



**U.S. Department of the Interior
Office of Inspector General**

AUDIT REPORT

**U.S. DEPARTMENT OF DEFENSE
CONTRACT FUNDS,
DEPARTMENT OF EDUCATION,
GOVERNMENT OF GUAM**

REPORT NO.00-I-172
JANUARY2000



United States Department of the Interior

OFFICE OF INSPECTOR GENERAL
Washington, D.C. 20240

JAN 10 2000

AUDIT REPORT

Honorable Carl T.C. Gutierrez
Governor of Guam
Office of the Governor
Hagatña, Guam 969 10

Subject: Audit Report on U.S. Department of Defense Contract Funds, Department of Education, Government of Guam (No. **00-I-172**)

Dear Governor Gutierrez:

This report presents the results of our audit of U.S. Department of Defense contract funds received by the Department of Education, Government of Guam. The objective of our audit was to determine whether the Government of Guam complied with Federal and local laws and procedures applicable to funds received under its contracts with the U.S. Department of Defense. The audit was requested by three former directors of the Guam Department of Education.

BACKGROUND

Title 17, Section 3 101, of the Guam Code Annotated established the Department of Education within the Government of Guam. Section 3 102 of the Code states, "The Department shall be administered through the Territorial Board of Education which shall be the governing and policy-making body of the Department." Further, Section 3 102(a) of the Code states that the Territorial Board of Education will "select and hire a Director and Deputy Director of Education." However, on March 25, 1999, Guam Public Law 25-03 was enacted, which eliminated the Board of Education. Chapter 4, Section 18, of the Public Law states that "the governing of the Department of Education shall temporarily revert to [the Governor of Guam] until further legislative action. The Board of Education currently in place ... shall cease to exist. [The Governor] shall not appoint a Board, but shall assume all functions, powers, duties and responsibilities of the Board." As a result of the change, on March 31, 1999, the contracts employing the Department of Education's Director and Deputy Director were terminated, and an Acting Director was appointed by the Governor.

During the period of fiscal years 1989 through 1997, the U.S. Department of Defense executed three successive contracts with the Government of Guam for the Department of Education "to provide public education services for Department of Defense dependents residing on U.S. military installations in Guam." Each contract provided for annual

payments to the Government of Guam based on a fixed cost for each military dependent child who attended a Guam public school. The contracts required that the contract payments be used to raise teacher qualifications, recruit teachers, improve curriculum and instruction, provide staff development training, repair and maintain facilities, and perform other educational functions. The third contract, which covered the period of fiscal years 1994 through 1998, stated that the Department of Defense would pay the Government of Guam \$5,920 per child based on an estimated enrollment of about 2,700 military dependent children in Guam's public schools.

In an April 23, 1999, memorandum for the record, the former Deputy Assistant Secretary of Defense for Personnel Support, Families and Education¹ stated. "In July 1997, the Assistant Secretary of Defense ... notified [the Guam Congressional Representative] that the Department of Defense was canceling its contract with the government of Guam to provide funds for the education of military children in Guam public schools effective September 30, 1997. Furthermore, [the Assistant Secretary of Defense] informed [the Congressional Representative] that the Department of Defense would open its own school system on Guam." In the memorandum, the former Deputy Assistant Secretary further stated, "In September 1997 I traveled to Guam to present a check for the final payment of the contract (\$12,417,441.08) to [the Governor of Guam]."

During the period of October 1, 1988, to January 15, 1997, the Government of Guam's Department of Defense Education Contract Office administered the U.S. Department of Defense contract funds within the Department of Education. However, through Executive Order 97-O 1, on January 15, 1997, the Governor transferred the Contract Office to the Guam Department of Administration. For fiscal year 1998, the Contract Office reported revenues of \$21.3 million (including the final contract payment of \$12.4 million), expenditures of \$6.6 million, and transfers out of \$13.3 million. For fiscal year 1999 (through December 31, 1998), the Contract Office reported revenues of \$75,104,200, expenditures of \$1.1 million, and transfers out of \$880,753. During fiscal year 1999, the Contract Office had an Administrator and 10 staff members and an operating budget of \$660,000 and a Capital Improvement Project budget of \$7.7 million.

SCOPE OF AUDIT

The scope of the audit included a review of transactions related to Department of Defense contract funds that occurred during fiscal years 1998 and 1999 (through December 31, 1998). To accomplish the audit, we reviewed pertinent records and interviewed officials of the

¹During the period of October 1993 to October 1998, the Deputy Assistant Secretary of Defense for Personnel Support, Families and Education was responsible for Department of Defense education activities; morale, welfare, and recreation programs; adult and continuing education programs; and family programs. In November 1998, the Deputy Assistant Secretary of Defense was appointed to the position of Assistant Secretary of the Navy for Manpower and Reserve Affairs.

Government of Guam's Department of Administration, Department of Defense Education Contract Office, Department of Education, Bureau of Budget and Management Research, Department of Public Works, and Waterworks Authority. We -also interviewed (by telephone) U.S. Department of Defense officials in Washington, D.C., and Okinawa, Japan, regarding the contracts with the Government of Guam.

Our review was made, as applicable, in accordance with the "Government Auditing Standards," issued by the Comptroller General of the United States. Accordingly, we included such tests of records and other auditing procedures that were considered necessary under the circumstances.

