

**Audit**



**Report**

OFFICE OF THE INSPECTOR GENERAL

ARMED FORCES RECREATION CENTER-EUROPE

Report No. 94-047

February 28, 1994

**Department of Defense**

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### **Acronyms**

AFRC	Armed Forces Recreation Center-Europe
AR	Army Regulation
CFSC	Army Community and Family Support Center
COR	Contracting Officer's Representative
FAR	Federal Acquisition Regulation
NAF	Nonappropriated Fund
RCO	Regional Contracting Office
T&M	Time-and-Materials



INSPECTOR GENERAL  
DEPARTMENT OF DEFENSE  
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ARLINGTON, VIRGINIA 22202

February 28, 1994

**MEMORANDUM FOR ASSISTANT SECRETARY OF DEFENSE FOR  
PERSONNEL AND READINESS  
AUDITOR GENERAL, DEPARTMENT OF THE ARMY**

**SUBJECT: Audit Report on Armed Forces Recreation Center-Europe  
(Report No. 94-047)**

We are providing this report for your review and comment. The report addresses DoD Hotline allegations about facility management and contracts at Armed Forces Recreation Center-Europe. Comments on a draft of this report were considered in preparing the final report.

DoD Directive 7650.3 requires that all audit recommendations be resolved promptly. As a result of management comments and discussions with Army officials, we added one recommendation addressed to the Army and revised recommendations addressed to the Army and to the Assistant Secretary of Defense for Personnel and Readiness. Therefore, all addressees must provide final comments on the unresolved recommendations and monetary benefits by April 29, 1994. See the chart at the end of each finding for the unresolved recommendations and the specific requirements for your comments.

We appreciate the courtesies extended to the audit staff. If you have any questions on this audit, please contact Mr. Joseph P. Doyle, Program Director, at (703) 692-3218 (DSN 222-3218) or Ms. Deborah L. Culp, Project Manager, at (703) 692-3343 (DSN 222-3343). The distribution of this report is listed in Appendix E. The audit team members are listed inside the back cover.

*David K. Steensma*

David K. Steensma  
Deputy Assistant Inspector General  
for Auditing



## Office of the Inspector General, DoD

Report No. 94-047  
(Project No. 2CK-0066.01)

February 28, 1994

### ARMED FORCES RECREATION CENTER-EUROPE

#### EXECUTIVE SUMMARY

**Introduction.** The audit was performed in response to DoD Hotline allegations concerning the facility management and contracts for the Armed Forces Recreation Center-Europe (AFRC). AFRC supports the U.S. European Command by providing recreation, hospitality, and other morale and welfare enhancing activities.

Army Regulation 215-1, update 16, "Administration of Army Morale, Welfare, and Recreation Activities and Nonappropriated Fund Instrumentalities," October 10, 1990, establishes a system to categorize activities according to their relationship to the Army mission and their ability to be financially self-sustaining. Self-sustaining businesses capable of funding most of their own expenses are Category C activities and should receive very limited direct appropriated fund support.

A review conducted by Pannell, Kerr, Forster in 1984 stated that AFRC was not self-sufficient or cost-effective. A financial statement report for FY 1992 disclosed that AFRC depends on appropriated fund support for its continued operations. The nonappropriated fund financial statements also reported that AFRC operated with a FY 1992 nonappropriated fund loss of about \$0.37 million after depreciation.

**Objectives.** The audit objectives were to review the allegations, the AFRC facility management, the use of contracts for AFRC, and the related internal controls.

**Audit Results.** The allegations were generally valid. See Appendix A for details of the allegations and the results of our review. See the findings in Part II for additional results of our review.

- o AFRC incorrectly used appropriated funds to maintain, clean, and improve the facilities during FYs 1991 and 1992 (Finding A).

- o AFRC and the contracting offices did not have adequate work management and contract controls. AFRC personnel ineffectively managed at least \$3.7 million of appropriated fund contracts and did not follow facility management and contract administration regulations. The Regional Contracting Office personnel awarded inefficient contracts and did not follow contract award and contract administration regulations (Finding B).

- o AFRC was not capable of being self-sustaining without being subsidized with appropriated fund support even though AFRC operated at near capacity. For FYs 1991 and 1992, AFRC reported a net operating loss of \$2.2 million, after \$29.7 million of appropriated and about \$5 million of nonappropriated funds subsidies. The U.S. Government will be required to continue to subsidize AFRC operations until a cost-effective alternative is provided or unless AFRC becomes financially self-sustaining (Finding C).

**Internal Controls.** The audit identified material internal control weaknesses. AFRC did not follow guidance to prevent inadequate contracting and work management controls. See Part I for internal controls reviewed and Part II for details on the weaknesses.

**Potential Benefits of Audit.** Monetary benefits can be realized by improving contracting procedures and either making the AFRC financially self-supporting or selecting a cost-effective alternative to continue AFRC operations. However, we could not quantify the amount. Potential monetary benefits of about \$1.6 million will result from the reimbursement of appropriated funds. Appendix C details the potential benefits resulting from the audit.

**Summary of Recommendations.** We recommended that the Assistant Secretary of Defense for Personnel and Readiness review all activities at AFRC and determine the proper classification for each activity and prohibit the use of appropriated funds for architectural and engineering services at AFRC. We recommended that the Army reimburse \$1.6 million of incorrectly used appropriated funds and establish procedures to use the U.S. Army Center for Public Works to properly classify work. We also recommended that Army implement internal controls for AFRC appropriated fund operations. The report further recommended that the Army determine whether AFRC is necessary, and perform a study to determine whether AFRC can exist as a self-sustaining business (without appropriated fund support). The study should determine whether recreational services can be provided more cost-effectively by the use of local accommodations and facilities and base morale, welfare, and recreation support.

**Management Comments.** The Assistant Secretary of Defense for Personnel and Readiness nonconcurred with classifying all AFRC activities as Category C but agreed the policy is unclear and recommended further clarification of AFRC activities. The Assistant Secretary disagreed with prohibiting appropriated funds for architectural and engineering service for nonappropriated fund construction projects, but stated there was a need to better define when the services were appropriate for an AFRC activity. The Assistant Secretary also agreed to review the economic analysis of AFRC.

The Army disagreed there was a need to reimburse \$1.6 million of nonappropriated funds to the proper appropriated funds account. The Army concurred in principle to review the other appropriated funds used during FYs 1991 and 1992 but did not agree to reimburse appropriated funds for any incorrectly used appropriated funds. The Army generally agreed to clarify the maintenance and repair regulations and to improve work management and appropriated fund internal controls. The Army concurred with conducting a study to determine whether AFRC is necessary and agreed to conduct a study that will consider the current demand for AFRC, the impact of changing the rate structure, and status of comparable local competition. A discussion of the responsiveness of management comments is in Part II of this report. The complete text of management comments is in Part IV.

**Audit Response.** We revised a recommendation to review all AFRC activities and determine the appropriate classification for each activity. We strongly disagree with the Army position that they will not reimburse appropriated funds for the incorrect use of appropriated funds. Also, the Army planned study does not determine whether AFRC can exist as a self-sustaining business and whether alternative recreational services can be provided more cost-effectively. Comments on this final report are requested from the Assistant Secretary of Defense for Personnel and Readiness and the Army by April 29, 1994.

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This report was prepared by the Contract Management Directorate, Office of the Assistant Inspector General for Auditing, DoD.



# **Part I - Introduction**

## Introduction

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## Background

The audit was performed in response to DoD Hotline allegations concerning the management, internal controls, and use of contracts for the Armed Forces Recreation Center-Europe (AFRC), Army Community and Family Support Center (CFSC).

AFRC supports the U.S. European Command by providing recreation, hospitality, and other morale and welfare enhancing activities and by providing meeting facilities. AFRC offers restaurants, hotels, golf, skiing, sailing, tennis, tours, and a variety of other recreational activities. AFRC was established after the conclusion of World War II to operate recreational facilities in Berchtesgaden, Chiemsee, and Garmisch. In April 1991, the operation of Berchtesgaden transferred to the U.S. Army, Europe.

AFRC operates under Army regulations and guidance. Facilities maintenance was provided by the Garmisch Community Directorate of Engineering and Housing until October 1990, when AFRC became responsible. The size of the AFRC engineering staff decreased as troop strength and appropriated fund support were reduced.

Appropriated fund contracting for AFRC is performed on a reimbursable basis by a Regional Contracting Office (RCO), U.S. Army Contracting Command, Europe. Nonappropriated fund (NAF) contracting is performed by AFRC. AFRC accomplished the majority of its repair and maintenance work using appropriated fund time-and-materials (T&M) contracts. Separate T&M contracts were awarded for plumbing, carpentry, painting, glazing, heating, masonry, metal, and electrical trades (appropriated fund T&M trade contracts).

## Objectives

The audit objectives were to review the allegations, the AFRC facility management, the use of contracts for AFRC, and the related internal controls. Appendix A details the allegations reviewed. Allegations concerning personnel issues were reviewed by CFSC. The findings in Part II discuss additional results of our review.

## Scope and Methodology

We reviewed 63 appropriated fund contracts for FYs 1991 and 1992, valued at about \$4.69 million,<sup>1</sup> at AFRC Garmisch and Chiemsee. The appropriated fund contracts reviewed included T&M trade, design, golf course upgrade, grounds maintenance, custodial services, minor construction, and maintenance and repair.

We discussed AFRC work classification and project management with personnel from the Assistant Secretary of Defense for Personnel and Readiness (formerly the Assistant Secretary of Defense [Force Management and Personnel]); Department of the Army, Center for Public Works (Public Works Center); CFSC; and AFRC. We limited our review of the use of appropriated funds to expenditures for repair and maintenance, minor construction, custodial services, and employee housing. We also reviewed the responsibilities of contracting officers and their representatives.

For the purposes of the audit and the audit results, we used existing guidance, which fails to place all AFRC activities into categories. Therefore, we considered activities such as AFRC administration as Category A for purposes of this audit.

We relied on computer-processed service and work order data for appropriated fund T&M trade contracts for FYs 1991 and 1992. The data were used to determine the description and dollar value of work performed. The computer-processed data were reliable for our purposes in obtaining descriptions of work and value of work performed.

This economy and efficiency audit was made from September 1992 to October 1993 in accordance with auditing standards issued by the Comptroller General of the United States as implemented by the Inspector General, DoD. We included such tests of internal controls as were considered necessary. Appendix D lists the organizations visited or contacted during the audit.

## Internal Controls

**Internal Controls Reviewed.** We reviewed internal controls related to work management and contracts for AFRC and RCOs and internal controls over the use of appropriated funds. We also evaluated the implementation of the Federal Managers' Financial Integrity Act at AFRC. The audit identified material internal control weaknesses as defined by Public Law 97-255, Office of Management and Budget Circular A-123, and DoD Directive 5010.38.

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<sup>1</sup>The official DoD exchange rates used throughout the report were 2.03 Deutsche Marks per dollar for FY 1991 and 1.80 Deutsche Marks per dollar for FY 1992.

## Introduction

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**Internal Control Weaknesses Identified.** AFRC did not implement an internal management control program as required by the Federal Managers' Financial Integrity Act. AFRC did not place a high enough priority on internal controls for appropriated fund contract administration, property management, and repair and maintenance. As a result, AFRC did not ensure the proper use of appropriated funds, supervision, separation of duties, and documentation of property management and contract administration. Recommendation 4.b. in Finding A and Recommendations 3.a., 3.b., 3.e., 3.f., 3.g., and 3.h. in Finding B, if implemented, will correct the internal control weaknesses. The other potential benefits that can be realized by implementing the recommendations are described in detail in Appendix C. Copies of the report will be provided to the senior official responsible for internal controls within the Department of the Army.

## Prior Audits and Other Reviews

The Inspector General, DoD, issued three audit reports concerning T&M contracts since 1990. The reports identified inappropriate award and administration of T&M contracts. The Inspector General, DoD, also issued a report that identified the failure to separate duties in contract administration. Two certified public accounting firms issued reports concerning AFRC operations and financial statements.

The Army Audit Agency issued one report concerning ineffective NAF contracting policies and procedures at AFRC. Another Army Audit Agency report identified the improper use of appropriated funds for morale, recreation, and welfare activities at Army installations in the United States. Additional details on the reports are shown in Finding C and Appendix B.

## Other Matters of Interest

U.S. Army Contracting Command, Europe, plans to award one contract for maintenance operations at AFRC. The contract is not expected to be awarded until about June 1994. The majority of the appropriated fund T&M trade contracts expire in early FY 1994. For the interim, RCO Fuerth justified and approved the extension of the Garmisch appropriated fund T&M trade contracts for an additional 6 months. AFRC Chiemsee will operate with new purchase orders on a case-by-case basis.

As a result of the audit, AFRC determined that the Office of Defense Costs of the German government did not reimburse the U.S. Government for housing charges collected from NAF local national employees, AFRC collected about \$90,000 in housing charges that were not reimbursed. AFRC personnel stated the amount will be forwarded to the proper U.S. Government account.

## **Part II - Findings and Recommendations**

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## Finding A. Use of Appropriated Funds

AFRC incorrectly used appropriated funds to maintain, clean, and improve the Garmisch and Chiemsee facilities. This condition occurred because of an insufficient priority on controls for appropriated fund contracts, unfamiliarity with regulations, and unclear guidance. As a result, AFRC should have used NAF for about \$1.6 million of the \$3.1 million of appropriated funds reviewed.

### Background

Morale, welfare, and recreation activities operate using appropriated funds and NAF. Appropriated funds, funds from the U.S. Treasury or "taxpayers' money," are received based on the morale, welfare, and recreation activity's ability to generate revenue. NAF are generated primarily through the sale of goods and services on military installations.

Army Regulation (AR) 215-1, update 16, "Administration of Army Morale, Welfare, and Recreation Activities and Nonappropriated Fund Instrumentalities," October 10, 1990, establishes a standard system for authorization of appropriated fund support. The categorization is based principally on the activity's relationship to readiness factors.

Table 1 shows the classification system that categorizes activities according to their relationship to the Army mission and the activity's ability to be self-sustaining.

<u>Category</u>	<u>Activity Description</u>	<u>Examples</u>
A	Mission Essential	Gymnasiums and Libraries
B	Community Support	Child Development Centers
C*	Self-sustaining Business	Golf Courses and Guest Houses

\*Category D has not been officially revised to Category C in AR 215-1.

Category A activities have virtually no capacity to generate NAF revenue and are supported almost entirely with appropriated funds. Category B activities receive a substantial amount of appropriated fund support but do have the ability to generate a limited amount of revenue. Category C activities are considered business activities and receive very limited direct appropriated fund support because they have the greatest capability to generate revenue.

## Finding A. Use of Appropriated Funds

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The primary characteristic of Category C activities is that they compare to self-sustaining businesses capable of funding most expenses. Category C activities have the potential to provide NAF revenues, have less of an impact on readiness, receive minimal appropriated fund support, and must be sustained almost entirely by NAF.

### Questioned Use of Appropriated Funds

AFRC incorrectly used about \$1.6 million of appropriated funds during FYs 1991 and 1992. Details on the amounts of questionable use of appropriated funds were provided to the AFRC General Manager in a list in December 1993. The questioned uses of appropriated funds were identified on about 2,400 orders from 26 T&M appropriated fund trade contracts and invoices from 3 custodial and 3 other appropriated fund contracts. Because of the length of the list, the details are not included in this report and can be provided upon request.

Table 2 shows the appropriated funds reviewed in detail during the audit and found to be questionable.

**Table 2. Amount of Appropriated Funds Reviewed and Questioned**

	<u>Reviewed</u>	<u>Questioned</u>
T&M trade contracts	\$2,492,194	\$1,382,345 <sup>1</sup>
Custodial contracts	401,187	188,093 <sup>2</sup>
Other contracts	<u>207,911</u>	<u>32,520</u>
Total	<u>\$3,101,292</u>	<u>\$1,602,958</u>

<sup>1</sup>Includes \$173,124 for employee housing.

<sup>2</sup>Includes \$47,126 for employee housing.

The \$3.1 million of appropriated fund contracts reviewed in detail contained three types of expenses: maintenance and repair, minor construction, and custodial services. The audit did not review the remaining \$26.6 million of appropriated fund support for AFRC.

## **Finding A. Use of Appropriated Funds**

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### **Management Priority on Internal Controls**

AFRC management stated that internal controls on appropriated fund T&M contracts were not always implemented because management did not place a high enough priority on the internal controls. The mandate to operate profitably meant that AFRC personnel had to respond quickly to customer needs because lost sales affected profits.

AFRC did not have an effective internal management control program for appropriated fund contract administration, property management, and repair and maintenance. See Finding B for additional details on internal controls weaknesses at AFRC.

The desire to operate profitably contributed to the incorrect use of appropriated fund contracts. According to the AFRC Director of Engineering and staff, AFRC did not have any NAF repair and maintenance contracts until November 1991. Because no other contracts existed, the appropriated fund contracts were used to accomplish NAF work; however, NAF did not reimburse appropriated funds for the facility repairs.

The NAF contracts in FYs 1992 and 1993 were also unable to meet the AFRC facility requirements. The FY 1992 NAF contracts were only valued at about \$300,000; however, the FY 1992 appropriated fund T&M trade contracts were valued at about \$1,250,000. In addition, AFRC did not award NAF contracts to four trades (glazing, heating, painting, and plumbing) for FY 1992. In FY 1993, AFRC Garmisch operated without any NAF trade contracts for repair and maintenance work. We believe that without NAF trade contracts, a higher probability exists for appropriated funds to be misused.

### **Categorization of Activities**

AFRC was able to receive substantial appropriated fund support (\$29.7 million) for FYs 1991 and 1992 because at the time of our audit AR 215-1 did not specifically list all AFRC activities as Category C. AFRC classified activities as Category A, B, or C because AFRC believed each activity at a recreation center could be classified separately. Furthermore, AFRC management believed each department of each activity could be classified separately. AR 215-1 stated "Armed Forces Recreation Centers (accommodations/dining and resale facilities)" were Category C activities. However, the regulation did not state whether all activities at AFRC were Category C or just "accommodations/dining and resale facilities."

