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U.S. Naval Academy Officials Did Not Adhere to  
Contracting and Gift Policies

# Report Documentation Page

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## Acronyms and Abbreviations

AAM	American Association of Museums
ADA	Antideficiency Act
ASN(M&RA)	Assistant Secretary of the Navy (Manpower and Reserve Affairs)
BUPERS	Bureau of Naval Personnel
DONHAMS	Department of Navy Heritage Asset Management System
GAO	Government Accountability Office
NAAA	Naval Academy Athletic Association
NABSD	Naval Academy Business Services Division
NAF	Nonappropriated Fund
NAFI	Nonappropriated Fund Instrumentalities
NHHC	Naval Heritage and History Command
SECNAV	Secretary of the Navy
SFFAS	Statement of Federal Financial Accounting Standards
SJA	Staff Judge Advocate
U.S.C.	United States Code
USD(C)/CFO	Under Secretary of Defense (Comptroller)/Chief Financial Officer, DoD
USNA	United States Naval Academy





INSPECTOR GENERAL  
DEPARTMENT OF DEFENSE  
400 ARMY NAVY DRIVE  
ARLINGTON, VIRGINIA 22202-4704

November 7, 2011

MEMORANDUM FOR UNDER SECRETARY OF DEFENSE (COMPTROLLER)/CHIEF  
FINANCIAL OFFICER, DOD  
CHIEF OF NAVAL OPERATIONS  
NAVAL INSPECTOR GENERAL  
AUDITOR GENERAL OF THE NAVY  
SUPERINTENDENT, U.S. NAVAL ACADEMY  
DIRECTOR, NAVAL HERITAGE AND HISTORY COMMAND

SUBJECT: U.S. Naval Academy Officials Did Not Adhere to Contracting and Gift Policies  
(Report No. DODIG-2012-017)

We are providing this report for review and comment. We performed this audit in response to a request from staff of the Senate Armed Services Committee. U.S. Naval Academy officials improperly contracted for the production of a short motion picture and television commercials and wasted about \$3.5 million on the contract. In addition, they allowed the acceptance of in-kind gifts without proper authorization, did not properly record all in-kind gifts, inappropriately accepted \$343,208 in corporate sponsorship funds, and accepted monetary gifts without reviewing for prohibited sources. This report discusses a potential violation of the Antideficiency Act. We considered management comments on a draft of this report when preparing the final report.

DoD Directive 7650.3 requires that recommendations be resolved promptly. The Assistant Secretary of the Navy (Manpower and Reserve Affairs) responded for the Chief of Naval Operations; Superintendent, U.S. Naval Academy; and the Director, Naval Heritage and History Command. The Assistant Secretary comments on Recommendations B.2.a, E.1, and E.2 are partially responsive and comments on Recommendations A.2, B.1.a, B.1.b, and D.2 are not responsive. We request additional comments by December 7, 2011. Please see the recommendations table on the back of Results in Brief.

If possible, send a .pdf file containing your comments to [audfmr@dodig.mil](mailto:audfmr@dodig.mil). Copies of your comments must have the actual signature of the authorizing official for your organization. We are unable to accept the /Signed/ symbol in place of the actual signature. If you arrange to send classified comments electronically, you must send them over the SECRET Internet Protocol Router Network (SIPRNET).

We appreciate the courtesies extended to the staff. Please direct questions to me at (703) 601-5868 (DSN 329-5868).

*Patricia A. Marsh*  
Patricia A. Marsh, CPA  
Assistant Inspector General  
Financial Management and Reporting







# Results in Brief: U.S. Naval Academy Officials Did Not Adhere to Contracting and Gift Policies

## What We Did

We determined whether the U.S. Naval Academy (USNA) and its supporting organizations were properly disbursing, recording, accepting, and reporting donations, gifts, and nonappropriated funds (NAFs). From January 1 through December 31, 2010, USNA received 381 monetary gifts, totaling \$5.7 million, and 153 in-kind gift donations, valued at \$25.1 million.

## What We Found

USNA officials did not have adequate processes for disbursing, recording, accepting, and reporting gifts and NAFs. Specifically, the Naval Academy Business Services Division (NABSD) Director improperly contracted for a short motion picture and television commercials. This occurred because the USNA Deputy for Finance (Deputy) did not provide proper oversight of the contract and NABSD did not have a contracting officer. As a result, the NABSD Director wasted about \$3.5 million. USNA may have augmented its budget by \$3.5 million and may have committed a potential Antideficiency Act (ADA) violation.

The USNA Museum Director did not properly record all of its in-kind gifts into its inventory system and never conducted a complete inventory. This occurred because Museum officials did not have policies and procedures in place for recording in-kind gifts. As a result, inventory was vulnerable to loss and theft.

The Deputy accepted over \$184,000 of in-kind gifts from an alumnus without obtaining the proper authorization and failed to inventory the gifts. This occurred because he bypassed the Navy gift receipt process. The acceptance gives the appearance of impropriety, and failing to inventory increases the risk of loss or theft.

The NABSD Director inappropriately accepted \$343,208 in corporate sponsorship funds. This occurred because the Deputy did not provide adequate oversight. As a result, the NABSD Director retained unauthorized funds.

The Deputy and USNA Comptroller did not review USNA Foundation monetary gifts to determine whether they were received from prohibited sources. This occurred because the USNA and the Foundation memorandum of understanding did not require the Foundation to review gifts for prohibited sources or to provide the donor source. As a result, USNA could be receiving gifts from prohibited sources.

## What We Recommend

The Under Secretary of Defense (Comptroller)/Chief Financial Officer, DoD (USD(C)/CFO), should initiate a preliminary review for a possible ADA violation. The Chief of Naval Operations should establish a quality assurance program for contracts at USNA. Among other things, the USNA Superintendent should establish policies and procedures for accepting, recording, and inventorying in-kind gifts, conduct an inventory of in-kind gifts, deposit sponsorship funds with the U.S. Treasury, and develop procedures for reviewing donations for prohibited sources.

## Management Comments and Our Response

Comments from USD(C)/CFO were responsive. We request additional comments from the Assistant Secretary of the Navy (Manpower and Reserve Affairs), who responded for Chief of Naval Operations, USNA Superintendent, and Director, Naval Heritage and History Command. Please see the recommendations table on the back of this page.

## Recommendations Table

Management	Recommendations Requiring Comment	No Additional Comments Required
Under Secretary of Defense (Comptroller)/Chief Financial Officer, DoD		A.1
Chief of Naval Operations	A.2	
Superintendent, U.S. Naval Academy	B.1.a, B.1.b; B.2.a; D.2; and E.1, E.2	A.3; B.1.c, B.1.d, B.1.e, B.1.f; B.2.b; C.; D.1; and E.3
Director, Naval Heritage and History Command		B.3.a, B.3.b, and B.3.c

**Please provide comments by December 7, 2011.**

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# Introduction

We performed this audit in response to a request from staff of the Senate Armed Services Committee. We met with Committee staff and discussed their request for potential audits of the U.S. Naval Academy (USNA), the U.S. Military Academy, and the U.S. Air Force Academy gift and nonappropriated funds (NAFs). The Committee staff agreed with a phased audit approach for reviewing the Military Academies starting with the USNA. The Committee staff asked us to review the USNA policies and procedures over its gifts and NAFs processes and adequacy of the corrective actions taken on allegations substantiated by the Naval Inspector General.

## Audit Objective

Our objective was to determine whether the USNA, its nonappropriated fund instrumentalities (NAFIs),<sup>1</sup> and its supporting nonprofit organizations were properly disbursing, recording, accepting, and reporting gifts and nonappropriated funds. We also reviewed the adequacy of the corrective actions taken on allegations substantiated by the Naval Inspector General. See Appendix A for a discussion of the scope and methodology and prior coverage related to the objective.

## Background on U.S. Naval Academy

The Naval Academy is the Navy's primary undergraduate educational institution. Its mission is

To develop Midshipmen morally, mentally and physically and to imbue them with the highest ideals of duty, honor and loyalty in order to graduate leaders who are dedicated to a career of naval service and have potential for future development in mind and character to assume the highest responsibilities of command, citizenship, and government.

The nonprofit organizations supporting USNA are the Naval Academy Athletic Association; USNA Alumni Association; and USNA Foundation. The USNA NAFIs also support the USNA. See Appendix B for a description of these nonprofit organizations and NAFIs.

USNA and its NAFIs must comply with Secretary of the Navy (SECNAV) and other Federal regulations for administrative matters, personnel, and procurement, including the following:

- Office of the Chief of Naval Operations Instruction 5450.330A, "Mission, Functions and Tasks of the United States Naval Academy, Annapolis, MD," December 28, 2009, provides the functions and tasks of the USNA.
- Secretary of the Navy Instruction (SECNAVINST) 5401.2A, "Establishment, Management, and Control of Nonappropriated Fund Instrumentalities and Financial Management of Supporting Resources," January 21, 2004, describes the establishment, management, and control of NAFIs and financial management of supporting resources and applies to all military and civilian NAFIs within the Department of the Navy.

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<sup>1</sup> A NAFI is a fiscal entity of the U.S. Government that is fully or partially supported by nonappropriated funds.

- Bureau of Naval Personnel Instruction (BUPERSINST) 7043.1B, “Procurement Policy for Bureau of Naval Personnel (BUPERS) Nonappropriated Fund (NAF) Activities,” August 23, 2000, provides NAFI procurement guidance.

USNA must also comply with the accreditation and athletic regulations of the Commission on Higher Education of the Middle States Association of Colleges and the National Collegiate Athletic Association.

The key senior managers for the USNA are the USNA Superintendent, the Deputy for Finance, the Director of the Naval Academy Business Services Division (NABSD), the Comptroller, and the Director of the Museum. The Superintendent reports to the Chief of Naval Operations. The Deputy for Finance reports to the Superintendent. The NABSD Director and the Comptroller report to the Deputy for Finance. The Director of the Museum reports to the Academic Dean and Provost, who reports to the USNA Superintendent.

## **Gift Definition**

Federal Accounting Standards Advisory Board, Statement of Federal Financial Accounting Standards (SFFAS) No. 7, “Accounting for Revenue and Other Financing Sources and Concepts for Reconciling Budgetary and Financial Accounting,” April 1996, defines donations as “contributions to the Government, i.e., voluntary gifts or resources to a government entity by a nonfederal entity. Donations may be financial resources, such as cash or securities, or nonfinancial resources such as land or buildings.”

## **Naval Inspector General Report**

On November 17, 2009, the Naval Inspector General issued a report, “Senior Official Case 200801937: Alleged Misuse of Gift Funds and Nonappropriated Funds (NAF),” that identified misuse of USNA gift and NAFs. Specifically, the former USNA Superintendent authorized a subordinate to expend gift funds for unauthorized purchases and entertainment. The USNA Deputy for Finance established an unauthorized contingency fund bank account, executed an improper contract, failed to follow USNA gift receipt procedures, and improperly gave a gift to a superior.

After the Naval Inspector General report was issued:

- The USNA Deputy for Finance was suspended for 5 days.
- The NABSD Director was suspended for 7 days.
- The Command Master Chief was rotated to another assignment.

In addition, the former USNA Superintendent retired in August 2010. The Deputy for Finance left USNA in January 2011.

The Naval Inspector General identified several issues at the USNA and substantiated six allegations. We conducted our audit to determine whether the USNA took corrective actions and to test the controls, if any, that were established to correct the internal control weaknesses identified. Specifically, we conducted our audit to identify causes of the internal control weaknesses, determine effects, and make any recommendations on Navy policies and

procedures, as necessary. We also reviewed the gift and NAF processes at the USNA. See Appendix A for additional information on the scope and methodology for our review. See Appendix C for a summary of the allegations that were substantiated by the Naval Inspector General and the corrective actions we reviewed.

## **Internal Controls Over Gifts and Nonappropriated Funds**

We identified internal control weaknesses as defined by DoD Instruction 5010.40 “Managers’ Internal Control Program (MICP) Procedures,” July 29, 2010, at USNA over its contracting and gift processes. The USNA officials did not have adequate processes for disbursing, recording, accepting, and reporting donations, gifts, and NAFs.

The Deputy for Finance did not provide proper oversight of a contract for a short motion picture and six television commercials, and the USNA NABSD did not have a contracting officer to ensure that contracting procedures were followed. In addition, the USNA Museum did not have policies and procedures in place for recording in-kind gifts. The Museum Director did not provide oversight of the inventory system, and personnel did not receive guidance on using the Naval Heritage and History Command inventory system. Additionally, the USNA Deputy for Finance bypassed Navy gift receipt processes, and USNA guidance for accepting in-kind gifts was inadequate. The Deputy for Finance did not provide adequate oversight over USNA acceptance and expenditure of corporate sponsorship funds. Furthermore, USNA did not have a memorandum of understanding with the USNA Foundation to provide the donor source. We will provide a copy of the report to the senior official responsible for internal controls at USNA.



## **Finding A. Improper Contracting Actions and Questionable Payments**

The USNA Deputy for Finance (Deputy) allowed improper contracting for the production of a short motion picture and six television commercials. In addition, the USNA, Naval Academy Business Services Division, Director<sup>2</sup> (NABSD Director) did not:

- seek competitive bids or properly justify a sole-source award,
- obtain the required legal review,
- have authorization to issue the contract, and
- use a Government contract.

