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Chairman Thibault, Chairman Shays, and distinguished members of the Commission, good morning and thank you for the opportunity to appear before you on behalf of the Department of Defense (DoD) Office of Inspector General (IG) to discuss critical challenges and improvements that must be made to DoD's wartime contracting. Contracting cannot be viewed as a series of singular, unrelated events or actions set in a vacuum that fail to recognize the operational environment and challenges. Contracting must be viewed and executed as part of an interwoven process and a key element of success in Southwest Asia. Many in the Department have been working long and hard to improve contingency contracting. However, we continue to find the same contracting problems occurring. The Department continues to struggle to get it right in the beginning and ensure it actually gets what it pays for.

Today I will discuss the most important recommendations using our framework for reform of contingency contracting; effectiveness of recommendations; provide an update on work since our last testimony; and challenges going forward.

PRESENCE IN THE REGION

Since the start of operations in Southwest Asia, over 200 DoD IG personnel have been deployed into the region for a significant amount of time, providing "boots on the ground" oversight. The DoD IG continues to sustain its highest operating level in Southwest Asia; 53 DoD IG auditors, evaluators, and investigators are currently deployed in Iraq, Afghanistan, Kuwait, and Qatar on six to 12 month rotations. In addition, there are also teams of auditors, agents, inspectors and engineers continually entering and exiting the region on temporary duty assignments. For example, Ambassador Moorefield, the Deputy Inspector General for Special Plans and Operations, and 5 of his staff are currently in Afghanistan reviewing the development of the logistics sustainment capability of the Afghanistan National Army. In addition, 5 auditors are in the United Arab Emirates on temporary duty to review efforts supporting the implementation of the Afghan National Army Air Corps and English Training task order. Last month, the

Principal Deputy Inspector General and I returned from a trip to Southwest Asia where we attended the Iraq drawdown rehearsal of concept drill and met with senior military leaders to discuss the drawdown efforts.

Matching the Department's current Southwest Asia operational tempo and focus, the DoD IG primary oversight focus is operations in Afghanistan while maintaining necessary oversight in Iraq and its remaining operations. We have also adjusted our investigative presence in Iraq in line with the military drawdown. Currently, we have three special agents and one administrative support employee in Iraq. Two additional special agents are deployed to Kuwait. By the end of 2011, our special agents in Kuwait, Germany, and the United States will investigate allegations of fraud and corruption in Iraq.

MOST IMPORTANT PREVIOUS RECOMMENDATIONS

Last year we issued our report "*Contingency Contracting: A Framework for Reform*"[1] which identified important areas for improving DoD's wartime contracting. We identified 10 systemic challenges related to deficiencies in the contract management process during contingency operations: requirements, contract documentation, contract type, source selection, contract pricing, oversight and surveillance, inherently governmental functions, property accountability, award fees, and financial management. For those areas, I would like to highlight and discuss our completed efforts since we last testified before the Commission in May 2010 using the following five recommendations that are key to improving contingency contracting. These recommendations were:

- ensuring all requirements are fully defined;
- selecting the appropriate contract type;
- competing future procurements properly;
- purchasing supplies and services at fair and reasonable prices; and,
- developing a Quality Assurance Surveillance Plan (QASP) and adequately overseeing the contract.

[1] Report No. D-2010-059, "Contingency Contracting: A Framework for Reform," May 14, 2010

In simplified terms, we stress that contingency contracting has to be done "right from the beginning" and there must be appropriate oversight of the contractor performance to ensure the Department gets what it pays for.

Get It Right In The Beginning. Ensuring that the mission requirements are translated into a clear statement of work with deliverables that will help the Department accomplish its mission is critical. Other key aspects of getting it right in the beginning include adequately documenting key decisions and the basis for those decisions in the contract files, selecting the appropriate contract type, determining a fair and reasonable price, and properly competing the contract. This effort to get it right in the beginning reduces the chance that billions of contracting dollars in Southwest Asia will be wasted. However, our oversight efforts have found these important steps do not always occur correctly.

- **Ensure Requirements Are Fully Defined.** DoD officials in contingency operations make decisions on requirements definition which must be implemented right in the beginning so that the procurement can be executed correctly. However, we recently issued a report that identified where Army officials did not adequately manage and administer the Logistics Civil Augmentation Program (LOGCAP) support contract.[2] Specifically, LOGCAP officials instructed the LOGCAP contractor to perform work that was outside the scope of the contract, including developing requirements for at least 71 non-LOGCAP contracts or task orders for requirements valued at approximately $1 billion. This out-of-scope work created additional problems because the contractor was writing statements of work that its subcontractors would want to bid on. Further, the support contractor was then provided access to the proprietary data of other contractor's without their permission. The contracting officer did not address potential organizational conflicts of interest or the appropriateness of the LOGCAP support contractor's access to another contractor's proprietary information. In response to the report,

[2] Report No. D-2011-032, "Logistics Civil Augmentation Program Support Contract Needs to Comply With Acquisition Rules," January 7, 2011

the Assistant Secretary of the Army for Acquisition, Logistics, and Technology agreed to review the actions of the LOGCAP contracting personnel.