We believe the intent of AR 215-1 was not to separate each activity by department to determine the categorization. We further believe that the resort activities at AFRC supported one recreation center, not a collection of separate activities and departments. The two other AFRCs located in Hawaii and Korea do not have as many recreation activities but are considered as one Category C entity. The following examples show how AFRC separately classified activities and departments.

## Finding A. Use of Appropriated Funds

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**Categorization of Ski Lodge Rooms.** AFRC personnel classified the separate rooms of the ski lodge, which resulted in the various rooms receiving A, B, and C categorizations. For example, AFRC believed the ski office located in the ski lodge was administration (Category A) and not related or classified the same as the other ski activities located in the same facility.

**Categorization of Outdoor Recreation Activities.** AFRC personnel did not properly classify individual outdoor recreation activities, which resulted in unauthorized appropriated fund support for work projects. The personnel incorrectly classified ski slopes, ski lifts, ski rental activities, and travel camps as Outdoor Recreation, or Category B, activities.

The activity "Outdoor Recreation" was defined in Section IV of AR 215-1 as Category B. However, individual outdoor recreation activities were further defined in AR 215-1 and AR 215-2, "The Management and Operation of Army Morale, Welfare and Recreation Activities and Nonappropriated Fund Instrumentalities," October 10, 1990. Appendix E in both AR 215-1 and AR 215-2 classifies individual outdoor recreation activities as A, B, and C categories. Therefore, the appendixes contradict the single Category B classification listed in Section IV of AR 215-1.

AFRC engineering personnel were unaware of and did not use Appendix E of the AR 215-2. The AR 215-2 classification includes the following outdoor recreation activities as Category C:

- o ski slopes, ski lifts, and ski resale and rental activities;
- o campgrounds/travel camps for overnight lodging and large recreational vehicles; and
- o equipment rental activities.

AFRC management stated that none of the departments associated with the ski program, travel camp, or equipment rental were Category C. However, the ski program included a ski slope, ski lifts, ski resale space, and ski equipment rental. The AFRC travel camp had overnight lodging, recreational vehicles, a retail store, equipment rental, and a bathhouse. In addition, the NAF revenue generated from the ski program, the travel camps, and equipment rental was about \$3.7 million for FYs 1991 and 1992. Based upon the AR 215-1 and AR 215-2 guidance and the amount of NAF revenue generated, we believe the outdoor recreation activities were clearly Category C in their entirety.

**Categorization of Employee Housing.** AFRC personnel classified housing provided to AFRC employees as a Category A activity because AR 215-1 failed to provide guidance for classifying housing. The classification as Category A resulted in appropriated fund support paying for unreimbursed housing costs for all employees. DoD officials have not determined whether appropriated funds were authorized for the unreimbursed employee housing costs. We believe that NAF should pay for the unreimbursed employee housing costs because about 90 percent of the housed employees were NAF employees.

## Finding A. Use of Appropriated Funds

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### Clarity of Regulations

Army regulations for work classifications were unclear. In AR 215-1, update 16, the definition for recurrent, day-to-day maintenance was deleted. Update 16 authorizes Category C activities appropriated fund support for routine ground maintenance, and maintenance and repair work to:

Prevent or correct all life safety deficiencies.

Ensure the structural and operational integrity of the building components (such as roofing, foundations, ceilings, floors, walls, windows, doors etc.), and installed building equipment and systems (such as plumbing, heating, ventilating, cooling, air conditioning, electrical, fire protection and, security, etc.).

Preserve the exterior of a facility.

The regulation does not authorize appropriated funds for all other work to maintain or repair building components of Category C activities.

**Regulation Intentions.** An August 10, 1987, Assistant Secretary of Defense (Force Management and Personnel) report advised Congress that recurrent, day-to-day, periodic, or scheduled work were NAF costs at Category C activities. The Public Works Center, the final authority of Army work classification, applied the Assistant Secretary of Defense (Force Management and Personnel) report in writing the maintenance and repair section for AR 215-1. Personnel from the Public Works Center stated routine repair and maintenance was intended to be NAF costs for Category C activities. Also, personnel from the Public Works Center stated that life safety deficiencies were intended to be severe and probable life threatening hazards.

Army Audit Agency Report No. WR 93-805, "Appropriated Versus Nonappropriated Fund Support," July 8, 1993, stated that recurring and routine maintenance on Category C facilities should be paid for with NAF. The Assistant Secretary of the Army (Manpower and Reserve Affairs) agreed to reimburse appropriated funds for facility maintenance and equipment repair needed to support Category C operations. The Army Deputy Chief of Staff for Personnel also directed CFSC to inform the major commands of the recommended actions.

**Contrasting Interpretations.** Officials in the chain of command responded differently to funding authorization questions. For example, interior painting was classified as an appropriated fund cost by some officials of CFSC and AFRC because they believed interior painting related to the structural and operational integrity of a building. However, other officials of CFSC said interior painting was a NAF cost. Officials in the Office of the Assistant Secretary of Defense for Personnel and Readiness said interior painting was intended to be a NAF cost but was probably being interpreted differently by each installation.

The AFRC Director of Engineering believed that the word "routine" in AR 215-1 applied to both grounds maintenance and repair and maintenance. However, we believe "routine" only applies to grounds maintenance. The

examples (life safety, structural integrity, preserve exterior, etc.) refer to repair and maintenance only. Although the regulations need to be more clearly written, AFRC engineering personnel could have obtained additional clarification from the Public Works Center.

## Time-and-Material Trade Contracts

AFRC personnel incorrectly used about \$1.38 million (56 percent) of appropriated funds of the \$2.49 million expended on the appropriated fund T&M trade contracts. AFRC engineering personnel agreed during the audit that about \$312,000 of the T&M contract work should have used NAF. AFRC spent unauthorized appropriated funds for a variety of T&M trade contracts, such as:

- o NAF repair and maintenance projects,
- o NAF minor construction projects, and
- o unreimbursed employee housing costs.

Figure 1 shows the appropriated fund expenditures reviewed on the appropriated fund T&M trade contracts for FYs 1991 and 1992. The expenditures reviewed were classified by questioned use of funds, employee housing costs not fully reimbursed, and use of funds not questioned.

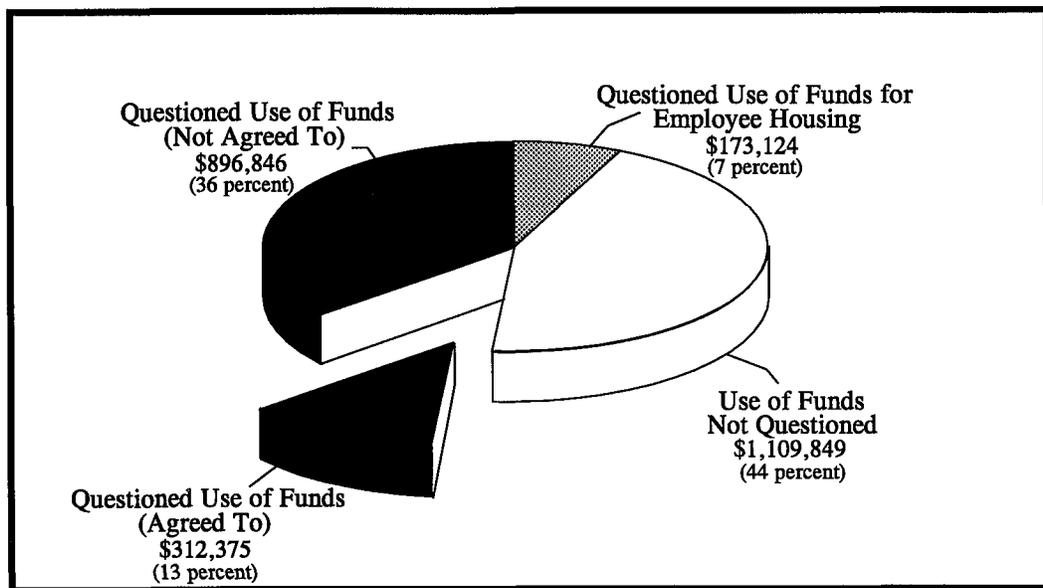


Figure 1. Appropriated Funds Used on T&M Contracts for FYs 1991 and 1992

## **Finding A. Use of Appropriated Funds**

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**Questioned Use of Funds Agreed to by Engineering Personnel.** AFRC engineering personnel agreed during the audit that about \$312,000 of appropriated funds to support maintenance and repair and minor construction projects should have been funded with NAF, but the appropriated funds were not reimbursed. The Director of Engineering at AFRC provided a written statement to us in September 1993 that separated the agreed-upon incorrectly funded NAF work into two categories: NAF work that "should have been clearly apparent at the time of execution" and NAF work that became apparent during the audit based upon the Director of Engineering's present awareness of guidance and regulations. However, CFSC management has since contradicted the statement made by the Director of Engineering at AFRC. CFSC states that AFRC does not agree with any of questioned work except for work that should have been clearly NAF at the time of execution.

Work was misclassified because of the lack of familiarity with AR 215-1, update 16. Some work was misclassified by the engineering staff members who did not have adequate training in how to classify expenditures as appropriated funds or NAF. For example, the staff ordered work for fish tanks and beer line connections from the appropriated fund plumbing contractor when clearly the work should have been NAF. Even though AFRC personnel agreed the appropriated fund expenditures were misclassified, AFRC personnel did not use NAF to reimburse appropriated funds.

Further examples of NAF projects funded with appropriated fund support included:

- o repairs to hotel furniture (desks, televisions, curtain rods, mirrors);
- o repairs to appliances (hair dryers, vacuums, steam cleaner);
- o repairs to kitchen equipment (fryer, waffle-iron, meat slicer);
- o disconnection of Christmas lights;
- o construction of ski lift platforms;
- o relocation of a hotel linen room; and
- o installation of campground barbecue grills.

**Public Works Center Guidance.** In consultation with the Army Public Works Center at Fort Belvoir, Virginia, we determined that AFRC personnel misclassified about \$897,000 of NAF work as appropriated fund work. The use of appropriated funds occurred partly because AFRC personnel did not refer questions on work classification through CFSC to the Public Works Center as required by AR 420-10, "Management of Installation Directorates of Engineering and Housing," July 2, 1987.

**Maintenance and Repair.** AFRC personnel incorrectly used about \$761,000 of appropriated funds for NAF maintenance and repair work because the proper Public Works Center guidance was not applied. The interpretations used by AFRC were almost opposite to the Public Works Center interpretations. AFRC personnel believed that appropriated fund support was authorized if the item was connected to the building, its systems (such as plumbing, heating, etc.), or a potential danger.

## Finding A. Use of Appropriated Funds

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According to the AFRC Director of Engineering and his staff, AFRC had always used appropriated funds for routine maintenance and repair work for facilities. Furthermore, AFRC personnel believed that using appropriated funds for all repair and maintenance work concerning health or safety was authorized. For example, fly screen repairs and store room wall painting were considered appropriated fund costs for health reasons.

The Public Works Center personnel disagreed with AFRC's interpretation and stated that life safety criteria included threats with a high hazard severity and probability. AR 385-10, "The Army Safety Program," May 23, 1988, provides guidance on hazard severity and accident probability. The routine maintenance and repairs that AFRC personnel incorrectly classified and that should have been funded with NAF included:

- o building repairs (interior doors, light fixtures, and headboards);
- o system repairs (leaking faucets, toilet seats, electrical outlets); and
- o potential danger (door locks, loose carpeting, street light repairs).

**Minor Construction.** AFRC personnel also used about \$136,000 of appropriated funds for NAF minor construction projects. Generally, construction projects for Category B or C activities were NAF costs. However, if the project was to correct a life safety deficiency, appropriated funds were authorized. AFRC personnel interpreted the phrase "to correct life safety deficiencies" from AR 215-1 as "to correct all safety deficiencies." Examples of minor construction projects incorrectly classified to correct life safety deficiencies were:

- o rooms built at the ski lodge,
- o rails installed at hotel entrance,
- o "no dogs allowed" signs installed, and
- o speed bumps constructed at the hotel.

## Custodial Contracts

AFRC personnel incorrectly used about \$188,000 (47 percent) of appropriated funds of the \$401,000 expended on the appropriated fund custodial contracts. AR 215-1 states that custodial service for Category C activities is a NAF expense.

AFRC personnel used about \$141,000 of appropriated funds for custodial contracts to clean the campground, ski lodge, and golf course buildings when only NAF was authorized. AFRC personnel failed to categorize the campgrounds and ski activities as Category C as defined in AR 215-2. Additionally, AFRC used unauthorized appropriated funds for custodial services for the golf course buildings even though golf courses are defined as Category C under AR 215-1.

## Finding A. Use of Appropriated Funds

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Additionally, about \$47,000 of appropriated funds spent on cleaning employee housing was not recovered from the employees and reimbursed to appropriated funds. Figure 2 shows the unauthorized appropriated fund expenditures, employee housing costs not fully reimbursed, and appropriated fund costs not questioned.

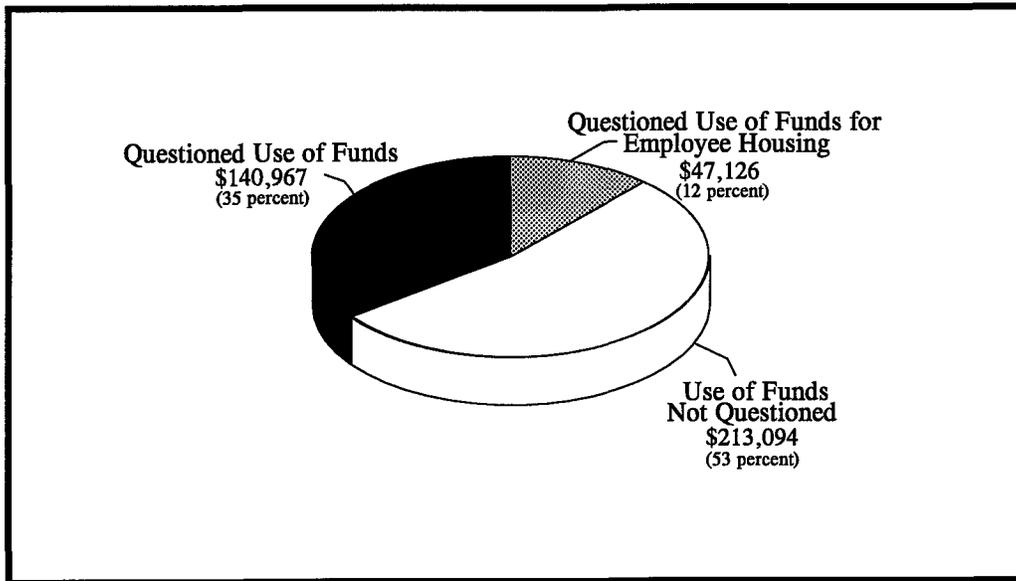


Figure 2. Appropriated Fund Custodial Contracts Costs for FYs 1991 and 1992

## Employee Housing

At least \$220,000 of appropriated funds used for NAF employee housing maintenance and repair, minor construction, and custodial costs were not reimbursed to appropriated funds. The formulas that determine both the local national and U.S. civilian employee maintenance and utility charges did not cover the pro-rata share of the facilities expenses.

**Reimbursement Regulations.** U.S. Army, Europe, regulations require that housed employees be charged for rent, maintenance, and utilities. AFRC provides housing for the employees at AFRC facilities and charges the employees for rent, maintenance, and utilities. Updated annually, the charges are based on the cost to house the employees. Rent collected from the employees reverts to the German authorities; however, the maintenance and utility charges revert to the U.S. Government.

The amount collected from the AFRC employees did not cover the costs to house the employees. We compared the employee housing amounts collected for maintenance charges with the amounts expended for maintaining employee housing facilities. We estimated about \$173,000 of the amounts not recovered were from appropriated fund T&M trade contracts and about \$47,000 were

## Finding A. Use of Appropriated Funds

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from an appropriated fund custodial contract. Because at least 90 percent of the AFRC employees housed were NAF during FYs 1991 and 1992, we believe that NAF should pay for the amounts not recovered during that period.

The analyses included only the appropriated fund T&M trade and custodial contracts. However, we believe that additional but unknown amounts of unreimbursed employee housing costs related to utility, minor construction, administration, and other repair and maintenance work were not recovered.

### Other Contracts

AFRC incorrectly used about \$33,000 of appropriated funds on three contracts for minor construction projects because regulations were not followed and work was improperly classified. AFRC personnel agreed that AR 215-1 was not properly followed when about \$23,000 of appropriated funds was incorrectly used for new dining room doors and festival tent rentals. Also, the installation of ski lift video monitors, valued at about \$10,000, was classified as a life safety project. However, the Public Works Center stated the ski lift video monitors should be classified as NAF equipment.

### Conclusion

AFRC used about \$1.6 million of appropriated funds incorrectly for three types of expenses: maintenance and repairs, minor construction, and custodial service. The audit results were based on existing guidance that did not specifically categorize all AFRC activities. The only categorizations questioned were the ski slopes, ski lifts, ski rental activities, campgrounds/travel camps, and equipment rental activities.

If the other \$26.6 million of appropriated fund expenses were reviewed at AFRC, there may be additional amounts of appropriated fund support that may be questioned. If all of the AFRC activities were categorized as a single entity as Category C, then AFRC operations would be funded with limited appropriated fund support as we believe Congress intended for NAF instrumentalities. AFRC was able to use substantial amounts of appropriated funds because AR 215-1 did not classify AFRC activities as a single Category C entity.

