

UNITED STATES DEPARTMENT OF EDUCATION  
OFFICE OF INSPECTOR GENERAL



AUDIT SERVICES

March 18, 2011

**FINAL ALERT MEMORANDUM**

**TO:** Philip Maestri  
Director, Risk Management Service  
Office of the Secretary

**FROM:** Keith West /s/  
Assistant Inspector General for Audit

**SUBJECT:** Insufficient Controls for the Puerto Rico Department of Education's Use of Education Funds for Personal Services Contracts  
**Control Number ED-OIG/L04K0018**

The purpose of this **final alert memorandum** is to apprise you of continuing risks with the Puerto Rico Department of Education's (PRDE) use of U.S. Department of Education (Department) funds for personal services contracts (PSCs). We conducted an investigation and an audit and identified issues with PRDE's award and administration of PSCs, resulting in the misuse and abuse of Department funds. Specifically, our investigation found that PRDE awarded fraudulent PSCs, and our audit found that PRDE had insufficient controls over PSCs. Based on the results of our work, we consider PSCs to be a high-risk contracting vehicle and recommend that the Department take action to protect Department funds from potential abuse and misuse.

PRDE awards PSCs to individuals that provide services either not provided through regular work programs or required for exceptional situations. Activities carried out through PSCs include special projects such as after-school and summer school programs, and administrative activities such as the processing of backlogs of invoices from third-party contractors.

**Fraudulent PSCs**

In our joint investigation with the Federal Bureau of Investigation and the Office of the Comptroller of Puerto Rico, we identified fraud at PRDE committed through the use of PSCs. The fraud resulted in unearned PRDE payments of approximately \$450,000 to individuals through fraudulent PSCs. Specifically, we found that the Director of PRDE's Community Integrated Services Program (CISP)<sup>1</sup> conspired with seven others<sup>2</sup> to award false PSCs to themselves, to former independent contractors, and to fictitious contractors from 2002 through 2006. The false contracts were awarded to provide services to CISP participants. The individuals billed PRDE through false invoices and attendance

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<sup>1</sup> This program used PSCs as a means for providing educational and vocational training offerings to single mothers and fathers, pregnant teenagers, unemployed persons, and families living in special communities and public housing projects.

<sup>2</sup> These included four PRDE employees and three other individuals who were family members and acquaintances.

sheets and collectively received about \$450,000 in payments for services that were not rendered.<sup>3</sup> The CISP Director awarded PSCs through the CISP and authorized the necessary documentation to obtain the payments from PRDE.

On April 25, 2008, a Federal grand jury indicted the eight individuals, all of whom were convicted on charges of conspiracy to commit program fraud. The individuals were sentenced on different dates from December 1, 2008, through February 5, 2010, and were ordered to pay restitution of the funds fraudulently obtained. Because the investigation raised concerns about potential weaknesses in PRDE's system of internal controls that provided the opportunity for fraud, we initiated an audit of PRDE's award and administration of PSCs.

### **Insufficient Internal Controls Over PSCs**

In January 2011, we reported<sup>4</sup> that PRDE lacked sufficient controls to ensure compliance with State and Federal laws in awarding PSCs and in ensuring that those services were allowable and adequately supported. We also found deficiencies in PRDE's contracts and amendments and identified a total of \$164,914<sup>5</sup> in unsupported or questioned costs related to inadequate support for services provided, services provided prior to contract approval, hours paid in excess of contracted hours, and errors in contract compensation rates paid.

In addition, PRDE provided unreliable expenditure data that did not reconcile with payment data for \$161,527,366 in payments made during calendar years 2006 through 2008, resulting in a discrepancy of \$15 million. PRDE also did not maintain a registry of PSCs corresponding to \$159,474,554 paid through its paper-based payments system. As a result, we could not validate the number of awarded PSCs associated with the total payments to reconcile the expenditure data.

The significant deficiencies found are of considerable concern, and they resulted from a substantial lack of controls and accountability as follows—

- An inadequate archiving system to effectively retrieve PSCs and documentation supporting compliance with regulations governing the award process and support of payments;
- Lack of a centralized registry of PSCs that complied with applicable requirements;
- Insufficient controls to adequately safeguard contract documentation against unauthorized changes; and
- Lack of standardized written policies and procedures governing the PSC award and payment processes.

