14 shows the details.

Table 14

Awarding contracts of shorter durations

	Duration (Month)	Value (\$ million)		
Correctional Institution C				
Old contract	24	1.16		
Current contract	18	1.26		
Correctional Institution D				
Old contract	24	1.21		
Current contract	18	1.16		

Source: Audit analysis of CSD records

Table 14 shows that if the contract period for the two current contracts had remained to be 24 months, their contract values would likely have exceeded \$1.43 million (thus requiring tender procedures).

Audit observations and recommendations

4.23 According to SPR 205, financial limits (e.g. the limit for tender procedures) should be interpreted strictly and should not be evaded by dividing procurement requirements or reducing the durations of contracts (see para. 3.3(a)). Audit considers that the CSD's award of the four contracts of smaller scopes or shorter durations does not comply with the principles of SPR 205.

- 4.24 Overall, Audit could not find documented justifications for the strategy currently adopted by the CSD for procuring cleaning services. In particular, there are no documented justifications for awarding eight contracts of a duration of 12 or 18 months and five of 24 months (see Appendix D). Audit estimates that if all the current contracts of a duration of 12 or 18 months (Contracts 6 to 13) had specified a duration of 24 months instead, six of them (Contracts 6 to 11) would have had a contract value exceeding \$1.43 million (Note 20) and would have required tender procedures.
- 4.25 In mid-January 2012, upon enquiry, the CSD informed Audit that cleaning service contracts of different scopes and durations had been awarded to suit operational needs of individual correctional institutions taking into account development plans in the pipeline and for the sake of further enhancing the administration and monitoring of the cleaning services provided by the contractors. However, the CSD was unable to provide details or documentation on how it had used the different contract scopes and durations to achieve such purposes.
- As mentioned in paragraph 3.2, achieving best value for money and maintaining open and fair competition are the twin policy objectives for government procurement. Audit considers that the CSD's direct procurement of cleaning services does not provide assurance that the objectives are achieved. In Audit's view, the CSD needs to review the cleaning service requirements on an overall basis and adopt an appropriate procurement strategy, including determining the optimal contract scopes and durations.

Audit recommendations

- 4.27 Audit has *recommended* that the Commissioner of Correctional Services should:
 - (a) review the cleaning service requirements on an overall basis and adopt an appropriate strategy to procure such services, including determining the optimal contract scopes and durations, with a view to achieving best value for money and maintaining open and fair competition;

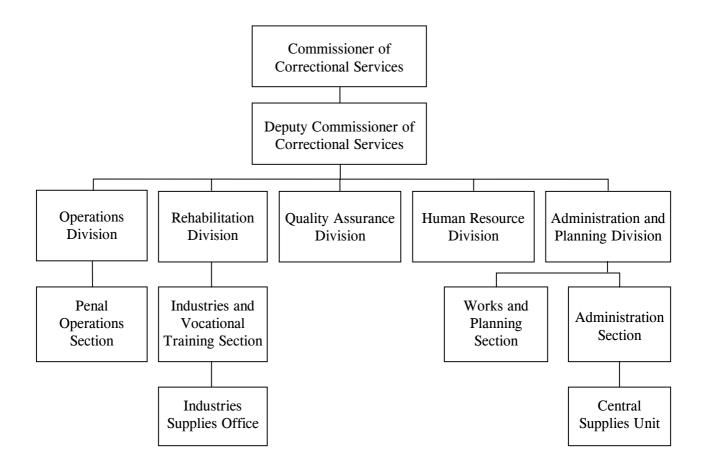
Note 20: Audit divided the current contract value by the current contract duration to derive the "contract value per month" for estimation purposes.

- (b) regularly remind CSD officers responsible for procuring cleaning services of the need to interpret the financial limits strictly; and
- (c) tighten control to guard against any non-compliance with the laid-down financial limits (such as dividing procurement requirements or reducing the durations of contracts).