## Finding A. Use of Appropriated Funds

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### Recommendations, Management Comments, and Audit Response

**Revised Recommendation.** Based on management comments, we revised Recommendation 1. to review all activities and departments at AFRC and to determine the appropriate classification.

1. We recommend that the Assistant Secretary of Defense for Personnel and Readiness review all of the activities and departments at the Armed Forces Recreation Center-Europe and determine the appropriate classification for each activity and department, including employee housing. Any Armed Forces Recreation Center-Europe activity or department to be considered for Category A or B should be presented to the House Armed Services Committee, Morale, Welfare and Recreation Panel, for review.

**Management Comments.** The Assistant Secretary of Defense for Personnel and Readiness nonconcurred with the draft report recommendation to treat AFRC as one entity and to classify all the activities and departments for AFRC as Category C. The Assistant Secretary agreed that existing policy is unclear and recommended further clarification of the policy for classifying the activities and departments in the AFRC. The Assistant Secretary stated that, to assure the proper use of appropriated and nonappropriated resources, funding authority is based on the service or activity provided, and not the provider.

**Audit Response.** We revised the recommendation in response to the comments from the Assistant Secretary. We request the Assistant Secretary to respond to the revised recommendation to review all activities and departments at AFRC and to determine the appropriate classification. We further request a completion date for the review.

2. We recommend that the Assistant Secretary of the Army (Financial Management) determine whether unauthorized appropriated funds were spent for Armed Forces Recreation Center Garmisch and Chiemsee facilities. The determination should include the estimated \$26.6 million of appropriated fund expenses not reviewed by our audit for FYs 1991 through 1993. The unauthorized amount should be identified and reimbursed to the proper Army appropriations.

**Management Comments.** The Army concurred in principle and stated that it will review the elements of expense that comprise the \$26.6 million and will review ARs 215-1 and 215-2. The Army acknowledged that a small amount of appropriated funds were used improperly; however, the Army stated that no mechanism exists to restore those funds to the proper Army appropriations. Further, to reimburse the U.S. Government by depositing nonappropriated funds in the general fund (miscellaneous receipts) penalizes soldiers and their families by taking away nonappropriated funds earmarked for morale, welfare, and recreation programs. The Army planned to complete the review by September 1994.

## Finding A. Use of Appropriated Funds

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**Audit Response.** The Army's planned actions are not considered responsive to the recommendation. The purpose of the review is to identify improper expenditures of funds and to reimburse the correct appropriations. The argument that reimbursing the U.S. Government for the improper use of appropriated funds penalizes soldiers by taking away nonappropriated funds earmarked for morale, welfare, and recreation programs is a distortion of facts. The reimbursement is for the Government to be repaid for the past incorrect uses of appropriated funds by AFRC. We request the Army to reconsider its position and to provide comments on the recommendation as part of its comments on the final report.

3. We recommend that the Commander, U.S. Army Community and Family Support Center:

a. Repay \$1,602,958 of nonappropriated funds identified in this report to the Operations and Maintenance, Army, appropriation. The amounts that should be repaid are \$746,015 for FY 1991 and \$856,943 for FY 1992.

**Management Comments.** The Army nonconcurred and stated that the Army will not direct any reimbursement to appropriated funds from NAF. The Army stated that the \$1.6 million in question had undergone a detailed review jointly by AFRC and the auditors during the audit. The AFRC agreed that only \$15,559 was incorrectly used. The disagreement in the amounts is due to differences in the interpretation of Army policy by the auditors and CFSC. The Assistant Secretary of the Army (Financial Management) will conduct an independent review of the disputed use of appropriated funds, and appropriate action shall be initiated against individuals responsible for the improper expenditures. The Army planned to complete the review by September 30, 1994.

**Audit Response.** We strongly disagree with the Army's position that the Army will not direct any reimbursement to appropriated funds from NAF. The Army has agreed that at least \$15,559 of appropriated funds were incorrectly used. We still believe that the \$1.6 million of appropriated funds identified in the report was improperly used and that CFSC should reimburse the proper appropriations from NAF. The planned review by the Assistant Secretary of the Army (Financial Management) will attempt to fix responsibility for the improper expenditures but will have no impact on the recovery of improperly used appropriated funds. The primary purpose of the recommendation is to recover the appropriated funds improperly used by AFRC.

The Army refusal to reimburse the appropriated funds for any improperly used funds is not consistent with the Army response to the Army Audit Report No. WR 93-805. The report recommended that the NAF reimburse appropriated funds for improperly funded equipment repair and repair and maintenance. Both the Assistant Secretary of the Army (Manpower and Reserve Affairs) and CFSC concurred with the recommendation in the report and we see no difference in either the recommendation or the circumstances. We request the Army to reconsider its position and to provide comments on the recommendation as part of its comments on the final report.

## Finding A. Use of Appropriated Funds

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b. Request the U.S. Army Center for Public Works to rewrite the maintenance and repairs element of expense in Appendix C of Army Regulation 215-1, update 16, "The Administration of Army Morale, Welfare and Recreation Activities and Nonappropriated Fund Instrumentalities." The terms life safety, structural and operational integrity, and installed building equipment should be specifically defined.

**Management Comments.** The Army concurred with the recommendation and stated that the required changes will be incorporated into the next update of the regulation. The Army provided a target date of the fourth quarter of FY 1994 for completing the action.

4. We recommend that the General Manager, Armed Forces Recreation Center-Europe:

a. Discontinue the use of appropriated funds for recurrent, day-to-day, periodic, and scheduled maintenance and repair work for Category C activities.

**Management Comments.** The Army concurred and stated that expenditures of appropriated funds for recurrent, day-to-day, periodic, and scheduled maintenance and repair will be in accordance with the guidance published in AR 215-1 and the categorization of the activity being serviced. The Army stated that the action has been completed.

**Audit Response.** We do not consider the Army comments responsive because the Army comments do not specifically state that AFRC will discontinue the use of appropriated funds for recurrent, day-to-day, periodic, and scheduled maintenance and repair work for Category C activities. The recommendation was clearly to discontinue the use of appropriated funds for recurrent, day-to-day, periodic, and scheduled maintenance and repair work for Category C activities. We made this recommendation because we believe that AFRC will continue to incorrectly interpret AR 215-1, which will result in the continued incorrect use of appropriated funds.

If AFRC continues to use appropriated funds for recurrent, day-to-day, periodic, or scheduled maintenance and repair work, those actions will be in direct conflict with existing DoD and Army guidance. AFRC believed it was complying with the AR 215-1 when it improperly used about \$1 million of appropriated funds for recurrent, day-to-day, periodic, and scheduled maintenance and repair work for Category C activities. An Assistant Secretary of Defense (Force Management and Personnel) report in 1987 advised Congress that recurrent, day-to-day, periodic, or scheduled work were NAF costs at Category C activities. Personnel from the Public Works Center, the final authority of Army work classification, stated routine repair and maintenance are to be NAF costs for Category C activities. The Army also concurred in Army Audit Agency Report No. WR 93-805, which stated that recurring and routine maintenance on Category C facilities should be paid for with NAF. We request the Army to reconsider its position and to provide comments on the recommendation as part of its comments on the final report.

## Finding A. Use of Appropriated Funds

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b. Establish procedures and controls requiring the Armed Forces Recreation Center-Europe Engineering Department to ask the U.S. Army Center for Public Works for work classification determinations.

**Management Comments.** The Army concurred in principle and stated that guidance published in AR 420-10 for work classification will be followed. The Army stated that it is CFSC and AFRC policy to consult the Assistant Chief of Staff for Installation Management if classification of work is in doubt.

**Audit Response.** The Army comments were not fully responsive. The CFSC and AFRC track record on this issue is clearly laid out in the report. CFSC and AFRC either never doubted the correctness of their work classifications or failed to comply with their own policy. The recommendation is clear. The General Manager at AFRC should establish procedures and controls that require AFRC's engineering department to ask the Public Works Center for work classification determinations. We request the Army to reconsider its position and to provide comments on the recommendation as part of its comments on the final report.

### Response Requirements Per Recommendation

Responses to the final report are required from the addressees shown for the items indicated with an "X" in the chart below.

Number	Addressee	Response Should Cover:			
		Concur/ Nonconcur	Proposed Action	Completion Date	Related Issues <sup>1</sup>
1.	ASD (P&R) <sup>2</sup>	X	X	X	
2.	Army	X	X	X	
3.a.	Army	X	X	X	M
4.	Army	X	X	X	IC

<sup>1</sup>M = monetary benefits; IC = material internal control weakness.

<sup>2</sup>Assistant Secretary of Defense for Personnel and Readiness.

## Finding A. Use of Appropriated Funds

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### Management Comments and Audit Response on the Finding

The Army stated that the need for revising Army policy should have been the major thrust of this finding. Instead, the Inspector General, DoD, placed greater emphasis on the incorrect use of \$1.6 million of appropriated funds. The Army comments on specific items in the finding are as follows:

- o It is neither an Army policy nor management priority to place profitability above regulatory requirements.

- o The Army believes that the report statement about the other \$26.6 million in appropriated funds support is misleading in that it implies a direct relationship between the \$26.6 million and the \$3.1 million of appropriated funds contracts reviewed.

- o The statement on custodial contracts in the report does not recognize Army policy on outdoor recreation. Appendix E to AR 215-2 established AFRC as a Category B activity.

**Audit Response.** The \$1.6 million of appropriated funds that were incorrectly used was based on a thorough examination of funds used and a reasonable interpretation of existing guidance. The unclear guidance and the need to revise Army policy is one of the root causes discussed in the finding. We agree that misuse of appropriated funds was partly the result of unclear guidance and misinterpretation of Army regulations. However, other factors contributing to the misuse of funds included the lack of internal controls over appropriated funds and AFRC personnel unfamiliarity with the regulations, and their desire to operate profitably.

The audit results do not support the Army position that it is not a management priority to place profitability above regulatory requirements. During the audit, AFRC management repeatedly stated that it could not afford the expensive work management programs and internal controls required by Army or DoD regulations. Finding B discusses the lack of work management and internal controls in detail.

We did not state that the \$3.1 million of appropriated funds contracts reviewed is related to the other \$26.6 million of appropriated funds not reviewed. The report states only that a review of the \$26.6 million of appropriated funds may identify additional questionable amounts. We continue to disagree with the classification of the campground/travel camp as a Category B activity. AR 215-1 states that campgrounds/travel camps for overnight lodging and large recreational vehicles and equipment rental activities are Category C activities. This issue clearly demonstrates the internal disparity between Army regulations.

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## **Finding B. Work Management and Contract Internal Controls**

AFRC and the contracting offices did not have adequate work management and contract internal controls. Inadequate controls were caused by AFRC management belief that supervision, separation of duties, and documentation for work management and contracts were not high priority. As a result, AFRC personnel improperly managed at least \$3.7 million of appropriated fund contracts and did not follow facility management and contract administration regulations. In addition, the Regional Contracting Office (RCO) personnel awarded inefficient contracts and did not follow contract award and contract administration regulations.

### **Background**

Appropriated fund contracting support for AFRC transferred to RCO Fuerth in June 1992 when RCO Augsburg closed. However, RCO Augsburg operations had effectively slowed in October 1991. RCO Augsburg awarded appropriated fund T&M trade contracts for AFRC in FYs 1991 and 1992 valued at about \$2.5 million.

T&M contracts may be used only when no other type of contract is suitable. Federal Acquisition Regulation (FAR) 16.601, "Time-and-materials Contracts," states "a time-and-materials contract provides no positive profit incentive to the contractor for cost control or labor efficiency. Therefore, appropriate Government surveillance of contractor performance is required to give reasonable assurance that efficient methods and effective cost controls are being used."

Internal controls are integral parts of an overall management system for organizations. Internal controls should provide reasonable assurance that resources are adequately safeguarded and protected against fraud, waste, and mismanagement. DoD Directive 5010.38, "Internal Management Control Program," identifies standards that should be included in internal control programs.

### **Work Management Controls**

Appropriated fund contracts were inappropriately used on projects that could have been more efficiently accomplished. The AFRC Engineering Department did not have an adequate system to determine what work was needed, when it

## **Finding B. Work Management and Contract Internal Controls**

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would be done, or how much it would cost. AFRC management stated it cannot afford the expensive work management programs required by Army or DoD regulations.

**Facility Planning.** The AFRC Engineering Department failed to prepare annual and long-term plans to coordinate maintenance and repair projects with planned construction projects as required by AR 210-20, "Master Planning for Army Installations," June 12, 1987, and AR 420-17, "Real Property and Resource Management," December 13, 1976. Technical Note 420-10, "Management of Installations-Directorate of Engineering and Housing Resources Management Systems Handbook," November 1, 1991, recommends management have:

- o a master plan,
- o an unconstrained requirements report,
- o an annual work plan, and
- o a resource management plan.

First, the master plan shows the composition and development of the installation for 20 years. Next, an unconstrained requirements report lists the requirements needed to operate and maintain the real property investment without resource constraints. Third, the annual work plan coordinates construction projects with maintenance and repair projects for the current year. Finally, the resource management plan coordinates the above plans.

The only engineering planning documents prepared by the AFRC Engineering Department in FYs 1991 and 1992 were the capital projects major construction list and the project status report. The capital projects major construction list prioritized projects and their costs. The project status report listed whether the project was appropriated funded or NAF and the status of the project. Neither document showed the relationship, sequence, and coordination of projects. The AFRC General Manager stated that AFRC was not a typical Army installation; therefore, the Army's facility planning regulations did not apply to AFRC. The General Manager also stated the suspension of the new hotel complex in 1990 contributed to the planning problems in Garmisch. The following examples show the results of inadequate planning by AFRC.

**Golf Course Clubhouse.** AFRC Garmisch spent about \$529,000, including about \$35,000 in design costs, to rebuild and upgrade a substandard golf course clubhouse originally built in 1930. However, the \$500,000 NAF construction and maintenance and repair limitation, which required CFSC approval, was avoided because AFRC used appropriated funds for repairs and NAF for the utility upgrades. AFRC records did not document that the extensive repairs were within Army guidance.

**Planned Construction.** Initially, AFRC planned to build with NAF a new clubhouse consisting of about 75 percent more interior space. The basic structure and site work was estimated at about \$499,000. The plans

## Finding B. Work Management and Contract Internal Controls

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changed after German authorities required new sewer lines that increased the estimated construction costs to about \$570,000. AFRC's request to exceed the NAF limitation was disapproved by CFSC. As a result, AFRC had to incur an additional design costs of about \$35,000 to repair the existing, smaller clubhouse.

**Extensive Repairs.** Appropriated funds paid about \$392,000 to design and repair the existing clubhouse and NAF paid about \$137,000 to upgrade utilities. Basically, the clubhouse repair project replaced everything. The repair removed the roof and gutted the building; only the walls were left standing. AFRC management also required a roof upgrade from asphalt to tile to match other facilities. This unplanned roof upgrade restricted funds available for planned facilities for the disabled. Other clubhouse appropriated fund repairs included:

- o new electrical, plumbing, sewage, heating, telephone and security systems; and
- o new fixtures, doors, windows, carpeting, ceilings, and plaster.

**Army Approval.** AFRC did not document a decision analysis before AFRC started the extensive repairs to the golf course clubhouse. AR 420-10 requires a decision analysis and Department of the Army approval when the repair cost exceeds 50 percent of the construction of a new facility of the same size. However, AFRC did not provide a decision analysis that documented the condition of the property, an economic evaluation of alternatives, or the determination to either repair or replace the facility. Therefore, we could not determine whether AFRC circumvented the 50-percent rule when the golf course clubhouse was repaired with appropriated funds.

**Kitchen Project.** A \$358,423 contract to repair a kitchen ceiling and ventilation system was inadequately planned and awarded to obligate appropriated funds before the funds expired. The repair to the kitchen ceiling and ventilation system was contingent upon the completion of other kitchen work. The contract was awarded 1 week before the end of FY 1992. The contract should not have been awarded in FY 1992 because AFRC knew the relocation of the existing kitchen to a temporary kitchen was not possible for 5 months.

AFRC personnel believed the use of the FY 1992 appropriation could be questioned and lost if work was not started before January 1993. The contractor started in December 1992 but stopped within a week because ceiling work interfered with the kitchen operation and the temporary kitchen was unavailable. A claim by the contractor is anticipated for the Government delay because the contractor's workers and equipment were idle.

**Architectural Services.** The AFRC Engineering Department inadequate planning for projects resulted in the questionable use of about \$263,000 of appropriated funds on eight design contracts. The cost of the planned projects was not included in the AFRC budget and was significantly underestimated by AFRC engineering personnel.

## **Finding B. Work Management and Contract Internal Controls**

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**Design Award.** The use of appropriated funds for design contracts at AFRC was not based on funds being available for the project to be designed. Instead, it was based on the AFRC Engineering Department's use of appropriated funds "while they are available" because it was "normal engineering practice to have designs on the shelf in case funds became available" for the project.

The design contracts were awarded despite the fact that the projects were not planned or included in the budget. The AFRC Director of Engineering explained that design contracts were awarded to architectural and engineering firms to prevent the expiration of appropriated funds.

AR 215-1 implemented the Assistant Secretary of Defense (Force Management and Personnel) report that authorizes the use of appropriated funds for all architectural and engineering services whether the planned project is appropriated fund or NAF. We believe that appropriated funds should not be authorized for the design of NAF projects.

**Design Estimates.** AFRC underestimated the cost of the golf course sprinkler system by about 219 percent, but did not suspend the project until the project design was almost completed. The AFRC engineering personnel estimated the NAF golf course sprinkler system project at \$400,000. However, the architectural and engineering firm estimated the project at \$876,000. The general manager said the project would never pass the scrutiny required of a NAF project more than \$500,000, and therefore suspended the project.

An analysis showed that AFRC engineering estimates averaged 240 percent below the contractors' estimates. The project costs were drastically underestimated by the AFRC engineering personnel; therefore, the design contracts were stopped to prevent further use of funds.