- **Select the Appropriate Contract Type.** Contracting officials can utilize different types of contracts to acquire the wide variety of supplies and services required by DoD. Therefore, the decision the contracting officers make on contract type significantly influences the DoD's level of risk and the remaining contract process. For example, the Naval Sea System Command structured a contract for engine repair parts as a prohibited cost-plus-percentage-of-cost-type of contract which potentially allowed the contractor to inappropriately earn $1.4 million in fees for the first 3 years of the contract.[3] This type of fee structure does not incentivize the contractor to control costs because the more the contractor spends, the more fees the contractor receives. In response to the report, the Director, Program Analysis and Business Transformation for the Deputy Assistant Secretary of the Navy (Acquisition and Logistics Management) agreed to not use a contract clause that created the potential for cost-plus-percentage-of-cost recovery in price adjustments in all future contracts and modify or replace the clause in existing contracts. Going forward, the type of contracts used by DoD will continue to be included in the scope of our audits.

- **Compete Future Procurements Properly.** Full and open competition is one of the cornerstones of our acquisition process and helps ensure fair and reasonable prices are paid for the goods and services received. Unfortunately, we continue to find contract actions that jeopardize the integrity of this very cornerstone. For example, in Afghanistan, the Army Research Development and Engineering Command had a contractor working on a sole-source task order for operating foreign aviation systems at Kabul International Airport.[4] The Command wanted to issue another sole-source follow-on contract. However, the Command's Office of

[3] Report No. D-2010-087, "Weaknesses in Oversight of Naval Sea Systems Command Ship Maintenance Contract in Southwest Asia," September 27, 2010

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

General Counsel stated there was no valid reason to limit the competition for this effort. Despite this warning from the General Counsel, the Command issued a solicitation notice requiring a detailed bid within 2 days. Only the incumbent submitted a bid for $22 million within the two days. These actions limit competition and cast doubt on the integrity of the DoD contracting process and furthers the perception that favoritism, which may lead to higher prices and mediocre performance, is acceptable.

- **Contracting Officials Should Purchase Supplies and Services at Fair and Reasonable Prices.** The contracting officers are responsible for evaluating offered prices in order to determine whether the Department is paying fair and reasonable prices for all goods and services. However, we continue to find examples where the contracting officials did not always obtain fair and reasonable prices during the contract negotiations. For example, in the contract for foreign aircraft maintenance at the Kabul International Airport, the contracting officer stated that the labor rates were fair and reasonable based on the rates in a prior contract.[5] We looked at the prior contract which said labor rates were fair based on another prior contract. We traced this "chain" of price reasonableness claims through five previous contracts to the original contract where we found there was no price reasonableness determination by a contracting officer. This is not a acceptable method of price analysis. In response to the report, the Executive Director, Army Contracting Command agreed with the report stating ACC will perform a program management review of the contracts and task orders cited in the report focusing on competition requirements, price reasonableness determinations, and justifications for use of time and material contracts. Administrative actions would be taken against the contracting officers if appropriate.

[5] ibid

Adequately Oversee the Contract. After the Department gets it right in the beginning, DoD needs to have consistent and effective processes in place to verify that the contractor actually delivers the goods and services in accordance with the terms of the contract. However, we find that the Department continues to struggle in this area.

- **Develop a Quality Assurance Surveillance Plan (QASP).** Proper oversight is the best way to ensure DoD gets the goods and services contracted for. As required by the Federal Acquisition Regulation[6] the QASP is a critical part of an effective oversight process. The QASP is the key Government-developed surveillance process document that is used in Performance-Based Service Contracting to assess contractor performance by ensuring that systematic quality assurance methods are used to validate that the contractor's efforts are timely, effective, and are delivering the results specified in the contract or task order. The QASP directly corresponds to the performance objectives and standards (for example, quality, quantity, timeliness) specified in the Performance Work Statement and details how, when and by whom the Government will survey, observe, test, sample, evaluate, and document contractor performance to determine whether the contractor has met the required standards for each objective in the Performance Work Statement.

- **Oversee the Contract.** The Department must adequately oversee performance contracts, especially in contingency operations. However, we continue to find examples where the Contracting Officer's Representative (CORs) are either absent or ineffective. The COR is an individual who is designated and authorized in writing by the contracting officer to perform specific technical or administrative functions on contracts or task orders. CORs are the eyes and ears of the contracting officer. The key role of the COR is to observe, document, and communicate contractor performance to both the contracting officer and contractor. For example, the Marine Corps Systems Command Joint Program

[6] Federal Acquisition Regulation Subpart 46.4—Government Contract Quality Assurance.

Office procured $815.4 million in Field Service Representative and New Equipment Training Instructor Services for the Mine Resistant Ambush Protected Vehicles (MRAP) vehicle.[7] There was no written quality assurance process and instead the officials relied on the contractors themselves or complaints from individual units to monitor the Field Service Representatives. In response to the report, the Assistant Secretary of the Navy for Research, Development, and Acquisition and the Commander, Marine Corps Systems Command agreed to improve oversight of the Field Service Representatives by developing a QASP and designating and training CORs for the contract.

