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BEFORE SENATE COMMITTEE ON HOMELAND SECURITY AND
GOVERNMENTAL AFFAIRS, AD HOC SUBCOMMITTEE ON CONTRACTING
OVERSIGHT



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Madame Chair, Ranking Member Brown, and distinguished members, I want to thank you for the opportunity to testify on the importance of contract audits in detecting and preventing fraud, waste, and abuse in government contracts. I also want to express my thanks for your continued support of Inspectors General and for the Subcommittee's strong commitment to oversight.

The Office of Inspector General (OIG), General Services Administration (GSA), relies heavily on its auditing function to fulfill its mission to detect and prevent fraud, waste, and abuse in federal contracts.

The OIG identifies and prevents a significant amount of procurement-related misconduct. Additionally, the OIG has expanded collaboration and increased cross-agency efforts to reduce fraud, waste, and abuse in contracting through its involvement with the former National Procurement Fraud Task Force and the Attorney General's current, comprehensive Financial Fraud Enforcement Task Force.

I will outline the OIG's major contract audit functions and results as well as some current contract oversight challenges.

I. Scope of Contract Audit Work

GSA is the Federal Government's primary acquisition agency. It was created to centralize the procurement of commonly used goods and services for the Government. GSA leverages about \$66 billion of procurement annually, and also contributes to the management of about \$500 billion in U.S. Federal property. GSA is home to the largest interagency contracting program in the Federal Government, the Multiple Award Schedules (MAS). In fiscal year (FY) 2010 sales for this program were \$38.9 billion with 18,396 contracts. In addition, GSA received \$5.5 billion in American Recovery and Reinvestment Act (ARRA) funds for public building construction projects.

Because of the volume of GSA's acquisition buying power, GSA's OIG plays a crucial oversight role in detecting and preventing fraud, waste, and abuse.

A. Four Main Types of Contract Audit Work

One of the OIG's most important oversight mechanisms for scrutinizing procurement is contract auditing. We define contract auditing as the examination of the books and records of a company doing business with GSA. We have approximately 140 auditors and analysts performing audits and reviews. The Office of Audits devotes between 50 and 60 percent of its direct audit hours specifically to contract reviews.

We perform several different types of contract audit work. These include pre-award and post-award MAS reviews, claim audits, and providing assistance to the Department of Justice (DOJ) on False Claims Act cases.

We conduct pre-award reviews before a contract is awarded, and post-award reviews after a contract is awarded. The OIG devotes most of its contract audit time to conducting pre-award MAS reviews, which are used to provide information to GSA contracting officers for use in contract negotiations. By providing information on the proposal, such as whether the information provided by the contractor is current, accurate, and complete, we enable the contracting officer to negotiate better terms. However, the information we provide is solely for the contracting officer to use as he/she sees fit and is not in any way binding.

We also perform audits after the MAS contract is awarded (post award reviews) to verify that the vendors have complied with their contractual obligations. These audits determine if the MAS vendors have billed their GSA customers in accordance with the pricing, terms, and conditions of the contract. Again, however, we provide recommendations to the agency, which then decides whether or not to implement those recommendations. Both types of reviews can find significant irregularities that could indicate fraud. As appropriate, we refer these to OIG Investigations and/or the DOJ.

The OIG provides significant audit assistance to the DOJ on False Claims Act cases. The False Claims Act provides for liability for triple damages and a penalty per claim for anyone who knowingly submits or causes the submission of a false or fraudulent claim to the Federal Government. The Act allows for a private citizen, known as a "relator," to bring a lawsuit on behalf of the United States, where the citizen has information that the named defendant has knowingly submitted or caused the submission of false or fraudulent claims to the United States. These are referred to as "*qui tam*" cases. While some cases in which we are involved are based solely on *qui tams*, many others involve issues that we identified and referred to DOJ during our pre- and post-award reviews.

A claim audit is an examination relative to the contractor's assertion of monetary damages resulting from alleged Government-caused delays and disruptions. The purpose of the audit is to evaluate the quantum (amount of monetary adjustment) and to determine if the claimed costs are allowable, allocable, and reasonable, supported by accurate and complete information, and

in accordance with the contract provisions and cost principles set forth in the Federal Acquisition Regulations (FAR). The majority of claims result from construction, and we anticipate a substantial volume of work in ARRA construction claims.

