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Congress of the United States

House of Representatives

COMMITTEE ON OVERSIGHT AND GOVERNMENT REFORM

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MEMORANDUM

March 10, 2008

To: Members of the Committee on Oversight and Government Reform

Fr: Chairman Henry A. Waxman

Re: Employment Practices of Blackwater Worldwide

Today I am sending letters to three federal agencies — the Internal Revenue Service, the Small Business Administration, and the Department of Labor — regarding Blackwater's compliance with federal tax, small business, and labor laws. This memorandum summarizes the evidence before the Committee and why I am taking this action.

Executive Summary

On October 22, 2007, I wrote to Blackwater CEO Erik Prince raising concern that Blackwater evaded millions of dollars in federal tax payments through its improper classification of security guards as "independent contractors" rather than "employees." My letter was based in part on a March 2007 Internal Revenue Service ruling, which concluded that Blackwater violated federal tax law by designating an armed guard as an independent contractor. Committee staff estimated that Blackwater failed to pay or withhold up to \$50 million under its contract with the State Department.

Since then, the Committee's investigation has revealed two other contexts in which Blackwater appears to have improperly exploited this "independent contractor" designation. First, despite the fact that Blackwater is one of the largest private military contractors, receiving nearly \$1.25 billion in federal contracts since 2000, Blackwater has sought and received special preferences normally reserved for small businesses. As it did in the tax context, Blackwater claimed that its security guards were not "employees" for the purpose of counting the company's total number of staff. As a result, Blackwater obtained small business contracts without competing with other qualified bidders that properly designated their guards as employees. The Committee staff has identified at least 100 small business set-aside contracts, worth over \$144 million, that have been awarded to Blackwater since 2000.

In addition, Blackwater has refused to cooperate with an audit by the Department of Labor into Blackwater's potentially discriminatory employment practices. The audit seeks to determine whether Blackwater has complied with affirmative action and anti-discrimination laws imposed on all federal contractors. Blackwater has argued that it is not bound by these laws since it classifies its security guards as "independent contractors" rather than "employees." On this basis, Blackwater has refused to turn over documents requested by the Department of Labor, stalling the Department's inquiry for the last six months.

In all three instances, Blackwater has asserted in official communications that its security guards are independent contractors because the company does not exercise sufficient control over their activities in Iraq or Afghanistan. Blackwater has claimed in official communications that its security guards are "in no way directly supervised or controlled by Blackwater"; that they "do not report to any of the Blackwater entities regarding their work in the field"; and that they "do not report to Blackwater regarding their operations in country." Blackwater has also claimed that it "plays no role in the development or planning of the contractors' security missions" and "has little if any knowledge regarding the location or activities of these independent contractors." According to Blackwater, its "only real involvement is to pay the independent contractors."

All of these claims appear to be false. During the course of this investigation, the Committee staff has reviewed more than 20,000 documents and interviewed multiple State Department officials. The staff has also spoken with several former Blackwater security guards. This evidence indicates that Blackwater exercises what Mr. Prince has described as "tight control" over its security guards.

Blackwater's claims also contradict the position its own lawyer, Fred F. Fielding, took in civil litigation before he became the White House Counsel to President Bush. After the estates of four security guards who died in Fallujah sued Blackwater for wrongful death, Mr. Fielding argued that the guards could not recover from Blackwater because they were "employees" limited to recovering only workers' compensation. In his legal brief, Mr. Fielding asserted that the company's security guards were "employees as a matter of law" and described this conclusion as "inescapable."

Because Blackwater's contentions before the Internal Revenue Service, the Small Business Administration, and the Department of Labor appear dubious, I am writing the three agencies to ask them to investigate Blackwater's business practices and initiate appropriate enforcement action if warranted.