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<sup>3</sup> The CISP received State funds and Department funds from the Adult Education Program and the Safe and Drug Free Schools Program.

<sup>4</sup> Refer to final audit report titled "Puerto Rico Department of Education's Award and Administration of Personal Services Contracts," Control Number ED-OIG/A04J0005, dated January 21, 2011. The report is posted on the OIG Internet Web site at <http://www2.ed.gov/about/offices/list/oig/auditreports/fy2011/a04j0005.pdf>, under the heading Office of Elementary and Secondary Education.

<sup>5</sup> Our review covered 61 PSCs and related payments totaling \$459,609 for services provided during the period of August 29, 2005, through June 30, 2009.

PRDE's internal control deficiencies resulted in the lack of documentation supporting compliance with the PSC award process, unauthorized changes made to two PSCs, PSCs and amendments with format and content deficiencies, and unsupported or questioned costs representing nearly 36 percent<sup>6</sup> of the total payments reviewed for the PSCs. PRDE uses a significant amount of Department funds for PSCs to obtain and provide needed services. According to payment data provided by PRDE, during the 3-year period from January 2006 through December 2008, PRDE paid about \$161,527,366 in PSCs funded with Department funds.

In our January 2011 report to PRDE, we recommended that the Department require PRDE to—

- Develop and implement internal controls over PSC records and related documentation that support compliance with regulations and payments.
- Either provide adequate and reliable documentation of unsupported payments and contracts or refund the unsupported amount to the Department.
- Return to the Department questioned costs related to services provided before the contract was approved, payment for hours in excess of contracted hours, and payment for errors in contract compensation rates.
- Reconcile the \$15 million discrepancy between PSC expenditures paid with Department funds, recorded in PRDE's financial accounting system with payment data from its payments system and its Part-Time and Irregular Employees System; have an independent audit office or CPA firm assess PRDE's reconciliation and issue an opinion on its accuracy; and return to the Department all of the amounts that cannot be reconciled.
- Record all PSCs awarded in a centralized registry of PSCs.

The General Education Provisions Act (20 U.S.C. Section 1234c) authorizes the Department to take any action authorized by law when a recipient is failing to comply substantially with any requirement of law applicable to Federal program funds. Without sufficient controls over PSCs, significant funds are at increased risk. As such, the Department should prohibit PRDE's use of Department funds for PSCs until PRDE demonstrates that it has implemented sufficient controls to assure those funds are used for intended purposes.

## **RECOMMENDATIONS**

We recommend that your office—

- 1.1 Require PRDE to demonstrate that it has implemented sufficient controls over PSCs to ensure that Department funds are safeguarded; and, if it cannot, impose special conditions on all Department grants awarded to PRDE, including grants awarded under the American Recovery and Reinvestment Act of 2009, prohibiting PRDE's use of grant funds for PSCs.
- 1.2 Closely monitor PRDE's implementation of internal controls over PSCs included in its corrective action plan provided in response to the January 2011 report.

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<sup>6</sup> We identified \$164,914 of \$459,609 in payments reviewed as either unsupported or unallowable.

## **Department Comments**

In its response to the draft alert memorandum, the Department's Office of the Secretary, Risk Management Service (RMS) agreed that the issues with PRDE's award and administration of PSCs are significant and warrant corrective actions. According to RMS, it requested that by April 15, 2011, PRDE provide evidence of the controls implemented over PSCs to ensure that Department funds are safeguarded. Also, RMS requested that PRDE direct its Internal Audit Office (IAO) to review the PSC controls and their effectiveness to determine any further RMS action to be taken. Finally, RMS agreed with Recommendation 1.2 and stated that during future site visits, it will closely monitor PRDE's implementation of internal controls over PSCs. The Department's response in full is included as Attachment 2.

## **OIG Response**

To recognize RMS actions underway, we slightly modified Recommendation 1.1. We commend RMS for initiating actions to address Recommendation 1.1. Any evidence of controls over PSCs provided by PRDE and the IAO's assessment of those controls will be useful in determining what additional action, if any, is needed to protect Department funds from potential abuse and misuse.

We conducted our work in accordance with the OIG quality standards for alert memoranda.

Corrective actions proposed (resolution phase) and implemented (closure phase) by your office will be monitored and tracked through the Department's Audit Accountability and Resolution Tracking System (AARTS).