In addition, the NABSD Director made the following questionable payments using NABSD NAFs. The NABSD Director:

- paid \$1.18 million before the contract was signed,
- paid \$980,248 more than the contract price, and
- paid \$3.5 million without obtaining invoices.

This occurred because the Deputy did not provide proper oversight of the contract and NABSD did not have a contracting officer.<sup>3</sup> As a result, the NABSD Director wasted approximately \$3.5 million.

The USNA may have augmented its budget by \$3.5 million and may have committed a potential Antideficiency Act violation.

### **NABSD Director Contracted for a Short Motion Picture and Six Commercials**

In May 2008, the NABSD Director contracted with an independent contractor to produce a short motion picture to be shown at the USNA Visitor Center and two commercials to be aired during USNA televised sporting events. Specifically, the NABSD Director contracted for the production of a 10-minute motion picture and one 30-second and one 60-second commercial. The original contract price was \$2.5 million. The NABSD Director subsequently agreed to pay the contractor to produce four additional 30-second commercials without a signed contract. During an audit interview, the Deputy referred to Chief of Naval Operations diversity goals as justification for awarding this contract. He stated that USNA needed to make significant

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<sup>2</sup> The NABSD Director reports to the Deputy for Finance.

<sup>3</sup> The former USNA Superintendent was the NAF contracting officer, and although he was authorized to re-delegate this authority, he did not delegate it to any NABSD personnel.

changes for the class of 2013, entering the USNA in the summer of 2009, to meet diversity goals and had only fall 2008 and winter 2009 to reach out to newly targeted markets. However, the Staff Judge Advocate (SJA) and Comptroller did not provide any documentation of the Chief of Naval Operations diversity goals.

## **Improper Contracting Actions**

The NABSD Director improperly contracted for the production of a short motion picture and six television commercials. The NABSD Director did not:

- seek competitive bids or properly justify a sole-source award,
- obtain a required legal review,
- have authorization to issue a contract, or
- use a Government contract.

## ***Insufficient Sole-Source Justification***

The NABSD Director did not seek competitive bids for the contract, and the sole-source award was not properly justified. DoD Directive 4105.67, “Nonappropriated Fund (NAF) Procurement Policy,” May 2, 2001, states that NAF procurements are to use competitive negotiation procedures to the maximum extent practicable, and offers are to be solicited from a reasonable number of sources, except when noncompetitive procurement is justified. Further, NAF contracts are to be awarded to offerers who provide the best value to the NAFI.

USNA/Annapolis Area Coordinator Instruction (USNA/AACINST) 7010.2A, “Nonappropriated Fund Procurement Policy,” September 16, 1991, states that procurements above \$2,500 require competition; that reasonable solicitation of qualified suppliers is to be made to ensure that the procurement is made to the advantage of the fund; and that, generally, solicitation may be limited to three suppliers. USNA/AACINST 7010.2A further states that provisions of the Federal Acquisition Regulation should be followed, if feasible.

BUPERSINST 7043.1B, “Procurement Policy for Bureau of Naval Personnel (BUPERS) Nonappropriated Fund (NAF) Activities,” August 23, 2000, requires contracts to be competitively awarded. In addition, BUPERSINST 7043.1B requires the sole-source

*The sole-source justification did not explain why other sources were not acceptable.*

justification to contain an explanation of why other sources are not acceptable. The sole-source justification did not explain why other sources were not acceptable. Furthermore, it did not contain any evidence of reviewing other sources. In addition, the Deputy backdated the sole-source justification. Although the sole-source justification from the Deputy to the NABSD Director was dated April 30, 2008, we obtained an e-mail dated May 1, 2008, which stated that the Deputy needed to write a sole-source justification for the record. Therefore, even the April 30, 2008, date of the sole-source justification was not accurate.

The NABSD Director did not issue a request for proposals because he decided to select a contractor who was already promoting a branding<sup>4</sup> concept to the Navy. The Deputy stated in the sole-source justification that the USNA motion picture and television commercials should be consistent with the Naval Recruitment Command's recruitment campaign to form a foundation for branding Navy-wide. However, at the time the NABSD Director entered into negotiations, the contractor had not developed a unique and innovative branding concept for the Naval Recruitment Command. The Naval Recruitment Command decided not to use this contractor upon discovering that the experience presented on the contractor's resume was inaccurate. After the contractor's short motion picture was completed and the television commercials aired in 2008, the former SJA conducted a due-diligence review of the contractor's qualifications in March 2009. The review determined that the contractor overstated its background but had not committed any criminal acts.

### ***No Evidence of a Legal Review***

The NABSD Director relied on statements made by the Deputy, who stated that the SJA had reviewed the contract for correctness. However, the contract files did not contain any evidence that a legal review occurred before the contract was signed. DoD Instruction (DoDI) 4105.71, "Nonappropriated Fund (NAF) Procurement Procedure," February 26, 2001, requires the USNA Superintendent to establish procedures for obtaining a legal review. BUPERSINST 7043.1B states that the contracting office is responsible for obtaining a legal review.

### ***No Authorization to Issue a Contract***

The NABSD Director signed the contract on May 15, 2008, without appropriate authority. The former USNA Superintendent was the only individual authorized to sign a USNA NABSD contract over \$25,000. USNA/AACINST 7010.2A states that the USNA Superintendent must approve all procurements over \$25,000. The former USNA Superintendent was authorized to delegate his signing authority, under SECNAVINST 7043.5B, "Nonappropriated Fund Procurement Policy," April 18, 2002. However, he had not delegated the signing authority when the NABSD Director signed the contract.

### ***NABSD Director Did Not Use a Government Contract***

The NABSD Director did not use a Government contract; instead, he used one developed by the contractor. DoDI 4105.71, section 6.2.2, "Solicitation Development and Contract Formation," states that all NAF contracts should include the use of NAF contract clauses. DoDI 4105.71 also states that NAF procurements are to be accomplished by trained procurement personnel to the best advantage of the NAFI. The contract the NABSD Director signed did not contain the required NAF clauses, and therefore, it was not in the best interest of USNA NABSD.

BUPERSINST 7043.1B, states that "formal contracting procedures shall be used for amounts above \$25,000." The contract did not contain the Government clauses required by BUPERSINST 7043.1B, which are designed to protect the interests of the Federal Government.

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<sup>4</sup> Branding involves the process of creating a unique name and image in the public's mind through advertising campaigns with a consistent theme.

For example, BUPERSINST 7043.1B states that USNA can audit the contract up to 3 years after the expiration date and final payment is made. The contract the NABSD Director signed limited the time the USNA could audit the contract to 1 year after the final payment was made.

## **Questionable Payments**

The NABSD Director made \$3.5 million in questionable payments on the contract. Specifically, the NABSD Director disbursed funds before the contract was signed, made payments exceeding the contract price without contract modifications, and did not obtain invoices or other documentation from the contractor showing the expenses incurred.

### ***Payments Made Before the Contract Was Signed***

The NABSD Director paid the contractor \$1.18 million before the contract was signed (see Table 1). Further, he authorized the contractor to begin work before the contract was signed. Specifically, the contract was signed on May 15, 2008, with an effective date of March 1, 2008. However, Section 1501, Title 31, United States Code, (31 U.S.C. § 1501), “Documentary Evidence Requirements for Government Obligations,” states that an amount is to be recorded as obligation only when supported by documentary evidence of a “binding agreement between an agency and another person that is in writing, and for a purpose authorized by law.” See Appendix D for an example of a payment made before the contract was signed.

**Table 1. Payments Made Before Contract Was Signed**

<b>Days Before Contract Signed</b>	<b>Date</b>	<b>Amount</b>
36	April 9, 2008	\$784,864
13	May 2, 2008	392,432
	<b>Total</b>	<b>\$1,177,296</b>

### ***Payments Exceeded Contract Price***

The NABSD Director paid \$980,248 more than the contract price, without contract modifications. The contract was signed on May 15, 2008, for \$2,527,568; however, the NABSD Director paid the contractor a total of \$3,507,816, which was \$980,248 more than the contract price. According to 31 U.S.C. § 1501, an amount is to be recorded as an obligation of the U.S. Government only when supported by documentary evidence of a binding agreement in writing and for a purpose authorized by law. In addition, BUPERSINST 7043.1B states that contract modifications must always be confirmed in writing by use of an SF-30, “Amendment of Solicitation/Modification of Contract.”

### ***Payments Made Without Invoices***

The NABSD Director did not obtain invoices or other documentation from the contractor to support the expenses incurred. The NABSD Director made eight vendor payments, totaling \$3,507,816, without obtaining invoices or other documentation showing the actual expenses incurred. Without invoices, the NABSD Director was not able to validate the appropriateness of the payment. DoD Financial Management Regulation, Volume 10, Chapter 7 “Prompt Payment Act,” updated December 2009, states that before making a payment, DoD Components must ensure that appropriate payment documentation is established to support payment of invoices.



This documentation includes the contract, receipt/acceptance report, and a proper invoice. BUPERSINST 7043.1B also requires invoices and states that payment by the NAFI is due upon receipt of a proper invoice from the contractor. A proper invoice must include the invoice date, name of contractor, contract number, date of shipment, and name and address to send payment. See Appendix E for an example of the contractor’s payment request.

## **No Contract Oversight and No Contracting Officer**

The NABSD Director improperly contracted for the short motion picture and television commercials and made questionable payments because he did not follow procedures. In addition, the Deputy did not provide proper oversight of the contract and NABSD did not have a contracting officer. The Deputy stated he bypassed standard contracting practices and instructed the NABSD Director to award the contract because of the urgency to produce the television commercials. However, he could not provide support for the urgency.

DoDI 4105.71 states that NAF procurements are to be accomplished by trained procurement personnel in a fair, equitable, and impartial manner, and to the best advantage of the NAFI. A contracting officer should have the expertise to ensure that DoDI 4105.71 requirements are met. In addition, BUPERSINST 7043.1B states that the contracting office is responsible for analyzing the requirement, obtaining competition, determining the source, performing contract administration, and obtaining legal reviews. Contracting officers should have the expertise to ensure that a contract meets BUPERSINST 7043.1B requirements.

Although the former USNA Superintendent was the NAF contracting officer, he had not delegated his contracting authority to the NABSD Director. Without a contracting officer, the NABSD Director was not able to ensure all contracting actions and payments were completed according to established NAFI procurement policies. The Chief of Naval Operations should establish a quality assurance program for the USNA to ensure that future contracts are awarded and administered in accordance with contracting regulations.

## **NABSD Director Wasted Funds**

The NABSD Director wasted<sup>5</sup> approximately \$3.5 million. USNA spent \$3,507,816 to produce one 10-minute short motion picture and five 30-second and one 60-second commercials. After

*USNA spent \$3,507,816 to produce one 10-minute short motion picture and five 30-second and one 60-second commercials.*

paying for the short motion picture and commercials, the USNA’s audiovisual department spent additional time editing the short motion picture. It was also necessary to use an additional contractor to edit the short motion picture. The 2008 short motion picture produced for the USNA Visitor Center did not achieve its purpose, which

was to describe the USNA mission. USNA employees, alumni, and visitors stated the contractor’s video did not describe the USNA mission and did not portray typical careers USNA

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<sup>5</sup> DoD Directive 7050.4, “Awards for Cost Savings Resulting from the Disclosure of Fraud, Waste or Mismanagement,” October 21, 2004, defines waste as the extravagant, careless, or needless expenditure of DoD funds; or the consumption of DoD property that results from deficient decisions, practices, controls, or systems.

graduates pursued. For example, the motion picture did not mention the Marine Corps and submariners as career options. A USNA official stated the motion picture “misrepresented what the USNA produces.”

The cost of the commercials and motion picture was excessive. As a comparison, in 2006, the USNA produced one 30-second and one 60-second commercials for \$14,000. The 2006 commercials had the same purpose as the 2008 commercials. They were used for recruiting. The commercials were sent to broadcast networks and aired during televised sporting events. The 2006 USNA Visitor Center short motion picture was produced for approximately \$200,000. The USNA received the 2006 short motion picture as a \$200,000 gift from the USNA Class of 1965 through the USNA Foundation.

We concluded that the USNA wasted \$3.5 million because the short motion picture did not adequately describe the USNA mission and did not portray all the USNA career paths. In addition, the USNA’s audiovisual department spent additional time editing the short motion picture before the product could be used. Furthermore, the cost of the short motion picture and commercials was excessive. They could have been produced by the USNA’s audiovisual department with the assistance of the existing USNA contractor so that costs would have been closer to what the USNA paid in 2006. The USNA decision to contract for the production of a short motion picture and six television commercials was deficient and the expenditure of DoD funds was careless and extravagant. The improper contracting actions and questionable payments resulted from deficient controls and practices.

Furthermore, the contractor used USNA film footage and commercials in its promotional materials without the required USNA disclaimers and permission. Without the required disclaimers, the promotional materials gave the appearance the USNA was endorsing the contractor.