B. Additional OIG Audit Functions

Another main audit function of the OIG is internal auditing, defined as reviewing the various programs and processes within GSA. To complement our audits, we have established an Office of Forensic Auditing to detect procurement fraud. Forensic auditing utilizes audit, investigative, legal, and technical skill sets to collect, analyze, and evaluate evidentiary material concerning potential fraud. We have identified and referred for investigation several individuals for potential crimes such as wire fraud, theft, and misrepresentation.

II. Effectiveness and Success

The OIG has employed contract audits to great success. Over the last two years, the OIG has conducted reviews of 200 contracts that have estimated values of nearly \$25 billion. Our preaward reviews and claims have identified \$1.1 billion in potential cost avoidances and our post-award reviews have identified \$33 million in questioned costs. Based in large part on our contract audit work, twenty three False Claims Act cases have been settled during the last two years for a total of over \$400 million.

Audits and reviews of federal contracts can be long and very complex; some take years along with perseverance and extensive resources to complete. The results we have achieved are a testament to the expertise, skill, and capability of our auditors and the OIG. Recent False Claims Act settlements illustrate that our work is vital to the integrity of the contracting process and the economy of the acquisition programs. Below are some examples of recent, noteworthy results that were based in large part on our audit efforts.

- Our review of EMC, a large information technology vendor with MAS volume of \$100 million per year, led to an \$87.5 million settlement. Our audit found that EMC had not made full disclosure of its commercial pricing practices to GSA, was not offering GSA pricing comparable to its best commercial customers, and was not complying with its GSA MAS contract requirements. For example, EMC was supposed to conduct a price comparison to ensure that the government received the lowest price provided to any of the company's commercial customers making a comparable purchase for each government order under the contract. However, our auditors found that EMC knew that it was not capable of conducting such a comparison, and so EMC's representations during the negotiations – as well as its subsequent representations to GSA that it was conducting the comparisons – were false. Agency contracting officials supported the preaward review position, and did not renew EMC's MAS contract. In addition to our review results, which we referred to the DOJ, a *qui tam* was filed alleging that information technology vendors such as EMC were engaged in an illegal kickback scheme designed to influence the government to purchase specific company's products. We provided substantial support and resources to the DOJ in pursuing this case.

- In 2004, Hewlett Packard (HP), a large MAS information technology vendor, was named in a *qui tam*. Subsequently, in 2007, HP notified GSA and the DOJ that it was not in compliance with the price reduction clause and other contract requirements. It offered to pay GSA less than \$2 million to settle the issue. Our auditors reviewed the information provided by HP, including the commercial discounting disclosures made by HP prior to the award of its GSA contract, and found these disclosures were inaccurate and resulted in the government customers paying more for HP products than they would have had HP disclosed accurate information. Our analysis of the data showed the damages to the Government were considerably more than the \$2 million calculated by HP. We worked closely with the DOJ, and the company and the Government reached a \$55 million settlement.
- An audit of another MAS contractor, Comstor (a.k.a. Westcon), identified that this vendor had a business arrangement with another company (Cisco) to sell Cisco's goods. Cisco, a large information technology company, did not sell its products directly to the Government under its own MAS contract. Instead, Cisco sold to GSA through a third party distributor, Comstor. As part of this arrangement, both Cisco and Comstor were required to disclose discounting information to GSA. Our auditors found that Cisco and Comstor knowingly provided incomplete information to GSA contracting officers during negotiations in regard to Comstor's contract with GSA, which resulted in defective pricing of Cisco products and submission of false claims to the United States. We referred this matter to the DOJ, and the company agreed to pay the government \$48 million to resolve these contract fraud allegations.
- Audits of Fastenal, a national hardware store distributor, identified significant contract compliance issues, including with the accuracy of commercial sales practices and the price reduction clause. We worked closely with the DOJ to pursue our findings, and Fastenal agreed to pay \$6.25 million to resolve allegations that it (1) did not provide current, accurate and complete information about its commercial sales practices, including discounts afforded to other customers during negotiations and (2) failed to comply with the price reduction clause of its contract, when it overcharged Government customers and improperly assessed delivery and sales tax charges on Government sales.
- We also have identified a growing concern regarding the use of unqualified labor on MAS contracts. We find that once the qualifications for labor categories have been established the contractor does not always follow these requirements. In a recent audit of ManTech Advanced Systems International we found that the vendor billed a person as a scientist that required a bachelor's degree plus two years of experience or a high school degree with four years of experience. While the person had a bachelor's degree, his experience did not appear relevant to the position of scientist, in that the company counted work at a department store and a grocery store as experience. ManTech has already provided refunds/credits to the government in the amount of \$285,000. Our work in this area is on-going.