I. Blackwater's Failure to Pay and Withhold Taxes

According to IRS regulations, when an employer exercises significant control over its workers, it is supposed to classify them as employees. A worker is considered an employee for tax purposes if the worker is "subject to the will and control of the employer not only as to what

shall be done but how it shall be done.”¹ For example, when an employer provides training, instructions, tools, or a place to work, the worker is considered an employee. Only when workers exercise significant independence from their employers are they considered independent contractors.²

This distinction is significant because federal law requires employers to pay and withhold a variety of taxes on wages paid to employees, but not on payments to independent contractors. Employers must withhold federal income tax, pay and withhold Medicare and Social Security taxes, and pay federal unemployment tax on the wages of employees. They are not required to pay or withhold taxes on payments to independent contractors.³

On March 30, 2007, the IRS issued an opinion ruling that Blackwater’s designation of one of its security guards working on the State Department contract as an “independent contractor” was “without merit.”⁴ The IRS examined the extent to which Blackwater controlled the work of the guard, the financial arrangement between the parties, and evidence of how the parties perceived their relationship. In its letter to Blackwater, the IRS made the following observations:

- “[Y]ou retained the right to change the worker’s methods and to direct the worker to the extent necessary to protect your financial investment”;
- “[T]he worker did not invest capital or assume business risks, and therefore, did not have the opportunity to realize a profit or incur a loss”; and
- “The worker was not engaged in an independent enterprise, but rather the services performed by the worker were essential to your client.”⁵

Applying the law to these facts, the IRS ruled that the Blackwater security guard it evaluated “was an employee of the firm for Federal employment tax purposes, and not an independent contractor.”⁶

¹ 26 C.F.R. § 31.3121(d)-1(c)(2); § 31.3306(i)-1(b); and § 31.3401(c)-1(b) (relating to the Federal Insurance Contributions Act (FICA), the Federal Unemployment Tax Act (FUTA), and federal income tax withholding on wages, respectively).

² Internal Revenue Service, *Publication 15-A: Employer’s Supplemental Tax Guide* (Jan. 2007).

³ *Id.*

⁴ Letter from Internal Revenue Service to Blackwater Security Consulting LLC (Mar. 30, 2007).

⁵ *Id.*

⁶ *Id.*

Prior to issuing its ruling, the IRS gave Blackwater 30 days to provide evidence justifying its classification of the security guard as an independent contractor.⁷ When the IRS received no response within this timeframe, it waited an additional three months for Blackwater's submission. After Blackwater finally submitted a response on March 27, 2007, the IRS issued its ruling on March 30, 2007.

On October 22, 2007, I wrote to Erik Prince, the Chairman of the Prince Group, which owns Blackwater, to inquire whether Blackwater's failure to pay Social Security, Medicare, unemployment, and related taxes for its security guards was "significant tax evasion."⁸ Applying the IRS ruling to Blackwater's other security guards, my letter estimated that Blackwater failed to pay or withhold up to \$50 million in taxes under its contract with the State Department.

My letter also raised concerns that Blackwater sought to conceal the IRS ruling by entering into a nondisclosure agreement with the security guard who was the subject of the ruling, prohibiting him from sharing it with "any politician" or "public official."⁹

After receiving my letter, Blackwater called the IRS ruling "unreliable." Blackwater claimed that the ruling was no more than a "form letter" filled out at the "tiny IRS SS-8 office in the small town of Newport, Vermont. Nothing more."¹⁰ Blackwater contended that such a letter "has little, if any, legal effect."¹¹ Blackwater also erroneously claimed that it had been provided "little meaningful opportunity to participate in the process."¹² Finally, Blackwater argued in the alternative that even if it had improperly designated its security guards as independent contractors, the company should not be penalized. Blackwater argued that its actions fell into a "safe haven" in the tax code because they were based on advice obtained "several years ago" from an accounting firm.¹³

As described in part IV, the evidence before the Committee does not appear to support Blackwater's contention that it is in compliance with federal tax laws.

