

STATEMENT OF PAUL A. DENETT
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BEFORE THE
SUBCOMMITTEE ON GOVERNMENT MANAGEMENT,
ORGANIZATION, AND PROCUREMENT
COMMITTEE ON OVERSIGHT AND GOVERNMENT REFORM
UNITED STATES HOUSE OF REPRESENTATIVES

April 15, 2008

Chairman Towns, Ranking Member Bilbray, and Members of the Subcommittee, I appreciate the opportunity to appear before you today to discuss the Administration's regulatory efforts to strengthen contractor ethics and protect the government from fraudulent conduct in the award and performance of federal contracts and subcontracts. You have asked me to address H.R. 5712, the Close the Contractor Fraud Loophole Act, and issues raised in a March 20, 2008 letter from the Committee. In particular, you asked that I address the regulatory exemptions for overseas contracts and commercial item contracts that the civilian and defense acquisition regulatory councils proposed for public comment last November.

Let me begin by assuring the Subcommittee that the Administration is committed to an acquisition process with high standards of integrity and effective management controls to reduce fraud, waste, and abuse in government contracting. The Office of Federal Procurement Policy (OFPP) and procuring agencies have been working closely with the Department of Justice on its Procurement Fraud Task Force to review

regulations and policies for possible improvements to promote early detection, prevention, and prosecution of procurement fraud.

On May 23, 2007, OFPP received a request from Alice Fisher, Assistant Attorney General of Justice's Criminal Division, to consider amending the Federal Acquisition Regulation (FAR) to, among other things, require contractors to notify the government, without delay, when they become aware of a violation of criminal law or contract overpayment. In response, my office asked the Federal Acquisition Regulatory Council (FAR Council) to initiate a case to consider proposed regulatory changes to address Justice's recommendations.

By way of brief background, the FAR Council oversees the FAR. It manages two Councils: the Civilian Agency Acquisition Council (CAAC) and the Defense Acquisition Regulations Council (DARC). These bodies are comprised of agency representatives throughout the Executive Branch and are responsible for issuing changes to the FAR. The CAAC and DARC are assisted by six drafting teams with subject matter expertise in different parts of the FAR. The ethics rules you have asked about were drafted by the FAR Acquisition Law Team.

At the time of the Justice Department request, the FAR Acquisition Law Team was already well on the way to drafting regulatory changes to strengthen ethics requirements for government contractors and subcontractors. In February 2007, three months before the Justice Department request, the CAAC and DARC published proposed changes to the FAR that would, for the first time, establish government-wide requirements for government contractors to have a written code of business ethics and related requirements for posting "fraud hotline" posters to encourage contractor employees to report possible fraudulent contract activity.

In November 2007, the CAAC and DARC finalized the first rulemaking (FAR Case 2006-007). In addition, also in November, the two Councils issued a second proposed rule (FAR Case 2007-006), published in the *Federal Register* on November 14, 2007, that responded to the Justice Department's proposal. Through their issuance of the final rule and the proposed rule, the Councils put into place requirements for contractor ethics codes and, at the same time, gave contractors and other interested members of the public fair notice and an opportunity to comment on the Justice Department's proposed disclosure requirements.

Under the November proposed rule, contractors for the federal government would be required to disclose to an agency whenever the contractor has reasonable grounds to believe that a violation of criminal law has occurred in connection with award or performance of a contract or subcontract. The proposal would also require contractors to establish internal control systems and employee training programs to ensure compliance.

Both the final rule and the proposed rule include exemptions for overseas contracts. These exemptions are patterned after pre-existing Department of Defense regulations, dating back to 1988, that exempted overseas contracts from contract clauses that required "hotline posters" – i.e., posters that are placed in the contractor workplace with information on how contractor employees can report suspected fraud and other misconduct. The November rulemakings also include an exemption for commercial item contracts, in light of provisions in the Federal Acquisition Streamlining Act that require the acquisition of commercial items to resemble customary commercial marketplace practices to the maximum extent practicable.

Following the issuance of the November proposed rule, my office asked the Councils' Acquisition Law Team to carefully consider whether exemptions for overseas contracts and commercial item acquisitions are necessary. In response, the Councils recently sent a draft proposed rule to OMB, which we received on April 8th. This draft proposed rule is a follow-up to the November proposed rule. I am inclined to favor the elimination of exemptions for overseas contracts and commercial item acquisitions for purposes of this rulemaking. The draft proposed rule is currently under interagency review pursuant to Executive Order 12866 and will be subject to public notice and comment. These processes will ensure appropriate consideration of public and agency comments.

You have asked me to discuss H. R. 5712. This bill would, in effect, impose statutory requirements on federal contractors that are similar to the November proposed rule, except that H.R. 5712 would also apply these requirements to overseas and commercial item contracts. As I just mentioned, the Councils recently submitted a draft proposal to OMB for review, and I believe the rulemaking process will ensure that the concerns underlying this legislation will be appropriately addressed, without the need for new legislation.

In sum, the Administration is creating stronger, government-wide ethics requirements for government contractors. I am confident that when deliberations are concluded and regulatory changes are finalized and fully implemented, we will have taken significant steps to protect the government and our taxpayers from fraud in government contracting.

This concludes my prepared remarks. I am happy to answer any questions that you may have.