As part of our review, we evaluated the system of internal controls related to the financial and operational management of the contract funds by the Contract Office and by the Department of Education to the extent that we considered necessary to accomplish the audit objective. Based on our review, we determined that the Contract Office generally managed the processing of purchase orders and invoices in compliance with the contract and applicable regulations. However, we identified internal control weaknesses in the use of contract funds by the Government of Guam and in the timely use of contract funds by the Department of Education. These weaknesses are discussed in the Results of Audit section of this report. Our recommendations, if implemented, should improve the internal controls in these areas.

PRIOR AUDIT COVERAGE

Although the Office of Inspector General did not perform any audits of the Department of Defense contracts with the Government of Guam during the past 5 years, prior reports were issued as follows:

- On March 15, 1993, the U.S. Department of the Interior, Office of Inspector General, issued the audit report "Selected Special Revenue Funds, Government of Guam" (No. 93-I-706), which stated that the Department of Education (1) did not make timely use of about \$13 million of maintenance and repair funds received under the contracts and (2) lost about \$2 million in potential contract funds by not identifying all military dependent students. Our current audit also disclosed that the Department of Education had not used contract funds in a timely manner.

- On January 20, 1995, the U.S. Department of Defense, Office of the Inspector General, issued the audit report "DOD [Department of Defense] Contracts With the Department of Education, Government of Guam" (No. 95-082), which stated that the Department of Education had made a concerted effort to use contract funds in a timely manner and had efficiently expended contract funds specified for repair and maintenance projects.

▪ An independent public accounting firm's single audit reports for the Government of Guam for fiscal years 1996 and 1997 did not report any deficiencies in the Department of Education's management of Department of Defense contract funds.

RESULTS OF AUDIT

Although the Government of Guam's Department of Defense Education Contract Office used contract funds under its control in conformance with the contract, the Government of Guam did not ensure that contract funds transferred to the Public Service Recovery Fund and to the Department of Education General Fund were used for contract purposes and in a timely manner. The requirements for the use of Department of Defense contract funds were contained in the 5-year contract dated September 30, 1993, between the U.S. Department of Defense and the Government of Guam. However, the Government (1) assumed that after fiscal year 1997 it no longer had to comply with the contract because the contract would not be renewed; (2) needed the additional funds because of declining local revenues, and (3) did not establish an adequate planning and monitoring system to ensure the effective use of the contract funds. As a result, as of December 31, 1998, the Government had expended \$4.3 million, obligated \$1.1 million, and retained an additional \$802,810 for noneducational purposes. In addition, the Department of Education used \$35,075 for noneducational purposes and did not use \$3.5 million of contract funds in a timely manner.

Contract Requirements

Section B.2.c.2 of the contract dated September 30, 1993, between the Department of Defense and the Government of Guam states that payments are made "subject to the Department of Education compliance with the Section C, Statement of Work, and Section H, Special Provisions." Section C of the contract states that "the Department of Education agrees that it shall provide appropriate education services (grades kindergarten through 12) for eligible DoD dependents in accordance with the Department of Education standards and practices and the requirements set forth below [in the contract]." The remainder of Section C defines the requirements for the Department of Education in the areas of employee qualifications, recruitment of teachers, curriculum and instruction, performance evaluations of professional educators, staff development and inservice training, special education, capital improvements, and repair and maintenance of facilities. Section H defines special requirements related to the contract funds, including contract monitoring by Department of Defense representatives, budgetary procedures, and use of funds.

During a September 1997 meeting with the Governor of Guam, the former Deputy Assistant Secretary of Defense for Personnel Support, Families and Education presented a check for \$12.4 million to the Governor "to be used to benefit the Guam public schools." Subsequent to receiving the \$12.4 million final contract payment, the Governor of Guam and the Chairperson of the Board of Education entered into an agreement on November 21, 1997, in which the final contract payment of \$12.4 million was to be used as shown in Table 1.

Table 1. Planned Uses of the Final Contract Payment

<u>Description</u>	<u>Allbtment</u>
Textbooks	\$2,400,000
Staff Development Training	1,500,000
High School Bleachers/Playground Equipment	1,000,000
Technology	1,800,000
School Buses	2,532,000
Dededo Middle School Library	68,000
Infrastructure Support	1,900,000
Astumbo Recreational Facility	<u>1,200,000</u>
Total Final Contract Payment	<u>\$12,400,000</u>

However, as discussed in the paragraphs that follow, the funds were not used for the purposes described in the November 21, 1997. agreement.

Department of Defense Contract Fund

During fiscal years 1998 and 1999 (through December 31, 1998), the Contract Office had revenues totaling \$22 million (including the \$12.4 million final contract payment), expenditures totaling \$7.7 million, and transfers to other Government funds totaling \$14.2 million. According to Contract Office records, a total of 1,990 transactions were processed during this period. We selected a judgmental sample of 51 transactions, totaling \$7.9 million (expenditures of \$1.8 million and transfers of \$6.1 million), for testing to determine whether the Contract Office had complied with contract provisions. We determined that Contract Office expenditures were made for the purposes specified by the contract. However, the amounts transferred to other Government funds were not used in compliance with the contract or in a timely manner.