⁷ Letter from Internal Revenue Service to Blackwater Security Consulting LLC (Nov. 30, 2006).

⁸ Letter from Henry A. Waxman, Chairman, House Committee on Oversight and Government Reform, to Erik Prince, Chairman, the Prince Group (Oct. 22, 2007).

⁹ Settlement & Mutual Release Agreement between Andrew Howell, General Counsel, Blackwater USA, and former Personal Security Specialist, Blackwater USA (June 6, 2007).

¹⁰ Blackwater Worldwide, *Blackwater's Model of Using Independent Contractors is Consistent with Law and Good Practice* (Nov. 30, 2007).

¹¹ *Id.*

¹² *Id.*

¹³ *Id.* The Committee requested a copy of this advice, but Blackwater refused to provide it to the Committee, claiming it was protected by attorney-client privilege. Letter from Stephen M. Ryan, Counsel for Blackwater Worldwide, to Henry A. Waxman, Chairman, House Committee on Oversight and Government Reform (Feb. 14, 2008).

II. Blackwater's Claim to be a "Small Business"

Blackwater is one of the largest companies in the private security field. Since 2000, it has been awarded over \$1.2 billion in federal contracts.¹⁴ Blackwater's single largest security contract is the State Department's Worldwide Personal Protective Services II contract. Under this contract, Blackwater is authorized to have 920 personnel in Iraq, including more than 600 individuals conducting security operations.¹⁵ Blackwater was paid \$499 million under this contract between 2006 and 2007.¹⁶

Despite the fact that Blackwater is one of the largest private military contractors, it has sought and received special preferences normally reserved for small businesses. As it did in the tax context, Blackwater claimed that its security guards were not "employees" when it counted the company's total number of staff. As a result, Blackwater obtained these contracts without competing with other qualified bidders that properly designated their guards as employees. The Committee staff has identified at least 100 small business set-aside contracts, worth over \$144 million, that have been awarded to Blackwater since 2000.¹⁷

In one example, the Department of the Navy issued a solicitation in May 2005 for a \$93 million contract to provide helicopter replenishment services to Navy vessels based in Guam. According to its terms, this solicitation was a "100% small business set-aside," meaning that only companies classified as small businesses were eligible for the contract. According to the Small Business Act and its regulations, a company seeking to provide "Nonscheduled Chartered Air Freight Transportation" services such as these would qualify as a small business only if the company and its affiliates combined had fewer than 1,500 employees.¹⁸

On July 13, 2005, a Blackwater affiliate, Presidential Airways, submitted a bid "self-certifying" that it was eligible to compete for the contract because the total number of employees at Presidential and all other Blackwater affiliates was less than 1,500.¹⁹ Based on this self-

¹⁴ Eagle Eye, Inc., *Eagle Eye Federal Prime Contracts Database* (compiling data from the Federal Procurement Data System for fiscal year 2000 through the first quarter of 2008).

¹⁵ U.S. Department of State, *Fact Sheet: WPPSII Contracts Awarded to Blackwater, Triple Canopy, and DynCorp* (undated).

¹⁶ Eagle Eye, Inc., *Eagle Eye Federal Prime Contracts Database* (compiling data from the Federal Procurement Data System for fiscal year 2006 and 2007).

¹⁷ *Id.* (compiling data for fiscal years 2001 through 2007).

¹⁸ U.S. Small Business Administration, *Table of Small Business Size Standards Matched to North American Industry Classification System Codes* (Oct. 1, 2007).