- The largest contract fraud settlement in which we have been involved is NetApp for \$128 million. NetApp is a computer storage and data management solutions company that had MAS contracts to sell hardware, software, and storage management services. Based on a *qui tam*, we conducted extensive audit work to assist the DOJ. Our audit work contributed significantly to the settlement, which resolved allegations that NetApp knowingly failed to provide GSA with current, accurate and complete information about its commercial sales practices, including discounts offered to other customers, and that it knowingly made false statements to GSA about its sales practices and discounts. The settlement also resolved allegations that NetApp knowingly failed to comply with the price reduction clauses by failing to pass on to the Government greater discounts that it gave to its commercial customers.
- A final example illustrates the results we have achieved in the construction area and demonstrates how long a case may take. Morse Diesel International, Inc. (a.k.a. MDI, AMEC), started as an audit of a \$2.5 million change order proposal for the removal of hazardous waste at the St. Louis Courthouse in 1995. While reviewing the bond cost for the change order, our auditors were provided with a bond invoice that did not match the invoice that was included in the GSA contract file. The key fraud issue was that the GSA contracting officer would not approve payment of the bond without proof of payment and MDI submitted a "paid" invoice that indicated the bond was paid months before the invoice was actually dated. The auditors verified that the invoice was not paid as of the date shown on the invoice that MDI provided to the contracting officer and that the submitted "paid" invoice was false. We also reviewed other MDI contracts and discovered similar issues with the San Francisco Customs House and Sacramento Courthouse. During the following four years, several additional audits of MDI claims, change orders, and payments (over \$25 million in value) uncovered other illegal acts on all three of these projects. The case resulted in two criminal convictions - one in 2000, in St. Louis for a false statement where the company paid a \$500,000 fine and one in 2001, in Sacramento for major fraud against the Government where the company paid a \$689,000 fine. The DOJ became involved in 1999 and we worked on the case until final settlement in 2009. In total there were recoveries, avoidances, and forfeitures of \$113.1 million.

III. Ensuring Quality in the Contract Auditing Process

The above examples attest to the quality of OIG audit efforts. The efficiency of the GSA OIG was recognized by the Government Accountability Office (GAO) when it reported a dollar return of \$19.33¹ for every dollar invested in the GSA OIG. We also have developed substantial expertise in the areas we audit, both through formal and on-the-job training, and we continually work to expand and reinforce that training. We also continually seek improvement and adjust as circumstances change, such as the passage of ARRA. Regular peer reviews reinforce compliance with applicable standards. Put simply, we are proud of the work we do.

¹ Appendix 1. Government Accountability Office, *Inspectors General: Actions Needed to Improve Audit Coverage of NASA 33-35* (GAO 09-88, December 2008).

We are also aware that, to be effective, we must protect our independence. We understand that a perceived lack of auditor independence at certain other agencies has prompted a suggestion for the creation of a new Federal Contract Audit Agency. At the outset, we firmly believe that the GSA OIG is the only audit entity needed at GSA. We also believe that developing and strengthening the audit divisions of the cognizant Offices of Inspector General (OIGs) would provide a better solution. OIGs are already familiar with each agency's subject matter and would be in a better position to become familiar with the distinctive characteristics of the contracts of each agency and develop the requisite expertise in each agency's contracts. Furthermore, the OIGs already have an existing and independent framework and structure within which to perform this work.

IV. A Current Contract Oversight Challenge

Obtaining prompt access to contractor records is essential for audits to perform contract reviews. However, the OIG has on occasion encountered difficulties in obtaining prompt and complete access to contractor records, needlessly delaying audit work.

Contractors in several cases have refused to disclose requested records during pre-award reviews, citing various regulatory clauses and asserting that they are not legally obligated to disclose the requested information. Currently we conduct pre-award reviews under the auspices of the contracting officer. If the contracting officer does not fully support the OIG's efforts, the contractor has an incentive to delay and try to obtain a contract before the OIG review can be completed.

