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The Special Counsel

January 31, 2001

The President
The White House
Washington, D.C. 20500

Re: OSC File No. DI-99-0862

Dear Mr. President:

In accordance with 5 U.S.C. § 1213(e)(3), I am transmitting a report and supplemental report from the Honorable Frank S. Holleman, III, Deputy Secretary, United States Department of Education, sent to me pursuant to 5 U.S.C. §§ 1213(c) and (d). I transmitted the disclosure to the Honorable Richard Riley, Secretary. Secretary Riley delegated authority to Deputy Secretary Holleman to respond pursuant to 5 U.S.C. § 1213(c). The reports set forth the findings and conclusions of the agency's review of disclosures of information allegedly evidencing violations of law, rule, or regulation, gross mismanagement, a gross waste of funds, and an abuse of authority by officials of the Department of Education, Washington, D.C.

The whistleblower, Mr. John Gard, provided comments on the agency reports to this office pursuant to 5 U.S.C. § 1213(e)(1), which I am also transmitting.

We have carefully re-examined Mr. Gard's original disclosures and reviewed the agency's response and Mr. Gard's comments. As described below, I have determined that the agency's findings appear reasonable within the meaning of section 1213(e)(2), with the exception of the agency's conclusion that the investigative report did not reveal "gross mismanagement" within the meaning of applicable law.

The Whistleblower's Disclosures

Mr. Gard alleged that since 1997, the OCF&CIO has failed to maintain adequate controls over billions of dollars of Federal grant money, has been unable to account for grant monies, and has made improper disbursements to grant recipients. He alleged that a new financial management system, the training and planning for which was begun by the OCF&CIO in 1997, and which was implemented in 1998, does not contain proper internal and external security controls, audit trails, or accounting functions. As a result, the system, known as the Grants Administration and Payment System (GAPS), has caused the agency to make payments to unknown or unidentified organizations, to adjust the cash accountability of an

account without any legal basis for the adjustment, and to file reports containing amounts not supported by the system.

Mr. Gard also alleged that despite his warnings about the serious flaws in the system, the agency recklessly proceeded with the implementation of the new system and failed to properly track data transmitted from the old system to the new. Consequently, independent auditors reviewing the agency's accounts issued a disclaimer of opinion on the agency's financial statements for fiscal year 1998. The audit found that weaknesses in the system's ability to perform a year-end closing process or produce automated consolidated financial statements prevented reconciliation of the accounts. The agency could not adequately perform reconciliations and could not provide sufficient documentation supporting transactions. Mr. Gard asserts that had the agency heeded his warnings in 1997, these problems could have been avoided or minimized.

In May 1998, Mr. Gard became aware that serious security gaps existed in the system. For instance, he alleged that government employees and contractors assigned to a system Hotline were releasing recipient UserIDs and passwords over the phone; that management provided Hotline personnel with paper lists of the recipient UserIDs and passwords, and that copies of such confidential lists were found unsecured in the office; and that management released one common UserID and password to employees and contractors in response to a system deficiency that prevented over 500 recipient accounts from drawing funds, with the result that every employee and contractor would be able to alter critical information in the system without being identified. The lack of controls over UserIDs and passwords rendered the system vulnerable to fraud and left it without an audit trail.

Mr. Gard also alleged that the GAPS system contained a substantial number of incorrectly mapped accounts and that management failed to track accounts during the system conversion. In May 1998, Mr. Gard identified additional irregularities when he was assigned to work on cash reconciliations and reports. Amounts that he entered on the reconciliations were supported by the accounting system. Some of the amounts Mr. Gard entered were changed by senior officials and/or the budget office, according to Mr. Gard. He believed that the changes were made in attempts to balance the agency's accounting records, which he believed to be out of balance by millions of dollars.

Summary of Report

The agency report reviewed the activities and functions of the Office of the Chief Financial Officer (OCFO) within the context of Mr. Gard's allegations. The report states that the issues raised by Mr. Gard were widely known within the OCFO and have been extensively documented independent of the OSC transmittal. According to the report, Mr. Gard's allegations closely align with concerns raised by the agency's Office of Inspector General (OIG) since the implementation of GAPS, the grantee payment arm of the agency's financial management system.

The report cites statistics showing that the agency has satisfied most of the concerns raised. It states that the OIG listed forty-six recommendations for corrective action as of September 1998. As of April 2000, the OCFO had implemented all of the OIG recommendations. Additional concerns raised by the General Accounting Office (GAO) and the agency's independent financial statement auditor discussed below in detail are being addressed. The supplemental report indicated that of four recommendations made in the GAO report, three were complete by October 2000, and work on the final recommendation was on track to be completed in November. With respect to the status of financial statement audits, 15 of 139 issues remain unresolved, 14 issues were scheduled for completion in November and December, and one item is scheduled for completion in September 2001. The report asserts generally that through the implementation of GAPS and continuous internal process improvements, GAO's recommendations have been addressed.