## **Augmentation of Funds and Potential Antideficiency Act Violation**

A potential Antideficiency Act (ADA) violation may have occurred when the Deputy and NABSD Director used NAFs for the contract. The Deputy and the NABSD Director may have augmented the USNA budget by using NAFs instead of appropriated funds for the contract. Fund augmentation occurs when a Federal agency supplements its appropriations without specific statutory authority. While the Navy had the statutory authority to accept the 2006 short motion picture received as a gift from the USNA Class of 1965 under 10 U.S.C. § 6973<sup>6</sup>, the

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<sup>6</sup>10 U.S.C. § 6973: “Gifts, bequests, and loans of property: acceptance for benefit and use of USNA (a) The Secretary of the Navy may accept, hold, administer, and spend any gift or bequest of personal property, and may accept, hold, and administer any loan of personal property other than money, that is made on the condition that it be used for the benefit of, or for use in connection with, the USNA or the USNA Museum, its collection, or its services. Gifts and bequests of money and the proceeds from the sales of property received as gifts shall be deposited in the Treasury in the fund called ‘United States Naval Academy Gift and Museum Fund.’ The Secretary may disburse funds deposited under this subsection for the benefit or use of the USNA (including the USNA Museum) subject to the terms of the gift or bequest.”

NABSD Director may not have had the authority to award the May 2008 contract for the production of a 10-minute motion picture and one 30-second and one 60-second commercials.

The GAO, Office of the General Counsel, “Principles of Federal Appropriations Law,” Third Edition, Volume II, February 2006, states that an agency may not augment its appropriations from outside sources without specific statutory authority. If an agency gets additional funding from another source without specific statutory authority, it has more budget authority than the funding level Congress appropriated for those purposes during that time. When an agency operates beyond its appropriated funding level with funds derived from another source, the agency is circumventing congressional budget controls. By using NAFs instead of appropriated funds for the contract, USNA circumvented Congress’s role and budget controls by obtaining excess funds without congressional approval.

Appropriated funds were required for this contract; however, the NABSD Director used NAFs instead. DoDI 1015.15, “Establishment, Management, and Control of Nonappropriated Fund Instrumentalities and Financial Management of Supporting Resources,” October 31, 2007, prohibits the use of NAFs for public affairs activities or to benefit select individuals or groups. DoDI 1015.15 also states that NAFs should only be used for the benefit of the military community. The USNA Comptroller stated he was not aware of any request from NABSD to fund the short motion picture; however, USNA’s appropriated funds were not available at the time of contract award because they were already committed to other labor and material projects. There was no evidence that the Deputy or the NABSD Director ever requested appropriated funds. In addition, the USNA Comptroller stated that the Deputy was aware that all appropriated funds had already been committed to other projects. The Under Secretary of Defense (Comptroller)/Chief Financial Officer, DoD (USD(C)/CFO), should initiate a review to determine whether the USNA violated the ADA by augmenting its budget by using NAFs instead of appropriated funds.

## **Corrective Management Actions**

In February 2010, USNA hired a contracting officer to manage the NAFI contracts and ensure that contracts meet requirements. The former USNA Superintendent appointed the contract specialist to act also as contracting officer for NAFI procurements. The former USNA Superintendent issued USNAINST 7010.2B, “United States Naval Academy (USNA) Nonappropriated Fund (NAF) Procurement Policy,” July 28, 2010, which states that fund approval must be obtained before beginning the procurement process. USNAINST 7010.2B also states that procurements in excess of \$250,000 require prior written approval by the Superintendent. The USNA Superintendent issued USNAINST 7010.3, “United States Naval Academy (USNA) Nonappropriated Fund (NAF) Policy,” March 1, 2011, which aligns USNA NAF policy with DoD and Department of the Navy policy. USNAINST 7010.3 explicitly excludes the use of NAF for public affairs functions and for activities or programs outside the purpose for which the NAFI was established.

## **Conclusion**

We followed up on the work performed by the Naval Inspector General, as requested by the Senate Armed Services Committee staff, to determine whether corrective actions were taken, the adequacy of the corrective actions, and whether any other additional actions were needed. Based

on the internal control weaknesses that were previously identified and the ones we identified, we concluded that additional actions were needed. A potential ADA violation may have occurred because USNA used NAFs for the contract. Specifically, USNA may have augmented the USNA budget by using NAFs instead of appropriated funds for the contract. Therefore, USD(C)/CFO should initiate a preliminary review to determine whether the USNA augmented its budget. We also concluded that the USNA made numerous improper contracting actions and \$3.5 million in questionable payments.

## **Recommendations, Management Comments, and Our Response**

**A.1. We recommend that the Under Secretary of Defense (Comptroller)/Chief Financial Officer, DoD, initiate a preliminary review to determine whether the U.S. Naval Academy augmented its budget by using nonappropriated funds instead of appropriated funds, resulting in a potential Antideficiency Act violation.**

### ***USD(C)/CFO Comments***

The Deputy Chief Financial Officer agreed that a preliminary ADA review should be performed as required by DoD Regulation 7000.14-R, "Department of Defense Financial Management Regulation," Volume 14, Chapter 3, "Preliminary Reviews of Potential Violations," November 2010. An investigating officer from the office of Assistant Secretary of the Navy (Financial Management and Comptroller) was assigned to do the preliminary investigation.

### ***Our Response***

The Deputy Chief Financial Officer comments were responsive, and no further comments were required.

**A.2. We recommend that the Chief of Naval Operations establish a quality assurance program for the U.S. Naval Academy to ensure that future contracts are awarded and administered in accordance with contracting regulations.**

### ***Chief of Naval Operations Comments***

The Assistant Secretary of the Navy (Manpower and Reserve Affairs [ASN(M&RA)]) responded for the Chief of Naval Operations, stating that the Chief of Naval Operations agreed and that USNA implemented this recommendation following the 2009 Naval Inspector General investigation by having the Commander, Navy Installations Command's Fiscal Oversight Team, perform annual audits of the USNA NAFIs to ensure compliance with DoD guidance on fiscal management standards.

### ***Our Response***

The ASN(M&RA) comments were not responsive because it was not clear whether the annual audits for ensuring compliance with DoD guidance on fiscal management standards include a review of whether contracts are awarded and administered in accordance with contracting regulations. We request that the ASN(M&RA) provide comments on the final report.



**A.3. We recommend that the U.S. Naval Academy Superintendent revise USNAINST 7010.2B, “United States Naval Academy (USNA) Nonappropriated Fund (NAF) Procurement Policy,” July 28, 2010, to include periodic reviews of the U.S. Naval Academy contracting office to ensure that it follows procedures.**

### ***USNA Superintendent Comments***

ASN(M&RA) responded for the USNA Superintendent, stating that the USNA Superintendent agreed and that USNA would modify the command evaluation schedule conducted by the USNA Inspector General to ensure NAFI compliance with procurement procedures. He also stated that the annual audits by the Commander, Navy Installation Command, and USNA command evaluation reviews will provide the USNA Superintendent the visibility required to ensure compliance with the recommendation.

### ***Our Response***

The ASN(M&RA) comments were responsive, and no further comments were required. Although USNAINST 7010.2B will not be revised, the proposed actions, if implemented, will meet the intent of the recommendation.

## Finding B. Improvements Are Still Needed Over the USNA Museum’s Recording of In-Kind Gifts

The USNA Museum personnel did not properly record in-kind gifts or heritage assets.<sup>7</sup> The Museum Director did not record all of the in-kind gifts into the inventory system, and a complete inventory of all items had never been done. In addition, about 21,700 of nearly 53,000 in-kind gifts in the Museum’s inventory system did not have an identification number or a complete identification number. The USNA Museum inventory system also did not have security controls established to prevent unauthorized modification or deletion of in-kind gifts in the inventory system. Finally, the USNA Museum did not use the Naval Heritage and History Command (NHHC) inventory system.

In-kind gifts were not recorded because the Museum Director did not have policies and procedures in place for recording in-kind gifts. The lack of security controls occurred because the Museum Director did not provide any oversight of the inventory system. The USNA Museum staff did not use the NHHC inventory system because they had not received any guidance from NHHC. As a result, the USNA Museum in-kind gift inventory assets were vulnerable to loss and theft. In addition, Department of the Navy Balance Sheet, Note 10, “General PP&E [Property, Plant, and Equipment],” section, “Heritage Assets and Stewardship Land,” may be understated.

### USNA Museum and In-kind Gifts Definition

In August 2005, the Vice Chief of Naval Operations approved a functional realignment of all Navy Museums under NHHC. The Vice Chief of Naval Operations stated that all policy and financial decisions would be consolidated at NHHC. The USNA Museum, established in 1845, is located at Preble Hall and underwent a complete renovation from December 2007 to January 2009 to turn the building into a modern museum. Changes included new exhibits, improved collection storage areas, and upgraded office space. The Museum officially reopened in summer 2009. Its holdings include ship models, paintings, prints, flags, uniforms, swords, firearms, medals, sculptures, manuscripts, rare books, photographs, ship instruments and gear, and a wide variety of personal memorabilia gifted by U.S. citizens. The USNA Museum’s primary mission is to serve the educational needs of the USNA Brigade of Midshipmen and the faculty and staff. The USNA Museum Director, as a faculty member, comes under the authority of the USNA Academic Dean and Provost and must respond to USNA and NHHC directives and policies. USNA Museum personnel are employees of NHHC.

*The USNA Museum Director . . . must respond to USNA and NHHC directives and policies.*

The USNA Museum’s in-kind gifts or heritage assets are defined by SFFAS No. 29, “Heritage Assets and Stewardship Land,” as property, plant, and equipment that are unique for one or more

<sup>7</sup> In-kind gifts that go to the USNA Museum are classified as heritage assets.

of the following reasons: cultural, educational, historical, or natural significance. Heritage assets are collections of objects gathered and maintained for exhibition.

USNAINST 4001.5, "Acceptance of Gifts for the USNA Gift and Museum Fund," August 5, 2008, provides guidance for accepting and recording in-kind gifts at USNA. However, USNAINST 4001.5 does not provide specific guidance for recording and handling USNA Museum in-kind gifts.

## **In-Kind Gifts Not Recorded in USNA Museum Inventory System**

The Museum Director did not record all of the in-kind gifts into the inventory system and a complete inventory of all items has never been done. The Museum Director stated that not all the in-kind gifts at the Museum were entered into its Filemaker Database System. The Museum uses the Filemaker Database System to track its in-kind gift inventory. Many in-kind gifts at the USNA Museum were still in boxes or on shelves (see Figures 1 and 2).

**Figure 1. Boxed In-kind Gifts Not Entered Into the Filemaker Database System**



**Figure 2. In-kind Gifts on Shelves and Not Entered Into the Filemaker Database System**



Naval Audit Service Report No. 055-C-94, "Fiscal Year 1993 Principal Financial Statements of the United States Naval Academy Museum Fund," June 30, 1994, recommended the USNA Museum conduct a wall-to-wall inventory. Therefore, 10 years later, in November 2004, a USNA internal auditor conducted a spot inventory of USNA Museum items. The November 2004 spot inventory report stated that adequate controls still do not exist to account for and control all historical property.

In-kind gifts were not recorded because the Museum Director did not have policies and procedures in place for recording in-kind gifts. In addition, since August 2005, when the Vice Chief of Naval Operations consolidated policy-making at NHHC for all Navy museums, the NHHC Director has not issued any policies and procedures to the USNA Museum for recording in-kind gifts. As a result of our audit, the NHHC Director started developing policy for all Navy museums for handling and recording in-kind gifts. However, the working draft Navy Museum Manual did not establish USNA and NHHC duties and responsibilities over the USNA Museum. Specifically, the working draft did not address the separate lines of authority over the USNA Museum between the USNA Superintendent and the NHHC Director for accepting, recording, and accounting for the Museum gifts. In addition, the working draft did not follow standards set forth by the American Association of Museums (AAM). Navy Museums need to follow this guidance to be an accredited museum.

As a result, the Museum in-kind inventory assets were vulnerable to loss and theft. In addition, the Navy General Fund Balance Sheet, Note 10, "General PP&E" section, "Heritage Assets and Stewardship Land," may be understated because the Filemaker Database System information was incomplete. Financial information from the Filemaker Database System is provided to NHHC staff, who provides this information to the Defense Financial and Accounting Service for inclusion in the Navy's General Fund Balance Sheet, Note 10, "General PP&E" section, "Heritage Assets and Stewardship Land."

SFFAS No. 29 states that heritage assets should be quantified by units within major categories. The appropriate level of aggregation and the units of measure for each major category should be meaningful and determined by the preparer based on the entity's mission, type of heritage asset, and management of the asset. The Museum Director should conduct an inventory of the Museum's holdings and accurately record all its in-kind gifts into the NHHC inventory system.

## **In-Kind Gift Identification Numbers**

The Museum Director needs to improve controls for recording in-kind gifts. For example, about 21,700 of nearly 53,000 in-kind gifts in the Museum's Filemaker Database System did not have an identification number or a complete identification number. Specifically, 20,239 inventory items were not assigned a number, and 1,445 items did not have a complete number in the Filemaker Database System.

An identification number is needed to locate in-kind gift items within the Museum. The identification, or "accession," number identifies the year the in-kind gift was received, the gift number, and the subunit or unit number for categorizing the items. Furthermore, Museum staff stated that an accession number is needed for every item at the Museum to comply with the AAM standards and to receive their accreditation.