¹⁹ Under SBA regulations, two entities are considered "affiliates" if one has the power to control the other or if a third entity can control both. 13 C.F.R. § 121.103. The Size Determination Memorandum identified a total of 29 Blackwater affiliates, including Blackwater Lodge and Training Center, Inc.; Blackwater Security Consulting, LLC; Presidential Airways, Inc.; Prince Manufacturing Corp.; and Prince Group, LLC. U.S. Small Business Administration, *Size Determination Memorandum* (File Number 3-2007-3-4-5) (Nov. 2, 2006).

certification, the Navy awarded the contract to Presidential. At the time of this self-certification, Blackwater and its affiliates designated fewer than 1,500 workers as “employees,” but they classified more than 1,000 other workers as “independent contractors.” If these independent contractors had been classified as employees, Presidential would not have been eligible to compete for the contract.²⁰

After the contract was awarded, several unsuccessful bidders brought challenges to Presidential’s classification as a small business, arguing that it misclassified its workers as independent contractors. On November 2, 2006, SBA issued a “Size Determination Memorandum” concluding that “Blackwater security contractors are not employees” and allowing the award to stand.²¹

When SBA issued its ruling on the small business contract, it appears to have relied in part on Blackwater’s tax practices. Blackwater’s submissions to the SBA highlighted the company’s refusal to pay employment taxes on the wages of security workers. Blackwater wrote: “The company pays contractors a daily rate for each day they are deployed, but does not withhold employment taxes.”²² The Size Determination Memo gave weight to this argument, citing the fact that Blackwater “does not withhold taxes” as a justification for its ruling.²³ The SBA issued its size determination on November 2, 2006, five months before the IRS ruled that Blackwater’s “independent contractor” designation was without merit.

As described in part IV, the evidence before the Committee does not appear to support Blackwater’s contention that it is a small business.

III. Blackwater’s Refusal to Allow Anti-Discrimination Compliance Review

Executive Order 11246, first issued by President Lyndon Johnson in 1965, requires federal contractors to take affirmative steps to avoid discrimination against applicants and employees. The executive order states:

The contractor will not discriminate against any employee or applicant for employment because of race, color, religion, sex, or national origin. The contractor will take affirmative action to ensure that applicants are employed, and that employees are treated during employment, without regard to their race, color, religion, sex or national origin.²⁴

²⁰ Another large business that bid on the contract, Evergreen Helicopters, had its bid disregarded because it did not meet the 1,500 employee standard.

²¹ U.S. Small Business Administration, *Size Determination Memorandum* (File Number 3-2007-3-4-5) (Nov. 2, 2006).

²² Letter from David C. Hammond, Counsel for Presidential Airways, Inc., to U.S. Small Business Administration (Oct. 26, 2006).

²³ U.S. Small Business Administration, *Size Determination Memorandum* (File Number 3-2007-3-4-5) (Nov. 2, 2006).

²⁴ Exec. Order No. 11246 § 202(1).

Under the executive order, the Department of Labor is required to investigate potential violations. Specifically, the Department's Office of Federal Contract Compliance Programs is charged with enforcing equal opportunity and anti-discrimination laws for federal contractors and can impose sanctions, including the cancellation of federal contracts and debarment from future contracts.²⁵ The order also requires contractors to provide "information and reports" and access to "books, records, and accounts ... for purposes of investigation to ascertain compliance."²⁶

In early 2007, the Compliance Office initiated a "compliance review" to determine whether Blackwater was in violation of Executive Order 11246. The first step in this review was a "desk audit" to determine the adequacy of Blackwater's affirmative action plans (AAPs) and to uncover any patterns of discrimination.²⁷ The Compliance Office requested copies of Blackwater's affirmative action plans and supporting documents in order to conduct this desk audit.

To date, Blackwater has refused to comply with the request and has provided the Compliance Office with no affirmative action plans or supporting documents relating to its security guards. On July 30, 2007, Blackwater wrote to the Compliance Office to explain its refusal by claiming that its security guards were not employees. Blackwater stated:

[T]he security personnel about whom you inquired are not included in BLTC's [Blackwater Lodge and Training Center's] AAPs because they are not BLTC employees. These individuals are highly skilled independent contractors who provide protection to personnel and assets in war zones, including Iraq and Afghanistan.²⁸

As a result of Blackwater's position, the Department of Labor's compliance audit has been stalled for several months, and Blackwater's potentially discriminatory employment practices have not yet been addressed.