The report contains a compilation of extensive documentation that the agency believes demonstrates that the OCFO worked continuously in a genuine team effort with the OIG to resolve problems and concerns. The report is accompanied by 24 exhibits, including OIG audit reports and action memoranda, and agency responses to same; reports of agency testimony before GAO; and GAO's report to Congress and the agency response to same.

A. Internal Controls

1. GAPS Reconciliation

The report addresses Mr. Gard's allegations that GAPS has caused the agency to adjust the cash accountability of an account without any legal basis for the adjustment, and to file reports containing amounts not supported by the system. Although not expressly stated, the report appears to substantiate Mr. Gard's allegations that the agency lacked adequate management controls over the process for reconciling GAPS with recipient records. When the agency converted from EDPMS to GAPS, problems occurred in reconciling actual expenditure activity under each grant to amounts reported in GAPS. The prior system, EDPMS, tracked grant awards that an institution had in the aggregate. GAPS tracks by individual grant awards. According to the report, in order to convert records to GAPS, the agency decided to charge the individual grant awards for an institution against the existing, pooled, award balance. This process required reliance on the grant recipient to adjust GAPS, either on-line or by calling the agency's hotline. Because the process is dependent upon recipients identifying required adjustments, the agency lacked internal controls over the reconciliation process. Both the agency and the OIG identified this issue as a high priority for resolution.

The report concluded that the activities identified do not violate any law, rule, or regulation. The supplemental report concludes that the allegations do not rise to the level of gross mismanagement, because a finding of gross mismanagement must establish that the agency consciously refused to remedy known legal deficiencies or, at the very least, pursued a pattern of conscious disregard for the truth. To the contrary, the report states that the agency

has been very active in recognizing and attempting to remedy financial accounting issues brought to its attention. The report maintains that the agency's responses to the issues are evidence of corrective actions taken with an eye toward accomplishment of the agency's mission to support education grant programs. The report contains assurances that "it has and will continue to commit appropriate resources to correct conditions that challenge internal controls."

The supplemental report also concludes that there has been no gross waste of funds, because there is no evidence that the agency wasted funds implementing GAPS or that any expenditure was significantly out of proportion to the benefits received by the agency. The supplemental report also claims that although there were system implementation problems, GAPs will provide benefits to the agency's financial management capabilities. Finally, the supplemental report concluded that there was no abuse of authority arising from the allegations.

The report stated that the agency is currently engaged in a reconciliation effort between GAPS and the Financial Management Software System (FMSS), the agency's present financial management system. The stated plan is to reconcile grantees' accounts all the way back to the implementation of GAPS in May 1998. The plan includes synchronizing summary transactions in GAPS and summary postings in FMSS; identifying and correcting general ledger account balance errors; and determining if the old financial system data used for the GAPS conversion was out of balance with FMSS, and if so, rectifying the errors. If differences are identified, the agency has pledged to "work closely with the appropriate U.S. Treasury Department authorities to insure that correcting adjustments are properly executed and recorded."

The supplemental report describes the reconciliation project as complete. The agency is continuing to validate a series of adjustments that will fully reconcile FMSS and GAPS from May 1998 through June 2000.

The report also states that a new core financial management system (FMS) implementation began October 1, 1999, to address the agency's historical problems with producing auditable financial statements, and to accurately reflect account balances for all the subaccounts that fall under each of 200 appropriations. The agency projects full implementation of the new FMS by the close of FY 2001.

2. Financial Statements Inauditable

The report substantiated Mr. Gard's allegations that the agency's financial statements were deemed inauditable for FY 1998. The report acknowledged violations of the Chief Financial Officers Act, the Federal Financial Management Improvement Act, and the Credit Reform Act. The violations occurred: 1) because the agency was found lacking in adequate, integrated financial management systems, reports, and oversight to prepare timely and accurate financial statements; 2) because the agency had neither fully implemented a capital planning

and investment process, nor performed an assessment of the information resource management knowledge and skills of agency personnel, including a plan to correct deficiencies; and 3) because the agency did not transfer excess funds related to FFELP to the Department of Treasury as required.

Again, the agency assures that it has and will continue to commit appropriate resources to correct conditions that challenge internal controls. In addition to the items noted above, the report cites the following actions, which the agency asserts were initiated independent of the disclosure investigation and report ordered by OSC: 1) the agency has purchased and implemented reconciliation software to perform monthly cash reconciliations with Treasury; 2) the agency is implementing a capital planning and investment management process that is expected to be in place by the end of FY 2000; 3) the agency is liquidating fund balances and returned $1.8 billion to the Department of Treasury in February which put it into compliance with the Credit Reform Act. The agency expressed its commitment to not missing the deadline to return funds from this account.