Public Service Recovery Fund

Through Executive Order 98-12, on March 20, 1998, the Governor of Guam established the Public Service Recovery Fund, which was to be administered by the Department of Administration. The Executive Order stated that "the Governor has been relieved of all financial and contractual responsibilities to the Department of Defense under the agreement and is solely responsible for determining the utilization of the remaining unexpended and unobligated funds." The Executive Order also stated that "various agencies of the government of Guam have expended significant amounts of their own funding in support of the educational system, without reimbursement, and ... budget resources to these agencies have been severely compromised by the effects of recent disasters and diminishing revenue streams from lower business, resident, and visitor spending." The Executive Order further

stated that “expenditures from the Public Service Recovery Fund shall be expended for the following purposes: equipment and contracts directly related to public service; facilities and infrastructure repair, improvement and development for the public’s use and benefit; and reimbursement to autonomous agencies.”

On March 31, 1998, the Department of Administration transferred \$7.5 million from the Department of Defense Contract Fund to the Public Service Recovery Fund and then used these monies to reimburse the Department of Public Works and the Guam Waterworks Authority for noneducation expenses incurred by those agencies. According to documents provided by the Contract Office Administrator, the transfers were made based on the Government’s understanding that the requirements of the contract had lapsed when the contract was terminated. As a result, the Government of Guam used \$5.4 million (\$4.3 million expended and \$1.1 million encumbered) and may use the remaining \$802,810 in the Public Service Recovery Fund for noneducation purposes.

The Contract Office Administrator stated that the contract funds were transferred to the Public Service Recovery Fund as a result of the September 25, 1997, meeting between U.S. Department of Defense and Government of Guam officials. The Contract Office Administrator’s February 12, 1998, memorandum to the file on the results of the September 25, 1997, meeting states, “Upon presentation of the final check in the amount of \$12,417,441.08 in September 1997 ... the Deputy Assistant Secretary of Defense commented to the Governor that the contract was not being renewed.” The memorandum further stated that the Deputy Assistant Secretary of Defense told the Governor that “the expenditures of these funds were up to his [the Governor’s] discretion.” Based on this understanding, on February 18, 1998, the Contract Office Administrator issued a memorandum to the Director of the Department of Administration, informing him that “since the DOD [Department of Defense] contract between DOD and the Government of Guam has been terminated, it would be up to the Governor to decide how the funds would best be used.” The Administrator subsequently told us that she had not been informed of how the funds were expended once they were transferred from the Department of Defense Contract Fund to the Public Service Recovery Fund. However, in a February 20, 1999, telephone conversation, which was confirmed in an April 23, 1999, memorandum for the record, the former Deputy Assistant Secretary of Defense for Personnel Support, Families and Education told us that during the September 1997 meeting with the Governor of Guam, she presented a check in the amount of \$12.4 million to the Governor and “stressed that the money was to be used to benefit the Guam public schools.” (Emphasis added.) In the memorandum, the former Deputy Assistant Secretary also stated, “The Governor discussed his desire to devote part of the moneys to enhance technology in the schools. He also discussed construction needs and other equipment needs for the school system.” In the memorandum, the former Deputy Assistant Secretary further stated that “in February 1998, [an official of Guam’s Contract Office] called me to ask that I approve a list of items as appropriate expenses for the schools of Guam. I informed her that, with the suspension of the contract, the Governor was charged with the allocation of the moneys for the benefit of the public schools on Guam.” (Emphasis added.) Based on the Deputy Assistant Secretary’s statements, we believe that the Department of Defense clearly intended that the \$12.4 million be used for educational purposes. Therefore, we concluded that the statements of Government of Guam

officials that contract funds could be used for purposes other than educational was not supported.

Department of Administration records showed that, as of December 31, 1998, the Public Service Recovery Fund had revenues totaling \$8 million (the \$7.5 million transfer from the Department of Defense Contract Fund plus earned interest of \$482,028), expenditures and transfers out totaling \$6.1 million, and unexpended funds totaling \$1.9 million. We found that the \$6.1 million was used for operating expenses of the Department of Public Works (\$3.3 million), transfers to the Guam Waterworks Authority (\$1 million), and transfers to the Department of Education (\$1.8 million).

Department of Public Works. The \$3.3 million expended for operating expenses of the Department of Public Works was used for asphalt mix for road construction and repair (\$2.5 million), fuel charges (\$1,550), construction of a community gymnasium (\$56,237), salaries of employees of Public Works Highway Division (\$726,959), and the rental of dump trucks (\$43,740). In our opinion, none of these expenses directly benefited the Guam public schools, as required by the contract, and therefore were unallowable costs.

Guam Waterworks Authority. The \$1 million transferred to the Guam Waterworks Authority was used to reimburse the Authority for costs it incurred for routine operations. According to the Authority's Director, the Authority needed the funds because of shortfalls in local revenues and to recover costs incurred by purchasing water from the U.S. Navy water system at a higher cost than what the Authority was able to bill its customers. However, the Contract Office Administrator stated that the Authority's original claim for reimbursement was to recover the costs, totaling \$815,972, of extending waterlines at nine public schools. The Contract Office Administrator added that she had not been aware that the Authority was paid \$1 million to recover costs incurred in buying water. The Department of Administration's Federal Grants Supervisor, who authorized the transfer of the \$1 million to the Guam Waterworks Authority, stated that she requested that the Authority submit other documents to support its reimbursement claim because the Guam General Fund had incurred the cost of extending the waterlines at the public schools. In our opinion, the \$1 million transferred to the Guam Waterworks Authority was an unallowable cost because it was not used to reimburse the General Fund for the cost of services provided to **Guam's** public schools.