As described in part IV, the evidence before the Committee does not appear to support Blackwater's contention that it is exempt from anti-discrimination compliance audits.

IV. The Evidence Before the Committee

In the three contexts above, Blackwater has asserted repeatedly that its security guards are independent contractors because the company does not exercise sufficient control over their

²⁵ Exec. Order No. 11246 is implemented under regulations found at 41 C.F.R. Chapter 60.

²⁶ Exec. Order No. 11246 § 202(6).

²⁷ 41 C.F.R. § 60-1.20 (2005).

²⁸ Letter from Ashley C. Adams, Counsel for Blackwater, to the Office of Federal Contract Compliance Programs (July 30, 2007).

activities in Iraq or Afghanistan. For example, in a May 15, 2007, letter to the IRS, Blackwater asserted:

Blackwater does not control these independent contractors in the Middle East or remotely from its headquarters over 7,000 miles away in North Carolina. ... [T]he independent contractors are, as intended, operating independently, within the USG rules, but in no way directly supervised or controlled by Blackwater.²⁹

Similarly, in an October 26, 2006, letter to SBA, Blackwater asserted:

In fact, Blackwater — located thousands of miles from the war zones where its contractors work — plays no role in the development or planning of the contractors' security missions or the directions on implementing them.³⁰

And in a July 30, 2007, letter to the Department of Labor, Blackwater asserted:

The majority of the security contractors ... are deployed to war zones, where they operate under the federal government's direction and their own professional judgment.³¹

Blackwater has also repeatedly asserted to all three agencies that its management exercises no control over its security guards. In its letter to the IRS, Blackwater asserted:

As a general matter, Blackwater security contractors do not report to Blackwater regarding their operations in country. ... A USG official makes all personnel evaluations and recommendations, which are then further approved within the USG.³²

In an October 2006 affidavit submitted in conjunction with the SBA size determination, Blackwater President Gary Jackson asserted:

After being deployed, Blackwater has little if any knowledge regarding the location or activities of these independent contractors. Blackwater's only real involvement is to pay the independent contractors.³³

And in its July 2007 letter to the Department of Labor, Blackwater asserted:

²⁹ Letter from Edwin H. Green, Counsel for Blackwater Security Consulting, LLC, to the Internal Revenue Service (May 15, 2007).

³⁰ Letter from David C. Hammond, Counsel for Presidential Airways, Inc., to U.S. Small Business Administration (Oct. 26, 2006).

³¹ Letter from Ashley C. Adams, Counsel for Blackwater, to U.S. Department of Labor, Office of Federal Contract Compliance Programs (July 30, 2007).

³² Letter from Edwin H. Green, Counsel for Blackwater Security Consulting, LLC, to the Internal Revenue Service (May 15, 2007).

³³ Declaration of Gary Jackson, President, Blackwater USA (Oct. 26, 2006).

The majority of the security contractors do not report to any of the Blackwater entities regarding their work in the field.³⁴

All of these assertions by Blackwater appear to be contradicted by evidence obtained by the Committee during its investigation of Blackwater's business practices. In the course of the Committee's investigation, the Committee has reviewed more than 20,000 documents, held two hearings, and received testimony from six State Department officials who worked with Blackwater in Iraq. The majority staff has also spoken with several former Blackwater security guards. This evidence indicates that Blackwater exercises significant control over its security guards.

In an appearance on the *Today Show* in October before Chairman Waxman raised questions about whether Blackwater is engaged in tax evasion, Mr. Prince asserted that Blackwater exercised "tight control" over its security guards:

Mr. Prince: We do the most high-profile missions, protecting the high-profile targets, the ones that the bad guys want to kill the most and put it on camera. ... We track the vehicles via satellite tracking devices so we know where the guys are and where they're not.

