Enclosure D

U.S. Virgin Islands
Virgin Islands Department of Education
Virgin Islands Department of Health
Virgin Islands Department of Human Services
Special Conditions

PREAMBLE: These special conditions are imposed on grants made available by the U.S. Department of Education (Department or ED) to the U.S. Virgin Islands (Virgin Islands), the Virgin Islands Department of Education (VIDE), the Virgin Islands Department of Health (VIDH), and the Virgin Islands Department of Human Services (VIDHS) on or after the date of these special conditions. Additionally, these special conditions apply to grant funds previously awarded by the Department to the Virgin Islands, VIDE, VIDH and VIDHS that are still available for obligation or liquidation on the date of these special conditions. These grant awards are made in accordance with the Department's regulations governing "high risk" grantees in 34 CFR 80.12, and these special conditions are imposed, as explained further below, because the Virgin Islands failed to meet key provisions of the Compliance Agreement (Agreement) between the Virgin Islands and the Department that was signed on September 23, 2002 and expired on September 23, 2005. The Virgin Islands still needs to make significant improvements in its fiscal management of Department grant funds in order to ensure compliance with Federal grant requirements and fiscal accountability. Therefore, these special conditions are imposed to help ensure that grant funds awarded by the Department to the Virgin Islands, VIDE, VIDH, and VIDHS are expended in accordance with applicable legal requirements and the appropriate fiscal accountability measures and management practices and controls.

I. BACKGROUND

As a result of serious and recurring deficiencies in the administration of ED programs by the Virgin Islands, the Department entered into a comprehensive, three-year Agreement with the Virgin Islands. Under the terms of the Agreement, the Virgin Islands agreed to develop integrated and systemic solutions to problems in managing ED funds and programs, such that there would be fiscal accountability in these programs and administration and implementation of the programs in a manner that would benefit people in the Virgin Islands, in accordance with Federal requirements.

In a letter dated March 31, 2005 from former Under Secretary Edward R. McPherson to Governor Charles W. Turnbull, the Department notified the Virgin Islands of its concerns regarding the limited progress that the Virgin Islands had made in meeting the goals of the Agreement and required the Virgin Islands to demonstrate why the Department should not begin to take immediate remedial

action under the terms of the Agreement. Based on a response from Governor Turnbull submitted by the Virgin Islands in a letter dated April 15, 2005, the Department concluded, in a June 17, 2005 letter from former Under Secretary McPherson that the Virgin Islands had failed to meet on a timely basis key terms and conditions of the Agreement that are critical to successful compliance and would not be able to meet all of the terms and conditions by the time the Agreement ended on September 23, 2005. In particular, there was a significant lack of progress on the part of the Virgin Islands in developing and implementing a credible central financial management system (FMS) – the cornerstone of the Virgin Islands' financial management improvements that are critical to its ability to manage ED funds consistent with applicable Federal regulations concerning fiscal accountability and funds management. Therefore, in accordance with section II.A. of the Agreement concerning the application of additional special conditions, the Department notified the Virgin Islands that it would apply special conditions to the Virgin Islands' grant awards requiring the Virgin Islands to procure the services of a third party fiduciary agent, acceptable to the Department, to perform the financial management duties required under Federal regulations for all Department grant awards made to the Virgin Islands, except as otherwise noted. These conditions are set forth in further detail below. Because the Virgin Islands has not met the requirements in Part 80 of the Education Department General Administrative Regulations (EDGAR) regarding the management of ED funds by States, these special conditions require the Virgin Islands to comply with those provisions of Part 80 applicable to grantees other than States (such as, but not limited to, section 80.20(b) of EDGAR), which set forth more specific requirements for the financial management of ED funds.

II. SPECIAL CONDITIONS

A. Requirement for Third Party Fiduciary Agent

On August 25, 2006, the Virgin Islands entered into a contract with a third party fiduciary agent, Alvarez & Marsal (Agent), approved by the Department, as required by the special conditions imposed on ED grants awarded to the Virgin Islands in September 2005. The Virgin Islands must maintain this contract with the Agent, and the Agent must perform the financial management duties currently performed by the Virgin Islands Department of Finance (VIDF), the Virgin Islands Department of Property and Procurement (VIDPP), and the Governor's Office, required under 34 CFR Parts 75, 76, and 80 for all grants awarded by the Department to the Virgin Islands on or after the date of these conditions, and for all grants previously awarded by the Department to the Virgin Islands that are still available for obligation or liquidation on the date of these special conditions, and under the terms and conditions specified in the grant awards, except as otherwise noted herein.

