



New York State Office of the State Comptroller
Thomas P. DiNapoli

Division of State Government Accountability

Oversight of International Offices

Empire State Development



Report 2012-S-7

June 2013

Executive Summary

Purpose

To determine if Empire State Development (ESD) monitors the effectiveness of its international offices and manages payments to foreign representatives to ensure they are made only for authorized contract purposes. Our audit scope period was April 1, 2010 through October 17, 2012.

Background

ESD's International Division is responsible for promoting international trade and investment initiatives to improve global competitiveness for New York State companies. The International Division helps businesses increase exports and expand visibility of their business in the global marketplace; and develops and maintains a network of partners worldwide to attract foreign direct investment and create jobs for New Yorkers. This is accomplished through contracts with foreign representatives who assist businesses in these activities. Between April 1, 2010 and March 31, 2012 ESD paid its foreign representatives \$2.7 million to manage ten international offices. ESD has recently scaled back its international presence and closed offices in Australia, Brazil, Chile, China, Mexico and Turkey. ESD still has foreign representatives operating in Canada, Israel, South Africa and the United Kingdom.

Key Findings

- ESD does not have an appropriate performance monitoring system in place to evaluate foreign representatives' activities against contract requirements. Instead, performance reporting and monitoring efforts appeared to be informal and ad-hoc at best throughout most of the audit period. Lack of more rigorous performance monitoring may have contributed to poor results from certain international offices. ESD has recently implemented a new system called the Client Resource Management System to assist in the monitoring of these contracts.
- ESD has made significant improvements in managing payments to foreign representatives and correcting deficiencies found in a 2011 OSC review of payments. These improvements include requiring adequate documentation, such as bank statements and vendor invoices, to support the expenses claimed by the foreign representatives.

Key Recommendations

- Monitor international office contracts to ensure that international offices are meeting contract requirements and are operating to benefit New York companies and New York State economy.
- Ensure that foreign representatives are only reimbursed for actual and necessary expenses incurred in the operation of international offices.

Other Related Audits / Reports of Interest

[Empire State Development Corporation: Personal and Miscellaneous Services Contracts \(2009-S-62\)](#)

[Empire State Development Corporation: Funding Commitments for Economic Development Projects \(2008-S-162\)](#)

**State of New York
Office of the State Comptroller**

Division of State Government Accountability

June 28, 2013

Kenneth Adams
President & CEO of Empire State Development and
Commissioner of the Department of Economic Development
633 Third Avenue
New York, NY 10017

Dear Commissioner Adams:

The Office of the State Comptroller is committed to helping State agencies, public authorities and local government agencies manage government resources efficiently and effectively and, by so doing, providing accountability for tax dollars spent to support government operations. The Comptroller oversees the fiscal affairs of State agencies, public authorities and local government agencies, as well as their compliance with relevant statutes and their observance of good business practices. This fiscal oversight is accomplished, in part, through our audits, which identify opportunities for improving operations. Audits can also identify strategies for reducing costs and strengthening controls that are intended to safeguard assets.

Following is a report of our audit of the Empire State Development entitled *Oversight of International Offices*. This audit was performed according to the State Comptroller's authority under Article X, Section 5 of the State Constitution and Section 6278 (3) of McKinney's New York State Unconsolidated Laws.

This audit's results and recommendations are resources for you to use in effectively managing your operations and in meeting the expectations of taxpayers. If you have any questions about this report, please feel free to contact us.

Respectfully submitted,

*Office of the State Comptroller
Division of State Government Accountability*

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This report is also available on our website at: www.osc.state.ny.us

Background

Under the State's Economic Development Law, Empire State Development (ESD) is charged with encouraging and developing commerce with foreign countries by promoting international trade and investment initiatives to improve global competitiveness for New York State companies. To carry out this responsibility, ESD's International Division contracts with foreign representatives who operate foreign offices to provide services that assist New York State businesses to develop or expand export sales; and to attract foreign direct investments to create jobs in New York. The broad goals of ESD's international presence are to:

- help New York State companies increase exports and expand visibility of their business in the global marketplace;
- develop and maintain a network of partners worldwide to attract foreign direct investment and create jobs for New Yorkers; and
- simplify the process of international trade from New York State.