Mr. Lauer: So you have tight control over your employees.

Mr. Prince: Absolutely.³⁵

The evidence before the Committee substantiates this description. According to Blackwater's contract with the State Department, the company is required to exercise significant control over its security guards. Under the contract, Blackwater must "ensure that all work performed under this contract is accomplished in accordance with the applicable standards/standard operating procedures, general orders and specific orders issued by DS [Bureau of Diplomatic Security]."³⁶ In addition, Blackwater is expected to provide "[h]igh quality Contractor leadership of PRS [protective services] details" and "[h]igh quality Contractor planning of PRS details."³⁷ Blackwater is also responsible for providing ongoing, in-country training³⁸ and "all logistical support" for its personnel.³⁹ Finally, Blackwater must issue numerous detailed reports regarding the performance — and misconduct — of its personnel.⁴⁰

³⁴ Letter from Ashley C. Adams, Counsel for Blackwater Lodge and Training Center, to the Office of Federal Contract Compliance Programs (July 30, 2007).

³⁵ *Today Show*, NBC (Oct. 15, 2007).

³⁶ Worldwide Personal Protective Services II Contract, sec. C.4.1.1. (Aug. 25, 2004).

³⁷ *Id.* at sec. C.1.4.

³⁸ *Id.* at sec. C.4.3.2.1 ("The Contractor shall ... [e]nsure that all retraining and/or recertification of Contractor personnel is accomplished in-country, e.g., in the location in which the Contractor was tasked to provide the personnel protective service detail [and] [e]nsure that all

It appears that Blackwater has in fact exercised this control over its security guards. During an interview with Committee staff, the former head of the State Department office that oversaw Blackwater in Iraq stated that Blackwater “program managers and team leaders and senior people there in Iraq” would report directly to Blackwater headquarters in Moyock, North Carolina.⁴¹ This official said he “[a]bsolutely” understood that “those personnel reported ... through Blackwater up to Moyock.”⁴²

Evidence obtained by the Committee shows that Blackwater conducts detailed “Performance Appraisals” of its security guards, including an assessment of each security guard’s job performance. When these appraisals raise concerns, Blackwater regularly removes the guards from Iraq. As of September 2007, the company had fired at least 122 guards for improper behavior in Iraq. For example, Blackwater has fired guards for “broach[ing] initiatives with the client without the knowledge of Blackwater Management”;⁴³ “fail[ing] to follow orders given to him by his Blackwater supervisors”;⁴⁴ “demonstrating a cavalier demeanor to management”;⁴⁵ “decid[ing] to email his views and concerns to the President of Blackwater” rather than allow Blackwater’s “in-country leadership to address issues appropriately, at the lowest levels possible, and in a timely manner”;⁴⁶ “violating the Blackwater drug policy” and exhibiting “disregard for Blackwater policies and procedures”;⁴⁷ “violating Blackwater’s sexual harassment policy”;⁴⁸ and engaging in behavior that “reflected negatively upon Blackwater.”⁴⁹

armed PRS detail members and armed guard are re-qualified on all required firearms on a quarterly basis”).

³⁹ *Id.* at sec. C.4.3.8.1.1.

⁴⁰ *Id.* at sec. C.4.6.

⁴¹ Interview of former Manager, High Threat Protection Office, by Staff, House Committee on Oversight and Government Reform (Jan. 31, 2008).

⁴² *Id.*

⁴³ Blackwater Memorandum, Termination of Independent Contractor [redacted] (Nov. 15, 2006).

⁴⁴ Blackwater Memorandum, Termination of Independent Contractor [redacted] (Sept. 3, 2006).

⁴⁵ E-mail from [redacted], Blackwater Department of State Programs, to David R. Bennett (Dec. 20, 2006).

⁴⁶ Blackwater Memorandum, Termination of Independent Contractor [redacted] (Jan. 11, 2007).