Many in-kind gifts had incomplete identification numbers because the Museum Director did not have policies and procedures for recording in-kind gifts. As a result, the USNA Museum in-kind gift inventory was vulnerable to loss and theft. The Museum Director should establish formal policies and procedures that are consistent with NHHC policies and procedures for accepting and recording in-kind gifts. The Museum Director should also assign complete identification numbers to all in-kind gifts in their Filemaker Database System until the Museum staff starts using the NHHC inventory system.

## **USNA Museum's Inventory System Lacked Security Controls and Did Not Use NHHC Inventory System**

The Museum Director did not develop controls to prevent unauthorized modification or deletion of in-kind gift data in its inventory system. The Museum Director stated that when in-kind gifts are received, they should be entered into the Filemaker Database System. Further, he stated that his staff and volunteers had access to the Filemaker Database System and had the capability to modify or delete records. The ability to delete objects from the database should be limited to specific USNA Museum staff. The Filemaker Database System has the ability to limit access control levels to specific users; however, the USNA Museum staff acknowledged they did not know how to set the access controls. The Museum Director also stated that he relies on part-time volunteers to enter in-kind gifts into the Filemaker Database System. The lack of security controls occurred because the Museum Director did not provide any oversight of the Filemaker Database System. As a result, the Museum's in-kind inventory is vulnerable to loss and theft. The Museum Director should establish access and security controls to prevent unauthorized modification or deletion of in-kind gift records in the Filemaker Database System.

Finally, USNA Museum personnel did not use the required NHHC inventory system, the Department of Navy Heritage Asset Management System (DONHAMS), to track the in-kind gift inventory. DONHAMS is the Navy's property management system to record heritage assets. NHHC oversees the USNA Museum jointly with the USNA. However, Chief of Naval Operations Instruction 5450.330, "Mission, Function, and Task of U.S. Naval Academy," December 28, 2009, states that the NHHC Director manages the administrative and financial business of the USNA Museum. The NHHC Director also oversees all other Navy Museums. The USNA in-kind gift inventory was not recorded in DONHAMS because the NHHC Director did not provide any guidance to the Museum Director and staff. As a result, the USNA Museum in-kind gift inventory is vulnerable to loss and theft.

The USNA Museum Director should stop using the Filemaker Database System and start using DONHAMS. The USNA Superintendent should oversee a performance review of the Museum Director's actions related to not recording all in-kind gifts, not assigning identification numbers to gifts, not establishing controls to prevent unauthorized modification or deletion of in-kind gift records, and not using NHHC inventory system, and take administrative action, as appropriate. The USNA Superintendent should also direct the establishment of a time-phased plan, with metrics, to correct the internal control weaknesses identified at the USNA Museum.

## **Recommendations, Management Comments, and Our Response**

**B.1. We recommend that the U.S. Naval Academy Superintendent direct the U.S. Naval Academy Museum Director to:**

- a. Establish written policies and procedures for recording in-kind gifts that are consistent with Naval Heritage and History Command policies and procedures.**
- b. Provide additional oversight and status reports on recording in-kind gift inventory.**
- c. Conduct an inventory of the Museum in-kind gifts.**
- d. Implement the Naval Heritage and History Command inventory system, Department of Navy Heritage Asset Management System, and record all the in-kind gifts into the system.**
- e. Assign complete identification numbers to all in-kind gift records.**
- f. Establish access controls to the inventory system to prevent unauthorized modification or deletion of in-kind gift records.**

### ***USNA Superintendent Comments***

ASN(M&RA) stated that the USNA Superintendent agreed with these recommendations and, in conjunction with NHHC, had taken or planned to take the following actions.

- The Museum follows USNA Instruction 4001.5A, October 2010, and these policies and procedures are consistent with NHHC policies and procedures.
- Since the October 2010 USNA Instruction 4001.5A, all gifts to the Museum are processed through the Comptroller's Office, Deputy for Finance, and SJA and accepted by the Superintendent or the Under Secretary of the Navy.
- During the renovation of Preble Hall, Museum staff began inventorying the collection in accordance with AAM standards. Once completed, the Museum plans to verify the inventory on a 5-year cycle, which is an AAM standard.
- NHHC is developing a Web-based version of the DONHAMS database. After connectivity is achieved, expected September 2012, Museum staff can update the DONHAMS database directly via the Internet. Until then, it will periodically synchronize the FileMaker Database inventory files with the DONHAMS database.
- Accession numbers will be assigned to all USNA Museum assets by September 30, 2012, which is the end of its self-study for the AAM accreditation process.
- Access to the inventory system is now limited to the Museum Director and the Museum Registrar. This access control is consistent with NHHC policies,

## ***Our Response***

The ASN(M&RA) comments on Recommendations B.1.c through B.1.f were responsive, and no additional comments were required. The comments on Recommendations B.1.a and B.1.b were not responsive. ASN(M&RA) stated that the Museum followed USNAINST 4001.5A for gift acceptance. However, USNAINST 4001.5A did not have policies and procedures for the Museum for inventorying in-kind gifts into the Museum records. In addition, the comments did not state whether the Museum Director would establish written policies and procedures that complied with the new Navy Museum Manual.

Furthermore, ASN(M&RA) did not state whether the Museum Director would provide status reports on the number of in-kind gifts recorded and not recorded in the Museum inventory systems. The status reports would include in-kind gifts recently received and in-kind gifts that have not been previously recorded. The status reports would also include information on the progress in assigning identification numbers to all in-kind gift records. We request that the Assistant Secretary provide comments on the final report.

### **B.2. We recommend that the U.S. Naval Academy Superintendent:**

**a. Oversee a performance review of the Museum Director for not recording in-kind gifts, not assigning identification numbers to in-kind gifts, not establishing controls to prevent unauthorized modification or deletion of in-kind gift records, and not using the Naval History and Heritage Command inventory system, and take administrative action, as appropriate.**

**b. Direct the establishment of a time-phased plan, with metrics, to accomplish Recommendations B.1.a through B.1.f.**

### ***USNA Superintendent Comments***

ASN(M&RA) stated that the USNA Superintendent agreed and that USNA would perform annual performance reviews for all employees. He also stated that USNA had developed a timeline to implement Recommendations B.1.a through B.1.f.

## ***Our Response***

The ASN(M&RA) comments on Recommendation B.2.a were partially responsive, and the comments on Recommendation B.2.b. were responsive. He did not state whether the USNA Superintendent would oversee the Museum Director performance review. We request that the Assistant Secretary provide comments on the final report.

### **B.3. We recommend that the Director, Naval Heritage and History Command:**

**a. Complete the draft Navy Museum Manual.**

**b. Require the U.S. Naval Academy Museum Director to use the Naval Heritage and History Command inventory system, the Department of Navy Heritage Asset Management System.**

**c. Perform additional oversight of the U.S. Naval Academy Museum operations to ensure that the U.S. Naval Academy Museum Director is following the Naval Heritage and History Command policies and procedures.**

***Director, NHHC, Comments***

ASN(M&RA) responded for the Director, NHHC, stating that the Director, NHHC agreed and that NHHC had completed an extensive review and comment process for the draft Navy Museum Manual, which is scheduled to be completed in March 2012. In addition, ASN(M&RA) stated that NHHC was developing a Web-based version of the DONHAMS database, and Internet connectivity was expected by September 2012. Until then, the Museum planned to periodically synchronize its FileMaker Database inventory files with the DONHAMS database.

Furthermore, ASN(M&RA) stated that the Museum System Program Office had reviewed documents prepared by the Museum Director for the USNA Museum application for accreditation to AAM, which accepted the application. Additionally, the Director, NHHC and the Museum System Program Office were conducting monthly conference calls with Museum Directors to discuss new policies and procedures and other matters of interest to the Museum Directors.

***Our Response***

The ASN(M&RA) comments were responsive, and no further comments were required.

## Finding C. Unauthorized Acceptance of Gifts and Failure to Inventory Gifts

The USNA Deputy for Finance (Deputy) improperly accepted more than \$184,000 of in-kind (nonmonetary) gifts from an alumnus from 2005 through 2007 without obtaining the proper authorization. In addition, he did not inventory the gifts. This occurred because the Deputy bypassed the Navy’s gift receipt processes and USNAINST 4001.5, “Acceptance of Gifts for the U.S. Naval Academy Gift and Museum Fund,” August 5, 2008, was inadequate. The unauthorized acceptance of these in-kind gifts gives the appearance of impropriety and risks damaging the USNA’s reputation. Further, the failure to inventory the gifts increases the risk of their loss or theft.

### USNA Deputy Improperly Accepted In-Kind Gifts

The Deputy improperly accepted more than \$184,000 of in-kind gifts from an alumnus from 2005 through 2007 without obtaining the proper authorization. In addition, the Deputy failed to inventory the gifts. SECNAVINST 4001.2J, “Acceptance of Gifts,” August 12, 2009, states that the SECNAV is the acceptance authority for all gifts of real property and other gifts with a value in excess of \$60,000, and the USNA Superintendent can accept gifts not to exceed \$60,000. The SECNAV did not delegate the acceptance authority below the USNA Superintendent. Therefore, the Deputy did not have authorization to accept the gift from the alumnus. See Table 2 for the list of gifts inappropriately accepted by the Deputy.

**Table 2. Gifts Inappropriately Accepted by the Deputy for Finance**

Item	Description	Quantity	Value
Waterford Crystal	Stemware	754	\$72,505
	Serveware	92	29,174
	Chandeliers	8	38,515
Simon Pierce Pottery	Small Vases	12	1,500
	Large Vases	14	2,100
Baccarat Crystal	Glasses	22	2,310
	Vase	1	900
	Bowls	2	1,600
Alcoholic Beverages	Bottles of Wine	29	3,657
Bibles	Protestant Bible	312	8,733
	Catholic Bible	165	4,618
Daum Crystal	Vase	1	5,000
Artwork	Paintings	3	14,100
<b>Total Value</b>			<b>\$184,712</b>

The Deputy did not obtain proper authorization from the SECNAV or the USNA Superintendent when receiving these gifts. In addition, the Deputy did not inventory the gifts upon receipt and enter the gifts into the USNA property records. When USNA officials learned that these gifts

from the alumnus were not processed, the USNA Superintendent decided to treat them as one gift and submitted it to the Under Secretary of the Navy for approval. SECNAVINST 4001.2J states that when a donor makes a pledge or offer of a future gift, whether a one-time gift or a gift made in installments, the total cumulative amount of the future gift determines the appropriate acceptance authority.

These conditions occurred because the Deputy bypassed the normal gift receipt process. In addition, USNAINST 4001.5 was inadequate because it improperly delegated acceptance authority to individuals other than the USNA Superintendent. This guidance conflicts with SECNAVINST 4001.2J, which only allows the USNA Superintendent to accept gifts under \$60,000. Furthermore, SECNAVINST 4001.2J only authorizes eight individuals to delegate their acceptance authority and the USNA Superintendent is not one of these individuals. The USNA Superintendent has the authority to accept gifts under \$60,000, but does not have the authority to delegate his acceptance authority. The Deputy's acceptance of gifts may appear improper and risk damaging the USNA's reputation. Further, the failure to inventory the gifts increases the risk of their loss or theft.

## **Corrective Management Actions**

During our audit, the USNA Superintendent issued an action memorandum, "Gift to the United States Naval Academy (USNA); Crystal and Glassware for Buchanan House," March 22, 2011. The memorandum requested the Director, Navy Staff, to accept the crystal and glassware as gifts for the Buchanan House. As of July 27, 2011, the Director, Navy Staff had not accepted the gifts. In addition, the USNA Superintendent issued USNAINST 4001.5A, "Acceptance of Gifts to the United States Naval Academy," October 14, 2010, which removed gift delegation authorities from USNA officials other than the USNA Superintendent and established policy for soliciting, accepting, and processing gifts to the USNA. Clarifying the policy should help prevent future unauthorized acceptance of gifts; however, the USNA Superintendent should revise USNAINST 4001.5A to include performing periodic, independent, quality assurance reviews to verify that USNA personnel are complying with the policy.

## **Recommendations, Management Comments, and Our Response**

**C. We recommend that the U.S. Naval Academy Superintendent revise USNAINST 4001.5A, "Acceptance of Gifts to the United States Naval Academy," October 14, 2010, to include performing periodic, independent, quality control reviews to verify that U.S. Naval Academy personnel comply with the policy.**

### ***USNA Superintendent Comments***

ASN(M&RA) stated that the USNA Superintendent agreed and that USNA had integrated periodic, independent quality assurance reviews into the USNA Inspector General annual command evaluation program. Further, he stated that the Department of the Navy, Assistant for Administration, had reviewed the USNA gift acceptance process and recommended annual reviews to ensure compliance.



## ***Our Response***

The ASN(M&RA) comments were responsive, and no further comments were required. Although USNAINST 4001.5A will not be revised; the proposed actions, if implemented, are an acceptable alternative and meet the intent of the recommendation.

## Finding D. Inappropriate Acceptance and Use of Sponsorship Funds

The USNA NABSD Director inappropriately accepted \$343,208 in corporate sponsorship funds from the Naval Academy Athletic Association (NAAA) from April 2007 through March 2010. In addition, the NABSD Director improperly spent \$189,265 of the funds on activities that were not for the USNA midshipmen's benefit. The NABSD Director retained the remaining unauthorized funds in the USNA NABSD operating account. This occurred because the USNA Deputy for Finance (Deputy) did not provide adequate oversight of USNA NABSD operations. As a result, the NABSD Director held nearly \$153,943 in funds the USNA NABSD was not allowed to possess.