Foreign offices assist businesses in finding sales agents and distributors to enter or expand their sales in foreign markets and provide guidance on issues ranging from market viability to local laws and related product adaptation, modification or compliance. In addition, foreign representatives are required to administer trade events and develop investment targets. These efforts generally focus on five New York industry clusters:

- Clean Technology
- Education
- Financial Services
- Information and Nanotechnology
- Life Sciences and Biotechnology

ESD also contracts with the Council of Great Lakes Governors; a partnership of the governors of the eight Great Lakes States that facilitates economic growth in the Great Lakes region. The partnership has global interest in multiple foreign countries, but currently is only promoting and facilitating trade opportunities in South Africa.

In 2011, OSC's Bureau of State Expenditures examined payments made by ESD to several of its foreign representatives. That review made recommendations to address deficiencies in ESD's payment processes and the quality of the documentation retained by ESD in support of the payments, which raised questions about whether the expenses were necessary and appropriate.

Between April 1, 2010 and March 31, 2012, ESD paid \$2.7 million to seven foreign representatives for costs associated with operating ten international offices. Due to budget constraints and economic conditions, ESD has more recently scaled back its international presence and closed offices in Mexico, Turkey and China; along with three offices in Australia, Brazil and Chile that had been operated through the Council of Great Lakes Governors. ESD still has foreign representatives operating in the United Kingdom, Canada, Israel and South Africa.

Audit Findings and Recommendations

Our audit found adequate documentation available to support payments made to ESD's foreign representatives, indicating that significant improvements have been made to address the fiscal deficiencies identified by our Bureau of State Expenditures' earlier review in 2011. However, ESD's International Division still needs to continue to improve its monitoring of foreign representatives' activities to ensure they are meeting established contract performance standards and contributing positively to New York State's economy.

ESD Management Needs to Improve Monitoring of Foreign Representatives

ESD does not have an appropriate performance monitoring system in place to evaluate foreign representatives' activities against contract requirements. Instead, performance reporting and monitoring efforts appeared to be informal and ad-hoc at best throughout most of the audit period. Although ESD provided us with some information about specific international trade and investment successes, the information only spanned the most recent year. Furthermore, the information included data on performance standards that were inconsistent with contract requirements and appeared to have been created in response to our audit and other requests for information. More specifically:

- When asked to provide support for monitoring efforts, International Division officials directed us to their Trade and Foreign Direct Investment Report Card (FDI Report Card), which consists of a spreadsheet listing out the international offices, their expected contract performance measures (such as projected export sales) and their actual trade and investment results. However, our analysis found the spreadsheet only included data for the 2010-2011 fiscal year and the expected results did not coincide with performance measures specified in the corresponding contracts. Even with these limitations, it was clear that some offices did not meet expected results, while others had very little results recorded at all. For example, the Toronto office had projected export sales of \$1.2 million, but only reported \$175,000 in actual export sales. At the same time, the Turkey office reported no export sales whatsoever. The wide disparities call into question whether the FDI Report Card had actually been used to monitor foreign representatives' performance or for any related decision making.
- We also asked ESD to provide any internal management reports that had been created to document monitoring efforts, but were informed that such reports were discontinued in late 2007 at the request of management and replaced by the FDI Report Card.
- Another document supplied to us outlining the International Division's 2011 accomplishments appears to have been created specifically for our audit and, similar to the FDI Report Card, only includes major successes for a one-year period. Our review found that a former executive manager, who was responsible for oversight of the International Division at the time our audit began, contacted the international offices at about the same time ESD was notified of our audit. These contacts resulted in some of the international offices spontaneously self-reporting their recent accomplishments. We view this as an

indication that the International Division did not have performance information readily available for its own use and was not actively monitoring their foreign representatives' performance.

We found the lack of monitoring extends not only to individual foreign offices, but to entire programs as well. For example, ESD's Export Marketing Assistance Service is a program that helps New York State businesses find foreign sales agents and distributors. As part of this program, foreign representatives provide market-specific local intelligence and identify the best possible parties to represent businesses' sales interests. We found that businesses applying for this service were not being actively tracked, with program applications spread across several of ESD's regional offices. Division management had no system in place to monitor program activity, to track outcomes experienced by businesses that used this program, or even to inquire whether or not these firms were successful in meeting their exporting goals.