⁴⁷ Blackwater Memorandum, Termination of Independent Contractor [redacted] (Mar. 15, 2007).

⁴⁸ Blackwater Memorandum, Termination of Independent Contractor [redacted] (Mar. 29, 2007).

⁴⁹ Blackwater Memorandum, Termination of Independent Contractor [redacted] (June 20, 2006).

In one memorandum reviewed by the Committee, a Blackwater manager informed a State Department official that the Blackwater project manager had “issued a directive” banning alcohol consumption by Blackwater personnel in Iraq.⁵⁰ He further assured the State Department that “[f]raternalization and contact with local or third country national continues to be closely monitored by the Blackwater management team.”⁵¹

Documents obtained from Blackwater show that the company’s managers in the United States also have nearly immediate access to incident reports and witness statements, even before some State Department officials. In one instance, on the morning of May 24, 2007, a Blackwater motorcade was involved in a shooting incident and standoff with the Iraqi police. Within hours, Blackwater’s program manager in Virginia received an incident report. He forwarded it to several State Department officials, noting: “I will keep you posted re any new developments.”⁵² After missions involving escalations of force, Blackwater security guards submit to the company, on Blackwater letterhead, internal “PSD Incident Reports” or “After Action Reports.”⁵³

When Blackwater CEO Erik Prince testified before the Committee on October 2, 2007, he affirmed that his company exercises a large degree of control over its security guards. During his testimony, Mr. Prince acknowledged that Blackwater provides its security personnel with a handbook with “all the dos and don’ts of what they are expected to do and not do.”⁵⁴ According to Mr. Prince, Blackwater strictly enforces those rules:

If there is a — any sort of discipline problem, whether it’s bad attitude, a dirty weapon, riding someone’s bike that’s not his, we fire them. We hold ourselves internally accountable, very high.⁵⁵

Mr. Prince also stated that Blackwater, rather than the State Department, initiates terminations when the company’s personnel engage in misconduct:

It generally comes to our attention first. We as a company, we fire them. We send the termination notice to the State Department as to why we fired someone.⁵⁶

⁵⁰ Memorandum from WPPS Project Manager, Blackwater USA, to Contracting Officer, U.S. Department of State (Feb. 6, 2007).

⁵¹ *Id.*

⁵² E-mail from [redacted], Blackwater Program Manager, Department of State Programs, to Paul C. Isaac (May 24, 2007).

⁵³ Interview of former Regional Security Officer, U.S. Embassy Baghdad, by Staff, House Committee on Oversight and Government Reform (Dec. 11, 2007).

⁵⁴ House committee on Oversight and Government Reform, Testimony of Erik Prince, *Blackwater USA: Private Military Contractor Activity in Iraq and Afghanistan*, 110th Cong. (Oct. 2, 2007).

⁵⁵ *Id.*

⁵⁶ *Id.*

Blackwater's assertions that its guards are independent contractors also contradicts the position asserted by the company in civil litigation. In *Nordan v. Blackwater Security Consulting LLC*, the estates of four Blackwater guards killed by insurgents in Fallujah, Iraq, sued Blackwater, alleging that the company failed to provide necessary equipment and support. Blackwater responded that because the guards were employees, they were limited to the workers' compensation provisions of the Defense Base Act, rather than civil damages. In a brief filed in federal court in March 2005, Blackwater's attorney at the time, Fred F. Fielding, used two legal tests commonly employed by the Department of Labor to conclude that Blackwater's security guards were "employees as a matter of law."⁵⁷ He wrote:

[B]ased on either of the primary legal tests that the Department of Labor actually employs to determine whether 'an employer-employee relationship exists within the meaning of the [Defense Base Act,]' the Decedents are employees as a matter of law.⁵⁸

Mr. Fielding repeated this position in a second legal brief filed in the case in 2005. He provided multiple examples of the high level of control that Blackwater exercises over its security guards, including terminating guards "without notice at any time with or without cause," setting work hours in the company's "sole discretion," and providing "equipment and weapons" needed for missions.⁵⁹ Mr. Fielding asserted that the conclusion that Blackwater guards are employees is "inescapable."⁶⁰ Mr. Fielding is currently the White House Counsel to President Bush.