Additionally, the Agent must perform a more limited scope of financial management duties, as described in section II.C.2. below, for grants awarded by

the Department to VIDH under Part C of the Individuals with Disabilities Education Act (IDEA Part C). The Department's IDEA Part C grant awards to VIDH for FFYs 2001, 2002, 2003, 2004, 2005, and 2006 were awarded subject to special conditions that require a third party fiduciary contract, originally executed in June 2002, between VIDH and Lutheran Social Services (LSS).

The Virgin Islands, VIDE, and VIDHS agree that by accepting grant awards in accordance with the terms of these special conditions, the Virgin Islands, VIDE, and VIDHS may not draw down funds under the grants until such time as the Virgin Islands and the Agent have met the requirements of section II.D below (Drawdown of Funds).

B. Qualifications of Third Party Fiduciary Agent

The Virgin Islands, VIDE, VIDH, and VIDHS must ensure that the Agent continues to:

1. Have a sufficient number of personnel available with the skills and expertise in financial management functions necessary to perform the required financial management services for the ED grants awarded to the Virgin Islands, VIDE, VIDH, and VIDHS.

2. Be able to, and agree to, scale up operations to accommodate any increase in workload, whether long- or short-term, as a result of becoming the Agent.

C. Responsibilities of Third Party Fiduciary Agent, the Virgin Islands, VIDE, VIDH, and VIDHS

The Virgin Islands, VIDE, VIDH, and VIDHS must ensure that the following roles and responsibilities are carried out:

1. The Agent's role encompasses financial management responsibilities concerning the grants, including, but not limited to, processing payments and disbursements, maintaining financial records, financial reporting, and other duties as more fully described below. The Virgin Islands, VIDE, and VIDHS remain responsible for the provision of program services under the grants, including the review and approval of local educational agency (LEA) applications for subgrants under formula grant programs, determination of LEA allocations, and notification to the LEAs regarding their allocations under the grants.

2. For purposes of the IDEA Part C FFY 2004, 2005, and 2006 grants, the Agent is responsible only for the property procurement and management functions that are required to be performed under EDGAR at 34 CFR Part 80 (including 34 CFR 80.31, 80.32, 80.33 and 80.36(b) through (j)) by VIDPP, and any financial management functions needed to be performed by VIDF for the

IDEA Part C grants, and which are not being performed already under the contract between VIDH and LSS. Because VIDH's IDEA Part C grants for FFYs 2001 through 2006 include special conditions requiring the use of a third party fiduciary agent (LSS) that carries out VIDH's financial management and recordkeeping responsibilities in accordance with the applicable provisions of IDEA Part C and EDGAR, the Agent performing services under these special conditions is not required to assume responsibilities other than the responsibilities described above in this subsection. VIDH's IDEA Part C FFY 2004, 2005, and 2006 grant awards shall continue to include special conditions requiring the use of its third party fiduciary agent (LSS) for continued fiscal accountability and provision of services. In addition, VIDH's IDEA Part C grant funds must not be used to pay any costs charged by the Agent to the Virgin Islands.

3. At the beginning of the contract period and prior to any drawdowns or disbursements, the Virgin Islands, VIDE, or VIDHS must provide the Agent with a line item budget for the total amount of each grant and subgrant, if applicable, including amounts for State administration, State-level program activities, and LEA program activities. For purposes of the Consolidated Grant to Insular Areas (Consolidated Grant), the Virgin Islands and VIDE must provide the Agent with line item budgets for each of the programs under which the Virgin Islands and VIDE will use Consolidated Grant funds. The line item budget for each of these programs must be based on the total amount of Consolidated Grant funds to be used for each program and include amounts for State administration, State-level program activities, and LEA program activities. The Agent must use these line item budgets to track projected and actual expenditures for the programs under the grants. The Agent must ensure that the expenditures proposed are only for allowable purposes under each grant.