Alert memoranda issued by the Office of Inspector General will be made available to members of the press and general public to the extent information contained in the memoranda is not subject to exemptions in the Freedom of Information Act (5 U.S.C. Section 552).

For further information, please contact Denise M. Wempe, Regional Inspector General, Region IV, at (404) 974-9416.

Attachments

**Acronyms/Abbreviations/Short Forms Used in this Report**

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AARTS	Audit Accountability and Resolution Tracking System
CISP	Community Integrated Services Program
Department	U.S. Department of Education
ED-OIG	U.S. Department of Education / Office of Inspector General
IAO	Puerto Rico Department of Education's Internal Audit Office
PRDE	Puerto Rico Department of Education
PSCs	Personal Services Contracts
RMS	U.S. Department of Education, Office of the Secretary, Risk Management Service
U.S.C.	United States Code



UNITED STATES DEPARTMENT OF EDUCATION

OFFICE OF THE SECRETARY

Risk Management Service

March 4, 2011

MEMORANDUM

TO: Keith West  
Assistant Inspector General for Audit  
Office of Inspector General

FROM: Philip Maestri /s/  
Director, Risk Management Service  
Office of the Secretary

SUBJECT: Response to Draft Alert Memorandum,  
“Insufficient Controls for the Puerto Rico Department of Education’s Use  
of Education Funds for Personal Services Contracts”  
**Control Number ED-OIG/L04K0018**

Thank you for the opportunity to respond to the draft alert memorandum (memo) cited above. The purpose of the alert memo was to apprise Risk Management Service (RMS) of continuing risks with the Puerto Rico Department of Education’s (PRDE’s) use of U.S. Department of Education (Department) funds for personal services contracts (PSCs). The draft alert memo advises that the Office of Inspector General (OIG) conducted an investigation and an audit and identified issues with PRDE’s award and administration of PSCs, resulting in the misuse and abuse of Department funds. Specifically, the investigation found that PRDE awarded fraudulent PSCs, and the audit found that PRDE had insufficient controls over PSCs. Based on the results of this work, OIG considers PSCs to be a high-risk contracting vehicle and they recommend the Department take action to protect Department funds from potential abuse and misuse.

OIG requested comments on the information presented in the draft alert memo and a response on the recommendations provided. RMS agrees that these findings are significant and that the lack of sufficient controls for the award and administration of PSCs increases the risk for potential abuse and misuse of Department funds. RMS agrees that although PRDE has taken steps toward correcting the issues identified<sup>7</sup>, additional actions need to be taken and implemented in order to ensure these findings are addressed. Our specific responses on OIG’s recommendations are provided below.

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<sup>7</sup> As described in the final OIG audit report titled “Puerto Rico Department of Education’s Award and Administration of Personal Services Contracts,” Control Number ED-OIG/A04J0005, dated Jan. 21, 2011.

OIG Recommendation: OIG suggests that RMS impose special conditions on all Department grants awarded to PRDE, including grants awarded under the American Recovery and Reinvestment Act of 2009, prohibiting PRDE's use of grant funds for PSCs until PRDE demonstrates that it has implemented sufficient controls over PSCs to ensure that Department funds are safeguarded.

RMS Response:

In lieu of imposing additional special conditions, RMS has requested PRDE provide evidence that they have implemented sufficient controls over PSCs to ensure that Department funds are safeguarded. Specifically, RMS has requested PRDE to provide copies of all documentation on PSC controls implemented to date. RMS has also requested that PRDE direct its Internal Audit Office (IAO) to conduct a review of the PSC controls and their effectiveness in ensuring Department funds are in fact safeguarded. RMS has requested that the documentation and the review by the IAO be completed, and a final report on the results submitted to RMS, by Friday, April 15, 2011. Further RMS action will be determined based on the results of the review of the submissions.

OIG Recommendation: OIG suggests that RMS closely monitor PRDE's implementation of internal controls over PSCs included in its corrective action plan provided in response to the January 2011 report.

RMS Response:

During future site visits, RMS will closely monitor PRDE's implementation and the effectiveness of internal controls over PSCs included in its corrective action plan provided in response to the January 2011 report.

Again, we appreciate the opportunity to provide this response.