### USNA Received Corporate Sponsorship Funds

The NAAA transferred a total of \$343,208 in corporate sponsorship funds to USNA NABSD from April 2007 through March 2010 (see Table 3).

**Table 3. Corporate Sponsorship Fund Transfers**

<b>Date</b>	<b>Amount</b>
April 12, 2007	\$94,970
March 21, 2008	96,882
April 6, 2009	103,856
March 30, 2010	47,500
<b>Total</b>	<b>\$343,208</b>

The Deputy and NABSD Director maintained a contingency account for the \$295,708 in sponsorship funds transferred to the USNA through April 6, 2009, in an accounting system and bank account outside the supervision and control of the Federal Government. The NABSD Director improperly spent \$189,265 on activities that were not for the USNA midshipmen's benefit. In September 2009, the NABSD Director transferred the remaining sponsorship funds of \$106,443 to the official USNA NABSD operating account, which was supervised and controlled by the Federal Government. In March 2010, the NABSD Director received the \$47,500 in corporate sponsorship funds and, in April 2010, deposited the funds into the operating account. These funds were recorded in the NAFI accounting system. The remaining \$153,943 total represents the amount of corporate sponsorship funds in USNA NABSD's possession.

### NABSD Director Not Authorized to Accept Sponsorship Funds

The NABSD Director's acceptance of \$343,208 in corporate sponsorship funds from NAAA from April 2007 through March 2010 was inappropriate because NABSD did not have statutory authority to receive those funds. The 31 U.S.C. § 3302, "Custodians of Money," requires Government officials receiving money for the Government from any source to deposit it in the U.S. Treasury as soon as practical. Further, it requires that the Government official receiving the

funds have statutory authority to receive the funds. As a result, sponsorship funds received by USNA NABSD, which did not have statutory authority, are considered miscellaneous receipts and are to be deposited in the U.S. Treasury.

### ***Activities Not for the USNA Midshipmen's Benefit***

Of the \$343,208 in corporate sponsorship funds received, the NABSD Director spent \$189,265 on activities that were not for the USNA midshipmen's benefit. Instead, he spent the funds on various functions and events, such as catered, home football games; tailgate events; support for a Superintendent's dinner; receptions and pizza meals for contractors; holiday parties; and golf outings for USNA NABSD employees. These functions and events did not benefit USNA midshipmen.

### ***Oversight of NABSD Operations Was Inadequate***

This misuse of funds occurred because the Deputy did not provide adequate oversight of USNA NABSD operations. The Deputy and NABSD Director issued a memorandum, "Establishment of NABSD Contingency Account," April 10, 2007, that addressed the use of corporate sponsorship funds. The memorandum directed that corporate sponsorship funds "be accounted for and expended in such a manner as to allow maximum flexibility to NABSD in the context of conducting business in an academic institution." The memorandum stated corporate sponsorship funds could be used for the following NABSD activities:

- initiatives and events that promote NABSD to internal and external activities;
- procurement of promotional gifts that help to promote NABSD to internal and external customers;
- NABSD-sponsored events, including social events, that promote team building; and
- other expenses approved by the Deputy or NABSD Director on a case-by-case basis.

The NABSD Director spent funds on activities that did not benefit the midshipmen. The memorandum on establishing a contingency account and allowing maximum flexibility in spending the funds contradicted BUPERSINST 1710.11C, "Operation of Morale, Welfare, Recreation (MWR) Programs," March 3, 2003, on use of corporate sponsorship funds and should be rescinded. BUPERSINST 1710.11C states that corporate sponsorship funds should be used within the NAFI program for the benefit of midshipmen and that the funds should underwrite the NAFI program or event.

### **Holding Unauthorized Funds**

The NABSD Director improperly held \$153,943 that USNA NABSD was not authorized to have. The NABSD Director did not comply with 31 U.S.C. § 3302, "Custodians of Money," which requires a Government official receiving money for the Government from any source to deposit the money in the U.S. Treasury. As of April 2011, the NABSD Director was still holding the funds. The Superintendent should deposit the remaining \$153,943, plus any interest earned, in the U.S. Treasury.

## **Corrective Management Actions**

The USNA Superintendent issued USNAINST 7010.3, “United States Naval Academy (USNA) Nonappropriated Fund (NAF) Policy,” March 1, 2011, which aligns USNA NAF policy with DoD and Department of the Navy policy. USNAINST 7010.3 states that NAFs cannot be used to pay for employees not performing duties directly related to the NAFI function or mission and that NAF funds are only to be used for the benefit of the midshipmen.

USNA officials submitted a NAF report on the five NAFIs to the ASN(M&RA) on March 1, 2011. The report provides the required information on USNA NAFIs, in accordance with DoDI 1015.15, “Establishment, Management, and Control of Nonappropriated Fund Instrumentalities and Financial Management of Supporting Resources,” October 31, 2007. The report also includes the independent auditor’s opinion on the NABSD financial statements for FY 2010.

USNA officials drafted an amendment to 10 U.S.C. that would add section 6981, “Naval Academy Athletic Association: Support of Athletic Programs.” Section 6981, if adopted, would give the USNA statutory authority to receive funds from the NAAA that were generated by the athletic and physical fitness programs of the USNA and any other activity of the NAAA, and to retain and use such funds to further the mission of the USNA.

Because of our audit, on May 26, 2011, the USNA officials canceled the contingency account that was established in the memorandum, “Establishment of NABSD Contingency Account,” April 10, 2007. The memorandum stated that all authority for maintenance of a NAF or NABSD contingency account was canceled.

## **Recommendations, Management Comments, and Our Response**

### **D. We recommend that the U.S. Naval Academy Superintendent:**

**1. Perform periodic, independent, quality control reviews to ensure that U.S. Naval Academy personnel are not inappropriately accepting corporate sponsorship funds.**

**2. Deposit the remaining \$153,943, plus any interest earned, in the U.S. Treasury.**

### ***USNA Superintendent Comments***

ASN(M&RA) stated the USNA Superintendent agreed with Recommendation D.1 and that USNA NAFIs no longer accepted sponsorship proceeds from NAAA. In addition, ASN(M&RA) stated that the Superintendent disagreed with Recommendation D.2 and that USNA had prepared and submitted a proposal to Congress that would clarify USNA’s authority to use NAAA to secure sponsorship deals. Further, ASN(M&RA) stated that the USNA Superintendent suggested that the proceeds be processed as a gift from NAAA, and if USNA was not allowed to accept these funds as a gift, they should be returned to NAAA.

## ***Our Response***

The ASN(M&RA) comments on Recommendation D.1 were responsive, and no further comments were required. However, the comments on Recommendation D.2 were not responsive. The \$153,943 was not a gift from NAAA as defined in 10 U.S.C. § 6973, “Gifts, Bequests, and Loans of Property: Acceptance for Benefit and Use of Naval Academy.” Section 6973(a) authorizes the Secretary of the Navy to accept, hold, administer, and spend any gift or bequest of personal property other than money that is made on the condition that it be used for the benefit of, or for use in connection with, the USNA or the USNA Museum. Section 6973(a) states that bequests of money are to be deposited in the Treasury in the fund called “United States Naval Academy Gift and Museum Fund.” Under Section 6973(a), the Secretary of the Navy has the authority to disburse funds deposited pursuant to Section 6973(a) for the benefit or use of the USNA, including the USNA Museum. The USNA did not have independent statutory authority to retain the \$153,943 received from NAAA as a gift. We request that ASN(M&RA) provide comments on the final report.

## **Finding E. Review of USNA Foundation Monetary Gifts for Prohibited Sources Was Not Performed and Gifts Over \$60,000 Were Not Approved**

The USNA Deputy and USNA Comptroller did not review monetary gifts received from the USNA Foundation<sup>8</sup> for prohibited sources. In addition, the USNA SJA did not review monetary gifts to determine whether they were received from prohibited sources. The Deputy and Comptroller requested and received 30 disbursements from the USNA Foundation (Foundation) for \$60,000 each to avoid obtaining the required Under Secretary of the Navy approval. The multiple disbursement requests of \$60,000 appear to bypass all established oversight controls. This occurred because the USNA and the Foundation memorandum of understanding did not require the Foundation to review gifts and determine whether they were received from prohibited sources or require the Foundation to provide the donor source. In addition, the Comptroller had the ability to request funds from the Foundation.

As a result, the USNA might have indirectly received gifts from prohibited sources through the Foundation. Gifts from a prohibited source could reflect unfavorably on USNA officials and their ability to carry out responsibilities fairly and objectively. In addition, acceptance without a review for prohibited sources could create the appearance of an improper endorsement of the donor. Furthermore, it appears that the Comptroller was circumventing SECNAV policy.

### **Review of the Source of Gifts Not Performed**

The Deputy and Comptroller did not review gifts received from the USNA Foundation for prohibited sources. In addition, the SJA did not review monetary gifts to determine whether they were received from prohibited sources. USNA procedures did not require the Foundation to provide the donor source. Therefore, the Foundation may be acting as a conduit for USNA by accepting gifts from prohibited sources that the USNA would not be permitted to receive.

SECNAVINST 4001.2J, "Acceptance of Gifts," August 12, 2009, states that although foundations and other nonprofit organizations may provide valuable support to the Navy, they should not be used as conduits to make indirect gifts that Navy gift acceptance policies would not permit if offered directly to the Navy. SECNAVINST 4001.2J also states the acceptance of gifts from prohibited sources may give the appearance of influencing official decision-making or actions of the Navy. Before accepting a gift of more than \$10,000 from a prohibited source, the

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<sup>8</sup> In 1996, the USNA Superintendent requested that various entities join together to establish a single fund-raising entity to solicit private funds on behalf of the USNA. As a result, the Foundation and Alumni Association entered into an operating agreement in December 1999. Under the operating agreement, the Foundation is responsible for the solicitation and receipt of all private financial gifts. Gifts requested from the USNA Foundation include gifts from the USNA Alumni Association. Both the USNA Foundation and the Alumni Association are independent, not-for-profit corporations. However, both share a single president and CEO, and both operate as a fully integrated organization in support of the USNA and its mission.



USNA Office of General Counsel or the Navy/Marine Corps Judge Advocates must consult with the Assistant General Counsel for Ethics to determine whether the donor is involved in any claims, procurement actions, litigation, or other matters involving the Department of the Navy that might cause the acceptance authority to decline an offered gift.

The Foundation may be acting as a conduit for USNA by accepting gifts from prohibited sources the USNA would not permit if offered directly to USNA. The Foundation is an independent entity and is not required to follow USNA prohibited source regulations. Because the Foundation did not identify the gift sources, it may have given the USNA donations from prohibited sources without USNA officials' knowledge.

During our audit, we identified prohibited sources that donated to the Foundation. The "USNA Foundation Donor Report – 2009" lists contributing donors to the Foundation. SECNAVINST 4001.2J defines a prohibited source as an entity doing business with the Department of the Navy. We identified 13 donors listed on the Foundation Donor Report as entities doing business with the Department of the Navy. Therefore, these donors would be considered prohibited sources by USNA. The Comptroller stated that USNA does not perform an ethics review for gifts received from the Foundation. Furthermore, the SJA stated that gifts to the Foundation would not be reviewed for prohibited sources by his Office because they are not gifts to the USNA.

These conditions occurred because the USNA and the Foundation memorandum of understanding did not require the USNA Foundation to review gifts and determine whether they were received from prohibited sources or to provide the donor source to the USNA. As a result, the USNA might have indirectly received monetary gifts from prohibited sources through transfers from the USNA Foundation.

Gifts from a prohibited source may reflect unfavorably on the USNA's ability to carry out responsibilities and duties fairly and objectively. In addition, the acceptance without a review for prohibited sources could create the appearance of an improper endorsement of the donor. The USNA Superintendent should develop a memorandum of understanding between the USNA and the Foundation to ensure donations are reviewed to determine whether they were received from prohibited sources and to ensure donor sources are provided to the USNA.

## **Gifts to USNA Valued at More Than \$60,000**

The Deputy and Comptroller requested and received 30 disbursements of \$60,000 each from the USNA Foundation. The requests appeared to circumvent SECNAVINST 4001.2J, which states that the USNA Superintendent has the authority to accept gifts of \$60,000 or less. For an amount over \$60,000, the Under Secretary of the Navy must approve the gift. Therefore, it appears that the Deputy and Comptroller were purposely requesting gifts in installments of \$60,000 or less to avoid obtaining the Under Secretary of the Navy approval. SECNAVINST 4001.2J requires that "When a donor makes a pledge or offer of a future gift, whether a one-time gift or a gift made in several installments, the total cumulative amount of the future gift determines the appropriate acceptance authority." Therefore, the Under Secretary of the Navy should be the acceptance authority for a single or cumulative gift valued at more than \$60,000.