Formal monitoring systems are an important means for management to acquire performance data on a regular basis, which can then be compared with contract requirements. Management can use this information to identify contractors who are meeting or exceeding contract requirements, as well as those that are not. Performance measurement also creates an opportunity for management to provide additional monitoring, support and outreach during the life of the contract, thereby allowing programs the greatest likelihood of achieving their desired results and increasing economic activity in the State.

Performance data can also be useful to provide additional assurance when making contract payments, awarding future contracts and identifying international markets to exit or enter. However, during our audit, Division officials were unable to provide us with any up-front analyses or other documented basis for selecting the international markets that they entered. This poses particular concern because, during the course of our audit period, the Division had to close several international offices due to fiscal constraints. According to Division officials, these decisions were based on fiscal impact, not performance.

Had ESD been armed with comprehensive analyses of each market's potential, along with appropriate data acquired by monitoring contractor performance against those expectations, we believe officials would have been in a much better position to identify the offices that had strong international markets as well as strong contractor performance. This type of performance monitoring would have helped ESD objectively determine which offices had the greatest likelihood of contributing positively to New York State's economy.

ESD's lack of performance information dating back more than one year can be traced, at least in part, to a lack of consistent management approach over time. In discussions with ESD staff, we learned that various former executive managers had different approaches and requirements. Some wanted detailed monthly reporting of Division activities, while others did not. These changing practices have led to inconsistency within the Division and mostly informal monitoring of foreign representatives' activities.

ESD officials agree that improvements and greater consistency are needed, both in monitoring

its contracts with foreign representatives and in tracking performance. To this end, ESD has recently begun implementing a new Client Resource Management System (CRMS) designed to assist in data collection and reporting on international trade and investment attraction activities. Data should include tracking of actual export sales and investment amounts associated with each foreign representative. Although we did not test the capabilities of the CRMS, on its face it appears to be a more comprehensive tool which, if fully utilized, should enable management to more effectively monitor and track the performances of foreign representatives.

Improved Controls Over Payments to Foreign Representatives

ESD has improved the controls over payments to foreign representatives as a result of our Bureau of State Expenditures' review completed in early 2011. That review found various deficiencies in fiscal oversight, including payments made with little or no supporting documentation to show the purpose of claimed expenses or proof that they were actually incurred. Payment requests were often not supported by invoices or cancelled checks proving that vendors were paid for goods and services, and some of the invoices that were available had been submitted in foreign languages and reimbursed without translation. Similarly, there was sometimes no documentation assuring that foreign representatives had actually paid their local employees for claimed payroll costs.

Our current review found that ESD has made significant improvements when processing payments to foreign representatives. Recent payments contained more documentation to support the expenses claimed, including bank statements showing that foreign representatives paid vendors, actual invoices from the vendors and signed affidavits for salaries paid for those countries that cannot provide bank statements.

There were still some vouchers, particularly from Turkey and Israel, which included vendor invoices submitted in their native languages. ESD officials explained that, for these countries, it is difficult for the businesses to produce invoices in English. In each case, ESD had required the foreign representatives to itemize the expenses in English and convert the amounts to U.S. dollars. ESD's finance office staff used this information to match amounts with invoices and, in some cases, would reach out to other ESD staff who were able to translate the invoices.

Continued compliance with these strengthened controls should provide ESD management with reasonable assurance that they are paying for actual expenses incurred, which are related to activities authorized by the contracts with its foreign representatives.

Recommendations

1. Monitor the performance of foreign representatives to ensure that international offices are meeting contract requirements and are operating to the benefit of New York companies and economy.
2. Ensure that foreign representatives are only reimbursed for actual and necessary expenses incurred in the operation of international offices.

Audit Scope and Methodology

We audited whether Empire State Development monitors the effectiveness of its international offices and manages payments to foreign representatives to ensure they are made only for authorized contract purposes. Our audit scope included the period April 1, 2010 through October 17, 2012.