Response from the Administration

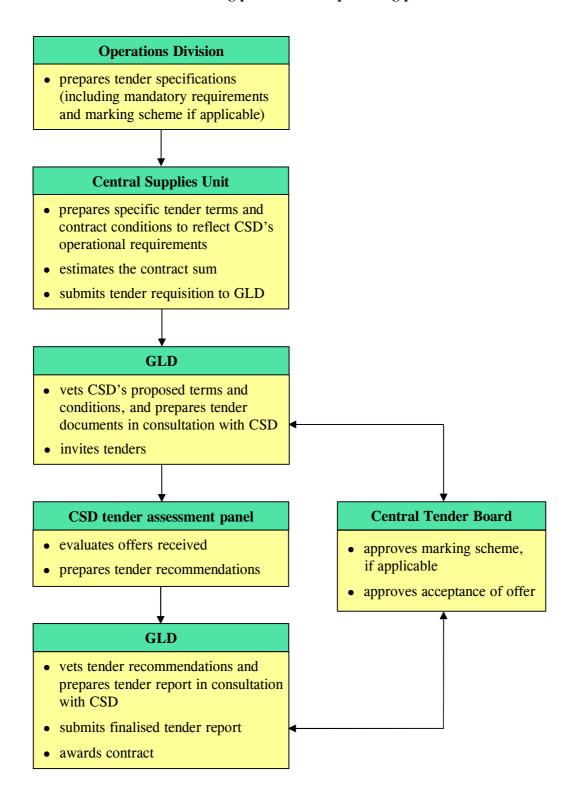
4.28 The **Commissioner of Correctional Services** agrees with the audit recommendations. He has said that a review of the cleaning service requirements and the strategy of procuring the services is expected to be completed by mid-2012.

Correctional Services Department Organisation chart (extract) (31 December 2011)



Source: CSD records

Flowchart of tendering procedures for procuring provisions



Source: CSD records

Repeated same-day direct purchases from same supplier

Case	Purchase number	Date of procurement request (Note 1)	Date of purchase	Amount (\$)
A	1	1 February 2011	2 February 2011	40,500
(Photographic	2	2 February 2011	2 February 2011	18,075
equipment)		Total pro	ocurement requirements	58,575
В	3		26 April 2010	20,286
(Inmates'	4	Not available (Note 2)	26 April 2010	49,680
clothing)		Total pro	ocurement requirements	69,966
С	5	4 March 2011	7 March 2011	48,090
(Photographic	6	4 March 2011	7 March 2011	49,690
equipment)		Total procurement requirements		
D	7	20 October 2010 (Note 3)	22 October 2010	23,100
(Polo shirts)	8		22 October 2010	49,500
	9		22 October 2010	49,500
	Total procurement requirements			122,100
Е	10	9 November 2010	12 November 2010	49,995
(Internal alarm	11	9 November 2010	12 November 2010	49,922
system)	12	9 November 2010	12 November 2010	49,993
	Total procurement requirements			149,910
F	13		26 August 2010	48,978
(Inmates'	14	Not available (Note 2)	26 August 2010	49,450
clothing)	15		26 August 2010	49,738
	16		26 August 2010	49,663
	17	3 August 2010	26 August 2010	49,738
		Total pro	ocurement requirements	247,567

Case	Purchase number	Date of procurement request (Note 1)	Date of purchase	Amount (\$)
G	18	5 July 2010	9 July 2010	473,000
(Materials for	19	5 July 2010	9 July 2010	966,600
field work shirts and trousers)		Total procurement requirements		1,439,600
Н	20	28 July 2011	4 August 2011	336,000
(Galvanised	21	28 July 2011	4 August 2011	630,000
steel tubes)	22	28 July 2011	4 August 2011	525,000
	Total procurement requirements			1,491,000
I	23	3 June 2009	19 June 2009	840,000
(Materials for	24	3 June 2009	19 June 2009	896,000
uniform shirts)	Total procurement requirements		1,736,000	

Source: Audit analysis of CSD records

Note 1: For each case (except Cases B and F), all the procurement requests were initiated by the same institution.

Note 2: The CSD could not produce for Audit examination the procurement requests for these six purchases.

Note 3: There was only one procurement request. The CSD obtained the required goods by making three purchases.

Remarks: In each case, items of a similar nature were purchased from the same supplier.

Cleaning service contracts (31 December 2011)

Contract number	Correctional institutions covered (Number)	Duration (Month)	Value (\$ million)
1	2	24	1.02
2	2	24	0.94
3	1	24	0.69
4	2	24	0.59
5	(Note)	24	0.08
6	2	18	1.42
7	3	18	1.26
8	4	18	1.16
9	6	12	1.24
10	1	12	1.07
11	1	12	0.96
12	1	12	0.59
13	2	12	0.26

Source: CSD records

Note: The contract covered certain administration facilities.

Appendix E

Acronyms and abbreviations

Audit Audit Commission

CSD Correctional Services Department

EMSTF Electrical and Mechanical Services Trading Fund

GLD Government Logistics Department

SPRs Stores and Procurement Regulations