During 2010, the Foundation provided most of the USNA monetary gifts that required only the USNA Superintendent's approval. To receive the monetary gifts from the USNA Foundation, the Deputy or Comptroller had to submit a "Request for Disbursement Form." This form indicates the purpose of the request, where the funds are to be deposited at the USNA, and from which accounts the funds should be withdrawn at the Foundation. The USNA made 30 gift requests to the USNA Foundation at the acceptance threshold of \$60,000, totaling \$1.8 million in 2010. Many of these monetary gift requests were for the same recipient and were made in several installments. For example, the Academic Center and the Admissions Outreach each received four gifts of \$60,000 each for a total of \$240,000 in 2010. The USNA requested these installments either on the same day, within weeks, or within months of each other.

For example, on January 26, 2010, the USNA deposited three donations for \$60,000 each from the Foundation. Two of the donations were for the Center for Ethical Leadership. In another example, on May 13, 2010, two gifts of \$60,000 each were given to Admissions Outreach. Both examples show the intent to bypass controls. They show that the USNA purposely requested gifts in \$60,000 installments to avoid obtaining the Under Secretary of the Navy approval. No requests were over \$60,000. (See Appendix F for the recipient, deposit dates, and amounts.) This occurred because the Comptroller had the ability to request funds from the Foundation. As a result, the Comptroller appeared to have circumvented SECNAV policy. The USNA Superintendent should follow the SECNAV policy and cease splitting donation requests to avoid proper approval.

## **Recommendations, Management Comments, and Our Response**

### **E. We recommend that the U.S. Naval Academy Superintendent:**

**1. Develop a memorandum of understanding between the U.S. Naval Academy and the U.S. Naval Academy Foundation to ensure donations are reviewed to determine whether they were received from prohibited sources and to ensure donor sources are provided to the U.S. Naval Academy.**

**2. Follow the procedures in SECNAVINST 4001.2J, "Acceptance of Gifts," August 12, 2009, for accepting donations from the U.S. Naval Academy Foundation.**

**3. Cease splitting donation requests to avoid obtaining Under Secretary of the Navy approval for cumulative gifts totaling more than \$60,000.**

### ***USNA Superintendent Comments***

ASN(M&RA) stated the USNA Superintendent agreed, in part, with Recommendation E.1 and that USNA and the USNA Foundation had updated the memorandum of understanding, which was under review and expected to be signed in November 2011. To improve the coordination between the USNA and USNA Foundation, the memorandum of understanding was to provide for a USNA liaison to the Foundation to increase visibility of the donor source.

Further, ASN(M&RA) stated that USNA would continue to comply with SECNAVINST 4001.2J by ensuring that gifts from prohibited sources received heightened scrutiny when those gifts were made directly to the USNA. He also stated that all gifts from prohibited sources given directly to the USNA were coordinated with the USNA Comptroller, Deputy for Finance, SJA, Superintendent, and the Secretariat, when applicable, before acceptance. In addition, he stated that although there was no automatic prohibition on gift acceptance from prohibited sources, USNA recognized that increased scrutiny and coordination were warranted.

ASN(M&RA) stated that the USNA Superintendent disagreed with Recommendation E.2 and was adhering to USNAINST 4001.5A to ensure compliance with SECNAVINST 4001.2J. He agreed to increase communication and transparency of donor source for gifts made to the USNA Foundation, but disagreed with performing prohibitive source reviews under SECNAVINST 4001.2J for gifts made directly to the USNA Foundation even if ultimately these funds made their way to the USNA. He stated that the USNA Foundation was not used as a conduit for accepting gifts that would not otherwise be acceptable if made directly to the Navy. It would be inappropriate to perform a prohibitive source analysis for gifts made from donors directly to the Foundation, which is a private organization. However, increased coordination and communication with the USNA Foundation through the USNA liaison would ensure that the USNA Foundation did not accept gifts the USNA would ultimately be prohibited from accepting.

In addition, ASN(M&RA) stated that the USNA Superintendent disagreed with Recommendation E.3 and the auditor conclusion that the USNA Comptroller was intentionally splitting donations to avoid obtaining Under Secretary of the Navy approval for cumulative gifts of more than \$60,000. The intent of the USNA Comptroller in drawing smaller amounts of funds was to ensure only the appropriate amount of money was drawn to meet current obligations of the USNA programs. However, to avoid any appearance of gift splitting, the USNA initiated a new practice in which the Foundation now offers annual gifts for Restricted Endowments, Restricted Funding, Unrestricted Funding, and Athletic and Scholarship funding. These offers of gifts are forwarded to the Secretary of the Navy for acknowledgment and acceptance to prevent the appearance that the USNA was splitting donations.

### ***Our Response***

The ASN(M&RA) comments on Recommendations E.1 and E. 2 were partially responsive. The establishment of a USNA liaison should improve coordination and communication between the USNA and the USNA Foundation and increase visibility of the donor source. However, the comments did not state whether a prohibited source review would be conducted on gifts from the USNA Foundation. We request that the Assistant Secretary provide comments on the final report.

The ASN(M&RA) comments on Recommendation E.3. were responsive, and no further comments were required. Although the USNA Superintendent disagreed with our recommendation, the proposed actions, if implemented, would meet the intent of the recommendation.

## Appendix A. Scope and Methodology

We conducted this performance audit from September 2010 through September 2011 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 the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

We reviewed the USNA NABSD 2008 contract for a short motion picture and six commercials. Specifically, we:

- Reviewed the sole source justification prepared by the Deputy of Finance and other documentation related to the decision for a sole-source award. We also interviewed SJA staff and reviewed the contract file to obtain evidence of a legal review. In addition, we reviewed DoD, Navy, and USNA policies regarding contract authority and the use of contracts other than Government contracts.
- Examined documentation for seven wire transfers totaling \$3,507,816 withdrawing funds from NABSD's nonappropriated operating bank account and crediting the contractor's bank account. We matched these wire transfers to email correspondence from the contractor.
- Reviewed a copy of the short motion picture to verify the existence and adequacy of the short motion picture. We also compared the cost of short motion picture and television commercials to the short motion picture and television commercials that were produced in 2006.
- Reviewed email correspondence between the Deputy of Finance and the NABSD Director regarding the contract.

We also reviewed the cost estimates, bids, and contract clauses for the two additional contracts awarded during 2008 and 2009. We also evaluated the request for proposals and bid analysis for one of the two contracts. We interviewed the new contracting officer appointed in February 2010 to obtain an understanding of the changes made to the USNA NABSD contracting process. In addition, we reviewed the new USNAINST 7010.2B, "United States Naval Academy (USNA) Nonappropriated Fund (NAF) Procurement Policy," July 28, 2010, and reviewed USNA NABSD contracting and purchase order procedures.

We reviewed gift fund processes at USNA, its nonprofit organizations, and its nonappropriated fund instrumentalities (NAFIs). We initially sampled donations of monetary and in-kind gifts accepted at USNA from January 1, 2010, through September 30, 2010. The universe for monetary gifts consisted of 308 items totaling \$4.8 million. We selected a non-statistical sample of 20 of the 308 monetary gifts totaling \$346,918. The universe for in-kind gift donations consisted of 98 items valued at \$24.1 million. We selected a non-statistical sample of six in-kind gift donations valued at \$86,476. These six gifts were the total in-kind gift donations received in 2010 for the Museum. We sampled these donations to ensure the USNA was properly accepting, recording, and depositing the donation according to the donor's intent.

We subsequently expanded our monetary donations and in-kind gift testing through December 31, 2010, to determine the effects from changes the USNA implemented because of our audit. From January 1, 2010, through December 31, 2010, USNA received 381 monetary gifts, totaling \$5.7 million and 153 in-kind gifts valued at \$25.1 million. We selected three additional monetary donations, totaling \$67,150.

We reviewed the in-kind gifts, valued at \$184,712, that were received from an alumnus and had not been recorded in the USNA property records to follow up on whether these gifts had been properly accepted by the USNA.

We also evaluated, for 2010, the sufficiency of new policies, procedures, controls, and staffing to prevent or detect:

- the recurrence of the substantiated allegations identified in the Naval Inspector General (IG) report, “Senior Official Case 200801937; Alleged Misuse of Gift Funds and Non-appropriated Funds (NAF),” November 17, 2009; and
- possible compliance issues within new gift funds and NAFs.

We reviewed four corporate sponsorship transfers to USNA NABSD from NAAA from April 2007 through March 2010. We traced these transfers to NABSD accounting records.

We reviewed a total of 23 monetary gifts totaling \$414,068, from the USNA Foundation, USNA Alumni Association, and private donors for compliance with DoD, Navy, and USNA regulations for donor designations, prohibited sources, and restrictions. We also examined 30 disbursements to the USNA at the \$60,000 limit.

## **Use of Computer-Processed Data**

We did not use computer-processed data to perform this audit.

## **Use of Technical Assistance**

We did not use any technical assistance in the performance of this audit.

## **Prior Coverage on Gift Policy and Procedures**

During the last 5 years, the Government Accountability Office (GAO), DoD Inspector General (DoD IG), Naval Inspector General, and the Commander, Navy Installations Command have issued four reports discussing proper gift and NAF procedures, NAFI operations, and contracting practices. Unrestricted GAO reports can be accessed over the Internet at <http://www.gao.gov>. Unrestricted DoD IG reports can be accessed at <http://www.dodig.mil/audit/reports>. Naval Inspector General and the Commander, Navy Installations Command reports are not available over the Internet.

## **GAO**

GAO Report No. GAO-09-486R, “Financial Management: DOD Needs to Clarify Its General Gift Fund Policies to Provide for Effective Oversight,” May 27, 2009

***DoD IG***

DoD IG Report No. D-2010-081, "Army Use of Time-and-Materials Contracts in Southwest Asia," August 27, 2010

***Naval Inspector General Report***

Naval Inspector General Report, "Senior Official Case 200801937; Alleged Misuse of Gift Funds and Nonappropriated Funds (NAF)," November 17, 2009

***Commander, Navy Installations Command***

Commander, Navy Installations Command, "Fiscal Oversight Review of the United States Naval Academy Non-Appropriated Fund Instrumentality," April 9, 2010

# Appendix B. Nonprofit Organizations and Nonappropriated Fund Instrumentalities Supporting the U.S. Naval Academy

The following nonprofit organizations support the USNA in meeting its mission.

## Naval Academy Athletic Association (NAAA)

The Naval Academy Athletic Association (NAAA) promotes and finances the USNA's intercollegiate athletic program. The NAAA is responsible for the coaching, equipping, travel and lodging, promotion, ticketing, and administrative support for all 32 varsity sports. The NAAA also operates and maintains Navy-Marine Corps Memorial Stadium, the USNA golf course, and other athletic facilities for the USNA. The NAAA works actively with outstanding high school student-athletes who are interested in applying to the USNA. Varsity coaches recruit young men and women according to the rules and regulations laid down by the National Collegiate Athletic Association.

## USNA Alumni Association

The USNA Alumni Association was incorporated in 1947. The mission of the USNA Alumni Association is to serve and support the United States, the Naval Service, the USNA, and its alumni: by furthering the highest standards at the Naval Academy; by seeking out, informing, encouraging, and assisting outstanding, qualified young men and women to pursue careers as officers in the Navy and Marine Corps through the USNA; and by initiating and sponsoring activities that related to the history, traditions, memories, and growth of the USNA.

## USNA Foundation

The USNA Foundation was incorporated in 1944 solely for the purpose of providing private support to the USNA, primarily to meet the needs of the Brigade of Midshipmen. It is the mission of the USNA Foundation

To support, promote, and advance the mission of the Naval Academy by working in conjunction with the Naval Academy leadership to identify strategic institutional priorities and by raising, managing, and disbursing private gift funds that provide a margin of excellence in support of the nation's premier leadership institution.

## Nonappropriated Fund Instrumentality

A NAFI is a fiscal entity of the U.S. Government that is fully or partially supported by nonappropriated funds. The USNA established the following NAFIs on December 10, 2010, so they reflect current Navy policy and guidance:

- **Naval Academy Business Services Division (NABSD).** NABSD operates 20 separate NAF activities in direct support of the Brigade of Midshipmen and the USNA as the Navy's undergraduate institution. These activities are required to support midshipmen in the official performance of their duties or to provide the services for faculty, staff, alumni, and visitors normally found at colleges and universities across the country.



NABSD also provides food service support to midshipmen during both liberty and non-liberty hours. NABSD functions in a similar manner to campus support services organizations at civilian institutions of higher education.

- **Midshipmen Welfare Fund.** The Midshipmen Welfare Fund is responsible for assisting the Brigade of Midshipmen by providing opportunities for structured extra-curricular involvement in recreational or other constructive activities at the individual, company or battalion level. The Midshipmen Welfare Fund functions in a similar manner to campus support organizations, including student unions and recreational organizations, at civilian institutions of higher education.
- **Midshipmen Ration Account.** The Midshipmen Ration Account is the account used to manage the subsistence allowance prescribed by the Secretary of Defense for midshipmen. The nonappropriated funds in this account are used to procure the food and food products necessary to provide for the subsistence of midshipmen.
- **Naval Academy Preparatory School Activity Fund.** The Naval Academy Preparatory School Activity fund provides for goods and services required by each midshipman candidate, such as textbooks, computer equipment, and Naval Academy Preparatory School Activity personal physical training gear. In addition, the Naval Academy Preparatory School Activity fund provides opportunities for structured extracurricular involvement in recreational or other constructive activities at the individual or battalion level.
- **Candidate Guidance Fund.** The Candidate Guidance Fund is the sole nonappropriated fund used to support the Dean of Admissions' mission. The fund acts as a collection and disbursing agent for various initiatives sponsored by the Office of Admissions for expenses incurred in connection with all Admissions Strategic Outreach activities through the collection and disbursement of program registration fees. Sponsored activities using the Candidate Guidance fund include the USNA Summer Seminar Program; Science, Technology, Engineering and Math Program; and other Strategic Outreach programs.