To accomplish our audit objectives, we interviewed ESD International Division and Finance officials. We reviewed: relevant State laws and regulations; ESD policies and procedures; organizational charts; and documentation provided by International Division officials supporting their monitoring efforts.

In addition, we reviewed a judgmental sample of 18 vouchers paid between April 1, 2010 and March 31, 2012. Our sample included large payments made to six foreign representatives around the time of the Bureau of State Expenditure's review and payments made after for comparison; and represented nine international offices including Canada, United Kingdom, Israel, Turkey, China, Australia, Brazil, Chili and South Africa.

We conducted our performance audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

In addition to being the State Auditor, the Comptroller performs certain other constitutionally and statutorily mandated duties as the chief fiscal officer of New York State. These include operating the State's accounting system; preparing the State's financial statements; and approving State contracts, refunds, and other payments. In addition, the Comptroller appoints members to certain boards, commissions and public authorities, some of whom have minority voting rights. These duties may be considered management functions for purposes of evaluating organizational independence under generally accepted government auditing standards. In our opinion, these functions do not affect our ability to conduct independent audits of program performance.

Authority

This audit was performed according to the State Comptroller's authority under Article X, Section 5 of the State Constitution and Section 6278 (3) of McKinney's New York State Unconsolidated Laws.

Reporting Requirements

We provided a draft copy of this report to Empire State Development officials for their review and comment. Officials agreed with our recommendations and reported already having taken steps to implement them. At the same time, officials also stressed that contract deliverables and other formal performance measures like trade success can often be impacted by unforeseen factors, including international economic and political events. While acknowledging that a comprehensive monitoring system was not in place, officials did provide examples of international trade and investment success that occurred during our audit period. However, these successes did not align with the factors mentioned in the contract terms. Officials expressed confidence that once fully implemented, certain new tools like their Client Resource Management System will greatly enhance their ability to monitor and oversee international offices. A complete copy of their response is included at the end of this report.

Within 90 days after final release of this report, as required by Section 170 of the Executive Law, the President and Chief Executive Officer of Empire State Development shall report to the Governor, the State Comptroller, and the leaders of the Legislature and fiscal committees, advising what steps were taken to implement the recommendations contained herein, and where recommendations were not implemented, the reasons why.

Contributors to This Report

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Vision

A team of accountability experts respected for providing information that decision makers value.

Mission

To improve government operations by conducting independent audits, reviews and evaluations of New York State and New York City taxpayer financed programs.

Agency Comments



April 12, 2013

Bob Mainello,
Audit Supervisor
Office of State Comptroller
110 State Street, 11th Floor
Albany, New York 12236

Re: Audit Report 2012-S-7 – Oversight of International Offices (Performance) – February 2013

Dear Mr. Mainello:

Empire State Development (ESD) is in receipt of the Office of the State Comptroller's (OSC) draft audit report, *Oversight of International Offices*, which details in part its findings relating to ESD's monitoring, assessment, and management of its overseas offices whose purpose is to promote international trade, global investment, and best position New York companies seeking profitable foreign markets.

ESD is sensitive to concerns raised in the draft audit report. The issues are important and require ongoing attention. Administratively, improvements have been made, as clearly noted in the draft audit report. These include OSC's acknowledgements of "significant improvements in managing payments," "correcting [previously identified] deficiencies," and "adequate documentation available to support payments."

It's important to emphasize that ESD evaluates its international endeavors in a larger context, mindful of the ongoing changes in trade policies, foreign markets, and protocols unique to each nation's specific corporate and financial environments. This evaluation method is not easily measured by an audit.

ESD wishes to underscore that previous information shared with your office which shows significant successes among our international offices is only partially reflected in the draft report. Although the audit findings acknowledge some of this information, it is not fully reflected.

Contrary to your audit findings, as one example, prior information provided indicated performance measurements were among the factors used by ESD management to assess vendor performance and make decisions involving overseas economic activities. This is not adequately reflected in OSC's draft.