Department of Education. Of the \$1.8 million transferred from the Public Service Recovery Fund to the Department of Education for "technology" purposes, only \$4,075 was not used for educational purposes in accordance with the contract provisions.

Department of Education General Fund

On December 12, 1997, subsequent to the Department of Education's November 21, 1997, agreement with the Governor, the Department of Administration transferred \$4.9 million of the \$12.4 million final contract payment to the Department of Education General Fund to be used for "textbooks, staff development training, and high school bleachers/playground equipment." On May 12, 1998, the Department of Administration transferred an additional

\$1.8 million from the Public Service Recovery Fund to the Department of Education to be used for “technology.”

According to Department of Education records, as of December 31, 1998, about \$2.9 million was expended and \$348,688 was encumbered (obligated) in four of the eight categories listed in the November 1997 agreement, as shown in Table 2.

**Table 2. Status of Contract Funds Transferred to
the Department of Education General Fund
as of December 31, 1998**

<u>Description</u>	<u>Nov. 1997 Agreement</u>	<u>Transfers to Education</u>	<u>Expenditures</u>	<u>Encumbrances</u>	<u>Balances</u>
Textbooks	\$2,400,000	\$2,400,000	\$2,400,000	0	0
Staff Development Training	1,500,000	1,500,000	45,437	0	\$1,454,563
High School Bleachers/Playground Equipment	1,000,000	1,000,000	359,923	\$348,688	291,389
Technology	1,800,000*	1,800,000**	58,595	0	1,741,405
School Buses	2,532,000*	0	0	0	0
Dededo Middle School Library	68,000*	0	0	0	0
Infrastructure Support	1,900,000*	0	0	0	0
Astumbo Recreational Facility	<u>1,200,000*</u>	<u> </u>	<u> </u>	<u>0</u>	<u>0</u>
Total Final Payment	<u>\$12,400,000</u>	<u>\$6,700,000</u>	<u>\$2,863,955</u>	<u>\$348,688</u>	<u>\$3,487,357</u>

*These five amounts, which totaled \$7.5 million, were transferred on March 31, 1998, to the Public Service Recovery Fund instead of to the Department of Education General Fund.

**The \$1.8 million was subsequently transferred From the Public Service Recovery Fund to the Department of Education General Fund.

Of the 277 transactions related to the expenditures of about \$2.9 million, we selected a judgmental sample of 30 transactions, totaling \$1.3 million, for testing to determine whether the Department of Education had used the funds as provided for in the Department of Defense contract and the agreement with the Governor of Guam. We found that only 2 transactions, totaling \$35,075, of the 30 tested were not for purposes intended by the contract and the subsequent agreement. One expenditure of \$3 1,000 was for a noncontract-related off-island trip, and the other expenditure of \$4,075 was for expenses of other Government agencies. According to the former Deputy Controller of the Department of Education, the former Director of Education had approved the use of contract funds in these two instances because the Department did not have other financial resources available to pay for these activities. The former Deputy Controller also stated that because of the

Department's shortage of cash for payroll and other critical operating costs, the Department used contract funds to relieve temporary cash flow shortages.

We also found that, as of December 31, 1998, the Department of Education had controlled \$4.9 million for more than 12 months and \$1.8 million for more than 7 months but had expended only \$2.9 million of the available contract funds. Of the remaining \$3.8 million, about \$349,000 had been obligated and \$3.5 million was available for contract-related educational expenses. The former Deputy Controller stated that, as of April 2, 1999, the Department of Education had not developed a detailed plan for using the remaining \$3.5 million other than for the general categories specified in the November 1997 agreement. On June 21, 1999, the Acting Director of Education stated, "In general, there is a continuing need for staff development training, supplies and equipment, and technology throughout the Department of Education." In our opinion, the Department of Education should develop plans and monitoring procedures to ensure that the available contract funds of \$3.5 million in the Department's General Fund are used promptly to achieve the purposes for which they were allotted, as defined in the November 1997 agreement with the Governor of Guam.

Recommendations

We recommend that the Governor of Guam:

1. Instruct the Director of the Department of Administration to reimburse the Department of Defense Contract Fund for the \$4.3 million expended and the \$1.1 million obligated for noneducational purposes and for the interest of \$482,028 earned on these funds while in the Public Service Recovery Fund and to use the funds only for the educational purposes defined in the Department of Defense contract.
2. Instruct the Director of the Department of Education to reimburse the Department of Defense account in the Department of Education General Fund for the \$35,075 used for noneducational purposes.
3. Instruct the Director of the Department of Education to establish controls to prohibit the Department from using Department of Defense contract funds for routine Department of Education operations when regular operating funds are not available because of cash flow shortages.
4. Instruct the Director of the Department of Education to develop and implement plans and a monitoring process for the timely use of the remaining \$3.5 million of Department of Defense contract funds.

Governor of Guam Response and Office of Inspector General Reply

The October 15, 1999, response (Appendix 2) to the draft report from the Governor stated that "the Government of Guam is compelled to dispute the Draft Audit findings and disagree with all of the recommendations. Furthermore, the Government of Guam does not intend to make any changes in the disposition of funds." Therefore, we consider the four recommendations unresolved (see Appendix 5).