In another example, the Air Force Center for Engineering and the Environment (AFCEE) contracting officer's representatives did not conduct site visits or monitor the contractors working in Iraq and Afghanistan.[8] The COR delegation letters outlined the duties, which included observing the contractor to ensure that they were complying with the task order requirements and documenting safety violations. Although AFCEE designated CORs for the six task orders, for five of the task orders the CORs did not monitor the performance of the contractors because the CORs were located in the U.S. and did not conduct site visits to Iraq and Afghanistan. Further, AFCEE essentially designated contractors to perform the quality assurance portion of contract surveillance of the construction contractors in Iraq and Afghanistan. Although the contractors identified many quality deficiencies, other deficiencies went unreported. The most critical incident was faulty construction and other serious engineering and construction issues which resulted in a fire at the Afghan National Army Barracks. Additionally, the Air Force was charged $24.2 million for labor that was not specified in the base contract or in the task orders issued. The Deputy Director, AFCEE agreed to correct the COR error, agreed to work with the Defense Contract Audit Agency

[7] Report No. D-2010-068, "Government Oversight of Field Service Representative and Instructor Services in Support of the Mine Resistant Ambush Protected Vehicle Program," June 17, 2010

[8] Report No. D-2010-078, "Air Force Use of Time-and-Materials Contracts in Southwest Asia," August 16, 2010

(DCAA) on incurred cost audits for the $24.3 million, and disagreed that they needed to develop quality assurance surveillance plans citing architect and engineering services acquired under FAR part 36 are outside the application of the policy that Performance Based Acquisition (FAR part 37) should be used when buying services. We disagreed with their interpretation and application of the FAR part 36. The lack of surveillance requirements in FAR part 36 does not suspend the requirements of FAR 46.401, which requires quality assurance surveillance plans.

In some contracts, award fees are used to create an incentive for a contractor to perform well. We found contractors on the LOGCAP support contract received questionable award fees. For example, the Army contracting officer did not develop or receive a requirements-based QASP or effectively communicate with the COR in-theater. The Award Fee board was unaware that the COR in Iraq was not monitoring the contractor employees or obtaining feedback from all users. Without consistent and reliable government oversight of the LOGCAP support contract, the Army officials had no assurance that the contractor's performance justified payment of $461,550 in performance-based award fees. In response to the report, the Assistant Secretary of the Army for Acquisition, Logistics, and Technology stated he will request a corrective action plan from the Rock Island Contracting Command and will conduct a procurement management review.

In overseeing the contact, the Department must also appropriately review invoices to determine if goods and services were actually received. For example, for more than three years, the Air Force Center for Engineering and Environment did not conduct invoice reviews on time and materials contracts in Iraq and Afghanistan.[9] Contracting officials should perform detailed reviews of every invoice before certifying that the invoice is correct and should be paid. In addition, these officials

[9] Report No. D-2010-078, "Air Force Use of Time-and-Materials Contracts in Southwest Asia," August 16, 2010

also should verify that DoD actually received the goods and services listed. Detailed invoice reviews do not always occur. The invoices we examined showed multiple discrepancies. One invoice showed a local construction inspector had 630 billable hours in a 27 day billing period. That person would have had to work on average 23.3 hours per day. The Deputy Director, Air Force Center for Engineering and the Environment agreed there was a weakness in the reviews of invoices and corrective actions had been taken. Air Force Center for Engineering and the Environment planned to hire contractors to help review invoices.

EFFECTIVENESS OF RECOMMENDATIONS

While DoD contracting activities are generally responsive when we identify a problem with a specific contract, the Department continues to struggle to ensure these corrective actions are implemented for all contracts. We still find and report on some of the same critical issues we notified the Commission of at the hearing almost a year ago. These issues include a lack of adequate contractor oversight, inadequate surveillance plans, and inadequate reviews of contractor invoices. Challenges in these key areas impede the Department from achieving its mission goals, exacerbate risks, and expose taxpayer dollars to increased chances of waste, fraud, and abuse.

For example, during our testimony in May 2010 before the Commission, we referenced our *Contingency Contracting Report* that identified 155 recommendations to improve oversight and surveillance. As of May 2010, 95 of the 155 recommendations were closed. Now, as of April 2011, 145 of the 155 recommendations are closed. We are pleased to report that the Department embraces our work as a means to breaking down barriers and obstacles in contingency contracting reform. DoD contracting leadership and military commanders in the field have used our report *Contingency Contracting: A Framework for Reform* as part of awareness and training on improving contingency contracting efforts. For example, the Director, Army Contracting Command and NATO Training Mission-Afghanistan/Combined Security Transition Command-Afghanistan

have taken action to use our report within the Commands as an awareness tool. We meet quarterly with the Director, Army Contracting Command and his staff to discuss current observations and challenges based on the *Framework for Reform* template. While this is encouraging, we recognize that the Department has to overcome significant challenges to consistently implement these recommendations for all its contracts in a contingency environment.