**Design Cancellation.** The design contracts averaged about 84 percent of completion before the projects were stopped. The AFRC Director of Engineering stated the contracts do not require cost estimate submittals until the pre-final design phase (95 percent). However, AFRC engineering personnel received preliminary "rough" cost estimates throughout the design process, which should have allowed AFRC to cancel the designs sooner. The AFRC Director of Engineering said the designs were canceled to prevent spending more money when it became apparent that AFRC engineering estimates significantly underestimated the project cost. However, AFRC never had funding initially for the project at the original AFRC estimate. Instead, AFRC awarded the design contracts with the hope that funds would become available for the project before the designs became outdated.

The Director of Engineering contended that the funds for the canceled design contracts were not wasted because the designs could be restarted, if feasible, when funds become available for the projects. However, the Public Works Center believes the designs may become outdated due to changes in technology. Appendix A further discusses the design contracts identified in the allegations.

## **Finding B. Work Management and Contract Internal Controls**

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**Management of Other Contracts.** AFRC engineering personnel also did not properly manage about \$249,000 work for other appropriated fund contracts. About \$221,000 was incorrectly classified appropriated fund costs for custodial and other contracts as noted in Finding A. In addition, an estimated \$28,000 of the AFRC Chiemsee grounds maintenance contract was not properly administered. See Appendix A for further details.

### **Contract Controls**

The RCOs did not have reasonable assurance that T&M type contracts were appropriate for AFRC. The RCOs did not properly justify, administer, or review the T&M contracts. In addition, AFRC did not have adequate staff, training, and an internal control system to properly monitor T&M contracts. The reasonable assurance standard, from DoD Directive 5010.38, states that internal control systems must provide reasonable, but not absolute, assurance that the objectives of the organization are accomplished and cost beneficial.

**Contract Justification.** The contracting offices did not properly justify the award of T&M contracts for AFRC. Specifically, the contracting officers did not use historical cost and performance data to determine cost realism of the contracts and did not recognize the lack of an adequate AFRC surveillance plan. As a result, the contracting offices award of T&M contracts was inappropriate and not in the best interest of the Government.

RCO Fuerth should have reviewed the requirements to ensure the contracts were structured to provide contracts that deliver goods and services efficiently and effectively. The RCO Chief of Contracting approved AFRC's contracts even though they believed that the "requirements were vulnerable to fraud, waste and abuse".

**Historical and Performance Data.** The RCOs awarded inappropriate T&M contracts because the duration of the work and the anticipated costs could be estimated. FAR 16.601, "Time-and-Materials Contracts," requires the award of other than T&M contracts if the duration and anticipated costs of the work could be estimated.

RCO Augsburg did not use the available data when determining that T&M contracts were the best contract type for AFRC. AFRC developed a performance work statement that detailed the work needed to maintain each facility. Since AFRC facilities were maintained by the U.S. Government since World War II, the performance work statement should have provided the contracting officer sufficient and accurate data to preclude the award of T&M contracts.

**Adequate Surveillance.** RCO Augsburg T&M contract justification that "AFRC's Government surveillance plan was adequate" was not accurate. AFRC did not have the personnel and training necessary to properly monitor T&M contracts. AFRC personnel were not aware of the amount of surveillance needed for T&M contracts.

## **Finding B. Work Management and Contract Internal Controls**

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The number of contracts and other duties assigned to the Garmisch Director of Engineering and the Chiemsee Facility Manager prevented the proper monitoring of contracts. Both the Director of Engineering and the Facility Manager were each assigned contracting officer's representative (COR) duties for at least 25 active contracts with the award of the T&M contracts. RCO Fuerth stated that the CORs at AFRC certified that they could dedicate the required amount of time when designated a COR. Based upon the number and complexity of contracts, RCO Fuerth contracting personnel believed the Director of Engineering and the Facility Manager would be required to spend almost 100 percent of their time just performing as a COR. However, the Director of Engineering stated only about 25 percent of his time was spent on COR duties.

**Contract Administration.** The T&M contracts for AFRC were not properly administered because the personnel associated with the contract did not have sufficient experience with T&M contracts. RCO Fuerth personnel only visited AFRC once in 15 months since becoming responsible for contract administration. Both AFRC and RCO Fuerth personnel stated they did not have adequate experience with T&M contracts. The RCO Fuerth contract administration personnel should have reviewed AFRC operations because RCO Fuerth personnel were aware the AFRC T&M contracts may be vulnerable to fraud, waste, and abuse.

**Inspections.** The CORs did not comply with the COR designation letters and FAR 16.601 that required CORs to inspect the contractors operations, establish (quality assurance) surveillance plans, document results, and report deficiencies to the contracting officer. In addition, the contractors did not provide an inspection system as required by FAR 52.246-6(b), "Inspection--Time-and-Material and Labor-Hour." At both Garmisch and Chiemsee, work was generally assumed to be satisfactory unless someone complained.

The CORs at Garmisch and Chiemsee did not properly inspect contractors' operations. The surveillance plans for Garmisch and Chiemsee stated that random inspections would be used for all work under 3,000 Deutsche Marks<sup>2</sup> and all work 3,000 Deutsche Marks or more would be inspected. AFRC assumed its inspection plan was acceptable because the RCOs did not object.

At Garmisch, all projects costing 3,000 Deutsche Marks or more were inspected at some time; however, projects requiring less than 2 hours to complete (about \$100) were generally not inspected. Overall, the inspectors at Garmisch estimated that 30 to 40 percent of the \$1.7 million of the appropriated fund T&M trade contract work was inspected at some time.

Chiemsee did not have sufficient staff to inspect about \$780,000 of the appropriated fund T&M trade contract work because Chiemsee did not have full-time inspectors. The Chiemsee COR relied on personnel who were not qualified to perform inspections for the contracts, and inspections that were

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<sup>2</sup>3,000 Deutsche Marks convert to about \$1,478 and \$1,667 for FYs 1991 and 1992, respectively.

## **Finding B. Work Management and Contract Internal Controls**

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performed usually occurred after completion of the work. For example, hotel maids, when cleaning the rooms, would informally inspect repairs in the rooms.

**Surveillance Systems.** Neither the contracting offices nor AFRC established a surveillance system suitable to T&M contracts. The RCO Fuerth Contract Administration branch made only one visit to an AFRC location (Chiemsee) between June 1992 and September 1993. AFRC was generally unaware of the extent of responsibility for monitoring the contractor time or material costs on T&M contracts. AFRC also had insufficient controls to document that contractors' T&M charges were reasonable or allowable.

**Labor Costs.** About \$1.68 million in invoices for contractor labor hours were not adequately monitored. The following show that contract terms were inconsistently applied and not followed.

- o AFRC personnel did not monitor and document the time the contractor arrived at or left the work site.

- o The Chiemsee COR instructed contractors to bill in 15-minute increments; however, the Garmisch COR used 30-minute increments.

- o The CORs at Garmisch and Chiemsee incorrectly administered travel time on the T&M trade contracts. Nineteen contracts failed to state whether travel time to and from work should be compensated. However, seven contracts did limit the contractor compensation to actual work on site. The COR at Garmisch allowed the contractors to receive labor costs for travel time to and from the work site regardless of contract terms. Conversely, the COR at Chiemsee never allowed labor costs for travel time to and from the work site.

- o The contracting officers at RCOs Augsburg and Fuerth did not direct the CORs at AFRC to withhold 5 percent of direct labor hours billed as required by FAR 52.232-7(a), "Payments under Time-and-Materials and Labor-Hour Contracts."

- o Contractors were compensated at hourly rates greater than the amount allowed by the contract. For example, the electrical contractor was paid about \$38 per hour instead of the \$29 per hour stated in the contract. The contractor based the rate on the skill level of his employees and not the rate specified in the contract.

- o The CORs at Garmisch and Chiemsee were not aware that the contractors had to obtain contracting officer approval before the contractors hired subcontractors. Also, the contracting officer was not notified when the contractor subcontracted work as required by FAR 52.244-3, "Subcontracts (Time-and-Materials and Labor-Hour Contracts)."

- o The CORs at Garmisch and Chiemsee did not verify the contractor individual daily job timecards or other documentation before labor payment was approved as required by FAR 52.232-7(a).

## **Finding B. Work Management and Contract Internal Controls**

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**Material Costs.** The CORs at Garmisch and Chiemsee did not document that about \$808,000 in material charges were allowable and reasonable or determine whether the materials were authorized. FAR 52.232-7 allows material costs to be reimbursed at their cost plus reasonable handling costs, or by an established list or catalog price (less discounts and rebates). The regulation also allows contractors to be reimbursed only for materials used or consumed directly in performance of the contract.

Neither Garmisch nor Chiemsee obtained contractors' receipts for materials as required by the contracts. The Garmisch COR and his staff did not know what costs were allowable and presumed the costs were reasonable without obtaining receipts. The Chiemsee COR realized material charges should have been verified but did not have the staff to monitor costs.

**Supplies Purchased.** The AFRC personnel did not follow proper FAR procedures when the appropriated fund T&M trade contracts were used to buy supplies in FYs 1991 and 1992. AFRC personnel did not know that T&M contracts should not be used to buy supplies. AFRC purchased about \$33,481 in supplies from its contractors and paid at least \$1,849 for labor costs that included delivery charges.

The supplies could have been bought for less through the Real Property Maintenance Activity. For example, AFRC Garmisch purchased 100 light bulbs using T&M contracts for about \$53, which included \$16 in labor charges. AFRC paid 83 percent more than the Real Property Maintenance Activity price of \$29. Similarly, AFRC Chiemsee purchased 200 light bulbs at a cost of about \$153. The price Chiemsee paid was 94 percent more than the Real Property Maintenance Activity price of \$79.

Supplies purchased also included shower hoses, padlocks, and paint. Supply purchases also went directly to support the AFRC hotels, golf course, and dining facilities even though the supplies are NAF costs. The use of T&M trade contracts for supply purchases was discontinued during the audit and the supplies are now procured through the Real Property Maintenance Activity; therefore, no recommendation was made.

**Invoices Processed.** CORs failed to promptly process about 65 percent of the FYs 1991 and 1992 T&M trade contract invoices. Of the 175 invoices at Garmisch, 113 were not approved by the COR within the 7 days required by U.S. Army Europe regulations, and 21 were approved 30 days or later. Similarly, 85 of 132 invoices at Chiemsee were not approved by the COR within 7 days, and 31 invoices were approved 30 days or later. Therefore, the CORs' delays in processing invoices prevented the finance office from paying contractors within a reasonable time.

**Contract Delay.** RCO Fuerth delayed the preaward review of the requests for contracting actions from AFRC and perpetuated the use of inappropriate T&M contracts. AFRC requested renewal contracts in February and March 1992 by submitting portions of prior contracts awarded by RCO Augsburg as examples of their requirements. However, the requests were not reviewed and processed by RCO Fuerth until July 1992. We believe the

## Finding B. Work Management and Contract Internal Controls

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delay was caused by RCO Fuerth's lack of T&M contract knowledge and processing of contract requirements for AFRC. Consequently, the delay prevented RCO Fuerth from awarding suitable contracts for FY 1993. RCO Fuerth has since implemented a tracking system for the contracting process; therefore, no recommendation was made.

### Internal Control Standards

AFRC did not have an adequate internal management control program that ensured work management and contract internal controls for appropriated fund T&M contracts. AFRC placed greater emphasis on internal controls for its NAF operations because unavailable rooms or services translate directly into lost sales. Work management and contract internal controls were not implemented because AFRC management did not give controls a high enough priority, and AFRC personnel had insufficient experience with T&M contracts.

AFRC was not exempt from DoD Directive 5010.38, which requires an internal management control program for contract administration, property management, and repair and maintenance. An effective internal management control program could have precluded the lack of supervision, separation of duties, and documentation.

**Supervision.** The actions of AFRC Engineering Department personnel were not reviewed by CFSC as required. The AFRC personnel could not remember and we could not determine when the last audit or headquarters review was performed to evaluate the AFRC Engineering Department compliance with AR 420-10.

Internal controls generally require adequate supervision, which includes providing qualified and continuous oversight to ensure that internal control objectives are achieved. Furthermore, personnel must be provided adequate guidance and training. The work performed by personnel must be reviewed and approved to the extent necessary to ensure that critical objectives are accomplished and that errors, waste, and wrongful acts are minimized.

**Training.** The AFRC Engineering Department personnel did not receive adequate training. Key personnel in the AFRC Engineering Department have not met the Army training requirement in AR 420-10, which requires key engineering personnel to attend the Directorate of Engineering and Housing Executive Management Course, the Facilities Management Engineering Course, and the Facilities Engineering Basic Course. The courses ensure that installation managers understand the policies, procedures, and regulations relevant to the operation of an Army activity and the constraints on appropriated funds. The Garmisch Director of Engineering and the Chiemsee Facility Manager have not attended any of these courses. The lack of training contributed to the poor work management and contract internal controls.

## **Finding B. Work Management and Contract Internal Controls**

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**Review of Appropriated Fund Authorization.** The AFRC Resource Management Office certified that the work to be performed was authorized appropriated funds without sufficient information. The Resource Management Office only reviewed the planned use of the funds when they certified the purchase request. However, the purchase request failed to include the specific location and description of work. Therefore, the AFRC Engineering Department had assumed the AFRC Resource Management Office responsibility to ensure the proper use of funds. The limited review enabled the AFRC Engineering Department to incorrectly use appropriated funds.

**Separation of Duties.** The Garmisch Director of Engineering and the Chiemsee Facility Manager have not maintained a separation of duties. Both individuals were responsible for the facility maintenance, planning, and COR duties. The separation of duties element of internal controls requires that different individuals should authorize, process, record, and review transactions. This primary element provides an effective system of checks and balances to reduce and detect fraud, waste, and abuse.

The Director of Engineering and the Facility Manager controlled both the use of contracts and the approval of payments to contractors. They told the contractors what to do, when to do it, and then approved the contractors' invoices for payment. Both individuals agreed they had too much control and authority vested in their positions but did not know who would, or could, accept additional responsibilities. The conflicting responsibilities of the Director of Engineering and the Facility Manager included:

- o acting as COR,
- o determining the projects' size, scope, and certifying need,
- o determining the projects' classification and funding authorization,
- o directing staff and contractors,
- o performing negotiations,
- o ordering and inspecting work, and
- o certifying invoices.

Because of the conflicting duties required as COR and as Director of Engineering and Facility Manager, the potential risk of inappropriate use of the T&M contracts increased with each additional duty assigned. Both the RCO Fuerth personnel and the CORs agreed that the potential for abuse was high when the duties were combined.

**Documentation.** AFRC did not adequately prepare facility project files or specifications and independent Government estimates. AR 420-17 requires that repair and maintenance data for all facilities be maintained.

## **Finding B. Work Management and Contract Internal Controls**

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Internal control documentation generally requires that transactions and significant events be clearly documented, and that documentation be available for examination. Documentation must be complete and accurate to facilitate tracking the transaction or event from inception to completion. Additionally, the documentation must be organized in a manner that allows auditors and others reviewing the files to clearly reconstruct the complete series of events.

**Project Files.** The facility project files did not document the condition of the property or whether the costs proposed and incurred were reasonable. For example, the painting files did not contain the date of work, the condition of the surface, the type of surface and surface preparation, the specification numbers of paints, and the number of coats. These useful data are needed to determine the performance of coatings applied and compatibility of future coatings. The project files contained the work requested and the contractor invoices, but not the detailed specifications and materials.

**Specifications and Independent Government Estimates.** Government specifications or independent Government estimates were not completed for any of the \$1.1 million FYs 1991 and 1992 Garmisch T&M projects that individually exceeded \$1,000. However, Chiemsee could not determine the number of projects costing more than \$1,000 because of the limited computer capability. The Chiemsee facility manager stated that the project files did not include specifications and independent Government estimates except for a few electrical specifications prepared by Garmisch personnel.

Generally, the Garmisch Director of Engineering and the Chiemsee Facility Manager told the contractor what they wanted and the contractor prepared a proposal. The CORs negotiated contractors' proposals when the costs were not reasonable. The COR discussions and agreements with contractors were not documented as required by the COR designation letters.

The T&M appropriated fund trade contracts required contractors to submit estimates to the CORs for projects expected to exceed 3,000 Deutsche Marks. Therefore, projects valued at more than 3,000 Deutsche Marks were estimated but not independently.

Specifications describe what the Government wants and includes criteria to determine whether the Government requirements were met. Without specifications, our office, and more importantly AFRC, had no objective way to determine the reasonableness of the contractor charges. Specifications and independent Government estimates are used to provide a basis for planning and cost control. Army Technical Note 420-10, "Management of Installations - Directorate of Engineering and Housing Resources Management Systems Handbook," suggests that when a project exceeds 40 staff-hours or \$1,000, cost controls are appropriate.

## Finding B. Work Management and Contract Internal Controls

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### Conclusion

Work management and contracts were inefficiently managed because AFRC personnel did not have adequate supervision, separation of duties, and documentation. Furthermore, AFRC management did not give the Engineering Department internal controls high priority. The T&M contracts awarded for AFRC, combined with the AFRC management belief, fostered the inadequately managed appropriated fund work.

### Recommendations, Management Comments, and Audit Response

1. We recommend that the Assistant Secretary of Defense for Personnel and Readiness prohibit the use of appropriated fund support for architectural and engineering services associated with nonappropriated fund construction projects.

**Management Comments.** The Assistant Secretary of Defense for Personnel and Readiness nonconcurred and stated that DoD Directive 1015.6 "Funding of Morale, Welfare and Recreation Programs" authorizes appropriated funding of architectural and engineering services regardless of category, for "construction, alteration and repair contracts." The Assistant Secretary asserted that the central issue is to distinguish those projects eligible for Architectural and Engineering services from routine maintenance and repair. Instead of generally prohibiting appropriated funding for architectural and engineering services, the Assistant Secretary recommended improving the definition of "construction, alteration and repair contracts" in the next update of DoD Directive 1015.6.