B. System Security

While not expressly stated, the report appears to substantiate Mr. Gard's allegations that serious weaknesses in system security existed, making the system vulnerable to fraud and lacking an audit trail. The report found no violation of law, rule, or regulation. Further, it found no evidence of gross mismanagement, gross waste of funds, or an abuse of authority.

The General Accounting Office (GAO) reviewed the agency's financial management system and manual internal controls over grantback activity and related funds control. The deficiencies identified in the GAO report were identified as financial management system deficiencies, inadequate systems of funds control, and manual internal control weaknesses. Deficiencies in the following five areas were cited: 1) pre-1998 pooling method of accounting for grant drawdowns; 2) general computer controls; 3) grant reconciliation efforts and funds control; 4) inadequate supporting documentation for transactions; and 5) lack of adherence to and inadequacy of the agency's policies and procedures. The GAO report specifically identified neither violations of law nor instances of fraud. GAO did find that the agency could not provide assurances that it was in compliance with statutory restrictions regarding the use of funds, and found that there continues to be an increased risk of fraud, waste, and mismanagement of grant funds.

Based on the GAO report, the agency developed a plan to improve accounting for grants tasks, to be implemented by September 2000. The supplemental report represented this plan to be on target for completion in November 2000. The detailed plan calls for reconciliations, implementation of adequate controls, and return of funds to Treasury. Policy revisions include initiatives to improve documentation and records, and to impose and enforce supervisory controls over adjustments and monthly reports to Treasury.

Finally, the report substantiates a violation of guidance issued by the Office of Management and Budget (OMB) in OMB Circular A-130, with respect to the misuse of user IDs and passwords. The report asserts that any remaining concerns about User IDs and passwords have been corrected.

C. Data Conversion

Mr. Gard alleged that GAPS contained a substantial number of incorrectly mapped accounts that management failed to track during system conversion. The report claims that management actions taken to convert to the new system prevented the problem stated in Mr. Gard's allegation from occurring. The report states that the agency does not believe the actions taken violated any law, rule, or regulation, or constitute gross mismanagement, a gross waste of funds, or an abuse of authority. The GAO report, however, confirmed that the agency did not maintain complete, detailed records from the discontinued accounting system when it converted to its new accounting system in October 1997. In addition, the GAO report found that the agency could not provide documentation to support that the grant balances in EDPMS at the time of conversion in May 1998 agreed to the beginning grant balances in GAPS, and that the true grantback activity at the time of conversion in October 1997 was properly transferred to the new general ledger system.

The GAO report indicates that the agency agreed with the recommendations and has implemented a detailed plan to address and correct the deficiencies.

Whistleblower's Comments on Report

Mr. Gard provided extensive comments on the report, including narrative commentary, a revised sequence of events, and documentation Mr. Gard asserts supports some of his initial disclosures. He seeks positive credit and recognition for bringing the allegations to the attention of the agency, and relief from the retaliation and reprisal he claims to have experienced as a result of his whistleblowing. While he states that Appendix X to the report is responsive to the allegations contained in the whistleblower complaint he filed with OSC, Mr. Gard asserts that it also provides further documentation of current and ongoing agency whistleblower reprisal. He is of the opinion that Appendix X indicates that the agency has finally recognized, in theory, the need to implement a number of financial management and system corrections that he and other former employees previously informed the agency would be necessary. Mr. Gard believes that the report is contradicted in many ways by the agency's own statements, actions, and internal documentation, and by the independent audit reports. He provides point-by-point analysis of the findings.

Mr. Gard questions the status of the security issues identified by the OIG and targeted for completion in March 1999. He claims that the report contains fabrications regarding the use of and/or discontinuance of a SuperUser ID and password during the period May 18, 1998, to June 17, 1998. He states that the agency did not plan on issuing nor did it intentionally

issue temporary GAPS UserIDs and passwords. He also alleges that "a dozen employees in [his] work area, including [Mr. Gard], were using or had the capability to use the released super UserID and password from May 18, 1998, through June 17, 1998, with the knowledge and consent of senior OCFO management officials." He points out that this is confirmed by the OIG action memoranda included with the report.

Mr. Gard also expressed the opinion that, even as modified, GAPS does not allow the agency to monitor the amount of funds being held by the grantee and to perform grantee off-site computerized cash management analysis as EDPMS did. As a result, the agency cannot monitor the amount of federal cash funds being held by a grantee. He believes that the agency's corrective action measures make it look like the agency is doing a better job of management, when in fact, the agency is burying the mismanagement. He asserts that the report is non-responsive to the allegation that reports were filed that were not supported by the agency's financial records. He claims that the employees of the agency are the true problem; they have designed and implemented accounting systems that do not work.