4. The Agent must establish, maintain, and manage a separate bank account for all of the funds under the grants from the Department. The Agent must provide the Virgin Islands, VIDE, and VIDHS, as appropriate, with written notice (e.g., copy of invoice) of when funds are needed for a disbursement under a particular grant. The Virgin Islands, VIDE, and VIDHS are responsible for: (i) executing their respective drawdowns of funds under the grants from the Department's Grant Administration and Payment System (GAPS) so that funds are deposited into the separate bank account established and maintained by the Agent; and (ii) providing to the Agent, for deposit into the separate bank account established by the Agent, any matching funds required for the grants. The Virgin Islands, VIDE, and VIDHS understand and agree that they must draw down funds and provide all matching funds to the Agent within 24 hours of receipt of the written notice from the Agent. Failure by the Virgin Islands, VIDE, or VIDHS to comply with this condition concerning the time within which they must draw down funds may result in the Department requiring the transfer of drawdown authority to the Agent for

that entity. In the event of the Virgin Islands', VIDE's, or VIDHS' failure to draw down funds in accordance with this condition, the Agent must notify the Department, and the Department will determine whether drawdown authority must be transferred to the Agent. If so, then immediately upon written notice of this decision from the Department, the Virgin Islands, VIDE or VIDHS, as appropriate, must take all steps necessary to provide the Agent with full authority to perform drawdowns, including providing any information and authorization that the Department needs to recognize the Agent as the entity with drawdown authority.

5. The Agent must use fiscal control and accounting procedures that meet the requirements imposed on non-State governmental grantees in accordance with 34 CFR 80.20(b) and 80.21.

6. The Agent must permit funds to be spent only for allowable costs of programs under the grants, in accordance with 34 CFR 80.22. Additionally, for purposes of the Consolidated Grant, the Agent must permit funds to be spent only for allowable costs under, and included in, Department-approved FFY 2004, 2005, and 2006 Consolidated Grant plans.

7. The Agent must determine the value of any in-kind property or services donated to or provided by the Virgin Islands, VIDE, and VIDHS that are used to meet cost sharing or matching requirements as required by 34 CFR 80.24 and must maintain records sufficient to document the bases for those valuations.

8. The Agent must take steps to prevent the lapsing of funds available under the grants, including ensuring timely disbursement of funds through the use of methods and procedures for payment that minimize the time elapsing between the transfer of funds and disbursement, in accordance with Treasury regulations at 31 CFR Part 205, as required by 34 CFR 80.21(b). For grant funds not included in the Virgin Islands' Treasury-State agreement, the Agent must meet the requirements in 34 CFR 80.20(b)(7). The Virgin Islands, VIDE, VIDHS, and the Agent must coordinate the timing of drawdowns and disbursements to ensure that payments to staff, vendors and providers are prompt and timely. To the greatest extent feasible, the Virgin Islands, VIDE, VIDHS, or the Agent, if it has undertaken drawdown responsibility, must draw down funds in a timely manner so that funds under the grants are deposited to the separate bank account on the same day that funds are drawn from the account to liquidate obligations under the grants. The Virgin Islands, VIDE, or VIDHS, as appropriate and at the Agent's direction, must draw down sufficient funds under a grant to cover each approved request for payment.

9. The Agent must allow funds under a grant to be charged only for costs resulting from obligations that were properly made during the funds' period of

availability, including any carryover period. To ensure against the lapsing of funds, the Agent must liquidate obligations no later than 90 days after the end of the funding period or during any extension of that period authorized by the Department, in accordance with 34 CFR 80.23.

10. The Agent may seek approval from the Department to charge allowable pre-award costs incurred by the Virgin Islands, VIDE, or VIDHS against a FFY 2004, 2005, or 2006 grant to which these special conditions apply. The Agent must submit any request for pre-award costs to the Department in writing and may not reimburse any pre-award costs unless it receives written approval from the Department.

11. The Agent must establish and maintain a process for tracking and reporting time and effort spent by all employees whose salaries are paid with ED grant funds, including distribution of time among different funding sources for split-time employees, and for properly allocating salary costs among ED grants, based on accurate time distribution and time and attendance records. The Agent must carry out these responsibilities consistent with Federal requirements in Office of Management and Budget (OMB) Circular A-87.

12. In disbursing funds for allowable costs under the grants, the Agent must distinguish between direct and indirect costs and use accurate methods to allocate funds correctly between these two cost categories. The Agent must ensure that the charging of direct and indirect costs against the grants is consistent with the indirect cost rate negotiated and established by the U.S. Department of Interior (the Virgin Islands' cognizant Federal agency) and the Virgin Islands, and provided to the Agent, and with the requirements of OMB Circular A-87 and 34 CFR 75.560-564 (discretionary grants), 34 CFR 76.560-569 (formula grants), and 34 CFR 80.22.