**Audit Response.** The Assistant Secretary of Defense for Personnel and Readiness proposed actions are not fully responsive to the recommendation. We agree that routine maintenance needs to be clearly defined and we addressed that concern in Recommendation 3.b. of Finding A. We did not question the definitions of construction, alteration, and repair contracts during our audit. However, Recommendation B.1. addresses the policy of using appropriated funding for architectural and engineering services in connection with nonappropriated fund construction projects. While these costs are permitted appropriated funding by DoD Directive 1015.6, we do not believe that appropriated funds should be used to pay for architectural and engineering services at nonappropriated fund activities such as hotels, ski lodges, ski lifts, or golf courses. We request the Assistant Secretary of Defense for Personnel and Readiness to reconsider his position and to provide additional comments to the final report.

2. We recommend that the Commander, U.S. Army Community and Family Support Center, establish procedures for periodic reviews of the operations of the Armed Forces Recreation Center-Europe Engineering Department for compliance with applicable guidance.

## **Finding B. Work Management and Contract Internal Controls**

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3. We recommend that the General Manager, Armed Forces Recreation Center-Europe:

a. Prepare installation master plans, unconstrained requirements reports, resource management plans, and annual work plan as required.

b. Authorize contract funds for individual projects only after the complete project is reviewed, approved, and budgeted.

c. Review all Engineering Department requests and cost estimates before outside architectural and engineering services are contracted.

d. Obtain estimated project costs from contracted architectural and engineering services before the pre-final phase.

e. Establish procedures to verify that personnel in the Engineering Department obtain the training required to meet minimum Army training goals.

f. Establish and implement procedures for the Resource Management Office to review and certify appropriated funded work orders.

g. Establish controls to separate the responsibility for inspecting contractors' work from the responsibility for ordering work.

**Management Comments.** The Army concurred with Recommendations 2, 3.a., 3.b., 3.c., 3.d., 3.e., 3.f., and 3.g and stated that all necessary actions to comply would be completed by September 30, 1994.

h. Maintain adequate project files and prepare specifications and independent Government estimates for all projects greater than \$1,000.

**Management Comments.** The Army concurred in principle and stated that, for projects of more than \$1,000, individual work orders will be filed by project and will be documented by independent government estimates. In addition, for maintenance and repair projects of more than \$50,000, the Army agreed to maintain official files and write specifications. The Army planned to complete the corrective actions by June 1994.

**Audit Response.** The Army comments are not completely responsive. The Army did not indicate whether specifications will be prepared for projects under \$50,000. The Federal Acquisition Regulation requires specifications for the acquisition of all supplies and services regardless of cost. The Federal Acquisition Regulation makes no exception for contracts under \$50,000. Further, the Army has not explained why the cost controls suggested by Technical Note 420-10 for Army projects more than \$1,000 are not appropriate at AFRC until a project exceeds \$50,000. We request the Army to reconsider its position on this recommendation and provide additional comments when responding to the final report.

## Finding B. Work Management and Contract Internal Controls

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4. We recommend that the Chief, Regional Contracting Office, Fuerth:
- a. Direct the contracting officer to stop awarding or exercising options on time-and-materials contracts for the Armed Forces Recreation Center-Europe.
  - b. Provide adequate training to the Armed Forces Recreation Center-Europe's, contracting officer's representatives in their responsibilities.
  - c. Establish an acceptable contract surveillance system to include the contractor, the contracting officer's representative, and the contract administration specialists.
  - d. Establish procedures for the contract administrators to perform periodic reviews of, or make site visits to, the Armed Forces Recreation Center-Europe.
  - e. Establish procedures for the contracting officer's representative to verify contractors and subcontractors charges for labor and material costs.
  - f. Establish procedures to verify that 5 percent of the labor costs on time-and-materials contracts is withheld.
  - g. Establish procedures to verify that the contracting officer's representative process contractors' invoices within 7 days.

**Management Comments.** The Army concurred and stated no new time-and-materials contracts were written for AFRC. A cost-plus-award-fee contract for maintenance work was scheduled for award by February 25, 1994 and the Defense Contract Management Area Office Frankfurt may manage the contract. If RCO Fuerth does manage future contracts, additional training and contract oversight procedures will be implemented. The overall action was to be completed by April 1994.

## Response Requirements Per Recommendation

Responses to the final report are required from the addressees shown for the items indicated with an "X" in the chart below.

Number	Addressee	Response Should Cover:			
		Concur/ Nonconcur	Proposed Action	Completion Date	Related Issues <sup>1</sup>
1.	ASD (P&R) <sup>2</sup>	X	X	X	
3.h.	Army	X	X	X	IC

<sup>1</sup>IC = material internal control weakness.

<sup>2</sup>Assistant Secretary of Defense for Personnel and Readiness.

## **Management Comments and Audit Response on the Finding**

**Management Comments on Golf Course Clubhouse.** The Army does not agree with the finding that AFRC-E "needed" to use appropriated funds to avoid the \$500,000 NAF funding limitation. The project cost should not have included architectural and engineering design costs in the total project cost when determining the regulatory funding threshold limitations.

**Audit Response.** The Army's comments are not germane because the word "needed" does not appear in the Golf Course Clubhouse section of the report, nor does the report state that AFRC violated any funding limitation.

**Management Comments on Kitchen Project.** The Army understands that the contract award in September 1992 raises an appearance of impropriety. However, the contract requirement was a bona fide need at the time, and AFRC-E management had no reason to suspect that construction startup would be delayed 5 months. The Inspector General, DoD, assumption that the contract should be canceled relies on hindsight. Mitigating factors against cancellation include escalating construction costs and time and labor expenses associated with resolicitation.

**Audit Response.** We do not agree with the Army's statement that the AFRC Director of Engineering had no reason to suspect that construction startup would be delayed 5 months. The Director of Engineering knew that the award of the kitchen ceiling and ventilation contract was premature. The contract for the design of the temporary kitchen was awarded 3 days after the award of the kitchen ceiling and ventilation contract. In addition, the Director of Engineering ordered work to begin in December 1992 because he believed that if work was not started the contract would violate the bona fide need rule and be canceled. The AFRC's most optimistic projection estimated the temporary kitchen would not be designed and available for 5 months. The temporary kitchen was not actually available for almost 7 months.

The report never recommended cancellation of this project. The projects included in the report were given as examples of poor project planning at AFRC.

**Management Comments on Architectural Services.** The Army stated that normal engineering practices of Technical Note 420-10-01 provides for early completion of the design work to be shelved while waiting for funds in the near future. Upon availability of funds, the projects can be quickly executed because the long lead time for the contracting, designing and reviewing process has been eliminated. When the design projects were approved, AFRC had no indication of the severity in appropriated fund cutbacks forthcoming for construction support in Europe. Although these projects had to be placed on hold, they are still valid requirements.

## **Finding B. Work Management and Contract Internal Controls**

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**Audit Response.** The Army correctly paraphrases the regulation when it state that designs may be completed in advance while waiting for funds in the near future. However, AFRC management did not document that funds were programmed, committed, or otherwise set aside for the projects designed. Written explanations for the canceled design projects consistently indicated that appropriated funds were used while they were available and that it was normal engineering practice to design projects before funds were available. These explanations were provided by the AFRC Director of Engineering.

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## Finding C. Subsidized Operations

AFRC was not capable of being financially self-sustaining without subsidized operations even though AFRC operated at near capacity. AFRC was not self-sustaining because the operations were not cost-effective. As a result, the U.S. Government will be required to continue to provide substantial subsidies to AFRC operations until a cost-effective alternative is provided.

### Background

**Evaluation of Operations.** The accounting firm of Pannell, Kerr, Forster evaluated AFRC operations in FY 1984 and concluded that AFRC received a disproportionate amount of appropriated fund support and was not self-sufficient or cost-effective. The report stated:

The major conclusion relating to the funding of AFRC as a nonappropriated fund instrumentality is that a disproportionate amount of appropriated fund support is being channeled to it . . . Thus, the spirit of self-sufficiency which should guide a Morale Welfare Recreation instrumentality is being completely violated by AFRC . . . and seems completely out of line to the scale of operations and its own revenue-generating potential.

The report also stated that an estimated \$30 million to \$50 million in capital improvements would be needed for the AFRC facilities. The report recommended the construction of new facilities in Garmisch and refurbishment of rooms at Chiemsee. However, the recommendation was only partially implemented. The Garmisch project was terminated after the construction of the foundation and parking garage. The Chiemsee rooms were refurbished. See Summary of Prior Audits and Other Reviews in Appendix B for additional information on the report.

**Audit of Financial Statements.** The accounting firm of KPMG Peat Marwick disclosed in the notes to the FY 1992 audited nonappropriated fund financial statements, April 15, 1993, that AFRC management expects that, if appropriated fund support is not received, AFRC will be able to continue its operations. AFRC management expects to continue operations with fewer employees and with increased rates for services.

## Finding C. Subsidized Operations

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### Cost of Operations

**Profitability.** AFRC reported a net operating loss of \$2.24 million for combined FYs 1991 and 1992 operations. Furthermore, the net operating loss does not include an appropriated fund subsidy of about \$30 million (includes the \$1.6 million misclassified appropriated fund expenses identified in Finding A).

**Subsidy.** AFRC received about \$34 million in additional support to operate its activities in FYs 1991 and 1992. About 87 percent (\$29.7 million of \$34.31 million) of the subsidy was appropriated fund support. AFRC received substantial appropriated fund support because AR 215-1 did not clearly categorize all of the AFRC activities as Category C. We believe AFRC is primarily a business activity and was intended to be supported almost entirely with NAF.

AFRC also spent about \$5 million from the NAF Army Recreation Machine Trust Fund (slot machines and video games). Table 3 shows the actual loss made up of the net loss and total subsidy (appropriated funds and NAF) for FYs 1991 and 1992.

**Table 3. Actual Loss of AFRC Operations  
for FYs 1991 and 1992**

	<u>FY 1991</u> (millions)	<u>FY 1992</u> (millions)	<u>Total</u> (millions)
Net loss	\$ (1.87)	\$ (.37)	\$ (2.24)
Subsidy	<u>(21.23)</u>	<u>(13.08)</u>	<u>(34.31)</u>
Total	<u>\$(23.10)</u>	<u>\$(13.45)</u>	<u>\$(36.55)</u>

The NAF financial statements reported revenues of about \$18 million and \$16 million for FYs 1991 and 1992, respectively. In addition to revenues, the AFRC operations would have required about \$36.5 million of appropriated fund and NAF contributions to break even in FYs 1991 and 1992. Therefore, AFRC would have had to increase revenues more than 100 percent just to break even without the appropriated fund and NAF support. We do not believe AFRC can continue without appropriated fund support because, even with about \$30 million of appropriated fund support, AFRC still reflected a net loss of about \$2.24 million operating at near capacity for FYs 1991 and 1992.

## Analyses of Subsidies for Operations

**Hotel Guests.** The U.S. Government and NAF subsidized AFRC at least \$51 per day for each hotel guest because operations were not cost effective. However, military retirees, civilians, and North Atlantic Treaty Organization military members represented 27 percent of all rooms rented. Thus, about \$8 million of appropriated funds was used for non-U.S. military recreation at AFRC. The remaining guests were active-duty military members and their family members. Table 4 shows that the subsidy per day for each hotel guest was \$62 and \$51 for FYs 1991 and 1992, respectively.

**Table 4. Subsidy Paid per Day per Hotel Guest**

	<u>Total Subsidy</u>	<u>No. of Guests</u>	<u>Subsidy per Guest</u>
FY 1991	\$21,227,000	341,525	\$62
FY 1992	\$13,080,000	257,815	\$51

**Occupied Rooms.** The U.S. Government and NAF subsidized at least \$115 for each occupied room per day at AFRC even though the hotels operated at near capacity. Even with the large subsidies, the AFRC operations reflected a loss of more than \$2 million for FYs 1991 and 1992. Therefore, the subsidies were necessary to ensure that AFRC could remain operational.

The Garmisch occupancy rates exceeded 90 percent for both FYs 1991 and 1992; Chiemsee rates averaged 82 percent. We used data AFRC provided for occupied rooms and occupancy rates to determine the number of rooms rented. Table 5 shows the room rate increase needed per occupied room to recover the subsidies.

## Finding C. Subsidized Operations

**Table 5. Room Rate Increase Required to Recover Subsidies**

	<u>Total Subsidy</u>	<u>No. of Rooms</u>	<u>Rate Increase per Room</u>
FY 1991	\$21,227,000	126,333	\$168
FY 1992	\$13,080,000	113,425	\$115

Therefore, the actual AFRC room cost per day would have had to have been \$209 (\$168 + \$41) in FY 1991 and \$156 (\$115 + \$41) in FY 1992 to recover the subsidies received.<sup>3</sup> Figure 3 shows the actual AFRC room cost per day to the customer, the taxpayer (appropriated fund subsidy) and the Army Recreation Machine Trust Fund (nonappropriated fund subsidy) for FYs 1991 and 1992.

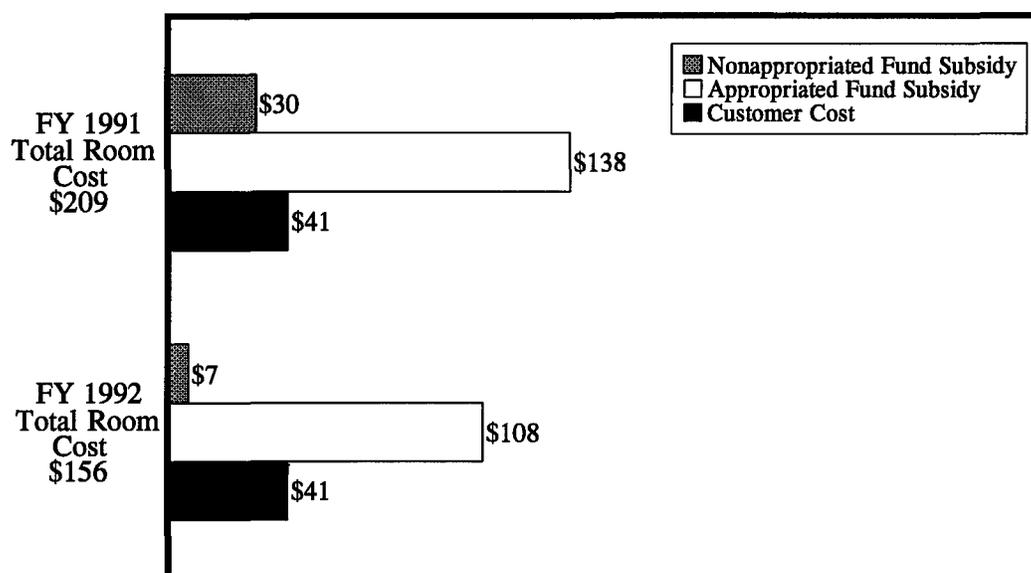


Figure 3. Actual AFRC Room Cost per Day for FYs 1991 and 1992

**Comparison with Local Economy and Per Diem.** The actual AFRC room cost also exceeds the Garmisch and Chiemsee local hotel rates and lodging per diem rates. The Garmisch and Chiemsee local hotel double occupancy rates per day averaged \$75 and \$85 for FYs 1991 and 1992, respectively. In addition, lodging per diem rates per day averaged \$59 and \$76 for the same time period. Figure 4 shows that the AFRC operations were not cost-effective when compared to the local hotel rates and lodging per diem.

<sup>3</sup>We assumed an average room rate of \$41. FY 1992 room rates ranged from \$30 to \$52.

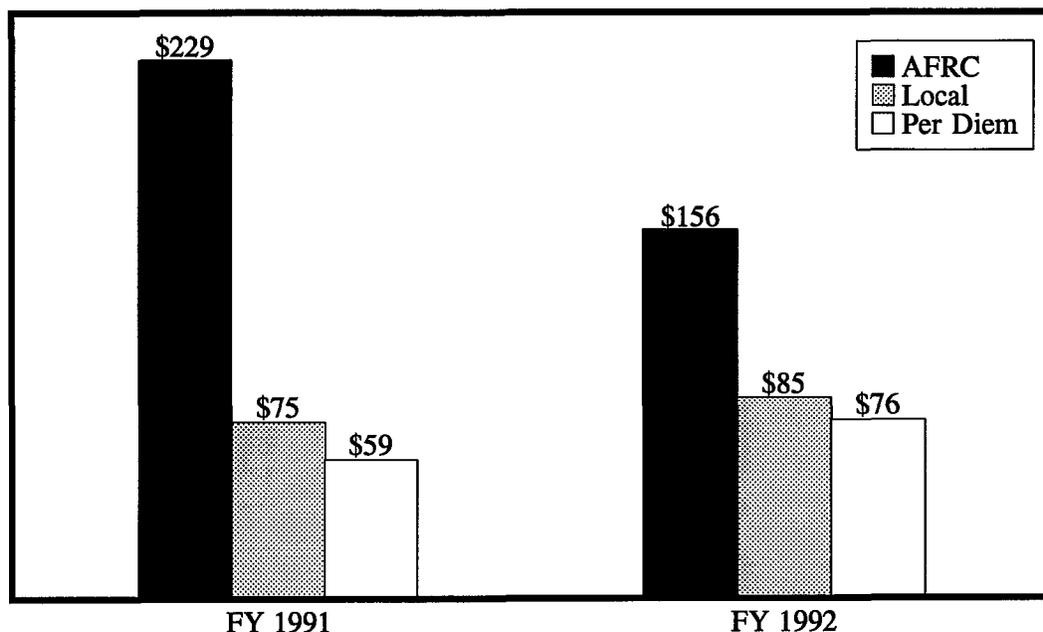


Figure 4. AFRC Lodging Cost Comparison for FYs 1991 and 1992

We applied the subsidy to the occupied rooms because AFRC hotel rooms generate the most revenue (about 37 percent), were used in the past to compare the efficiency of AFRC, and were easily comparable to local accommodations and per diem rates. Although AFRC operations include more than rooms, the overall costs including net losses and subsidies were not recovered by AFRC.