Blackwater's position also appears to be contradicted by a prior Department of Labor decision finding that a Blackwater security guard who died in Iraq was an employee. On October 18, 2004, the Labor Department filed a "Compensation Order" ruling that a Blackwater guard who had been killed by insurgents in Fallujah was entitled to workers' compensation under the Defense Base Act. The order states that the guard was "in the employ of the employer [Blackwater]" and died "while performing service as a [sic] employee for the employer."⁶¹

⁵⁷ Blackwater Defendants' Memorandum of Law in Opposition to Plaintiff's Motion for Remand, *Nordan v. Blackwater Security Consulting, LLC*, 382 F. Supp. 2d 801 (E.D.N.C. 2005) (Mar. 7, 2005).

⁵⁸ *Id.* The first test focuses on "the right to control details of the work," while the second examines "the relative nature of the work," including the skills and investment required by the worker, and the relationship to the employer's business. *American Stevedoring Ltd. v. Marinelli*, 248 F.3d 54, 61-64 (2d Cir. 2001). The IRS, SBA, and DOL all use employment standards that incorporate the key elements of these tests.

⁵⁹ Memorandum of Law in Reply to Plaintiff's Motion to Dismiss, *Nordan v. Blackwater Security Consulting, LLC*, 382 F. Supp. 2d 801 (E.D.N.C. 2005) (Mar. 11, 2005).

⁶⁰ *Id.*

⁶¹ U.S. Department of Labor, Compensation Order, Case No. 02-135369 (Oct. 18, 2004).

Moreover, Blackwater's own contracts with its security guards states that "for purposes of the Defense Base Act, Blackwater shall be the statutory employer of the Contractor."⁶²

It is also significant that other companies in Blackwater's position have taken a different position on this issue. DynCorp and Triple Canopy, the two companies that share the WPPS II contract with Blackwater, both treat their security guards as employees.⁶³

V. The Letters to the IRS, SBA, and Department of Labor

The evidence received by the Committee shows that Blackwater has taken inconsistent positions regarding whether its guards are employees or independent contractors. When the issue is whether Blackwater can be held liable for the wrongful death of Blackwater guards, Blackwater argues that the guards are "employees" and can recover only through the workers' compensation system. But when the issue is whether Blackwater must pay or withhold Social Security, Medicaid, and other taxes for the guards, whether Blackwater is eligible for small business preferences in contracting, or whether Blackwater must comply with anti-discrimination rules, Blackwater calls these same guards "independent contractors."

The implications of Blackwater's actions are significant. Committee staff have estimated that Blackwater has avoided paying or withholding up to \$50 million in federal taxes by treating its guards as independent contractors rather than employees.⁶⁴ It also appears that Blackwater has received more than \$144 million in small business contracts that may not be justified and has evaded oversight by the Department of Labor.

For these reasons, I am sending letters today to the Internal Revenue Service, the Small Business Administration, and the Department of Labor. These letters ask the agencies to investigate whether Blackwater has complied with federal tax and other laws and to initiate enforcement action where appropriate.

⁶² Blackwater Security Consulting, LLC, Independent Contractor Service Agreement (2005).

⁶³ U.S. Department of State, *Fact Sheet: WPPSII Contracts Awarded to Blackwater, Triple Canopy, and DynCorp* (undated) (stating that DynCorp treats its security personnel as "direct hire employees with company benefits" while Triple Canopy designates their security guards as "intermittent employees with partial company benefits").

⁶⁴ Letter from Henry A. Waxman, Chairman, House Committee on Oversight and Government Reform, to Erik Prince, Chairman, the Prince Group (Oct. 22, 2007).