The response further stated that "it was made clear" that as of September 1, 1997, the Governor had "no further obligation to provide educational services" to Department of Defense students. The response further stated that "[i]t was also clearly understood that the contract that had been entered into between the Government of Guam and the Department of Defense to provide educational services was simply that, a contract to provide educational services for which the Government of Guam would receive a dollar amount per student." Further, the response stated that "[t]his was simply a service that DOD [Department of Defense] agreed to pay for, and a service that was delivered fully and faithfully by the Government of Guam until the contract concluded on September 1, 1997."

In addition, the response stated that "a recent review of this contract by the Attorney General of Guam concurs and supports my position." The response also stated that in a letter dated September 20, 1999 (Appendix 3), the Guam Attorney General had requested that our office provide the "legal basis" for the conclusions contained in our draft report. The Attorney General stated in his letter that "there is no prospective language in the contract that would allow it to be used to evaluate the use of any money transferred ... subsequent to September 1, 1997." Further, the Governor's response stated, "Finally, I again reiterate that the \$12.4 million was in fact, spent on education."

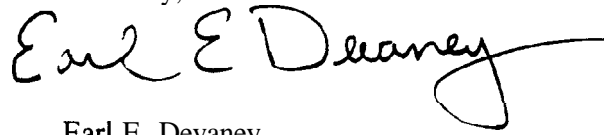
As indicated in our response (Appendix 4) to the Attorney General's letter, we believe, based on the contract provisions and statements made by a Department of Defense official, that the \$22 million (including the final \$12.4 million payment) available pursuant to the contract was to be used exclusively for educational purposes. However, as shown in our report, the money was not used exclusively for this purpose. Therefore, because there is a significant difference of opinion regarding how the \$22 million (including the final \$12.4 million payment) should have been used, we will refer the report to the Contracting Officer of the Department of Defense for a determination on the allowability of the questioned costs of \$5.4 million and for resolution of the matter.

Section 5(a) of the Inspector General Act (Public Law 95-452, as amended) requires the Office of Inspector General to list this report in its semiannual report to the U.S. Congress. In addition, the Office of Inspector General provides audit reports to the Congress.

In view of the above, please provide a response to this report by February 18, 2000. The response should be addressed to the Inspector General of the Department of Defense, and a copy should be provided to our Pacific Office, 415 Chalan San Antonio, Suite 306,

Tamuning, Guam 96911. The response should provide the information requested in Appendix 5.

Sincerely,

A handwritten signature in black ink, reading "Earl E. Devaney". The signature is fluid and cursive, with a long horizontal stroke extending from the end of the name.

Earl E. Devaney
Inspector General

cc: Acting Director, Department of Education -

CLASSIFICATION OF MONETARY AMOUNTS

<u>Finding Area</u>	<u>Questioned costs*</u>	<u>Funds To Be Put To Better Use*</u>
Public Service Recovery Fund	\$5,396,659	\$802,810
Department of Education General Fund	<u>• 35.075</u>	<u>3,487.357</u>
Total	<u><u>\$5,431,734</u></u>	<u><u>\$4,290,167</u></u>

*Amounts represent Federal funds.

OFFICE OF THE GOVERNOR
GUAM

OCT 15 1999

Earl E. Devaney
Inspector General
U.S. Department of Interior
Office of Inspector General
1849 C. Street, N.W.; Mail Stop 5341
Washington, D.C. 20240

Dear Mr. Devaney,

Thank you for this opportunity to respond to the **Draft** Audit Report on U.S. Department of Defense Contract Funds, Department of Education, Government of Guam dated August, 1999, number N-IN-GUA-004-97(E)-R.

First, it is important to set this matter in its proper perspective. Throughout the period of the contract in which the Government of Guam provided educational services to Department of Defense (DOD) students -- up to and including September 1, 1997, every dime spent by the Department of Defense reached the DOD students. The fact that DOD paid any funds to the Government of Guam subsequent to September 1, 1997 does not diminish in any way the preceding statement. Simply put, the Government of Guam utilized local money for the services provided to the DOD students, and any money received after September 1, 1997, was simply final settlement for services that had been rendered in full to the DOD students.

It is stated in the audit report, that three former directors of a politically embattled Department of Education motivated this audit. This I understand. What is beyond comprehension is the huge disparity that exists between the rationale of the audit report, and the legal analysis of the Attorney General of Guam as to the auditor's characterization of my legal obligations with regards to the \$12.4 million.

During a meeting with representatives of DOD on September 25, 1997, I received the check for \$12.4 million. At that time, it was made clear to me that as of September 1, 1997, 24 days earlier, I had no further obligation to provide educational services to DOD students. It was also clearly understood that the contract that had **been** entered into between the Government of Guam and the Department of Defense to provide educational

Mr. Devaney – US Inspector General
October, 1999
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services was simply that, a contract to provide educational services for which the Government of Guam would receive a dollar amount per student. The measure of our adherence to the DOD contract was in the education of the DOD students enrolled in the system. This was simply a service that DOD agreed to pay for, and a service that was delivered **fully and faithfully** by the Government of Guam until the contract concluded on September 1, 1997.