## Future Operations

AFRC management expects the appropriated fund support to decrease and estimates that NAF operations will become profitable in the near future. AFRC estimated that appropriated fund support will decrease to \$7.8 million in FY 1994 and \$4 million in FY 1995. Even though AFRC lost about \$500,000 as of the third quarter FY 1993 (unaudited), AFRC estimates a FY 1994 profit of more than \$1.3 million (excluding the NAF and appropriated fund subsidies).

AFRC had to rely on subsidies to operate its activities and has no official approved plan to be self-sufficient in the next 5 years. We question whether AFRC can achieve self-sufficiency in the foreseeable future. We believe that costs could escalate because of the age and condition of the existing facilities. Additionally, revenues and subsidies could decrease because of reductions in troop strength and budgets. Without corrective action, increased losses and a greater reliance on subsidies could result.

## Finding C. Subsidized Operations

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### Conclusion

Recreational activities are a vital part of the military morale, welfare, and recreation mission in Europe that needs to be continued. However, AFRC does not operate a cost-effective recreational operation in Europe. In light of reduced troop strength and budgets in Europe, more cost-effective methods of providing recreational activities need to be considered. We believe that alternatives such as the use of local accommodations and facilities and base morale, welfare, and recreation support could provide comparable services more cost-effectively.

### Recommendations, Management Comments, and Audit Response

**Added Recommendation.** In response to meetings with the Army, we added Recommendation 1. to the final report. The Army provided additional comments to Recommendation 1.

1. We recommend that the Assistant Secretary of the Army (Manpower and Reserve Affairs) determine whether Armed Forces Recreation Center-Europe is necessary.

**Management Comments.** The Army concurred in principle to the recommendation to determine whether AFRC is necessary. The Army stated that it agrees in Recommendation C.2. to a study that meets the intent of the recommendation. The results will be presented to the Army Morale, Welfare, and Recreation Board of Directors.

**Audit Response.** The Army comments were responsive. The study proposed in response to Recommendation C.2. will determine whether AFRC is necessary.

2. We recommend that the Assistant Secretary of the Army (Financial Management):

a. Conduct a study to determine whether the Armed Forces Recreation Center-Europe, can exist as a self-sustaining business (without appropriated fund support).

b. Determine in the study whether recreational services can be provided more cost-effectively by the use of local accommodations and facilities and base morale, welfare and recreation support.

**Management Comments.** The Army concurred and stated that it will conduct a study that will consider current demand for AFRC, the impact of changing the rate structure, and the status of comparable local competition. The target date for the study is first quarter of FY 1995.

**Audit Response.** We do not consider the Army comments to be fully responsive. The Army does not address whether the study will determine whether AFRC can exist as a self-sustaining business (without appropriated funds support) or will determine whether local accommodations will provide morale, welfare, and recreation support more cost-effectively than AFRC. These were integral parts of our recommendation. Accordingly, we request the Army to provide additional comments in Recommendations C.2.a. and C.2.b. in its comments on the final report.

3. We recommend that the Assistant Secretary of Defense for Personnel and Readiness review the study performed on the Armed Forces Recreation Center-Europe.

**Management Comments.** The Assistant Secretary of Defense for Personnel and Readiness concurred and stated the study will be reviewed within 90 days of receipt.

## Response Requirements Per Recommendation

Responses to the final report are required from the addressees shown for the items indicated with an "X" in the chart below.

<u>Number</u>	<u>Addressee</u>	<u>Response Should Cover:</u>		
		<u>Concur/ Nonconcur</u>	<u>Proposed Action</u>	<u>Completion Date</u>
2.	Army	X	X	X

## Management Comments and Audit Response on the Finding

**Management Comments.** The Army stated that AFRC is not required to be financially self-sufficient without appropriated fund support. It is also the Army's position to limit the profit potential and to utilize appropriated fund support to the extent authorized and available. The Army also stated it has informed the House Armed Services Committee, Morale, Welfare, and Recreation Panel, of current and future AFRC operations including the continued use of appropriated fund support.

The Army also questioned the use of 9-year-old data when providing background information. The Army did not agree with the methodology used in the Rooms Analysis. The Army stated the subsidy expenditure should be applied to all revenue and not just room revenue. Also, by not including the other AFRC operations generating the remaining 63 percent of revenue, any comparison substantially distorts the outcome and the conclusions. The Army recommended an adjustment to reflect other operations revenue or deletion from the report.

## Finding C. Subsidized Operations

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The Army stated that the future operations regarding the age and condition of existing facilities is misleading. The Army also stated that both Garmisch and Chiemsee were substantially renovated. The Army also disagreed with the comparison made to alternative recreational activities. The Army stated that the audit analysis does not demonstrate that local hotels and AFRC rooms are comparable in size and amenities.

**Audit Response.** AR 215-1 states that the primary distinction of activities such as the accommodations/dining and resale activities at AFRC is that they are comparable to self-sustaining businesses capable of funding most expenses. The regulation further states that these Category C activities receive very limited direct appropriated fund support. We believe that during the audited FYs 1991 and 1992, the direct appropriated funds AFRC received for its Category C activities was not limited but substantial. We used the Pannell, Kerr, Forster report from 1984 because it also detailed AFRC's reliance on appropriated fund support.

We consider the rooms analysis methodology to be a reasonable approach because it was previously used in the Pannell, Kerr, Forster report and accepted by AFRC. The audit report clearly states that rooms revenue represent 37 percent of the total revenue. However, overnight guests are the primary source of all revenue for AFRC activities. The distance of AFRC from U.S. military activities and the nature of activities mostly results in overnight stays. AFRC could not document the number of non-overnight customers. Further, AFRC NAF expenses and appropriated fund expenditures for the respective cost centers (rooms, food, skiing) were not available. Therefore, an analysis based on revenues and expenses of each cost center was not possible. We consider our analysis to be a reasonable estimate of the daily costs to provide morale, welfare, and recreational services at AFRC.

The Army comments concerning future repair and maintenance costs are inconsistent. The Army comments for Finding B stated that the canceled design projects are still valid requirements. This statement only adds to our belief that repair and maintenance of AFRC facilities may increase in the future. For our comparison of AFRC to local hotels, AFRC personnel provided the information from local hotels that it considered comparable to AFRC.

## **Part III - Additional Information**

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## Appendix A. Summary of Allegations

Personnel allegations in the DoD Hotline complaints were not evaluated because CFSC agreed to review the personnel issues. The results of the allegations we reviewed are discussed below.

### Allegations and Audit Results

**Allegation 1.** The T&M trade contracts for "unscheduled new work" violated the bona fide needs rule because the work was not needed when the contract was awarded.

**Audit Results.** The allegation was valid. We believe RCO Augsburg may have awarded T&M trade contracts that violated the bona fide needs rule. The contracts were not in the best interests of the Government because the contracts obligated funds that could have been used elsewhere for authorized projects. The T&M trade contracts for "unscheduled new work" were not bona fide needs because they used an Operations and Maintenance, Army, appropriation, and at the time of the award, the work needed was unknown. The "unscheduled new work" was removed from all of the T&M trade contracts awarded by RCO Fuerth.

**Allegation 2.** AFRC submitted requirements for T&M trade contracts that were vulnerable to fraud, waste and abuse.

**Audit Results.** The allegation was valid. See Finding B for further details.

**Allegation 3.** The use of a sole-source contract to inspect and maintain manually operated fire extinguishers was improper.

**Audit Results.** The allegation was valid. RCO Augsburg should have competed a requirement to inspect and maintain 60 manually operated fire extinguishers instead of modifying a sole-source small purchase contract. Contract DAJA10-91-M-0874 was awarded on a sole-source basis for \$3,308. The contract was awarded sole source because the contractor was the only firm in the area licensed to work on automatic fire extinguishing systems. The contract was later modified to add the inspection and maintenance of 60 manually operated fire extinguishers at a cost of \$4,505. We believe inspection and maintenance of manually operated fire extinguishers is different than the inspection of the whole automatic fire extinguishing system and could have been competed. No documentation was provided to document that competition was considered or that only one source was available as required by FAR 13.106(c)(2), "Competition and Price Reasonableness."

**Allegation 4.** AFRC incorrectly used appropriated funds for NAF expenses.

**Audit Results.** The allegation was valid. Appropriated funds were incorrectly used for NAF expenses. See Finding A for further details.

**Allegation 5.** AFRC management committed unauthorized procurement actions on design and construction contracts. The contracts were DACA90-90-D-0037, delivery orders 1 and 2.

**Audit Results.** The allegation was valid. The AFRC Executive Director made unauthorized changes to the two contracts identified in the allegations. The Executive Director directed the architect and engineering firm to make changes to two design contracts (DACA90-90-D-0037, delivery orders 1 and 2) without obtaining the contracting officer's approval. Prior written authorization by the contracting officer was required by FAR 52.243-3, "Notification of Changes."

**Allegation 6.** Work is not centrally scheduled and plans, specifications, and independent Government estimates were not prepared.

**Audit Results.** The allegation was partially valid. The allegation that work was not centrally scheduled was invalid. However, the allegation that plans, specifications, and independent Government estimates were not prepared was valid. Work was centrally scheduled by the work order assistant at Garmisch and the facility manager at Chiemsee. However, the AFRC Engineering Department had not prepared short- or long-term plans or coordinated its appropriated fund work. Similarly, specifications and independent Government estimates were rarely prepared for T&M trade contracts. See Finding B for further details.

**Allegation 7.** Service orders have exceeded the statutory limit of 16 man-hours and \$350 material costs.

**Audit Results.** The allegation was partially valid. The limits were not statutory. The limit for service order was changed to 40 staff hours or \$1,000 in September 1980. However, the limit was only guidance and not mandatory. AFRC exceeded the suggested limits without establishing cost controls. See Finding B for further details.

**Allegation 8.** The COR initiated many procurement actions and certified the pertinent invoices upon completion of the work.

**Audit Results.** The allegation was valid. Both the Garmisch Director of Engineering and Chiemsee Facility Manager were responsible for the facility maintenance, planning, and COR duties. They initiated procurement actions as the Ordering Officer and certified the invoices as COR. Both the contracting office personnel and the CORs agree that the potential for abuse was high when these duties were combined. See Finding B for further details.

## Appendix A. Summary of Allegations

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**Allegation 9.** The COR at Chiemsee did not enforce the clause, "Contractor shall provide Evidence/Proof (Invoices) on price paid to subcontractor/Vendors for spare parts/materials" on T&M trade contracts.

**Audit Results.** The allegation was valid. AFRC personnel did not obtain evidence of the cost of materials. See Finding B for further details.

**Allegation 10.** Various service contracts have been combined by the COR into a single task order to accomplish construction projects without any prior design.

**Audit Results.** The allegation was valid. Large projects were accomplished by using several contractors from the appropriated fund T&M trade contracts. For example, a Garmisch project, valued at about \$123,000, used eight contracts to convert hotel rooms to administrative office space.

**Allegation 11.** The COR at Chiemsee told a contractor to falsify labor hours to compensate for higher subcontractor labor rates and to add a percentage of profit to it.

**Audit Results.** The allegation could not be evaluated. The COR stated inflating of the number of labor hours was only a suggested method to cover the subcontractors' costs. However, no documentation existed to determine the hourly rates paid. The COR approved the invoices without knowing the amount of subcontractors hours; therefore, the rate paid could not be determined. The CORs did not adequately verify hourly labor rates. Garmisch experienced the same deficiencies with at least two subcontractors. AFRC should have verified that the labor rates paid were equal to or less than the amount stated in the contract.

**Allegation 12.** Abridged specifications have been prepared by non-design personnel at Garmisch that made the contractor performance impossible and inspection work meaningless. A project to install a workshop in a maintenance building was given as an example.

**Audit Results.** The allegation was valid. A contract to install a workshop at the golf course could not be awarded because the specifications did not include adequate dimensions or materials.

**Allegation 13.** The contractors' invoices were not processed promptly by the COR.

**Audit Results.** The allegation was valid. See Finding B for further details.

**Allegation 14.** Design projects have been terminated before completion or shelved after completion. The utilities project at the Abrams Hotel in Garmisch was alleged to be illogical and wasteful. The designs were split into four contracts to avoid dollar limitations on the size of projects.

**Audit Results.** The allegation was valid. The AFRC Director of Engineering stated projects were often designed in advance and then shelved until funds became available. None of the four design contracts for the replacement of the

heating, sewer, and interior and exterior water lines at the Abrams Hotel were used. AFRC should not have awarded four separate design contracts because walls, floors, and utility lines should have been coordinated in one combined project.

The award of four designs for the replacement of the plumbing and heating lines at the Abrams Hotel was illogical and cost about \$118,000 of appropriated funds. There was a \$75,000 limitation on design projects. See Finding B for further details on design projects.

**Allegation 15.** The COR failed to adequately track costs and spent more than was authorized on some contract line items.

**Audit Results.** The allegation was valid. The COR at Chiemsee exceeded at least 1 contract line item in all 12 of the appropriated fund T&M trade contracts reviewed although none of the contracts exceeded the total amounts of the contract. The COR at Garmisch exceeded at least 1 contract line item in 11 of 14 appropriated fund T&M trade contracts. Furthermore, two of the contracts exceeded the ceiling amounts and were subsequently ratified by the U.S. Army Contracting Command-Europe.

**Allegation 16.** The COR at Chiemsee was not aware of the contract terms for an indefinite-delivery type grounds maintenance contract. Also, delivery orders on the grounds maintenance contract were never issued before performance but were issued after the completion of work.

**Audit Results.** The allegation was partially valid. Delivery orders had incorrect pricing data because the COR and the ordering officer failed to verify delivery orders against the contract line item. The facility manager stated that about 25 percent of the 16 delivery orders were signed after the work had started. The ordering officer relied on the contractor invoice to prepare the delivery orders. The contractor used estimates to determine requirements instead of the actual work needed. Therefore, some delivery orders were incorrect and required modification when the estimated work did not match the actual work performed. In addition, not all delivery orders were correctly modified.

**Allegation 17.** The COR at Chiemsee permitted contractors 10-percent increases to their estimates without justification.

**Audit Results.** The allegation was valid; however, the practice was discontinued in September 1992 when the COR became aware that one contractor consistently submitted invoices 10 percent above estimates. The total amount of the cost overruns was unknown.

Generally, estimates were not prepared if a job was estimated at less than 2,000 Deutsche Marks. Alternatively, if the estimate or job was more than 2,000 Deutsche Marks, the contract required COR approval before proceeding. In either case, the contractor was responsible for the estimate. The Chiemsee COR permitted variances of up to 10 percent from the estimate without approval to allow for unexpected events. See Finding B for further details.

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## **Appendix B. Summary of Prior Audits and Other Reviews**

### **Inspector General, DoD**

Report No. 93-023, "Time and Materials Billings on Air Force Contract F33600-86-D-0295," November 13, 1992. The report stated that the contracting officer awarded a contract that did not define the limits of the T&M contract line items. The scope of the contract was left to the interpretation of each user. The report recommended that the Air Force establish specific procedures to strengthen internal controls for the award, administration, and funding of Air Force contracts. The report also recommended that the Air Force make appropriation adjustments and report any funding violations to the appropriate authorities. The Air Force concurred with the recommendations and initiated corrective actions.

Report No. 91-030, "Justification for Use of Time-and-Materials Contracts," January 8, 1991. The report stated that contracting officers failed to consider available historical cost and performance data when awarding contracts. Also, contracting officials did not perform effective surveillance of contractors performance or costs and did not ensure that contracts were properly paid. The report recommended that management implement and strengthen internal controls of surveillance and payments of T&M contracts. Management generally concurred with the recommendations.

Report No. 91-010, "Administration of Time-and-Materials Contracts at the U.S. Army Troop Support Command," November 7, 1990. The report stated that the contracts required the contractor to purchase nonexpendable equipment, thereby circumventing the normal procurement process and competition. The COR was not assigned to perform contract surveillance or request assistance. Army Troop Support Command paid at least \$145,552 for contractor personnel who did not possess the qualifications required by the contract. The report recommended that the commander assign a COR to monitor the contractor's performance and obtain a refund for overpayment. The U.S. Army Contracting Support Agency concurred with the recommendations.

Report No. 90-084, "Report on the Audit of Architect-Engineer Contracting at Ramstein Air Base," June 14, 1990. The report identified internal control weaknesses involving separation of duties, supervision, execution of transactions, documentation, and noncompliance with regulatory requirements for the award, administration, and completion of contracts. The report recommended 17 procedures for improving internal controls. The Air Force generally concurred and implemented the recommendations.

## Army Audit Agency

Report No. WR 93-805, "Appropriated Versus Nonappropriated Fund Support," July 8, 1993. The report identified that proper funds were not used to support morale, welfare, and recreation activities. About \$5.2 million of appropriated funds were incorrectly used and not reimbursed. The report stated that recurring and routine maintenance on Category C facilities should be paid for with nonappropriated funds. However, appropriated funds were incorrectly used to repair sliding doors, to unclog sinks, and to cut keys. The report further stated that policies and procedures detailing the amount and type of base support were inconsistently applied. The managers also did not ensure that the internal controls were in place and working. The report recommended that the nonappropriated funds reimburse appropriated funds for the labor, supply, and equipment repair, and repair and maintenance support. The report also recommended that appropriated fund program be reviewed, budgeted, and that guidance should be clarified and reissued. The Assistant Secretary of the Army (Manpower and Reserve Affairs) and CFSC agreed with the recommendations.