13. The Agent must establish contacts and working relationships with a group of prospective vendors that can provide goods and services that the Virgin Islands, VIDE, and VIDHS need under the grants. The Agent must work to identify prospective vendors who will provide the best pricing and values for goods and services ordered and who will provide prompt delivery of goods and services. The Agent must have authority to enter into contracts with vendors on behalf of the Virgin Islands, VIDE, VIDHS, and, as appropriate, VIDH, and in doing so, must comply with the provisions for procurement set forth in 34 CFR 80.36(b)-(j).

14. Within 24 hours of the Agent's receipt of a vendor invoice, the Agent must provide a copy of the invoice to the Virgin Islands, VIDE, VIDHS, or, as appropriate, VIDH, and ensure that the goods or services delivered are available for inspection and acceptance or rejection by the appropriate Virgin Islands, VIDE, VIDHS, or, as appropriate, VIDH, staff requesting the goods or services. Within 24 hours of receipt of the invoice, the staff must (i) accept

or reject the goods or services, and, if accepted, (ii) draw down funds for the vendor payment for deposit into the separate bank account maintained by the Agent. The Agent must pay vendors for the delivered goods or services and must, to the extent reasonably possible, disburse funds to the vendors on the same day that funds are deposited into the separate bank account maintained by the Agent. The Agent must make payments by electronic funds transfer (EFT) or by paper draft only if EFT is not available or possible for a particular vendor.

15. The Agent must manage all property procured under the grants, with a purchase price of $500 or greater, in accordance with the requirements of 34 CFR 80.32(a) and (c)-(g).

16. The Agent must maintain records that fully show the amount of funds under each of the grants; how the Virgin Islands, VIDE, or VIDHS uses the funds; the total cost of each project; the share of that cost provided from other sources; and other records to facilitate an effective audit, in accordance with 34 CFR 75.730 (discretionary grants) and 76.730 (formula grants). The Agent, acting on behalf of the Virgin Islands, VIDE and VIDHS, must retain records in accordance with the provisions of 34 CFR 80.42 of EDGAR, and recognizes that records maintained on behalf of the Virgin Islands, VIDE and VIDHS to meet the requirements of these conditions are not exempt under 34 CFR 80.42(a)(2) from the record retention requirements.

17. In general, the Agent must use fiscal control and fund accounting procedures that ensure proper disbursement of, and accounting for, Federal funds, in accordance with 34 CFR 75.702 (discretionary grants), 76.702 (formula grants), and 80.20(b).

18. The Agent must maintain insurance as required under the terms of the contract.

19. All transactions under the contract between the Virgin Islands and the Agent must be consistent with all applicable Federal requirements, including OMB Circular A-87 and EDGAR at 34 CFR Parts 80 and 75 or 76, as appropriate.

20. The Agent must comply generally with the requirements of 34 CFR 80.41. More specifically, the Agent must produce quarterly reports concerning financial transactions of the Virgin Islands, VIDE, and VIDHS for submission to those entities and the Department, detailing for each grant awarded to the Virgin Islands, VIDE, and VIDHS, including for each individual program for which the Virgin Islands and VIDE are using Consolidated Grant funds: a) the date of receipt, and the amount, of each approved payment request; b) the date and amount of each draw down deposit; c) the date and amount of each payment or disbursement by the Agent; and d) any interest or other funds remaining in the account at the end of the quarter. These amounts must also

be grouped by and comparable with the projections in the line item budgets described above in section II.C.3 and must be reconciled with the Department's GAPS. This reconciliation must include drawdown dates, drawdown amounts and available balances, by award. These reports shall be due within 10 working days after the end of each quarter.

21. The Agent must work with the Virgin Islands, VIDE, VIDHS, VIDF, and VIDPP to assist in the training of employees and to provide transition assistance (including, but not limited to, transfer of all necessary data from the Agent to a new credible central FMS being designed by the Virgin Islands, and communication of information from the Agent to the contractor implementing the new FMS), as the Virgin Islands implements the new FMS.

22. The Agent, the Virgin Islands, VIDE, and VIDHS must recognize that, notwithstanding the citation of specific EDGAR requirements in these special conditions, there are other provisions of EDGAR not specifically cited above that are applicable to grants awarded by the Department to the Virgin Islands, VIDE, and VIDHS. This includes, for example, the drug-free workplace requirements in Part 84 of EDGAR, which are applicable to the Agent, and the definitions of terms in Part 77 of EDGAR.