A recent review of this contract by the Attorney General of Guam concurs and supports my position on this matter. I also understand that the Attorney General has requested a response in writing **from** your office inquiring what legal basis your office relies upon to reach the conclusions proposed in this **Draft Audit**. I might note that to date, your office has not responded to the Attorney General, and therefore this letter must go without the benefit of your answer.

In addition to the auditors' reliance on an erroneous interpretation that the contract somehow controls the subsequent expenditure of the \$12.4 million, they asked the former Deputy Assistant Secretary of Defense for Personnel Support, Families and Education – **Ms. Carloyn Beecraft** – if she did in fact authorize the Government of Guam to expend this money in the manner that we did.

Witnesses present at the September 25, 1997 meeting between Ms. **Beecraft**, her **staff**, myself and my staff, clearly establish that in fact she did say that “the expenditure of these **funds** were up to his [the Governor's] discretion.” In this audit, however, Ms. **Beecraft**, two years later, contradicts her earlier public statement in a written memorandum to the auditors. Even assuming for the sake of argument that the later version of Ms. Beecraft's representation is correct, where is the federal authority that allows an administrator such as Ms. **Beecraft** to place enforceable conditions on an amount such as \$12 million simply through her oral statements?

Further in support of our position are written statements made on March 14, 1997 by Mr. J.J. Swizewski, the DOD-DOE Contracting **Officer**, noting Part 43 of the Federal Acquisition Regulation which specifies only Contracting Officers are empowered to execute contract modifications on behalf of the Government. Subsequent correspondence **from** Mr. Swizewski in July of 1997 stated that services **after** September 1, 1997 are not required under the contract due to the establishment of DOD schools.

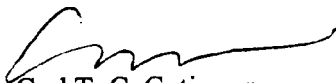
Given these circumstances, we believe it is self-evident that the audit report arrives at its conclusions unsupported by any legal argument and solely justified by the casual comments of administrators acting beyond the scope of their authority.

Mr. Devaney – US Inspector General
October, 1999
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Therefore, the Government of Guam is compelled to dispute the **Draft** Audit findings and disagree with all of the recommendations. Furthermore, the Government of Guam does **not** intend to make any changes in the disposition of **funds**.

Finally, I again reiterate that the \$12.4 million was in fact, spent on education.

very truly yours,



Carl T. C. Gutierrez
Governor of Guam

Carl T.C. Gutierrez
Maga'låhi
Governor



John F. Tarantino
Hiniråt Abugao
Attorney General

Madeleine Z. Bordallo
Tiñente Gubetnadora
Lt. Governor

Michael C. Stern
Atkådi Siundo. Mampråsiut
Chief Deputy, Prosecution

Ufisinan Hiniråt Abugao
Guåhan

Office of the Attorney General.
Guam

Kathleen E. Maher
Atkådi Sigundo, Sibit
Chief Deputy, Civil

September 20, 1999

Earl E. Devaney
Inspector General
U.S. Department of Interior
Office of Inspector General
1849 C. Street, N.W.; Mail Stop 5341
Washington, D.C. 20240

Dear Mr. Devaney:

Hafa Adai!

I am in receipt of the U.S. Department of the Interior Office of Inspector General, Draft Audit Report, over your signature, entitled U.S. Department of Defense Contract Funds, Department of Education, Government of Guam, dated August 1999, N-IN-GUA-004-97(E)-R.

In my capacity as the chief legal officer of the government of Guam, as provided for in 48 U.S.C. §1421g(d)(1), I am reviewing this audit report in order to determine whether any action on the part of my office is warranted or in the alternative to issue a formal opinion.

To that end I am requesting an explanation for certain matters contained in this **draft** audit report which I find troubling.

The stated scope of the audit included a review of transactions that occurred during fiscal years 1998 and 1999 which are allegedly related to Department of Defense contract funds.



Under the results of audit, contained on page 4 of the draft audit report, it is stated in part that:

"...the "Government of Guam did not ensure that contract funds transferred to the Public Service Recovery Fund and to the Department of Education General Fund were used for contract purposes and in a timely manner. The requirements for the use of Department of Defense contract funds were contained in the 5-year contract dated September 30, 1993, between the U.S. Department of Defense and the Government of Guam." (Emphasis added)

I find this language particularly troublesome because after reading the language of the contract referred to above it appears to me that as of September 1, 1997, a full month before the beginning of the 1998 fiscal year, the contract was no longer in effect. Additionally, there is no prospective language in the contract that would allow it to be used to evaluate the use of any money transferred from the Department of Defense to the Government of Guam subsequent to September 1, 1997.

Further, there is no language in the contract that requires an accounting of how the money is spent. The contract awarded to the Guam Department of Education for public education services for Department of Defense dependents residing on U.S. military installations in Guam is for the delivery of educational services, which were terminated on September 1, 1997. The money transferred to the Government of Guam subsequent to September 1, 1997 was not for any further performance but rather was a settling of accounts.

It is stated in the audit report that this audit was motivated by past directors of the Department of Education and I take no issue with that. However, I am concerned that your office would have difficulty understanding fundamental contract principles and use such a faulty premise in order to issue a report critical of the Government of Guam.

Therefore, I am requesting that you take the time to address this matter and please show me what it is that I may be missing in my analysis. It is my intent to determine whether any action on the part of my office is warranted or in the alternative to issue a formal opinion when the final draft audit report is published if the need for such an opinion is indicated. Therefore your assistance would be appreciated.