As we begin to plan our audit work for next year, we will identify which of these contracts and related closed recommendations will be audited again to assess the effectiveness of management corrective actions. The examples I have discussed show a pattern of poor oversight and highlight these recurring problems.

UPDATE OF WORK SINCE LAST TESTIMONY

For contingency operations, since May 2010, DoD IG has issued 42 audit and inspection reports and our investigative efforts have resulted in 12 indictments, 19 criminal informations,[10] 34 convictions, over $42 million in monetary recoveries, and over $90 million in restitution to the U.S. Government. In addition, our investigative efforts have resulted in prison sentences totaling more than 51 years, and 21 debarments from federal contracting related to contingency operations in Southwest Asia.

In Iraq we are focused on asset accountability, base closure process, and contractor demobilization and the transition of our security assistance mission from DoD to the Department of State. In addition, our investigators continue to focus on corruption and fraud matters. In Afghanistan, we are focused on a wide variety of issues including safety and protection of forces; the training, equipping, and mentoring of the Afghan National Security Forces; management and execution of the approximate additional

[10] "Information" is a criminal charge brought by a prosecutor without using a Grand Jury to get an indictment. The "Information" is filed in court and serves to notify the court and the accused of the charges. The "Information" must be in writing and must be supported by evidence submitted by the prosecutor, usually in the form of affidavits. The name is derived from the prosecutor providing information to the court to justify a prosecution.

$14.2 billion designated for the Afghan Security Forces Fund for fiscal years 2010 and 2011; military construction projects; financial management challenges related to the commander's emergency response program and vendor payments; and the development of the logistics sustainment capability of the Afghan National Army.

Completed Audits. As I indicated previously, DoD IG has issued 42 audit and inspection reports related to contingency operations in Southwest Asia. Because of their significance, I wanted to provide details on our audits of the Prime Vendor Contract for Subsistence in Afghanistan and the contract for the Defense Reutilization and Marketing Office (DRMO)-Camp Arifjan, Kuwait.

Prime Vendor Contract. We recently reported on the need for the Defense Logistics Agency to improve contract management of the subsistence contract for Afghanistan. Since the contract was awarded in 2005, DoD has paid the vendor about $1.6 billion for food and water and $1.4 billion for nonfood items as required by the contract.[11] However, the Defense Logistics Agency:

- overpaid the prime vendor potentially $98.4 million for transportation costs within Afghanistan from December 13, 2005, through December 31, 2008;
- overpaid the prime vendor approximately $25.9 million for triwall[12] costs from December 13, 2005, through May 28, 2010;
- paid the prime vendor approximately $454.9 million for services to airlift fresh fruit and vegetables from Sharjah, United Arab Emirates to Afghanistan from December 13, 2005, through May 28, 2010, without incorporating the airlift requirement in the contract or

Figure 3 Triwall container shipping fresh fruit to Southwest Asia

[11] Report No. D-2011-047, "Improvements Needed in Contract Administration of the Subsistence Prime Vendor Contract for Afghanistan," March 2, 2011

[12] Triwalls are three layered corrugated boxes used for packaging and shipping chilled or frozen food

documenting that the airlift price of $3.74 per pound was fair and reasonable; and

- did not know whether the quantity of triwalls billed was accurate or that all of the $103.6 million in triwall costs from December 2005 through May 28, 2010, were actually chargeable to the contract.

The problems with the in-country transportation, triwall, and airlift costs are due to the contracting officer not definitizing contract changes and issuing contract modifications. Since a verbal change order in August 2005, the Defense Logistics Agency has been paying the contractor based on provisional transportation rates for moving food within Afghanistan. Since 2008, the provisional transportation rates were known to be too high based on a subsequent DCAA audit of the contractor costs. Generally, contracting officers are required to definitize contract actions within 180 days. The Department is 5 years beyond that date.

We also identified that invoices were not adequately reviewed. For example, lacking invoice review procedures, the DLA did not adequately detect that the prime vendor billed excessive weights for the transportation of goods. To validate the prime vendor's invoice, the CORs stated that for each invoice they routinely review about 10 orders related to ground transportation and 6 orders related to air deliveries. Their reviews generally consisted of obtaining the billed weights for the individual orders, comparing them to the signed customer invoices, and annotating any differences. However, we had trouble reconciling the documents that the CORs provided. For example, we identified the weight listed on an invoice for an April 2009 air delivery showed 311 pounds transported while Troop Support personnel were billed for 356 pounds. The COR accepted the billed weight of 356 pounds. As of March 2010, the COR was unable to provide an explanation for the difference.

In addition, in September 2008, Troop Support contracting officials identified a problem where the prime vendor had overbilled for minimum order weights for deliveries made by a particular type of helicopter. Between May 2008 and August 2008, the prime vendor charged Troop Support 5,512 pounds as the minimum order weight instead of

2,000 pounds. The maximum capacity limit for this model of helicopter could not accommodate orders of 5,512 pounds. At the request of a contract specialist, the prime vendor researched the overbillings and determined that Troop Support was overbilled a total of $4.1 million, which was subsequently reimbursed in November 2008. Before April 2009, the COR's validation of transportation invoices did not review the minimum order weights. Had written procedures been established for reviewing invoices, the CORs may have detected the questionable amounts and possibly prevented the overpayments.