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Additionally, to suggest ESD performance monitoring is a cause of limited performance for any foreign offices is inaccurate, if not speculative, and could be misinterpreted by someone unfamiliar with the global economy and its complexities. Monitoring should be and is always reviewed for improvement, but international economic and political factors often directly impact trade success irrespective of the monitoring system.

Separate from these issues are complex cultural matters within each nation not easily reflected in report and performance data. South Africa, as one example, has eleven official languages. Although Mandarin is the language most often used for business in China, there are numerous officially recognized provincial languages as well. Such factors can have significant impact as export opportunities in a country such as China, may present themselves in a dialect that requires more extensive assistance to carry out discussions between New York businesses and Chinese collaborators. This often can lead to delays in sales performance or export goals that may be expected from specific businesses being assisted.

Response to Findings

1. ESD Management Needs to Improve Monitoring of Foreign Representatives

ESD concurs that improvements are needed for the monitoring of its foreign offices. That said, our agency had initiated a Client Resource Management System (CRMS) prior to your Audit to provide management with more comprehensive data tracking and performance information of ESD's foreign activities. The system continues to be implemented, and has nearly completed its "pilot" phase, and will provide an online and robust vehicle for reviewing international activity. The CRMS will report on management-identified metrics that capture activities such as: investment by foreign office and sector; sales; agent distributor results; work orders and lead information; regional tracking; and technical assistance and outreach data.

In addition, ESD has established a base level of oversight to monitor staff, assess results, and oversee international offices to address some of the points raised in the audit. ESD's quality improvement initiatives are an ongoing process to build on this foundation.

Foreign Direct Investment (FDI) Report Card & Unmet Goals for Performance

The audit raised a concern with the Division's summary Trade and Foreign Direct Investment Report Card spreadsheet that is used internally to assess performance of foreign activities. This spreadsheet, which was utilized by Division Directors as part of their oversight, supplements the review of the monthly reports staff receive from foreign offices. The summary Report Card is not intended to be used alone in performance measurement; the Report Card is one of several resources used to assess overall performance and ESD strategies.

In addition, ESD makes a distinction between projected results and performance measures. The Audit was critical of projected versus actual export sales. It should be noted, however, that there is a lag time for sales as reflected in projections and actual outcomes. Projected sales may not be realized for twelve or more months after initial engagement. Hence, a projection made in one period may not come to full fruition until much further in the business or contract cycle. This lag time is understood by Division staff when performing internal reviews and tracking.

Other activities, such as tradeshow, also do not automatically translate into easily measurable economic activity. Although they are an effective tool to market New York State, trade shows are not expected to be a vehicle for recording immediate direct sales. Their primary purpose is to introduce potential investors to the opportunities within New York, or provide New York businesses with direct connections to new markets and export opportunities. Trade shows help develop awareness of New York-produced products, establish relationships and initiate what can be a long communication process before potential sales are realized. Though contact with a company will be recorded, it does not presume sales will be generated.

Finally, projected sales often cannot anticipate foreign economic factors. A foreign nation's slow economic growth will impact New York's economic initiatives. Although this cannot always be factored into sales projections and actual outcomes, the following US Department of Commerce data is worth highlighting:

- In 2011, New York State merchandise exports were \$84.9 billion, a 22% increase over 2010 exports of \$69.7 billion.
- Through September 2012, year-to-date New York State merchandise exports amounted to \$60 billion.

It's important to highlight the groundwork to enable these successes constituted a long, ongoing process of building and nurturing business relationships. Despite the clarifications and the challenges outlined above, ESD is confident in its long-term performance goals and strategies, and in its ability to assess – and to continually improve – the performance of its international offices.

Discontinuity of Management Reports

ESD is committed to using only the best methodologies to gather, interpret, and internally report information about foreign trade initiatives, and ones lending themselves to a consistent management approach unaffected by any change in senior managers. The Client Resource Management System is an important, much needed solution to formalize and standardize reporting tools in place regardless of management changes.

Document Created Specifically for Audit

Information was not “created” for purposes of the audit as is posited in your report. In light of the unique and distant locations from which international business information originates, it must be processed and formalized in a manner suitable for an audit. Data was often formatted for ease of use and review by OSC.