Auditors, acting under the authority of the audit clause in the contract, have spent inordinate amounts of time trying to obtain contractor records. These delays can continue throughout an audit. Although auditors eventually obtain the requested documents by repeated requests and perseverance, the initial lack of cooperation and transparency causes significant delays and costs taxpayers money in additional administrative costs. Short of issuing a subpoena for the records, with the attendant paperwork and delay that could cause, we believe that legislation that specifically stated the OIG had access to those records would provide leverage we could use to more efficiently obtain these records.

Such barriers to information rightly owed to OIGs can hijack what has proven to be an effective contract oversight mechanism to the detriment of the Federal Government and the American Taxpayer.

V. Recommendation

We propose a legislative remedy to this challenge. Adopting clear, statutory language allowing OIGs to obtain contractor records would provide an effective tool for us in our contract audits.

The American Recovery and Reinvestment Act of 2009, Pub. L. 111-5 (Recovery Act), grants OIGs authority to examine records on contracts and grants awarded using Recovery Act funds. This provision in the Recovery Act eliminates any doubt about the OIGs' authority to review records.

I suggest expanding and extending this provision through an amendment to the Inspector General Act as follows:

Section 6 of the Inspector General Act, 5 U.S.C. App. 3, is amended—

By adding at the end of subsection (a) the following:

(10) Whenever in the judgment of the Inspector General it is necessary in the performance of the functions assigned by this Act, (a) to examine any records of any contractor or grantee, and of its subcontractors or subgrantees, or any State or local agency administering a contract, that pertain to, or involve transactions relating to, the contract, subcontract, grant, or subgrant.

Appendix I: Monetary Accomplishments Reported in OIGs' Semiannual Reports to the Congress for Fiscal Year 2007

Federal agency	IG total budgetary resources	Monetary accomplishments	Dollar return on IG's budget ^a
1 Social Security Administration	\$92,000,000	\$4,802,207,264	\$52.20
2 General Services Administration	58,000,000	1,121,385,515	19.33
3 Department of Transportation	71,000,000	1,086,688,396	15.31
4 Department of Education	50,000,000	639,389,462	12.79
5 Department of Health and Human Services	285,000,000 ^b	3,537,923,000	12.41
6 Department of Housing and Urban Development	121,000,000	1,347,799,879	11.14
7 Office of Personnel Management	19,000,000	188,856,301	9.94
8 Department of Defense	221,000,000	2,083,836,000	9.43
9 Department of Veterans Affairs	74,000,000	670,200,000	9.06
10 Department of Justice	89,000,000	754,357,601	8.48
11 Department of Labor	73,000,000	561,849,158	7.70
12 Small Business Administration	21,000,000	130,177,723	6.20
13 Federal Deposit Insurance Corporation	26,000,000	116,280,993	4.47
14 Agency for International Development	51,000,000	193,342,475	3.79
15 Department of the Interior	43,000,000	142,527,564	3.31
16 Department of Energy	42,000,000	99,409,187	2.37
17 Department of Commerce	23,000,000	51,736,992	2.25
18 Department of the Treasury	19,000,000	40,257,085	2.12
19 Environmental	54,000,000	92,792,457	1.72

	Protection Agency			
20	Corporation for National and Community Service	7,000,000	11,974,636	1.71
21	Department of State	34,000,000	52,500,036	1.54
22	Tennessee Valley Authority (TVA)	16,000,000 ^c	15,854,105	0.99
23	Department of Agriculture	91,000,000	81,412,378	0.89
24	Department of Homeland Security	128,000,000	100,916,585	0.79
25	Railroad Retirement Board	7,000,000	5,179,515	0.74
26	Treasury Inspector General for Tax Administration	135,000,000	54,902,108	0.41
27	National Aeronautics and Space Administration	34,000,000	12,103,809	0.36
28	Nuclear Regulatory Commission	10,000,000	495,065	0.05
29	Export-Import Bank of the United States	2,000,000	na ^d	na ^d
30	Central Intelligence Agency	na ^d	na ^d	na ^d
Total		\$1,896,000,000	\$17,996,355,289	\$9.49