In response to the report, the Acting Commander, Defense Logistics Agency Troop Support, agreed with all the recommendations and stated they were making every effort to determine fair and reasonable prices to definitize the 2005 verbal change order. Once the rates are finalized, Troop Support take actions to recover the difference between the reimbursement rates paid to the prime vendor and the finalized rates. The Acting Commander also stated that Troop Support will use contract modification 12 as the basis for future triwall payments until the contract is definitized, and will make every effort to recover [triwall] overpayments that were not paid in accordance with contract modification 12.

DRMO – Camp Arifjan, Kuwait.[13] In January 2011, we issued our report on DRMO operations in Camp Arifjan, Kuwait.[14] Among the critical findings were inadequate contract oversight, the lack of adequate contract requirements, and limited attention to obtaining fair and reasonable prices.

DLA hired a contractor in 2007 to operate six Defense Reutilization and Marketing Office (DRMOs) in SWA. We found inadequate oversight and weak surveillance at the largest DRMO, Camp Arifjan, Kuwait. Defense Reutilization and Marketing Office

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[13] Defense Reutilization and Marketing Office-Camp Arifjan, Kuwait, name changed to DLA Disposition Services Kuwait. For the purpose of this testimony, we refer to the office by its former name, DRMO – Camp Arifjan, Kuwait.

[14] Report No. D-2011-033, "DoD Needs to Improve the Management and Oversight of Operations at the Defense Reutilization and Marketing Office-Camp Arifjan, Kuwait," January 12, 2011

officials did not assign an appropriate number of CORs to perform oversight of the contractor's receiving operations. Although there were 18 CORs eligible to monitor contractor performance, on four different site visits conducted between January 2010 and February 2010, we did not observe any CORs present in the receiving area. We made recommendations to DLA Disposition Services officials to increase the number of CORs in the receiving area to validate contractor compliance with the contract. We also found a lack of contractor oversight in the demilitarization area and made similar recommendations.

Adequate contractor oversight on this contract could have detected and corrected the unacceptable conditions caused by the contractor. For example, the contractor should have covered items stored outdoors and protected DoD items from environmental damage. However, during our site visits to the DRMO yard, auditors observed collapsed containers containing Joint Service Lightweight Integrated Suit[15] items as shown in Figure 1.

Figure 1 Collapsed Containers Containing JLIST items at DRMO (Camp Arifjan, Kuwait)

[15] A JLIST provides protection against chemical and biological agents, radioactive fallout particles, and battlefield contaminants. As a result, instead of making the items available for reuse, the environmental damage may have rendered the items unusable.

In addition, auditors also observed approximately 75 open containers that contained Joint Service Lightweight Integrated Suit items and body armor sitting in the open environment becoming damaged as shown in Figure 2. Selecting just one container, we estimate the acquisition cost of that particular container of boots was approximately $39,000. The Executive Director at DLA agreed to improve oversight of the contract operations at the DRMO.

Figure 2 Exposed JLIST Items at DRMO (Camp Arifjan, Kuwait)

We reported instances of undefined requirements. Although operations at the DRMO, Camp Arifjan-Kuwait, required the handling and visual inspection of export controlled items, we identified that the DLA Disposition Services officials did not include a requirement in the contract to comply with all applicable export-control laws and regulations. In this instance, we found that foreign nationals had unsupervised access to potential export controlled items and technology.

In a contingency environment, determining that the offered prices are fair and reasonable can be challenging. For example, we found that the acquisition strategy for six DRMOs in Southwest Asia-which is responsible for the reutilization and disposition of excess equipment-was not developed to allow for the best value to the Government. Instead, the acquisition strategy and contract terms and conditions allowed the contractor to retain all

proceeds from the sale of scrap and useable items.[16] Although the contract cost was offset by the contractor's anticipated proceeds, in calendar year 2009 alone, the contractor was allowed to retain millions of dollars in proceeds of which the DLA did not equitably benefit. In this case, DLA Disposition Services officials did not consider the possibility of significant proceeds, as well as the potential impact of encouraging the contractor to achieve its highest revenue from the sale of scrap and useable property. Had officials considered these factors, they may have evaluated other strategies such as developing a profit-sharing ratio.

In July 2010, DLA Disposition Services terminated the contract and awarded multiple scrap removal contracts. Unlike the original contract, these new contracts require the contractor to pay the Government for the removal of scrap.

Ongoing and Completed Investigations. DCIS special agents in Southwest Asia are conducting 37 investigations pertaining to Overseas Contingency Operations (OCO), while DCIS agents in the United States and in Germany are conducting 198 OCO investigations. Examples of recent successes DCIS and its investigative partners have achieved are discussed below. These cases were selected to provide a broad spectrum on the types of allegations or schemes that our special agents investigate.