ESD, however, is aware information should be more readily available and formatted in a useable manner for ESD itself and for other offices, agencies, and departments.

Other Concerns

OSC’s draft report questions whether performance metrics were used for decision making during a time that several foreign offices needed to be closed due to a reduction in State funding. Performance metrics and the strategic economic importance of foreign offices were certainly factors used in determining which offices to close. When it was suggested that fiscal impact was a key factor – as the draft indicates, it was to the extent that all offices were engaged in a conversation about their funding needs and possible funding reductions. While several offices were able to modify their scope of services and accept reduced funding, there were some offices that indicated any further reductions would result in an inability to effectively carry out services for New York State. Some of these offices were closed.

ESD understands that the lack of a formal written analysis of the management decision making process causes OSC concern, but strongly disagrees that it indicates performance measures and strategic market information were absent from the process. ESD has International Policy and Strategic Business staff outside of the International Division who possess key knowledge about international trade policies and international markets, as well as key New York business sectors. Discussions with these staff were a key factor when assessing which international markets New York should pursue.

2. ESD Needs Improved Controls Over Payments to Foreign Representatives.

OSC acknowledges in the draft report that “adequate documentation [is now] available to support payments made to ESD’s foreign representatives...” It further “found that ESD has made significant improvements when processing payments to foreign representatives.” ESD concurs, but is committed to continuing quality improvement initiatives.

It’s worth noting that ESD has made every effort to ensure that documentation identified by OSC as obligatory was obtained, even when our agency questioned the need for certain items (e.g., requiring affidavits from recipients attesting to the fact that they actually received checks from ESD, which could have been otherwise verified). The threshold of proof required by OSC, especially when applied retroactively, required the expenditure of considerable time and effort on the part of our International and Finance staff for nearly a year.

Although not acknowledged in the report, ESD withheld payment in multiple cases where there was an absence of documentation for services provided. ESD does not reimburse foreign offices for work not performed satisfactorily or when documentation for competently performed work is not provided.

There is a performance monitoring system in place, though modifications to it are ongoing. ESD continues to seek and explore ways to optimize monitoring that can be easily adaptable to distinct markets. What may be appropriate in Canada, for example, may not be suitable for China. OSC's report raises an issue that ESD management has continually attempted to address.

As noted previously, the recently implemented CRMS is the best approach to date. Its effectiveness will be closely monitored and appropriate modifications will be made when they are identified. If CRMS continues to prove useful, as preliminary indications suggest, it will serve to stabilize performance management and control functions relating to ESD's international offices, regardless of changes that may occur in senior management.

ESD further concurs that continued "compliance with these strengthened controls should provide ESD management with reasonable assurance that they are paying for actual expenses incurred, which are related to activities authorized by the contracts with its foreign representatives."

Conclusion

While ESD does have foundation protocols in place to monitor payment and performance, improvements are continually sought. As stated, reporting and oversight will be greatly enhanced by CRMS and the Foreign Direct Investment Report Card. These tools also require ongoing review to maximize quality improvement.

OSC's recommendations for performance monitoring – to ensure that contract requirements are met and reimbursements are properly made – are taken very seriously by our agency. ESD recognizes that your outside review has helped highlight areas where greater focus can yield improved results.

As noted earlier, ESD again emphasizes that information shared with your office in the past, such as highlighted successes among international offices, is not fully acknowledged in the draft report. Two examples that were shared include a Long Island manufacturer that estimated its sales doubled in the United Kingdom due to assistance from ESD staff and London foreign office. The second was one of the largest paint manufacturers in Israel opening 3 showrooms in Manhattan and investing \$5 million. This Israel company also has plans to add a \$5 million paint mixing facility in Long Island City. Information and highlights such as this did show that performance measurements were among the factors used by ESD management to assess vendor performance and make decisions involving overseas economic activities. ESD requests this too be reflected in the final report.

Thank you for the opportunity to comment on the draft report. Ongoing quality improvement initiatives by ESD will benefit from OSC's input. ESD is mindful of the issues cited in the report and efforts are well underway to address them.

Sincerely,



Ed J Hamilton
Senior Deputy Commissioner, Finance and Administration