Senseramente,



JOHN F. TARANTINO



United States Department of the Interior

OFFICE OF INSPECTOR GENERAL
Washington, D.C. 20240

DEC 10 1999

Honorable John F. Tarantino
Attorney General of Guam
Suite 2-200E, Judicial Center Building
120 West O'Brien Drive
Hagatña, Guam 969 10

Subject: Draft Audit Report on U.S. Department of Defense Contract Funds,
Department of Education, Government of Guam
(Assignment No. N-IN-GUA-004-97-E)

Dear Mr. Tarantino:

This letter responds to your letter of September 20, 1999. In that letter, you requested an explanation of certain conclusions set forth in the draft audit report. You also expressed your disagreement with the following statement in the subject draft report:

"... the Government of Guam did not ensure that contract funds transferred to the Public Service Recovery Fund and to the Department of Education General Fund were used for contract purposes and in a timely manner."

I have set forth below our response to each of the comments you made about the above-quoted sentence. Your specific comments on this statement and our replies are as follows:

COMMENT

Should the scope of our audit (fiscal years 1998 and 1999) be applied to the Department of Defense contract, because, although the 5-year contract was originally intended to expire on September 30, 1998, the Department of Defense did not exercise the final 1-year option period and suspended the contract effective September 1, 1997, "a full month before the beginning of the 1998 fiscal year."

RESPONSE

The Scope of Audit section of our audit report states that we would review transactions occurring during fiscal years 1998 and 1999 relating to the use of contract funds that were paid to the Government of Guam. This scope included the final payment of \$12.4 million from the Department of Defense. The check for \$12.4 million was dated September 9, 1997, and was deposited by the Government of Guam on September 26, 1997, prior to suspension of the contract. The transactions charged against these funds that we reviewed were

expended during fiscal years 1998 and 1999. The purpose of our review was to determine whether the funds were used for educational purposes, and we found no indication that suspension of the contract eliminated the original purpose and intent of the contract payments, including all prior payments received under the contract but not disbursed by the Government of Guam as of the date that the contract was suspended.

COMMENT

“There is no prospective language in the contract that would allow it to be used to evaluate the use of any money transferred ... subsequent to September 1, 1997.”

RESPONSE

We believe that the contract provisions make it clear that funds paid pursuant to the contract, including the \$12.4 million final payment, were to be used for educational purposes. Regardless of the fact that the contract was not renewed for another option term, the final payment was still a payment made pursuant to the contract to fulfill the Department of Defense’s contractual obligation. The parties did not enter into any separate settlement-type agreement in connection with the final payment, which might have altered the terms of the original agreement. Accordingly, notwithstanding the characterization of this payment as a “settling of accounts,” the expenditure of these funds was subject to the same terms and conditions as all the other funds provided under the contract. Also, there is no language in the contract to suggest that funds provided under the contract could be used for anything other than educational purposes upon suspension of the contract. Specifically, Paragraph B.2.c(2) of the contract states:

Subject to the Department of Education compliance with Section C., “Statement of Work”, and Section H., “Special Provisions”, the Department of Education agrees that it shall receive the payment under contract line item 0001, in accordance with the following schedule for students enrolled in School Year (SY) 1993- 1994, adjust up or down depending on whether more or fewer than the estimated 2700 eligible dependent children receive educational services under this contract period of performance.

Additionally, Paragraphs B.3.c, B.4.c, B.5.c, and B.6.c state that, with respect to school years 1994-1995, 1995-1996, 1996-1997, and 1997-1998, respectively, “All other terms and conditions of clause B-2 Payments [B.2, “Payments,” of the contract] remain unchanged and in effect.” Finally, under Section H, Paragraph 5, the Department of Education agreed to ensure that “funds made available under this contract are used to supplement and increase the level of funding expended for the education of eligible DoD dependents attending schools operated by the Department of Education and that payments under this contract serve as a separate and net additional payment.”

COMMENT

“There is no language in the contract that requires an accounting of how the money is spent.”

RESPONSE

Section H, “Special Contract Requirements,” required the Department of Education to “establish written fiscal and funding accounting procedures that will ensure the proper disbursement of and accounting for DoD [Department of Defense] funds paid to the Department of Education” and “provide a full accounting of all funds received and disbursed under this contract. . . ninety (90) days after notification ... of the availability of funds and every ninety (90) days thereafter during the term of this contract.” Section H also states that “[n]one of the funds obligated under this contract shall be used for the performance of construction of facilities” and that “[o]bligated funds shall be expended consistent with the terms and conditions described herein.” Therefore, we believe that the intent of the contract was for funds provided by the Department of Defense to be used to improve the public school system on Guam and for the accounting of those funds.

COMMENT

“The money transferred to the Government of Guam subsequent to September 1, 1997, was not for any further performance but rather was a settling of accounts.”

