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## Acquisition – The Enemy Used Government Money to Fund Terrorist Activities

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### The Scenario

On the day the contracting officer returned to work from an extended absence, the Head of the Contracting Activity assigned the contracting officer a contract action. Another contracting officer had started the action but had not completed it. The head of the contracting activity did not communicate any of the policy changes that had occurred during the contracting officer's absence. The DoD flexibly priced contract action for \$100 million required the contractor to support contingency operations in both Iraq and Afghanistan.

The contracting officer awarded the contract using Federal Acquisition Regulation (FAR) and the DoD, Federal Acquisition Regulation Supplement (DFARS) compliant templates that were in place prior to the extended absence. Furthermore, the government auditors reviewed the contractor's accounting system, as DFARS 242.7502, "Policy" requires and audited the contractor's price proposal that met the criteria in FAR 15.4, "Contract Pricing." As a result of the pre-award accounting system review, the auditors knew that the contractor charged direct cost of performing on government contracts to suspense accounts. The auditors did not examine the practice and instead reported on the acceptability of the accounting system.

Prior to completing the pre-award process, rumors surfaced about the contractor's ties to potential terrorist groups. However, the contractor was able to persuade the contracting officer of its loyalty to the United States. The contractor stated that its competitors started the terrorist rumor. The contracting officer did not mention the rumor to the Head of the Contracting Agency. The contracting officer did not know about the listing of contractors that participated in terrorist activities (known as enemies of the United States) and awarded the contract without checking it. While on the extended absence, the DoD implemented a new policy prohibiting the award of contracts to enemies of the United States.

The new policy, DFARS 252.225-7993, "Prohibition on Contracting with the Enemy in the United States Central Command Theater of Operations (DEVIATION 2012-O0005) (JAN 2012)," requires that the Commander of the U.S. Central Command identify persons or entities actively opposing U.S. contingency operations and provide written notification to the Head of the Contracting Agency for them to take the appropriate action. The name of the contractor and its owners appeared on the notification listing.

The contract required an advance payment of \$1 million for the purchase of special supplies and for the contractor to submit invoices monthly for other direct and indirect costs. The government paid the cash advance for the special supplies. However, the contractor did not purchase the special supplies and instead told its employees to gather similar supplies from the warehouse. Eventually, the employees complained to the contracting officer's representative about supplies

not meeting contract specifications and charging their time to labor suspense instead of direct labor accounts. However, the contracting officer's representative did not communicate the employees' concerns to the contracting officer.

Several months into contract performance, the DoD, Office of the Inspector General (OIG) received a hotline complaint about the contractor. The complainant alleged that the contractor used contract money to fund terrorist activities. Immediately, the DoD OIG officials opened an investigation with audit assistance. The investigation determined that the contractor did not charge any costs to the contract. Also, the auditors determined that the contractor double counted direct costs by transferring direct costs from suspense accounts to indirect accounts after the government paid the invoices. The auditors reported the contractor's noncompliance with the provisions of FAR 31.201-1, "Composition of Total Cost;" FAR 31.202, "Direct Costs;" and FAR 31.203, "Indirect Costs" as well as Cost Accounting Standards' (CAS) 402, "Consistency in Allocating Costs Incurred for the Same Purpose."

### **Internal Control Weaknesses with Potential Indicators**

- The Head of the Contracting Agency did not communicate policy changes to the contracting officer prior to assigning the task for completing contract award.
- The contracting officer did inquire about changes in policy that occurred during his absence.
- The contracting officer's did not update templates used for awarding contracts.
- The contracting officer did not communicate the terrorist rumor to the Head of the Contracting Agency.
- The contracting officer's representative did not communicate the contractors' use of substandard supplies and the contractor employees' labor charging practice concerns to the contracting officer.
- The auditors did not evaluate the appropriateness of the contractors' suspense accounting practice in the pre-award phase of the contracting process.
- The contractor's failure to follow FAR and CAS are internal control weaknesses and potential fraud indicators.

### **General Comments/Lessons Learned**

The Head of the Contracting Agency, the contracting officer, the contracting officer's representative and the auditors' actions weakened DoD's internal controls for detecting and preventing potential fraud. The lack of or untimely communication of changes in policy to responsible officials may result in the improper use of federal funds. In this scenario, the untimely communication of the DFARS 252.225-7993 requirements to the contracting officer helped the contractor's plan to misuse government money. Also, the contracting officer did not

pursue the terrorist activity rumor which further advanced the contractor's plan. An assertion of loyalty to the United States does not replace internal controls designed to protect government resources. However, following internal control procedures increases the chances of detecting and preventing fraud before it occurs. Furthermore, the contracting officer's representative missed the potential fraud indicators that the contractor's employees communicated. Moreover, the auditors' evaluation of the contractor's suspense accounting practice might have identified the potential fraudulent practice earlier.