Report No. NR 93-802, "Contracting Operations - Armed Forces Recreation Center Europe," June 30, 1993. The report stated that AFRC generally did not implement nonappropriated fund contracting policies and procedures effectively, purchases were not adequately controlled, CORs did not effectively monitor service and concession contracts, and AFRC's implementation of the Army's internal management control program was not effective. The report recommended increased use of comparisons and competition, controls on the ordering and shipping of goods, preparation and use of surveillance systems, evaluation of inspection systems, and refresher training for CORs on the preparation and certification of invoices. All recommendations were linked to supervisory and major command oversight. CFSC concurred with the recommendations.

## KPMG Peat Marwick

"Armed Forces Recreation Center-Europe - Nonappropriated Funds Financial Statements for the Year ended September 30, 1992," April 15, 1993. The report provided an unqualified opinion on the financial statements for FY 1992. The audit reported revenues of \$15.8 million and a net loss of \$0.37 million for FY 1992.

The report disclosed that AFRC depends on appropriated fund support for its continued operations; the notes to the financial statements stated that AFRC received \$12.3 million of appropriated fund support in FY 1992. However, AFRC management expects that AFRC will be able to continue without appropriated fund support by operating with fewer employees and by increasing rates charged for services provided. The notes also refer to an audit being conducted by the Office of the Inspector General, DoD (the notes were referring to this audit report). The notes state that approximately \$200,000 of

## **Appendix B. Summary of Prior Audits and Other Reviews**

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appropriated fund expenditures are being questioned; however, AFRC "Management believes that it unlikely that AFRC-Europe will be required to repay any questioned amounts with nonappropriated funds."

### **Pannell, Kerr, Forster**

"Evaluation of the Army Management Structure of the Armed Forces Recreation Center in Germany," April 29, 1984. The report stated that the AFRC organization structure was not suited for a hospitality business and its facilities were old and in poor condition. The report also identified the amount and type of funds used to support AFRC. This evaluation concluded that AFRC received a disproportionate amount of appropriated fund subsidy and was not self-sufficient or cost-effective.

The report also stated that the Army regulations were unclear and resulted in contradictory interpretations when determining whether appropriated fund support was authorized. Further, AFRC guidance provided no direction or incentive for the management of morale, welfare, and recreation facilities to reduce appropriated fund support.

The main recommendations included the establishment of one command for AFRC, refurbishment of the hotel rooms in Chiemsee, and construction of a multi-purpose facility in Garmisch to replace the outdated, inefficient facilities. Army established CFSC to provide command support for AFRC and the rooms at Chiemsee were refurbished. However, the construction of the multi-purpose facility at Garmisch was stopped after the foundation and parking garage were constructed.

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## Appendix C. Summary of Potential Benefits Resulting From Audit

Recommendation Reference	Description of Benefit	Amount and/or Type of Benefit
A.1.	Economy and Efficiency. Reduces appropriated fund subsidized support.	Undeterminable. Some elements of expense are still allowed appropriated fund support for Category C activities.
A.2.	Economy and Efficiency. Reduces appropriated fund subsidized support of NAF activities.	Undeterminable. The review of the other elements of expense will determine the monetary amount.
A.3.a.	Economy and Efficiency. Reimburses appropriated funds by NAF.	Questioned costs of \$735,382 for FY 1991 and \$867,576 for FY 1992 of Operations and Maintenance, Army, funds.
A.3.b. and A.4.a.	Compliance. Provides guidance and helps verify the proper use of appropriated funds.	Undeterminable. The number and amount of future projects are unknown.
A.4.b.	Internal Controls. Establishes procedures and controls for proper classification of work.	Undeterminable. The number and amount of future projects are unknown.

## Appendix C. Summary of Potential Benefits Resulting From Audit

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Recommendation Reference	Description of Benefit	Amount and/or Type of Benefit
B.1., B.3.c., and B.3.d.	Economy and Efficiency. Reduces the use of appropriated funds and reduces outdated and unused designs.	Undeterminable because the number of future projects cannot be quantified.
B.2.	Economy and Efficiency. Reduces inefficient use of appropriated funds.	Undeterminable because the future efficiency of AFRC operations will determine the monetary benefits.
B.3.a., B.3.b., B.3.e., B.3.f., and B.3.h.	Internal Controls. Reduces the potential for fraud, waste, and abuse.	Undeterminable. Prevention of fraud, waste, and abuse will have continual future monetary benefits.
B.3.g.	Internal Controls. Reduces the potential for fraud, waste, and abuse by separating key administrative functions.	Undeterminable. Prevention of fraud, waste, and abuse will have continual future monetary benefits.
B.4.	Compliance. Improves AFRC contracting procedures and contract administration.	Undeterminable. Prevention of fraud, waste, and abuse will have continual future monetary benefits.
C.1., C.2., and C.3.	Economy and Efficiency. Determines whether AFRC is the most cost-effective operation to provide recreational services.	Undeterminable. The study and review are required to determine the monetary amount.

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## **Appendix D. Organizations Visited or Contacted**

### **Office of the Secretary of Defense**

Assistant Secretary of Defense for Personnel and Readiness, Washington, DC  
Deputy Director (Foreign Contracting), Office of the Director of Defense Procurement,  
Washington, DC

### **Department of the Army**

Assistant Secretary of the Army (Research, Development, and Acquisition),  
Washington, DC  
Office of the Administrative Assistant, Washington, DC  
U.S. Army, Europe, Heidelberg, Germany  
Inspector General, Heidelberg, Germany  
U.S. Army Contracting Command Europe, Heidelberg, Germany  
Regional Contracting Office, Fuerth, Germany  
U.S. Army Audit Agency Frankfurt, Germany  
Second Region, U.S. Army Criminal Investigation Command, Mannheim-Seckenheim,  
Germany  
Criminal Investigation Division, Augsburg, Germany  
U.S. Army Corps of Engineers, European Division, Frankfurt, Germany  
U.S. Army Center for Public Works, Fort Belvoir, VA  
Headquarters U.S. Army Community and Family Support Center, Alexandria, VA  
Armed Forces Recreation Center, Garmisch, Germany  
Armed Forces Recreation Center, Chiemsee, Germany

### **Defense Organization**

U.S. European Command, Stuttgart, Germany

### **Non-Defense Organizations**

General Accounting Office, Washington, DC  
European Office, Frankfurt, Germany

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## **Appendix E. Report Distribution**

### **Office of the Secretary of Defense**

Under Secretary of Defense for Acquisition and Technology  
Director of Defense Procurement  
Deputy Director (Foreign Contracting)  
Assistant Secretary of Defense for Personnel and Readiness  
Comptroller of the Department of Defense

### **Department of the Army**

Secretary of the Army  
Assistant Secretary of the Army (Financial Management)  
Assistant Secretary of the Army (Manpower and Reserve Affairs)  
Assistant Secretary of the Army (Research, Development, and Acquisition)  
Office of the Administrative Assistant  
Commander in Chief, U.S. Army, Europe  
Commander, U.S. Army Contracting Command, Europe  
Chief, Regional Contracting Office Fuerth  
Commander, Second Region, U.S. Army Criminal Investigation Command,  
Mannheim-Seckenheim, Germany  
Director, U.S. Army Center for Public Works  
Commander, U.S. Army Community and Family Support Center  
General Manager, Armed Forces Recreation Center-Europe  
Auditor General, Department of the Army

### **Defense Organization**

Commander in Chief, U.S. European Command

### **Non-Defense Federal Organizations**

Office of Management and Budget  
National Security and International Affairs Division, Technical Information Center,  
General Accounting Office

Chairman and Ranking Minority Member of Each of the Following Congressional  
Committees and Subcommittees:

Senate Committee on Appropriations  
Senate Subcommittee on Defense, Committee on Appropriations  
Senate Committee on Armed Services

Senate Committee on Governmental Affairs  
House Committee on Appropriations  
House Subcommittee on Defense, Committee on Appropriations  
House Committee on Armed Services  
House Subcommittee on Oversight and Investigations, Committee on Armed  
Services  
House Subcommittee on Readiness, Committee on Armed Services  
House Committee on Government Operations  
House Subcommittee on Legislation and National Security, Committee on  
Government Operations



## **Part IV - Management Comments**

# Assistant Secretary of Defense for Personnel and Readiness Comments

Final Report  
Reference



PERSONNEL AND  
READINESS

THE OFFICE OF THE ASSISTANT SECRETARY OF DEFENSE

4000 DEFENSE PENTAGON  
WASHINGTON DC 20301-4000



FEB 10 1994

MEMORANDUM FOR DIRECTOR, CONTRACT MANAGEMENT, DOD IG

SUBJECT: Draft Audit Report on Armed Forces Recreation Center, Europe (Project No. 2CK-0066.01)

We have reviewed the draft report and provide the following comments for OASD(P&R):

**Recommendation 1, Finding A, Use of Appropriated Funds**, suggests treating the Armed Forces Recreation Center, Europe, as one entity and classifying all its activities and departments in Category C. This recommendation is at variance with a fundamental principle of the morale, welfare and recreation program: the Department's construction, operating, and funding policies advocate using a single entity to provide multiple services and activities. To foster the capability and assure the proper use of appropriated and nonappropriated resources, funding authority is based on the service or activity provided – not the provider. We agree that the policy is unclear and recommend further clarification of the policy for classifying the activities and departments in the Armed Forces Recreation Center, Europe.

**Recommendation 1, Finding B, Work Management and Contract Internal Controls**, is a proposal to prohibit appropriated fund support for architectural and engineering (A&E) services. The DoD Directive 1015.6 "Funding of Morale, Welfare, and Recreation Programs" authorizes appropriated funding of A&E services, regardless of category, for "construction, alteration, and repair projects." We assert that the central issue is to distinguish those projects eligible for A&E from routine maintenance and repair. Instead of generally prohibiting appropriated funding for A&E services, we recommend improving the policy definition of "construction, alteration, and repair projects" in the next update of DoD Directive 1015.6.

We agree with **Recommendation 2, Finding C, Subsidized Operations**. The economic analysis on the Armed Forces Recreation Center, Europe, will be reviewed within 90 days of receipt.

If you have questions or need more information, please call Ms. Janis M. White, 697-7197.

Lester K.C. Chang  
Colonel (S), USAF

Acting Director, Personnel Support Policy and Services  
(Personnel Support, Families and Education)

Revised  
Recom-  
mendation 1  
Page 16

# Department of the Army Comments



REPLY TO  
ATTENTION OF

DEPARTMENT OF THE ARMY  
U.S. ARMY COMMUNITY AND FAMILY SUPPORT CENTER  
ALEXANDRIA, VA 22331-05



February 18, 1994

MEMORANDUM THRU ASSISTANT CHIEF OF STAFF FOR *John*  
INSTALLATION MANAGEMENT *2/18/94*

~~DIRECTOR OF THE ARMY STAFF D/IS~~  
~~ASSISTANT SECRETARY OF THE ARMY~~  
~~(MANPOWER AND RESERVE AFFAIRS)~~ *TAN* *18 FEB 94*

FOR THE INSPECTOR GENERAL, DEPARTMENT OF DEFENSE

SUBJECT: Working Final Inspector General, Department  
of Defense (DODIG) Audit Report, Armed Forces  
Recreation Center-Europe (AFRC-E), Project  
2CK-0066.01 -- INFORMATION MEMORANDUM

The Army response to the subject report is enclosed at TAB A. In our opinion, there is no need to classify or protectively mark any portion of this report.

AFRC-E activities promote the physical and mental well being of USAREUR soldiers and support the accomplishment of the basic military mission. AFRC-E also has a war time mission as a rest and recuperation site. As such, AFRC-E activities are authorized appropriated fund (APF) support in accordance with Army policy delineated in the AR 215 series. We agree that this policy requires revision to ensure the guidance is clear and concise. To that end, the Army is revising the AR 215 series.

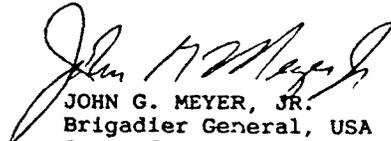
We disagree with the DODIG conclusion that \$1.6M of appropriated funds were erroneously used for maintenance and repair of AFRC-E facilities. The decisions to expend these funds were based on judgment or interpretation of policy that is not clear. We acknowledge that a small amount of appropriated funds were used improperly. However, we nonconcur with the DODIG recommendation to reimburse the appropriated fund account. The Assistant Secretary of the Army (Financial Management) will review the \$1.6M. Based on his findings, appropriate action shall be initiated against the individuals responsible for the improper expenditures.

- 2 -

We also agree that work management and contracting controls need improvement. While several examples used to support the finding require explanation, the Army will take action to correct contract administration deficiencies.

Lastly, we agree that the AFRC-E was not self-sustaining without APF support. This is as intended. Unlike the Dragon Hill Lodge and the Hale Koa Hotel, the AFRC-E concept, mission, and activities are broader in scope. Programs and activities are not categorized as an organizational entity, but receive APF and NAF support based on the functions or services provided. AFRC-E is authorized funding as similar installation MWR programs. However, because of self-sufficiency objectives and limited resources, the Army directed that APF support be the minimal essential. Beginning in FY 1995, AFRC-E will be limited to APF support to fund only utilities, maintenance and repair.

The Army recognizes the need for continuing oversight of the AFRC system. As a result, the Department of the Army Inspector General is planning regular oversight reviews of all AFRC operations.

  
JOHN G. MEYER, JR.  
Brigadier General, USA  
Commanding

Enclosure

**Army Response to  
Draft DODIG Audit Report of  
Armed Forces Recreation Center, Europe (AFRC-E)**

**Finding A: Use of Appropriated Funds.** AFRC incorrectly used appropriated funds to maintain, clean, and improve the Garmisch and Chiemsee facilities. The incorrect use of appropriated funds was caused by an insufficient priority on controls for appropriated fund contracts, unfamiliarity with regulations, and unclear guidance. As a result, AFRC incorrectly used about \$1.6 million of the \$3.1 million appropriated funds reviewed for NAF expenses.

**Army Response. Additional Facts:** The need for revising Army policy to clarify guidance should have been the major thrust of this finding. Instead, the DODIG placed greater emphasis on the incorrect use of \$1.6 million of appropriated funds (APF), which was based upon their interpretation of the intent of Army policy, rather than on definitive criteria. Our comments on specific items within the finding follow:

**Management Priority.** It is neither an Army policy nor a management priority to place profitability above regulatory requirements. Both AFRC-E's mission statement and the Army's response to Finding C support this position. The DODIG position in this finding (internal control) is directed towards the problem of conflicting interpretations of unclear Army policy. We agree that this is the root cause of the alleged incorrect use of appropriated funds.

**Regulations.** The DODIG referenced Army Audit Agency Report, WR 93-805, "Appropriated Versus Nonappropriated Fund Support", 8 July 1993. This Army Audit report supported our position on unclear Army guidance:

"The guidance in appendix C, AR 215-1 doesn't clearly state what type of base support is authorized and what must be reimbursed. Personnel at all the installations reviewed were confused about which expenses should be reimbursed and which should not."

**Questioned APF Support.** The statement on page 7 of the report relating to the other \$26.6 million in APF expense implied that this figure had a direct relationship to \$3.1 million of APF contracts reviewed. Therefore, additional amounts of APF support funds appear to be suspect based on the deficiencies cited in the report. We believe this statement is misleading because the elements of expense on the \$26.6 million were not directly related to the T&M trade contracts reviewed by the DODIG.

Revised

## Department of the Army Comments

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Final Report  
Reference

Incorrect Use of APF. We disagree with the \$1.38 million cited on page 11 of the report. AFRC-E agreed to the incorrect use of \$9,334, not \$312,000. We do not agree with the DODIG conclusion about the remaining \$1 million that was allegedly incorrectly used. It was based on interpretation of AR 215-1 and AR 215-2 by the DODIG and a representative from the U.S. Army Center for Public Works (CPW), rather than on definitive guidance. We agree that Army policy language is open to interpretation as illustrated by the DODIG comments under Contrasting Interpretations on page 10 of the report. However, Army's position and Management's goal remains to use good judgement and care in the selection of APF for repair and maintenance.

Reference DODIG comments on page 12 concerning AFRC-E personnel noncompliance with AR 420-10 or the CPW's guidance. It is AFRC-E policy to utilize the CPW when clarification on the proper use of funds is required. DODIG comments imply that the CPW had developed supplemental guidance to AR 215-1 and AR 215-2. This was not true according to representatives from CPW. The only information available regarding APF expenditures were DA regulations. CPW guidance was developed well after the APF expenditures occurred.

The statement on custodial contracts on page 13 of the report does not recognize Army policy on outdoor recreation. AR 215-2, para 5-32, authorizes APF support for AFRC-E. Categories A, B or C can be applied to recreational services within AFRC-E if the policy criteria is met. At the time of the audit, Army policy in Appendix E to AR 215-2, established the AFRC-E campground as a Category B activity. The issue is the policy, itself. Similar disagreement and confusion of interpretation exists on policy for other outdoor recreation services.

In summary, the conceptual definition of maintenance as discussed on page 11 of the report needs clarification since it related to the whole interpretation problem. According to the CPW, the word "routine" is an adjective used to describe the nature of maintenance and repair, but in reality it does not have a formal definition. A distinction between "routine" and "non-routine" maintenance and repair does not exist. The formal definitions for maintenance and repair are in AR 420-10.

### Recommendations for Corrective Action

**RECOMMENDATION A-2.** We recommend that the Assistant Secretary of the Army (Financial Management) determine whether unauthorized appropriated funds were spent for Armed Forces Recreation Center Garmisch and Chiemsee facilities. The determination should include the estimated \$26.6 million of appropriated fund expenses not reviewed by our audit for FYs 1991 through 1993. The

unauthorized amount should be identified and reimbursed to the proper Operations and Maintenance, Army, appropriation.