RESPONSE

While we acknowledge that a Department of Defense official told a Government of Guam official that she was no longer “in a position to approve or disapprove” the Governor’s actions with respect to the use of contract funds after suspension of the contract in September 1997, we believe that it was the intent of the Department of Defense that the \$12.4 million provided as a final payment under the contract be used for educational purposes. In that regard, in an April 23, 1999, Memorandum for the Record (Enclosure), Ms. Carolyn H. Becraft, who, in September 1997, was the Deputy Assistant Secretary of Defense for Personnel Support, Families and Education and was responsible for Department of Defense educational programs, stated:

In September 1997 I traveled to Guam to present a check for the final payment of the contract (\$12,417,441.08) to Governor Gutierrez. I stressed that the money was to be used to benefit the Guam public schools. The Governor asked if the check concluded the contract. I stated that it did and that the Department of Defense (DoD) had met its contractual obligations. I said that no further DoD funds for local schools would be forthcoming. At this point, RADM Janczak indicated that this did not prelude Guam from applying for IMPACT AID for the military dependents remaining in the government of Guam schools as this was a Department of Education program, not a DoD program. The Governor discussed his desire to devote

part of the money to enhance technology in the schools. He also discussed construction needs and other equipment needs for the school svstem. ...

Later, in February 1998, Ms. Rosie Tainatongo [the Government of Guam Department of Defense Funds Administrator] called me to ask that I approve a list of items as appropriate expenses for the schools of Guam. I informed her that, with the suspension of the contract, the Governor was charged with the allocation of the moneys for the benefit of the public schools of Guam, and that I was not in a position to approve or disapprove his actions. [Emphasis added.]

COMMENT

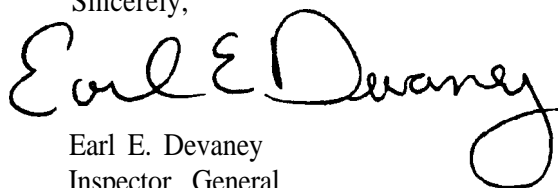
Concern was expressed that the Office of Inspector General “would have difficulty understanding fundamental contract principles and use such a faulty premise in order to issue a report critical of the Government of Guam.”

RESPONSE

As explained in our responses above, we do not believe that our understanding of the contract or the premise of our report is “faulty.” The purpose of our audit report was to assess the level of financial accountability, management controls, and compliance with applicable laws and regulations by the auditee. If, in our professional judgment, we believe that a deficiency exists in any of these areas, we are obligated by generally accepted auditing standards, the Inspector General Act of 1978, and (in the case of the insular areas) the Insular Areas Act of 1982 to report those deficiencies and to offer recommendations for improvement. We believe that the subject audit report when issued in final form will fulfill our audit oversight responsibilities in this regard.

If you have any questions regarding this matter, please contact Mr. Arnold E. van Beverhoudt, Jr., Director of Insular Area Audits, at (340) 774-8300 or Mr. Peter J. Scharwark, Jr., Senior Auditor, Pacific Office, at (671) 647-6060.

Sincerely,



Earl E. Devaney
Inspector General

Enclosure

cc: Honorable Carl T.C. Gutierrez, Governor of Guam
Ms. Carolyn H. Becraft, Assistant Secretary of the Navy,
Manpower and Reserve Affairs, Washington, D.C. 20250- 1000



THE ASSISTANT SECRETARY OF THE NAVY
(MANPOWER AND RESERVE AFFAIRS)
WASHINGTON, D.C. 20350-1000

MEMORANDUM FOR THE RECORD

FROM: Carolyn Becraft

SUBJECT: Department of Defense Funds

In July 1997, the Assistant Secretary of Defense, Fred Pang, notified Congressman Robert Underwood that the Department of Defense was cancelling its contract with the government of Guam to provide funds for the education of military children in Guam public schools, effective September 30, 1997. Furthermore, Mr. Pang informed Congressman Underwood that the Department of Defense would open it's own school system on Guam. Subsequently, I notified the Governor of Guam, Carl Gutierrez, that the contract would not be renewed.

In September 1997 I traveled to Guam to present a check for the final payment of the contract \$(12,417,441.08) to Governor Gutierrez. I stressed that the money was to be used to benefit the Guam public schools. The Governor asked if the check concluded the contract. I stated that it did and that the Department of Defense (DoD) had met its contractual obligations. I said that no further DoD funds for local schools would be forthcoming. At this point, RADM Janczak indicated that this did not preclude Guam from applying for IMPACT AID for the military dependents remaining in the government of Guam schools as this was a Department of Education program, not a DoD program. The Governor discussed his desire to devote put of the moneys to enhance technology in the schools. He also discussed construction needs and other equipment needs for the school system.

Present at the meeting were RADM Martin Janczak, Dr. Nancy Bressel (DoDEA), Ike Santos, Rosie Tainatongo, and myself.

Later, in February 1998, Ms. Rosie Tainatongo called me to ask that I approve a list of items as appropriate expenses for the schools of Guam. I informed her that, with the suspension of the contract, the Governor was charged with the allocation of the moneys for the benefit of the public schools on Gum, and that I was not in a position to approve or disapprove his actions.


Carolyn H. Becraft

STATUS OF AUDIT REPORT RECOMMENDATIONS

Finding/Recommendation Reference	Status	Action Required
1, 2, 3, and 4	Unresolved.	Provide a response to the Contracting Officer of the Department of Defense, with a copy of the response to our Pacific Office. The response should include a rationale for the Government of Guam's nonconcurrence with the recommendations.

**ILLEGAL OR WASTEFUL ACTIVITIES
SHOULD BE REPORTED TO
THE OFFICE OF INSPECTOR GENERAL**

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http://www.oig.doi.gov/hotline_form.html

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