Bribery. The investigation of Staff Sergeant (SSG) Stevan Ringo and Sergeant (SGT) Michael Dugger, U.S. Army, revealed that from December 2009 to February 2010, SSG Ringo accepted more than $400,000 in cash payments from a government subcontractor in exchange for creating and submitting fraudulent paperwork permitting that contractor to steal fuel from Forward Operating Base (FOB) Shank, a U.S. Army installation in Eastern Afghanistan. SGT Dugger aided and abetted SSG Ringo in the scheme and together they stole nearly $1.5 million of fuel.

[16] This practice is contrary to how DLA Disposition Services does business in the U.S. Specifically, DLA Disposition Services uses a profit-sharing arrangement with its U.S. based scrap contractors.

On August 19, 2010 and September 24, 2010, SGT Dugger and SSG Ringo pled guilty to receiving bribes, respectively. On November 12, 2010, SGT Dugger was sentenced to 30 months in prison and three years of supervised release. SSG Ringo was sentenced on January 7, 2011, to 90 months in prison followed by three years of supervised release. He was ordered to forfeit money and property valued at $408,495. SSG Ringo and SGT Dugger were ordered to pay restitution jointly and severally in the amount of $1,494,984. On July 14, 2010, SSG Ringo and SGT Dugger were suspended from contracting indefinitely by the U.S. Army and debarred on April 4, 2011. This investigation was conducted jointly by DCIS, the Federal Bureau of Investigation (FBI), and the Army Criminal Investigation Command – Major Procurement Fraud Unit (Army CID-MPFU).

Contract Fraud. The investigation of Captain Eric Schmidt, U.S. Marine Corps, revealed that while he was deployed to Iraq as a Marine Logistics Officer at Camp Fallujah, Iraq, CPT Schmidt received approximately $2.0 million from Iraqi contractors. Of that amount, at least $1.2 million originated from the sale of stolen military property, such as military generators and fuel tanks. CPT Schmidt also used his position in the contracting process to steer contracts to an Iraqi contractor, Al Methwad Company (Al Methwad).

Once the contracts were awarded, Al Methwad paid CPT Schmidt's wife, Janet Schmidt, for the goods to be furnished under the contract. CPT Schmidt's wife often purchased far fewer or inferior products than those called for under the contract. Once the goods arrived in Iraq, CPT Schmidt falsely certified that the goods received conformed to the contract. Armed with the false certification, Al Methwad sought and received payment from the United States.

In May 2010, CPT Schmidt pled guilty to conspiracy to commit wire fraud and filing a false tax return that concealed the illicit income from the IRS. On February 7, 2011, Schmidt was sentenced to 72 months in prison followed by 36 months of supervised release. Janet Schmidt pled guilty in March 2010 to a tax

offense and she was sentenced on April 4, 2011, to 12 months of home confinement and 36 months of probation. The Schmidts were jointly ordered to pay restitution in the amount of $1,692,472 to the Department of Defense and $458,141 to the IRS. This investigation was conducted jointly by DCIS, the Naval Criminal Investigative Service, IRS – Criminal Investigation, and the Special Inspector General for Iraq Reconstruction.

Theft. A third example of a successful OCO investigation is the case of Edwin Vando and Juan Lamboy Rivera, U.S. Army sergeants assigned to the finance office at Camp Eggers, Afghanistan. The investigation revealed that in May 2009, a representative of an Afghan contractor, thinking his company had been overpaid, contacted the finance office wanting to return the money. The finance office determined that the increase of payment was not a result of an overpayment but rather a result of a change in the currency exchange rate. However, the company representative was contacted, told it was an overpayment, and instructed to immediately wire the alleged overpayment to a specific account, which had been set up by an Afghan interpreter. The funds were then withdrawn from the account, and distributed among the conspirators.

On April 7, 2011, SGTs Vando and Lamboy Rivera pled guilty to embezzling over $1.2 million and they are awaiting sentencing. A Forfeiture Notice was also filed at the same time of the Criminal Information, requiring the defendants to forfeit eight silk Persian rugs and currency in the amount of over $1.2 million. This investigation was conducted jointly by DCIS, the Army CID-MPFU, and the FBI.

CHALLENGES GOING FORWARD

Consistent implementation of the ten primary recommendations cited in our *Contingency Contracting: A Framework for Reform* report is one of the key challenges the Department faces.

As previously discussed, while the Department usually addresses the problems we identify on specific contracts, the Department struggles to adopt these corrective actions for all contingency contracts. DoD also struggles to proactively implement measures that would provide the Department with reasonable assurance that these corrective actions are operating effectively for all contingency contracts. This is why we consistently find examples where the Department does not get it right in the beginning and lacks the effective contract oversight necessary to determine if the goods and services were actually received in accordance with the terms of the contract. We will continue to focus on these critical areas during our audits of contingency contracts and challenge the Department to step back from the individual problems we identify and recognize the need to more broadly implement corrective actions to ensure contractor's performance meets the Department's needs.

Of key importance is that DoD appropriately establishes the contract requirements for the Afghan National Security Forces. The pace of contingency operations in Southwest Asis accentuates the need to get it right in the beginning. We plan to continue reviewing the requirements determination processes used by NATO Training Mission-Afghanistan/Combined Security Transition Command-Afghanistan to determine whether the Department is establishing clear, complete, well-defined requirements.