**ARMY REPLY:** Concur in principle. The Army will continue to take a hard look to determine the best way to provide support to the military, based on the current readiness posture. The Army will conduct a review of the elements of expense that comprise the \$26.6 million and of Army regulations 215-1 and 215-2. The review will also identify what activities should be provided, and at what cost, to our soldiers. Although we acknowledge that a small amount of appropriated funds were used improperly, there is no mechanism available to restore those funds into the proper Operations and Maintenance, Army, appropriation. Further, to reimburse the Government by depositing nonappropriated funds in the general fund (miscellaneous receipts) penalizes soldiers and their families by taking away nonappropriated funds earmarked for morale, welfare and recreation programs. Target date: 30 September 1994.

**RECOMMENDATION A-3a.** Repay \$1,602,958 of nonappropriated funds to the Operations and Maintenance Army appropriation. The amounts that should be repaid are \$747,067 for FY 1991 and \$855,891 for FY 1992.

**ARMY REPLY:** Nonconcur. The \$1.6 million in question had undergone a detailed review jointly by Armed Forces Recreation Center, Europe management and the DODIG as part of the audit process. As a result of that review, the Armed Forces Recreation Center, Europe agreed that only \$15,659 was incorrectly used. The disagreement in the amounts (\$1,602,958 versus \$15,659) is due to differences in the interpretation of Army policy by the DODIG and the U.S. Army Community and Family Support Center. The ASA(FM) will conduct an independent review of the disputed use of APF. Based on his findings, appropriate action shall be initiated against individuals responsible for the improper expenditures. As discussed in our response to Recommendation A-2 above, the Army will not direct any reimbursement from nonappropriated funds. Target date: 30 September 1994.

**RECOMMENDATION A-3b.** Request the U.S. Army Center for Public Works to rewrite the maintenance and repairs element of expense in Appendix C of Army Regulation 215-1, update 16, "The Administration of Army Morale, Welfare and Recreation Activities and Nonappropriated Fund Instrumentalities." The terms life safety, structural and operational integrity, and installed building equipment should be specifically defined.

**ARMY REPLY:** Concur. The Assistant Chief of Staff for Installation Management will be requested to revise the section of Appendix C of AR 215-1 update 16 relating to the overall issue

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on the use of appropriated funds for maintenance and repair of grounds and facilities. The required changes will be incorporated into the next regulation update. Target date: 4th quarter, FY94.

**RECOMMENDATION A-4a.** Discontinue the use of appropriated funds for recurrent, day-to-day, periodic, and scheduled maintenance and repair work for Category C activities.

**ARMY REPLY:** Concur. The expenditure of appropriated funds for recurrent, day-to-day, periodic, and scheduled maintenance and repair work will be in accordance with the guidance published in AR 215-1, and the categorization of the activity being serviced. Action has been completed as of the date of our response.

**RECOMMENDATION A-4b.** Establish procedures and controls requiring the Armed Forces Recreation Center, Europe, Engineering Department to ask the U.S. Army Center for Public Works for work classification determinations.

**ARMY REPLY:** Concur in principle. Guidance published in AR 420-10 for work classification will be followed. It is policy within the U.S. Army Community and Family Support Center and AFRC-E, that if there is doubt regarding the classification of work to be accomplished, the Assistant Chief of Staff for Installation Management has and will be consulted.

**Finding B: Work Management Controls.** AFRC and the contracting offices did not have adequate work management and contract internal controls. Inadequate controls were caused by AFRC management belief that supervision, separation of duties, and documentation of work management and contracts were not high priority. As a result, AFRC personnel improperly managed at least \$3.7 million of appropriated fund contracts and did not follow facility management and contract administration regulations. In addition, the Regional Contracting Office personnel awarded inefficient contracts and did not follow contract award and contract administration regulations.

**Army Response. Additional Facts:** The Army agrees that work management controls and contracting controls need improvement, but takes exception to several examples used to support that finding:

**Golf Course Clubhouse.** We do not agree with the finding that AFRC-E "needed" to use appropriated funds to avoid the \$500,000 NAF funding limitation (page 19 of the report). The project cost was not \$529,000. The DODIG included \$32,224 in architectural and engineering design cost as part of the project cost. Both AR 420-10 para. 3-5 and AR 415-35 para. 2-2b(5) have classified design work as unfunded cost. This cost should not be considered when computing the total project cost for use in determining the regulatory funding threshold limitation(s). Since the total project cost at the contract award date was only \$428,749, it was unnecessary to consider the \$500,000 NAF funding limitation. This amount included \$137,000 NAF utilities upgrade which was for new work and could stand alone as a separate project. Final contract cost, including work modifications, was \$496,776. Appropriated funds were selected based on specific guidance contained in Update 16 to AR 215-1, effective 10 October 1990, which authorized appropriated funds for repair projects. Since Update 15 was unclear on this issue, NAF funds had initially been selected for use.

**Kitchen Project.** The Army understands that the contract award in September 1992 raises an appearance of impropriety. However, the contract requirement was a bona fide need at the time, and AFRC-E management had no reason to suspect that construction startup would be delayed five months. DODIG's assumption that the contract should be cancelled relies on hindsight. Mitigating factors against cancellation include escalating construction costs, and time and labor expenses associated with resolicitation.

**Architectural Services.** Reference the statement relating to inadequate planning on page 20 of the report. Normal engineering practices, per para.4-13, Technical Note 420-10-01, provide for early completion of the design work to be shelved while waiting for funds in the near future. Upon availability of funds, the projects can be quickly executed because the long lead time for

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the contracting, designing and reviewing process has been eliminated. When the design projects were approved, there was no indication of the severity in appropriated fund cutbacks forthcoming for construction support in Europe. Although these projects had to be placed on hold, they are still valid requirements.

We believe the statement that the AFRC-E Director of Engineering explained that design contracts were awarded to prevent the expiration of appropriated funds is a misinterpretation. At no time did the director imply this to be the case.

Contract Controls. On page 22 of the report, comment is made that legal counsel termed the proposed contract award to be "totally inadequate". The specifications initially submitted to the RCO, Fuerth were termed "totally inadequate" by legal counsel until changes to the specifications were made, whereupon legal counsel determined the contract award to be legally sufficient. Therefore, the comments addressing legal counsel's review are incorrect.

Recommendations for Corrective Action

**RECOMMENDATION B-2.** We recommend that the Commander, U.S. Army Community and Family Support Center, establish procedures for periodic reviews of the operations of the Armed Forces Recreation Center, Europe Engineering Department for compliance with applicable guidance.

**ARMY REPLY:** Concur. Assistant Chief of Staff for Installation Management team together with the appropriate USAREUR staff elements, will make an assessment during FY94 of engineering support activities at both the Armed Forces Recreation Center, Europe and the Garmisch military community. Corrective actions to address DODIG findings as well as other actions required to bring engineer support elements into compliance with applicable guidance will be identified. A schedule of periodic reviews by USAREUR and HQDA will be established.

**RECOMMENDATION B-3a.** Prepare installation master plans, unconstrained requirements reports, resource management plans, and annual work plan as required.

**ARMY REPLY:** Concur. Procedures will be implemented to ensure that the required installation master plans, unconstrained requirements reports, resource management plans, and annual work plan are developed in compliance with applicable Army requirements. Target date: 30 September 1994.

**RECOMMENDATION B-3b.** Authorize contract funds for individual projects only after the complete project is reviewed, approved, and budgeted.

**ARMY REPLY:** Concur. Except for authorized concept design projects, this requirement has and will continue to be Army current policy on this issue. Action has been completed as of the date of our response.

**RECOMMENDATION B-3c.** Review all Engineering Department requests and cost estimates before outside architectural and engineering services are contracted.

**ARMY REPLY:** Concur. Controls will be put in place to review engineering department requests and cost estimates for completeness prior to initiating any outside action. Target date: 2nd quarter, FY94.

**RECOMMENDATION B-3d.** Obtain estimated project costs from contracted architectural and engineering services before the pre-final phase.

**ARMY REPLY:** Concur. Procedures will be developed to require obtaining estimated costs on concept design projects prior to the execution of the pre-final phase. Target date: 30 June 1994.

**RECOMMENDATION B-3e.** Establish procedures to verify that personnel in the Engineering Department obtain the training required to meet minimum Army training goals.

**ARMY REPLY:** Concur. Action will be taken to provide adequate training to engineering personnel that will allow them to properly perform their assigned duties. The tentative target date, 30 July 1994, is contingent upon the impact recommendation B-2 will have upon the engineering operations.

**RECOMMENDATION B-3f.** Establish and implement procedures for the Resource Management Office to review and certify appropriated funded work orders.

**ARMY REPLY:** Concur. The Resource Management Office does validate and certify documents for projects, where appropriate, in accordance with AR 37-100 and AR 215-1. Action has been completed as of the date of our response.

**RECOMMENDATION B-3g.** Establish controls to separate the responsibility for inspecting contractors' work from the responsibility for ordering work.

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**ARMY REPLY:** Concur. Immediate steps will be taken to separate the inspecting and ordering duties in the performance of the contract administration duties. Target date: 31 March 1994.

**RECOMMENDATION B-3h.** Maintain adequate project files and prepare specifications and independent Government estimates for all projects greater than \$1,000.

**ARMY REPLY:** Concur in principle. Official files and prepared specifications and independent Government estimates will be maintained on maintenance and repair projects over \$50,000 in accordance with para 3-8 to AR 420-17 (Change 1). Individual work orders will be filed by project and will contain the documentation supporting the decision to perform the work along with an independent Government estimate when the cost exceeds \$1,000. Target date: 3rd quarter, FY94.

**RECOMMENDATION B-4a.** Direct the contracting officer to stop awarding or exercising options on time-and-materials contracts for the Armed Forces Recreation Center, Europe.

**ARMY REPLY:** Concur. No new T&M contracts have been written for AFRC. No additional options have been exercised. Some new contracts for Berchtesgaden have been written that contain a very small percentage of T&M features for emergency repairs. An AFRC base maintenance follow-on contract is scheduled for award in the 25 February 1994 and is expected to be transferred to Defense Contract Management Area Operations in Frankfurt by 1 April 1994. A cost-plus-award-fee contract is contemplated.

**RECOMMENDATION B-4b.** Provide adequate training to the Armed Forces Recreation Center, Europe's contracting officer's representatives in their responsibilities.

**ARMY REPLY:** Concur. If contract administration for the AFRC base maintenance follow-on contract is transferred to RCO Fuerth, training will be provided by RCO, Fuerth upon receipt of the awarded contract and the completion of a comprehensive contract administration plan. It should be noted that the HQ USAREUR/7A is pursuing transferring contract administration to the Defense Contract Management Area Operations, Frankfurt in April 1994.

**RECOMMENDATION B-4c.** Establish an acceptable contract surveillance system to include the contractor, the contracting officer's representative, and the contract administration specialists.

**ARMY REPLY:** Concur. In the event that contract administration for the AFRC base maintenance follow-on contract is transferred

**RECOMMENDATION B-3b.** Authorize contract funds for individual projects only after the complete project is reviewed, approved, and budgeted.

**ARMY REPLY:** Concur. Except for authorized concept design projects, this requirement has and will continue to be Army current policy on this issue. Action has been completed as of the date of our response.

**RECOMMENDATION B-3c.** Review all Engineering Department requests and cost estimates before outside architectural and engineering services are contracted.

**ARMY REPLY:** Concur. Controls will be put in place to review engineering department requests and cost estimates for completeness prior to initiating any outside action. Target date: 2nd quarter, FY94.

**RECOMMENDATION B-3d.** Obtain estimated project costs from contracted architectural and engineering services before the pre-final phase.

**ARMY REPLY:** Concur. Procedures will be developed to require obtaining estimated costs on concept design projects prior to the execution of the pre-final phase. Target date: 30 June 1994.

**RECOMMENDATION B-3e.** Establish procedures to verify that personnel in the Engineering Department obtain the training required to meet minimum Army training goals.

**ARMY REPLY:** Concur. Action will be taken to provide adequate training to engineering personnel that will allow them to properly perform their assigned duties. The tentative target date, 30 July 1994, is contingent upon the impact recommendation B-2 will have upon the engineering operations.

**RECOMMENDATION B-3f.** Establish and implement procedures for the Resource Management Office to review and certify appropriated funded work orders.

**ARMY REPLY:** Concur. The Resource Management Office does validate and certify documents for projects, where appropriate, in accordance with AR 37-100 and AR 215-1. Action has been completed as of the date of our response.

**RECOMMENDATION B-3g.** Establish controls to separate the responsibility for inspecting contractors' work from the responsibility for ordering work.

to RCO, Fuerth, adherence to the contract administration plan will be monitored by RCO, Fuerth, upon receipt of the awarded contract and the completion of a contract administration plan. However, HQ USAREUR/7A is pursuing transferring contract administration to the Defense Contract Management Area Operations, Frankfurt in April 1994.

**RECOMMENDATION B-4d.** Establish procedures for the contract administrators to perform periodic reviews of, or make site visits to, the Armed Forces Recreation Center, Europe.

**ARMY REPLY:** Concur. In the event that contract administration for the AFRC base maintenance follow-on contract is transferred to RCO, Fuerth, and upon receipt of the awarded contract and the completion of a contract administration plan, the administrative contracting officer will adhere to the contract administration plan, which will address periodic site visits by contract administrators as well as the procedures addressed in the recommendations below. However, HQ USAREUR/7A is pursuing transferring contract administration to the Defense Contract Management Area Operations, Frankfurt in April 1994.

**RECOMMENDATION B-4e.** Establish procedures for the contracting officer's representative to verify contractors and subcontractors charges for labor and material costs.

**ARMY REPLY:** Concur. Same comments as 4.d. above.

**RECOMMENDATION B-4f.** Establish procedures to verify that 5 percent of the labor costs on time-and-materials contracts is withheld.

**ARMY REPLY:** Concur in principle. We do not anticipate the award of a T&M contract for the AFRC follow-on base maintenance contract. A cost-plus-award-fee contract is contemplated. Target date: April 1994.

**RECOMMENDATION B-4g.** Establish procedures to verify that the contracting officer's representative process contractors' invoices within 7 days.

**ARMY REPLY:** Concur. Same comments as 4.d. above.

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**Finding C: Subsidized Operations.** AFRC was not capable of being financially self-sustaining without subsidized operations even though AFRC operated at near capacity. AFRC was not self-sustaining because the operations were not cost effective. As a result, the U.S. Government will be required to continue to provide substantial subsidies to AFRC operations until a cost effective alternative is provided.

**Army Response. Additional Facts:** AFRC-E is a quality of life and readiness enhancing program for soldiers and families. There is no requirement for AFRC-E to be financially self-sufficient without appropriated fund support. In this connection, it is the Army position to limit the profit potential (revenues) and utilize appropriated fund support to the extent authorized and available, to ensure that AFRC-E is affordable to the lower grade soldiers.

As recently as June 1993, the Army informed the HASC MWR panel of current and future AFRC-E operations including the continued use of appropriated fund support. AFRC-E is close to self-sufficient in NAF operations having attained a positive operating cash flow (net income before depreciation) since FY91. The total amount since FY91 to December 1993 is about \$3 million.

The use of 9 year old historical data to provide background information relating to AFRC-E operations does not present a true perspective on the issues dealing with financial self-sufficiency and cost effectiveness of AFRC-E operations during the audit period and beyond.

The methodology used to determine the Rooms Analysis on page 36 of the report is not complete. The subsidy expenditures should have been applied to all revenues, not limited to room revenues. By not including the other AFRC-E operations (e.g. outdoor recreation) generating the remaining 63% of revenues, any comparison made using the subsidized room costs substantially distorts the outcome as well as any conclusions based on the outcome. We recommend adjustment to reflect the other operations' revenue or deletion from the report.

The statement under Future Operations on page 37 regarding the age and condition of the existing facilities is misleading. The renovations to both Garmisch and Chiensee hotels were substantial (\$15 million in NAF) to bring them up to acceptable commercial hotel standards. These facilities are relatively new in terms of construction therefore, it's unlikely the repair and maintenance cost will escalate to maintain these facilities in the future as indicated.

We disagree with the statement on page 37 of the report that alternative recreational activities could provide comparable

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services cheaper. The analysis does not demonstrate that local and AFRC-E hotel rooms were comparable in size and amenities for cost comparison. It is also unclear whether this position makes service cheaper for soldiers or for the government. Furthermore, support was not sufficient to indicate that AFRC-E recreational services or food and beverage operations were not cost effective. AFRC-E's operational concept and the almost 50 years of Morale Welfare and Recreation programs for the soldiers, civilians and their families while assigned in Europe does not support seeking alternative recreation activities.

Recommendations for Corrective Action

**RECOMMENDATION C-1.** We recommend that the Assistant Secretary of the Army (Manpower and Reserve Affairs) determine if the existence of Armed Forces Recreation Center, Europe is necessary.

**ARMY REPLY:** Concur in principle. The Army will continue to review the best way to meet the recreational requirements of the soldier, as shown by the recent Secretary of the Army decision to return the management and operation of Berchtesgaden facilities from USAREUR to AFRC. On 16 June 1993, this decision was briefed to the House Armed Services Committee, Morale, Welfare and Recreation Panel. The Army has agreed in Recommendation C-2 to a study that meets the intent of this recommendation. The results will be presented to the Morale, Welfare, and Recreations Board of Directors.

**RECOMMENDATION C-2.** We recommend that the Assistant Secretary of the Army (Financial Management):

a. Conduct a study to determine whether the Armed Forces Recreation Center, Europe can exist as a self-sustaining business (without appropriated fund support).

b. Determine in the study whether recreational services can be provided more cost effectively by the use of local accommodations and facilities and base morale, welfare, and recreation support.

**ARMY REPLY:** Concur. The Army agrees to conduct a study which will consider current demand for the AFRC-E, the impact of changing the rate structure, and the status of comparable local competition. Target date: 1st quarter, FY95.

## **Audit Team Members**

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