# **Appendix C. Update on Substantiated Allegations From the Naval Inspector General Report**

## **Allegation 1**

The former USNA Superintendent misused Government gift funds by authorizing a subordinate to expend those funds for gifts and entertainment that was not in compliance with GAO guidelines and various USNA Instructions addressing policy and procedures for administering the USNA Gift Fund program.

### ***Actions Taken***

The former Command Master Chief, who was responsible for entertainment, was replaced by a new Command Master Chief.

USNA drafted a new instruction, USNA Draft Instruction 7000.4, “Guidelines on the Use of Gift Funds in Furtherance of the USNA Mission.” This instruction requires necessary and reasonable conditions to be met to use Gift Funds. Necessary expenses are expenses for which the “USNA’s mission cannot be accomplished as satisfactorily or as effectively without such expenditure.” Reasonable expenses are expense for which “the general public would not perceive the amount of the expenditure and/or the per capita benefit to be wasteful or extravagant.” To satisfy the “reasonableness” rule, an expenditure is permissible if it meets the following criteria: (1) Cost Per Person: Where a meal is provided, the cost of the meal should not exceed 200 percent of the local per diem rate per person. (2) Hosting Ratios: An appropriate ratio of authorized guests to DoD, Department of the Navy, USNA personnel is to be observed at officially hosted functions where Gift Funds are used. Midshipmen do not count in the hosting ratio calculation.

## **Allegation 2**

The former Superintendent improperly accepted personal gifts not in compliance with the Standards of Ethical Conduct, 5 C.F.R. § 2635.202, which addresses gifts from outside sources.

### ***Actions Taken***

The former USNA Superintendent received pendant necklaces for the 2007 and 2008 football seasons. After being informed that the acceptance of these pendant necklaces may be inappropriate, the former USNA Superintendent turned the pendant necklaces over to the SJA, who has held them since, pending a determination on their disposition. The necklaces were in their original boxes and had not been worn. The former USNA Superintendent did not want to purchase the pendant necklaces.

### **Allegation 3**

The USNA Deputy for Finance improperly established and used an “off-the-books” nonappropriated fund (NAF) Contingency Fund, which was not in compliance with DoD and Navy policy on NAF expenditures, Secretary of the Navy (SECNAV) and USNA gift policies and procedures, and the Miscellaneous Receipts statute.

#### ***Actions Taken***

In September 2009, NABSD transferred the remaining corporate sponsorship funds of \$106,443 to the official NABSD operating account. This account is supervised and controlled by the Federal Government. The \$106,443 was recorded in the NAFI accounting system.

### **Allegation 4**

The USNA Deputy for Finance improperly executed contracting and financial actions arising from an improperly constituted and funded video production contract not in compliance with DoD and Navy policy on NAF expenditures and contracting procedures and the Standards of Ethical Conduct.

#### ***Actions Taken***

NABSD hired a warranted contracting officer and also developed a new procurement manual, USNA Instruction 7010.2B, “United States Naval Academy (USNA) Nonappropriated Fund (NAF) Procurement Policy,” July 28, 2010. The warranted officer handles contracts with the NABSD. The new NABSD Procurement Manual provides contracting procedures and states, “The USNA Counsel or the USNA Staff Judge Advocate (SJA) will provide legal support and assistance to USNA NAF contracting efforts.”

### **Allegation 5**

The USNA Deputy for Finance executed multiple ethics violations arising from a personal relationship with a donor. The acceptance of gifts from this donor was not in compliance with SECNAV and USNA gift procedures, financial disclosure procedures, and the Standards of Ethical Conduct.

#### ***Actions Taken***

The USNA inventoried gifts improperly received by the USNA Deputy for Finance. In addition, the gifts were submitted to SECNAV for official approval and acceptance. The gift inventory included items, valued at \$184,712. The USNA inventoried gifts shown in table 4.

**Table 4. Gifts Inappropriately Accepted by the Deputy for Finance**

<b>Item</b>	<b>Description</b>	<b>Quantity</b>	<b>Value</b>
Waterford Crystal	Stemware	754	\$72,505
	Serveware	92	29,174
	Chandeliers	8	38,515
Simon Pierce Pottery	Small Vases	12	1,500
	Large Vases	14	2,100
Baccarat Crystal	Glasses	22	2,310
	Vase	1	900
	Bowls	2	1,600
Alcoholic Beverages	Bottles of Wine	29	3,657
Bibles	Protestant Bible	312	8,733
	Catholic Bible	165	4,618
Daum Crystal	Vase	1	5,000
Artwork	Paintings	3	14,100
<b>Total Value</b>			<b>\$184,712</b>

The USNA Superintendent issued an action memorandum on March 22, 2011, requesting the Director Navy Staff to accept the in-kind gifts received. The USNA Superintendent requested that the gifts be accepted by May 6, 2011.

### **Allegation 6**

The USNA Deputy for Finance gave a gift to an official superior, and the gift acceptance was not in compliance with the Standards of Ethical Conduct, 5 C.F.R. § 2635.302.

### **Actions Taken**

The former USNA Superintendent returned the bottle of champagne to the USNA Deputy for Finance. The Deputy for Finance resigned from the USNA in January 2011; however, as of March 2011, the champagne was in the former USNA Deputy for Finance's vacant office.

# Appendix D. Payments Before Contractor's Signature

TOTAL AGREEMENT

**From:** [REDACTED]  
**Sent:** Monday, May 12, 2008 11:39 AM  
**To:** [REDACTED]  
**Subject:** post production for this round

CASH FLOW SCHEDULE

Re: [REDACTED]  
The awarded budget for the 30, 60 and 10 minute fulfill your destiny spot totaled \$2,527,568 including post production.  
Below please find revised payment schedule:

4/7/08	-	\$784,864	PAID
5/1/08	-	\$392,432	PAID
5/12/08	-	\$478,920	DUE
5/23/08	-	\$392,432	DUE
6/30/08	-	\$478,920	DUE

1

# Appendix E. Illustration of Contractor's Payment Request



Robert [REDACTED]  
From: [REDACTED]  
[REDACTED]  
[REDACTED]  
[REDACTED]

PRODUCTION  
CASH FLOW SCHEDULE  
AND WIRE INSTRUCTIONS

[REDACTED] has set up the bank account for [REDACTED], I'm sending our wire information and I wanted to see if we could get the following payments wired into the account Please let me know if this is possible

- 1st Half Payment on April 7, in the the amount of \$784,864
  - 25% on May 1 preceding our first day of photography in the amount of \$392,432
  - final 25% May 23 the last day of principle photography in the amount of \$392,432
- Editorial - I'll send you that budget as soon as it's finalized

[REDACTED]  
[REDACTED]

Thank you!

[REDACTED]

## Appendix F. Disbursement Requests From the USNA of \$60,000

Table F.1. Disbursement Requests by Recipient

Date	USNA Recipient	Amount
3/11/2010	Academic Center	\$60,000
5/13/2010	Academic Center	60,000
11/17/2010	Academic Center	60,000
12/14/2010	Academic Center	60,000
<b>Subtotal</b>		<b>\$240,000</b>
1/12/2010	Admissions Outreach	\$60,000
2/18/2010	Admissions Outreach	60,000
5/13/2010	Admissions Outreach	60,000
5/13/2010	Admissions Outreach Marketing	60,000
<b>Subtotal</b>		<b>\$240,000</b>
1/26/2010	Center for Ethical Leadership Instructional Video	\$60,000
2/18/2010	Center for Ethical Leadership Instructional Video	60,000
<b>Subtotal</b>		<b>\$120,000</b>
1/26/2010	Center for Ethical Leadership	\$60,000
3/26/2010	Center for Ethical Leadership	60,000
5/27/2010	Center for Ethical Leadership	60,000
<b>Subtotal</b>		<b>\$180,000</b>
8/12/2010	Center for Middle East and Islamic Studies	\$60,000
2/18/2010	Distinguished Visiting IT Professor	60,000
3/11/2010	Distinguished Military Professor in Character Development	60,000
3/26/2010	Distinguished Visiting Professor in National Security	60,000
3/11/2010	Heinlein Professor of Aerospace	60,000
3/26/2010	Kinnear Science Chair	60,000
<b>Subtotal</b>		<b>\$360,000</b>
3/1/2010	McNeill Chair in Engineering	\$60,000
5/27/2010	McNeill Chair in Engineering	60,000
<b>Subtotal</b>		<b>\$120,000</b>
5/13/2010	Midshipmen Welfare Fund	\$60,000
7/14/2010	Naval Heritage Chair	60,000
8/12/2010	Naval Heritage Chair	60,000
<b>Subtotal</b>		<b>\$180,000</b>
1/26/2010	Rogers Chair in Aerospace Engineering	\$60,000
9/14/2010	Rogers Chair in Aerospace Engineering	60,000
<b>Subtotal</b>		<b>\$120,000</b>
3/1/2010	Science, Technology, Engineering and Math (STEM) Summer Program	\$60,000
3/26/2010	STEM Summer Program	60,000



<b>Date</b>	<b>USNA Recipient</b>	<b>Amount</b>
5/13/2010	STEM Summer Program	60,000
<b>Subtotal</b>		<b>\$180,000</b>
9/14/2010	Tetrault Director, Center for Ethical Leadership	\$60,000
<b>Subtotal</b>		<b>\$60,000</b>
<b>Total</b>		<b>\$1,800,000</b>

**Table F. 2. Disbursement Request Deposits by Date**

<b>Date</b>	<b>USNA Recipient</b>	<b>Amount</b>
01/12/10	Admissions Outreach	\$60,000
01/26/10	Center for Ethical Leadership Instructional Video	60,000
01/26/10	Center for Ethical Leadership	60,000
01/26/10	Rogers Chair in Aerospace Engineering	60,000
02/18/10	Admissions Outreach	60,000
02/18/10	Center for Ethical Leadership Instructional Video	60,000
02/18/10	Distinguished Visiting IT Professor	60,000
03/01/10	McNeill Chair in Engineering	60,000
03/01/10	Science, Technology, Engineering, and Math (STEM) Summer Program	60,000
03/11/10	Heinlein Professor of Aerospace	60,000
03/11/10	Academic Center	60,000
03/11/10	DMP in Character Development	60,000
03/26/10	Center for Ethical Leadership	60,000
03/26/10	DVP in National Security	60,000
03/26/10	Kinnear Science Chair	60,000
03/26/10	STEM Summer Program	60,000
05/13/10	Midshipmen Welfare Fund (DAS)	60,000
05/13/10	Academic Center	60,000
05/13/10	Admissions Outreach	60,000
05/13/10	Admissions Outreach Marketing	60,000
05/13/10	STEM Summer Program	60,000
05/27/10	Center for Ethical Leadership	60,000
05/27/10	McNeill Chair in Engineering	60,000
07/14/10	Naval Heritage Chair	60,000
08/12/10	Center for Middle East and Islamic Studies	60,000
08/12/10	Naval Heritage Chair	60,000
09/14/10	Rogers Chair in Aerospace Engineering	60,000
09/14/10	Tetrault Director, CEL	60,000
11/17/10	Academic Center	60,000
12/14/10	Academic Center	60,000
<b>Total</b>		<b>\$1,800,000</b>

# Under Secretary of Defense (Comptroller)/Chief Financial Officer, DoD, Comments



COMPTROLLER

OFFICE OF THE UNDER SECRETARY OF DEFENSE  
1100 DEFENSE PENTAGON  
WASHINGTON, DC 20301-1100

MEMORANDUM FOR PROGRAM DIRECTOR, FINANCIAL MANAGEMENT  
AND REPORTING, OFFICE OF INSPECTOR  
GENERAL, DEPARTMENT OF DEFENSE

SUBJECT: Response to Draft Audit Report, "U.S. Naval Academy Officials Did Not Adhere  
to Contracting and Gift Policies," (Project No. D2011-D000FP-0273.000)

This memorandum forwards the Office of the Under Secretary of Defense (Comptroller)  
response to the subject draft audit report. A copy of the response is attached.

The Department appreciates the opportunity to comment on the subject report. [REDACTED]

  
Mark E. Easton  
Deputy Chief Financial Officer

Attachment:  
As stated

**DOD OIG DRAFT REPORT DATED SEPTEMBER 6, 2011  
PROJECT NO. D2011-D000FP-0273.000**

**U.S. NAVAL ACADEMY OFFICIALS DID NOT ADHERE TO CONTRACTING AND  
GIFT POLICIES**

**OFFICE OF THE UNDER SECRETARY OF DEFENSE (COMPTROLLER)  
COMMENTS TO THE DOD OIG RECOMMENDATIONS.**

**RECOMMENDATION A.1:** We recommend that the Under Secretary of Defense (Comptroller)/Chief Financial Officer, DoD initiate a preliminary review to determine whether the U.S. Naval Academy augmented its budget by using nonappropriated funds instead of appropriated funds, resulting in a potential Antideficiency Act (ADA) violation.