We believe that effective training of Afghan National Security Forces is one of the keys to the success of the mission in Afghanistan. Contractors are tasked with the majority of the efforts to train Afghan National Security Forces. The Department must ensure that all the training contracts are clearly written, contain useful metrics on training, are effectively executed and receive high quality oversight.

THE COMMISSION'S SECOND INTERIM REPORT

The Commission requested that the DoD Inspector General comment on the impact of the Commission's report to the Inspectors General. The DoD IG appreciates insight and

transparency of the Commission's important body of work. The second interim report provides useful and substantial recommendations to improve contracting in contingency operations.

Recommendation 29 in the Commission's report will expand the authorities of inspectors general by: "Giving subpoena power to civilian inspectors general to include subpoenas for the attendance and testimony of witnesses, as is currently provided to the DoD inspector general. Providing both civilian and Defense inspectors general with authority to interview contractor and subcontractor personnel."

The DoD IG defer to the civilian inspectors general's opinions regarding the expansion of their subpoena authority to include testimonial subpoena authority similar to that currently exercised by the DoD IG. If such an expansion occurs, we believe that procedural safeguards must be put in place to ensure that the testimonial subpoena authority is utilized appropriately. However, in contingency contracting settings, the utility of subpoena authority may be problematic if the contractor or subcontractor does not have a physical presence in the United States. Without a physical presence the contractor or subcontractor cannot be compelled to appear in a U.S. federal district court rendering the subpoena effectively unenforceable. A more feasible alternative, therefore, might be to require the creation/insertion of a new contract clause, with flow down requirements, providing the U.S. Government with access to contractor/subcontractor records and personnel related to the performance of the instant contract.

Recommendation 30 in the Commission's report will raise the Program Fraud Civil Remedies Act dollar limit on claims, and allow monies recouped under this Act and/or under the False Claims Act (31 U.S.C. 3729, et seq.) to flow back to the originating agency rather than revert to the Treasury. While I express no opinion with regard to the primary issue of raising the ceiling for accessing the Program Fraud Civil Remedies Act, I find the concept of allowing monies recouped under this Act to flow back to the

originating agency rather than revert to the Treasury, to be something worth pursuing because it highlights a fundamental problem which has hampered DoD's ability to effectively combat procurement fraud.

The current fiscal law environment within DoD is such that an agency generally may have a strong financial incentive NOT to aggressively pursue fraud based investigations/claims against agency contractors/subcontractors. This is because fraud investigations require the expenditure of current fiscal year resources which must be diverted from resources needed to accomplish the agency's core mission, while any resulting monetary fraud recoveries will most likely be returned to either a lapsed prior fiscal year appropriation (if the loss occurred during one of the prior four fiscal years) which is of limited practical use to the agency, or the U.S. Treasury (if the loss occurred more than five years ago) which is of no practical use to the agency. A modification to current fiscal regulations (and the underlying statutory basis, if deemed necessary) to allow monetary fraud recoveries to be returned to the agency's current fiscal year appropriation, so that those funds could be utilized to address current agency requirements, would provide a powerful, positive incentive to agencies to vigorously pursue procurement fraud investigations.

Making this fiscal law change would produce a sea of change akin to the one created by the 1986 amendments to the False Claims Act which significantly increased the number of qui tam suits filed and has resulted in the Government's recovery of $28.8 billion in fraud damages that might otherwise never have been recouped.

ESTIMATE ON CONTRACT RELATED WASTE IN IRAQ AND AFGHANISTAN

The *History of Government Contracting*[17] identifies that there was fraud and waste in every conflict in our Nation's history. We are buying more expensive and complicated items than in prior conflicts. To date, the DoD IG overseas contingency operations

[17] Nagle, James F., History of Government Contracting, Second Edition, 1999

oversight efforts has identified almost $1.5 billion in potential monetary benefits, over $42 million in monetary recoveries, and over $90 million in restitutions. However, because we have not conducted an audit to determine the overall level of wasted contract dollars in Southwest Asia, I cannot opine on any estimate on these amounts.

TRENDS FOR CONTRACT FRAUD REFERRALS AND RELATED PROSECUTIONS

Between Fiscal Years 2003 and 2010, DCIS initiated 398 investigations involving fraud and corruption associated with OCO. For that time period, these investigations yielded 86 federal indictments, 73 criminal informations, 11 military Article 32 proceedings, and 114 felony convictions. These cases resulted in punishment totaling over 206 years of confinement, over $200 million in restitution to the U.S. Government, and over $18 million in forfeited assets.

The allegations that prompted these 398 investigations came from various sources. DCIS agents in Southwest Asia engage in significant outreach efforts to encourage individuals to report allegations of fraud and corruption and to discourage people from engaging in illegal activity. From FY 2003 through FY 2010, DCIS agents conducted 399 fraud awareness briefings in Southwest Asia. Additionally, DCIS initiated 36 investigative projects, which are proactive initiatives intended to identify fraud and corruption. One example of a proactive investigative project seeks to identify fraud associated with the drawdown in Iraq.