Mr. Gard believes that the "agency" destroyed the award archived database (an official record of the EDPMS archived award and grants authorization, payment, and expenditure amounts) because the use of this database would complicate management's attempt to cover-up Anti-Deficiency Act violations. He asserts that the agency cannot actually or legally reconcile the grantees' GAPS accounts, determine the correct authorization, payment, or expenditure amount of an award or grant, determine the validity of the request, defend the agency, or prosecute grantees, without using the award archived database.

Finally, Mr. Gard responded to the supplemental report with additional comments. He commented that the agency's claim that there has been no gross mismanagement or gross waste of funds is unfounded. The evidence of a lack of an appropriate accounting system and sloppy bookkeeping is sufficient to show gross mismanagement even if there has been some progress in implementing GAO's recommendation. Moreover, according to Mr. Gard, there is evidence of a gross waste of funds. The agency has disbursed unrecorded payments in an unknown amount; has made payments to grantees with false names; and has issued duplicate payments in excess of $150 million.

With respect to the allegations of an abuse of authority, Mr. Gard continues to allege that he has provided more than sufficient evidence that this has occurred. He cites the agency's actions in removing him, shunning him, failing to provide him meaningful work, and attempting to drive out employees as examples. He believes that the agency's report has not refuted a single fact put forth by him.

Special Counsel's Comments on Report

I have determined, pursuant to section 1213(e)(2), that the agency's report contains all of the information required under section 1213(d), and that the findings of the agency head

appear to be reasonable, with the exception of the negative finding of gross mismanagement, for the reasons stated below.

Notwithstanding the conclusions stated in the supplemental report, that agency officials did not engage in gross mismanagement, a gross waste of funds, or an abuse of authority, the detailed information provided by the agency with its report appears to substantiate Mr. Gard's allegations as to gross mismanagement. It appears that the agency was plagued by issues related to management, in part because of the deficiencies in GAPS and the agency's other financial management and accounting systems.

GAO found that although the agency had already taken, or planned, actions intended to resolve these problems, the agency plan lacked sufficient detail to ensure proper implementation and adequate oversight. The final GAO report also noted that although GAPS is expected to provide more sound funds control practices, the problems identified in the GAO review will require a sustained, high-priority effort by the agency's top management to ensure that these persistent and long-standing problems are fully resolved and do not continue under its new systems.

The agency's October 2000, response to the GAO findings contains assurances that through the implementation of GAPS, and continuous internal process improvements, GAO's recommendations are currently being addressed. The response outlines the agency's progress in completing corrective actions, including the development and implementation of detailed policies and procedures.

The agency argues in its supplemental report that Mr. Gard's allegations do not rise to the level of gross mismanagement as articulated by the courts and the MSPB. It asserts that a finding of gross mismanagement must establish that the agency consciously refused to remedy known legal deficiencies or, at the very least pursued a pattern of conscious disregard for the truth. The agency claims that because the OCFO took and is continuing to take corrective action, and is making significant progress in resolving problems, no gross mismanagement could have occurred.

The agency is incorrect that a finding of "gross mismanagement" requires a conclusion that it acted in deliberate disregard of known deficiencies. Instead, gross mismanagement exists where there has been management action or inaction that creates a "substantial risk of significant adverse impact upon the agency's ability to accomplish its mission." Nafus v. Dept. of Army, 57 M.S.P.R. 386, 395 (1993). Here, the fact that the agency as a whole was plagued by the failure to maintain adequate controls, to the extent that it could not produce auditable financial statements or account for billions of taxpayer dollars, suggests that management action or inaction *has* created a substantial risk of significant adverse impact upon the agency's ability to accomplish its mission. Indeed, GAO concluded that because of the deficiencies in the financial management system, and funds control and internal control weaknesses, there is "increased risk of fraud, waste, and mismanagement of grant funds," and

an increased risk that "Anti-Deficiency Act violations could occur and not be promptly identified and reported."

It is also notable that the agency had difficulty producing auditable financial statements for years prior to the conversion. This provides evidence of long-standing weaknesses in the agency's internal controls. Notwithstanding these pre-existing weaknesses, the agency's decision to update its financial management systems without first ensuring the stability of its current system security or providing for proper retention of data appears to fall within the legal definition of gross mismanagement.

Conclusion

As required by section 1213(e)(3), I have sent a copy of the report to the Chairmen of the Senate Committee on Health, Education, Labor and Pensions, and the House Committee on Education and the Workforce. We have also filed copies of the report and Mr. Gard's comments in our public file and closed the matter.

Respectfully,

Elaine Kaplan

Enclosure