**OUSD(C) RESPONSE:** Partially Concur. The Deputy Chief Financial Officer concurs that a preliminary ADA review should be performed as required by DoD Regulation 7000.14-R, "Department of Defense Financial Management Regulation (DoDFMR)," volume 14, chapter 3. However, the recommendation will be referred to the Office of the Assistant Secretary of the Navy, Financial Management and Comptroller, who will initiate the preliminary investigation in accordance with the DoDFMR, Volume 14, Chapter 3, paragraph 0303.

# Department of the Navy Comments



DEPARTMENT OF THE NAVY  
OFFICE OF THE ASSISTANT SECRETARY  
(MANPOWER AND RESERVE AFFAIRS)  
1000 NAVY PENTAGON  
WASHINGTON DC 20350-1000

October 6, 2011

MEMORANDUM FOR DEPARTMENT OF DEFENSE INSPECTOR GENERAL

SUBJECT: U.S. Naval Academy Officials Did Not Adhere to Contracting and Gift Policies  
(Project No. D2010-D000FP-0273.000)

By memorandum dated 6 September 2011, you requested that the Department of the Navy respond to the subject draft audit report prepared following an audit of the United States Naval Academy conducted at the request of staff of the Senate Armed Services Committee. Thank you for the opportunity to respond to the report and to provide the Department's responses to the findings and recommendations.

Following the release of the Naval Inspector General's Report of Investigation in December 2009 (Senior Official Case 200801937: Alleged Misuse of Funds and Nonappropriated Funds), the Department initiated a number of reviews and remedial actions. Specifically, we directed a comprehensive review and audit of the Naval Academy's non-appropriated fund instrumentalities (NAFIs) and a review of its financial management practices. We also directed a review of the Naval Academy's gift acceptance procedures and a thorough examination of the Naval Academy Athletic Association's (NAAA) involvement in the operations and management of the Naval Academy. The Naval Academy underwent the following audits and reviews:

- 1) Appropriated Funds Audit (May 2010)
- 2) Non appropriated Fund Audit (Jun 2010)
- 3) NAAA – USNA relationship review group. (August 2010)
- 4) Department of the Navy gift acceptance process review (Sep 2010 – Jan 2011)
- 5) Non appropriated Fund Audit (Aug 2011)

In light of these audits and reviews, the Superintendent developed a plan to implement the corrective actions called for by the Naval Inspector General and subsequent audits and reviews and the Naval Academy formed a working group dedicated to continuous improvement in the financial management practices at the Naval Academy. Today, the Superintendent reports progress on a quarterly basis to the Vice Chief of Naval Operations and to the Naval Academy Board of Visitors.

Over the past two years, the Naval Academy has updated guidance and improved procedures in the following fiscal-related areas:

- 1) Gift Acceptance
- 2) Gift Fund expenditure
- 3) Human Resources
- 4) Procurement
- 5) Fiscal Management

The Department values the thorough review and recommendations of your audit team and offers the following responses to the recommendations set forth in the draft audit report.

**Finding A. Improper Contracting Actions and Questionable Payments**

The DoD IG report inadvertently attributes many actions performed by the Deputy for Finance to the Director, Naval Academy Business Service Division.

A.1. The Naval Academy has no objections to an Anti-Deficiency Act inquiry and has met with

A.2. The Chief of Naval Operations agrees with and has already implemented this recommendation following the 2009 Naval Inspector General investigation. Commander, Navy Installations Command's Fiscal Oversight Team performs annual audits of the Naval Academy's NAFIs to ensure compliance with Department of Defense guidance on fiscal management standards.

A.3. The Naval Academy agrees with this recommendation and will modify the command evaluation schedule conducted by the Naval Academy Inspector General to ensure NAFI compliance with procurement procedures. Annual CNIC audits along with Naval Academy Command Evaluation reviews will provide the Superintendent the visibility required to ensure compliance.

**Finding B. Improvements Are Still Needed Over the USNA Museum's Recording of In-Kind Gifts**

B.1. The Naval Academy agrees with this recommendation and, in conjunction with the Naval History and Heritage Command (NHHC), has taken or will take the following actions specific to each recommendation.

- a. Gifts to the Naval Academy Museum are accepted by the Superintendent in accordance with 10 U.S.C. § 6973 and SECNAV Instruction 4001.2J. In addition, the Museum follows the instructions for gift acceptance (USNA Instruction 4001.5A) updated by the Naval Academy in October 2010. These policies and procedures are consistent with NHHC policies and procedures.
- b. Since the issuance of USNA Instruction 4001.5A on 14 October 2010, all gifts received by the Museum are now processed through the Naval Academy Comptroller's Office, the Deputy for Finance, the Staff Judge Advocate, and ultimately accepted by the Superintendent or the Under Secretary of the Navy.
- c. Coincident with the renovation of Preble Hall (November 2007 – August 2009), an inventory of the collection was conducted in accordance with American Association of Museum (AAM) standards. The Museum continues to verify the inventory database for

items stored in Preble Hall as well as those items stored off-site. When these inventories are completed, the Museum will initiate a program to verify the inventory on a five-year cycle. This five-year cycle is in accordance with American Association of Museum (AAM) standards.

- d. Because the Naval Academy Museum is not connected to the Navy Marine Corps Intranet (NMCI), it requires a separate standalone configuration of the Department of the Navy Heritage Asset Management System (DONHAMS). The NHHC is developing a web-based version of the DONHAMS collections management application (DONCOMS). After connectivity is achieved (expected September 2012), updates to the collections inventory could be made directly by the Naval Academy Museum staff into the database via the Internet. In the meantime, the Naval Academy Museum will periodically synchronize its FileMaker inventory files with the DONHAMS database.
- e. Accession numbers will be assigned to all USNA Museum assets by 30 September 2012, the end of the American Association of Museum (AAM) self-study period. AAM museum accreditation process is the national benchmark of professionalism for American museums.
- f. Access to the inventory system is now limited to the Museum Director and the Museum Registrar, consistent with NHHC policies, in order to prevent unauthorized modification or deletion of in-kind gift records.

B.2. The Naval Academy agrees with this recommendation.

- a. The Naval Academy agrees that annual performance reviews for all employees will be performed in accordance with performance review cycles.
- b. The Naval Academy has developed a timeline to implement the DOD IG recommendations. Note, Recommendations are B.1.a through B.1.f, there is no B.1.g identified in the recommendations.

B.3. The Naval History and Heritage Command agrees with this recommendation.

- a. The NHHC agrees with this recommendation. The Draft Navy Museum Manual recently completed an extensive review and comment process. On September 21, the Director, NHHC met, via conference call, with the Directors from all of the Navy museums to reconcile comments received and close-out the comment review process. The effort to incorporate all of the agreed upon comments and finalize the document is currently underway. The Navy Museum Manual is scheduled to be completed in March 2012.
- b. The NHHC agrees with this recommendation. The DONHAMS is officially the only authorized database software for collections management in the Department of the Navy. However, because the Naval Academy Museum is not connected to NMCI, it requires a separate standalone configuration of DONHAMS. As noted above, there is currently an effort underway to develop a web-based version of the DONHAMS collections



management application and internet connectivity is anticipated to be achieved by September 2012. In the meantime, the Naval Academy Museum will periodically synchronize its inventory files with the DONHAMS database.

- c. The NHHHC agrees with this recommendation. The Museum System Program Office (MSPO) already interacts frequently with the Director of the USNA Museum and his staff. The MSPO reviewed the documents prepared by the Director of the Naval Academy Museum and submitted to the AAM to support the museum accreditation process. The application submitted by the USNA Museum was accepted by AAM and the accreditation process for the museum has now begun. The NHHHC is continuously working to update and improve its oversight and communication with the Directors and their staff for all of the museums within the Command. The Director, NHHHC, along with MSPO, now participates in a monthly conference call with the museum directors to discuss newly established policies and procedures and other matters of interest to the museum directors. We believe that this, and other measures already in place, provides the necessary additional oversight that will ensure that the Director of Naval Academy Museum is following applicable policies and procedures.

**Finding C. Unauthorized Acceptance of Gifts and Failure to Inventory Gifts**

Please note that, although the Director of Navy Staff reviews the Naval Academy gift acceptance package for the Crystal and Glassware, he is not the acceptance authority. The Under Secretary of the Navy is the appropriate gift acceptance official. The gift acceptance package referenced is currently pending approval by the Under Secretary of the Navy.

C. We are encouraged that there was no indication in your audit of any mishandling of gifts to the Naval Academy after the Navy Inspector General report. The Naval Academy is properly accepting, recording, and depositing donations according to the donor's intent. We concur with the recommendation that periodic, independent quality assurance reviews are necessary. To this end, the Naval Academy integrated these reviews into the annual Command Evaluation Program. Moreover, the Department of the Navy/Assistant for Administration conducted a review of the gift acceptance process at the Naval Academy and recommended conducting annual reviews to ensure continued compliance. The Secretary adopted this recommendation, which will provide independent quality control reviews to ensure Naval Academy compliance until such time as a status of "no findings" is achieved.

**Finding D. Inappropriate Acceptance and Use of Sponsorship Funds**

D.1. The Naval Academy agrees with this recommendation. The Naval Academy NAF no longer accepts sponsorship proceeds from the NAAA. The Naval Academy prepared and submitted a legislative proposal that will clarify the authority for the Naval Academy to utilize the Naval Academy Athletic Association to secure sponsorship deals. Although it is no longer a general practice to accept funds from the NAAA, the Naval Academy will ensure there is appropriate fiscal authority and controls to accept and retain funds from the NAAA, if necessary.

D.2. The Naval Academy objects to this recommendation and suggests that the proceeds be processed as a gift from the NAAA pursuant to 10 U.S.C. § 6973. Should the Naval Academy be unable to accept these funds as a gift from the NAAA, the funds should be returned to the NAAA.

**Finding E. Review of USNA Foundation Monetary Gifts for Prohibited Sources Was Not Performed and Gifts Over \$60,000 Were Not Approved**

The Naval Academy has taken measures to increase the visibility of donor source for gifts direct to the Foundation to improve gift acceptance procedures.

E.1. The Naval Academy agrees with this recommendation in part. Specifically, the Naval Academy and the Foundation are in the process of updating their Memorandum of Understanding (MOU) in light of this report and a previous Department review. The updated MOU is being reviewed and is expected to be signed no later than November, 2011. To improve the coordination between the Foundation and the Naval Academy, the Naval Academy MOU will provide for a liaison to the Naval Academy Foundation to increase visibility of the donor source.

The Naval Academy will continue to comply with SECNAVINST 4001.2J by ensuring gifts from prohibited sources receive heightened scrutiny when those gifts are made directly to the Naval Academy. All gifts from prohibited sources given directly to the United States Naval Academy are coordinated with the Naval Academy Comptroller, Staff Judge Advocate, Deputy for Finance, Superintendent and the Secretariat, when applicable, prior to acceptance under improved procedures implemented after the Naval Inspector General investigation. While there is no automatic prohibition on gift acceptance from prohibited sources, we recognize that increased scrutiny and coordination are warranted and the Naval Academy will continue to perform these reviews in the future.

Although the Naval Academy agrees with the recommendation to increase communication and transparency of donor source for gifts made to the Foundation, the Naval Academy disagrees with performing prohibitive source analysis under SECNAVINST 4001.2J for gifts made directly to the Naval Academy Foundation - even if ultimately these funds make their way to the Naval Academy. The Naval Academy is compliant with Federal, Department of Defense and Department of the Navy guidance on the use of foundations and non-profit organizations. The Naval Academy Foundation is not used as a conduit to accept gifts that would not otherwise be acceptable if made direct to the Navy. We believe that it is inappropriate to perform a prohibitive source analysis for gifts made from donors direct to the Foundation, a private organization. However, we agree that increased coordination and communication with the Foundation via the Naval Academy liaison will ensure that the Foundation does not accept gifts the Naval Academy would be prohibited from ultimately accepting.

E.2. The Naval Academy is adhering to USNAINST 4001.5A, Acceptance of Gifts to the United States Naval Academy, updated in October 2010, to ensure compliance with SECNAVINST 4001.2J.



E.3. We are certain corrective action taken in light of previous reviews of the gift acceptance process are sufficient to prevent the appearance of gift splitting. The Naval Academy disagrees with the DoD IG opinion that the Comptroller was intentionally splitting donations to avoid obtaining Under Secretary of the Navy approval for cumulative gifts more than \$60,000. The intent of the comptroller in drawing smaller amounts of funds on a quarterly or semi-annual basis was to ensure only the appropriate amount of money was drawn to meet current obligations of the Naval Academy programs. However, to avoid any appearance of gift splitting, the Naval Academy initiated a new practice in which the Foundation now offers annual gifts for Restricted Funding, Restricted Endowments, Unrestricted Funding, and Athletic and Scholarship funding. These offers of gifts are forwarded to the Secretary of the Navy for acknowledgement and acceptance to prevent the appearance that the Naval Academy is splitting donations.



Juan M. Garcia





# Inspector General Department of Defense