The following table summarizes the sources of the allegations that prompted the 398 cases initiated from FY 2003 through FY 2010:

Information Received by another ICCTF Agency	131
Information Derived from a Proactive DCIS Project	47
Information Received/Generated by DCIS	45
Qui Tam	41
Information Provided by the Army, Air Force, Navy, or Marine Corps	38
Information Provided by an Informant	31
Information Provided by DCAA	24
DoD Hotline Referral	16
Information Provided by DCMA	10
Information Provided by the Department of Justice	9
Information Provided by a Contractor	9
Referral from Congress	5
Information Derived from an Undercover Operation	3
Information Provided by DoDIG Audit	2
DoD Voluntary Disclosure Program	1
Information Provided by a DoD Agency Not Otherwise Listed Herein	21
Information Provided by a Federal Agency (non-DoD) Not Otherwise Listed	11
Other Source Not Listed Herein	11

Note: Some allegations were received from more than one source.

CLOSING

Oversight of U.S. contingency operations in Southwest Asia is a top priority of the DoD Office of Inspector General. Effective contracting is critical in accomplishing the mission in Southwest Asia.

As the principal oversight agency for accountability within the Department of Defense, the DoD IG is committed to providing effective and meaningful oversight in Southwest Asia. Our priority is to assist the Department of Defense and Congress in identifying and deterring waste, fraud, and abuse of taxpayer monies; and, most importantly, ensuring the brave men and women serving in Southwest Asia are as well equipped and led as possible. Implementing improvements to Defense wartime contracting is critically important to effectively executing the Department's missions in Southwest Asia and

especially in times of great financial constraints as the Department and Nation face. The Department and taxpayers cannot afford inefficient and costly contracting practices.

Fostering an open dialogue and coordinating and integrating our efforts within the oversight community through our standing relationships and the Southwest Asia Joint Planning Group are critical to providing effective oversight in Afghanistan. Cooperation and coordination within the Federal oversight community, including the special inspectors general present today, are at an historic and unprecedented level. The Federal Inspectors General, the Special Inspectors General, along with the Service Audit Agencies and the Defense Contract Audit Agency are collectively deterring and detecting fraud, waste, and abuse, improving efficiencies in operations as well as protecting our warfighters, civilians, and contractors.

I thank you for the opportunity to testify and look forward to answering any questions you may have.

REPORTS RELATED TO THE TESTIMONY

1.	**Competition Issues and Inherently Governmental Functions Performed by Contractor Employees on Contracts to Supply Fuel to U.S. Troops in Iraq RESTRICTED REPORT (D-2011-049)**	**OIF**	**15-Mar-11**
2.	**Improvements Needed in Contract Administration of the Subsistence Prime Vendor Contract for Afghanistan RESTRICTED REPORT (D-2011-047)**	**OEF**	**2-Mar-11**
3.	**Improvements Needed on the Fleet and Industrial Supply Center, Sigonella, Ship Maintenance Contracts in Southwest Asia, (D-2011-043)**	**OIF/OEF**	**22-Feb-11**
4.	**Competition Should Be Used for Instructor Services for the Mine Resistant Ambush Protected Vehicles (D-2011-036)**	**GWOT OIF/OEF**	**3-Feb-11**
5.	**DoD Needs to Improve the Management and Oversight of Operations at the Defense Reutilization and Marketing Office-Camp Arifjan, Kuwait RESTRICTED REPORT (D-2011-033)**	**OIF/OEF**	**12-Jan-11**
6.	**Logistics Civil Augmentation Program Support Contract Needs to Comply With Acquisition Rules (D-2011-032)**	**OIF/OEF**	**7-Jan-11**
7.	**DoD Needs to Improve Management and Oversight of Operations at the Theater Retrograde-Camp Arifjan, Kuwait (D-2010-091)**	**OIF/OEF**	**30-Sep-10**
8.	**Controls Over the Accountability and Disposition of Government Furnished Property in Iraq (D-2010-088)**	**OIF**	**30-Sep-10**
9.	**Construction of New Kabul Compound Facilities for U.S. Forces-Afghanistan CLASSIFIED REPORT (D-2010-083)**	**OEF**	**30-Sep-10**
10.	**Weaknesses in Oversight of Naval Sea Systems Command Ship Maintenance Contract in Southwest Asia (D-2010-087)**	**OIF/OEF**	**27-Sep-10**
11.	**Army Use of Time-and-Materials Contracts in Southwest Asia (D-2010-081)**	**OIF/OEF**	**27-Aug-10**
12.	**Air Force Use of Time-and-Materials Contracts in Southwest Asia (D-2010-078)**	**OIF/OEF**	**16-Aug-10**
13.	**Government Oversight of Field Service Representative and Instructor Services in Support of the Mine Resistant Ambush Protected Vehicle Program (D-2010-068)**	**GWOT OIF/OEF**	**17-Jun-10**
14.	**Contingency Contracting: A Framework for Reform (D-2010-059)**	**OIF/OEF**	**14-May-10**