23. The Agent, the Virgin Islands, VIDE, and VIDHS may include any other such terms, consistent with those above, as they believe are necessary to ensure timely drawdowns and payments to staff, providers and vendors, and financial management consistent with applicable Federal regulations, under the grants.

D. Drawdown of Funds

The Virgin Islands, VIDE, and VIDHS are authorized to draw down funds under the grants upon (i) execution of a written, binding contract between the Virgin Islands and the Agent, consistent with the terms of these special conditions; (ii) certification by the Agent that it is prepared to manage the funds under the grants on behalf of the Virgin Islands, VIDE, VIDHS, and VIDH in accordance with sections II.A. and II.C.2 above, consistent with applicable Federal requirements, the contract, and these special conditions; and (iii) compliance with all other eligibility requirements applicable under the specific grants.

E. Notification and Approval of Amendments to Contract Between Virgin Islands and Agent

The Virgin Islands must notify the Department of any proposed amendment to the contract between the Virgin Islands and the Agent, and must submit the proposed amendment to the Department for approval prior to execution of the amendment by the parties.

F. Failure to Comply with Conditions

Failure of the Virgin Islands, VIDE, VIDH, or VIDHS to comply with any of these special conditions as to any grant award will negatively impact the ability of the Virgin Islands, VIDE, VIDH, or VIDHS to continue to receive grants from the Department. Specifically, in meeting the terms of these special conditions, the Virgin Islands, VIDE, VIDH, and VIDHS must:

1. Work cooperatively and in a timely manner with the Agent to implement the activities and responsibilities described in these special conditions;

2. Permit the Agent's personnel to have access to certain books, records, and reports of the Virgin Islands, VIDE, VIDH, and VIDHS, and to have discussions with personnel of the Virgin Islands, VIDE, VIDH, and VIDHS concerning the services the Agent is to perform under these special conditions, as provided for in the contract between the Virgin Islands and the Agent;

3. Notify the Department when any dispute arises between the Agent and the Virgin Islands, VIDE, VIDH, and VIDHS concerning the implementation or continuation of the contract with the Agent, or the implementation of activities supported by this grant, including the financial management of grant funds; and

4. Comply with all Federal laws and regulations that apply to the receipt and use of funds awarded under this grant.

G. Reconsideration and Modifications

At any time, the Virgin Islands, VIDE, VIDH, or VIDHS may request reconsideration of the above special conditions by contacting the Department and stating in writing the reasons why they believe the conditions are no longer needed. Further, the Department may impose additional special conditions or modify these special conditions as appropriate. The Department will remove the special conditions at such time as the Virgin Islands implements a credible central FMS and demonstrates, to the Department's satisfaction, the ability to manage ED funds and property purchased for use under the grants in a manner that complies with applicable Federal requirements concerning accountability and funds management.

H. Program-Specific Special Conditions

In accordance with 34 CFR 76.133(a)(5), the Virgin Islands and VIDE must submit an annual performance report to the Department, as required under 34 CFR 80.40, for each of the programs for which they are using funds received under the Consolidated Grant to Insular Areas. Each report must contain a comparison of actual accomplishments to the objectives established in the approved Consolidated Grant plans and the reasons for slippage if established objectives were not met.

Additional program-specific special conditions may be imposed on grant awards made under one or more programs, in addition to the special conditions that are contained herein, because in certain program areas, the Virgin Islands may still need to make significant improvements in the administration of program requirements. Each such program-specific special condition will be incorporated into the appropriate notification of grant award from the Department to the Virgin Islands, VIDE, VIDH or VIDHS.

I. Incorporation of Special Conditions as Addendum to Contract

Upon receipt of these special conditions, and before the Virgin Islands may expend funds under this grant, the Virgin Islands and the Agent must incorporate these special conditions as a further addendum to the contract between the Virgin Islands and the Agent, and must provide written notice to the Department that the conditions have been so incorporated. The terms of these special conditions supercede the terms of the special conditions issued on September 26, 2005, and attached as Addendum 1A to the contract, to the extent that any provisions in these special conditions have been modified and are now inconsistent with those in Addendum 1A.

J. U.S. Department of Education Contact

All communications with the Department regarding these special conditions, including submission of notices, requests, or reports under sections II.C.4, II.C.10, II.C.20, II.D, II.E, II.F, II.G, II.H, or II.I shall be directed to:

Mark Robinson
Office of the Secretary
U.S. Department of Education
400 Maryland Avenue, S.W.
Room 7E318
Washington, D.C. 20202

Dated: _____