

Testimony of

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“Subcontracting in Combat Zones: Who Are Our Subcontractors?”

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Chairman Tierney, Ranking Member Flake, and distinguished members of the subcommittee, thank you for inviting me to discuss the oversight of subcontractors in combat zones. This is a complex issue and one that deserves serious examination. I have been the Special Inspector General for Iraq Reconstruction (SIGIR) for more than six years and have traveled to Iraq 27 times. My statement will draw extensively on my personal observations as well as the specific work of my office.

In that spirit, Mr. Chairman, let me begin by observing that in a world where much of our stabilization and reconstruction effort is carried out by contractors, we must consider how we can keep subcontractors and those tiered below them from undermining national objectives as they attempt to carry out contracts. This is, of course, largely a matter of transparency and oversight — but it also requires hard thinking about the design of contracts before the operation starts.

Defense Department guidance now mandates that a detailed projection of contracting requirements be prepared as part of operational planning. Military and civilian planners must, however, also consider at the outset how the contracting that an operation pre-supposes might, in

fact, *undermine* national objectives, and how the downside of contracting and subcontracting can be controlled. Moreover, during the course of the operation, senior leadership, program officers, and acquisition personnel must understand the larger context of what the United States government is trying to achieve, and they must convey this as best they can to contractors. Government leaders must, in particular, remain alert to the fact that changing circumstances may require that contracting arrangements be re-evaluated and restructured. We need to be ready to act on what we learn.

Managers considering how to oversee contractors and subcontractors supporting U.S. operations and objectives in Iraq, Afghanistan, and other countries must balance the risks of operating in an unstable security environment, on the one hand, against the benefits of providing greater stewardship over taxpayer dollars, on the other. My testimony today discusses achieving that balance from three perspectives: policies, transparency, and accountability.

Before I address these specific issues, I want to make four overall points. First, the Iraq experience has shown that contracting in a hostile/combat environment is much more difficult and far more vulnerable to fraud and waste than is contracting in a benign environment. Second, the risks associated with contracting in an environment such as Iraq or Afghanistan can be mitigated through appropriate checks and balances, but those risks cannot be eliminated. Third, contracting and procurement practices have long been a focus of SIGIR's work; in July 2006, for example, we issued a lessons learned report aimed at improving those practices.¹ That report can be found at http://www.sigir.mil/files/lessonslearned/Lessons_Learned_July21.pdf, and I ask that it be incorporated into my testimony by reference. Fourth, SIGIR's past work has shown that contractor oversight problems affect all executive agencies operating in war zones.

To address these problems, SIGIR has made two key recommendations.

First, SIGIR has recommended that a working group led by the Department of Defense (DoD) explore the creation of an enhanced Contingency Federal Acquisition Regulation (Contingency FAR). The need for a Contingency FAR was reinforced during our discussions with the Commanding General of Multi-National Forces-Iraq (MNF-I) when he observed that there was a compelling need for a single, simplified, and uniform contracting process for use during contingency operations.

Second, SIGIR has proposed the creation of a new integrated office to manage stabilization and reconstruction operations, which would significantly enhance planning and execution. Developing policies and procedures for managing contractors in contingency operations is one of the issues that office would address (although it would not directly address actions taken in direct

¹ [Iraq Reconstruction: Lessons in Contracting and Procurement, Report Number 2, 7/2006.](#)

support of combat operations, such as the Host Nation Trucking contract addressed in the Subcommittee Majority Staff's recent report).²

POLICY CHOICES SET THE OVERALL FRAMEWORK FOR OVERSIGHT

U.S. policies for using contractors in war zones significantly affect the U.S. government's ability to accomplish oversight. Questions such as the extent to which contractors will be used, the types of services that will be performed, and the extent to which host- and third-country contractors will be used all affect the U.S. government's ability to provide oversight of contractors. The size and qualifications of the acquisition workforce available in a combat zone, and the ability of program managers to understand the contracting process and their role in it, are also important factors. Senior leaders must strike the proper balance on all of these questions, taking into account the need for proper stewardship of resources.

To illustrate these points, I want to focus on two policies implemented in Iraq. These policies, although designed to meet program goals and objectives, created a greater oversight risk for the U.S. government.

First, as a matter of policy, DoD relies heavily on contractors for services that were previously provided by troops — services such as site security and logistical support for U.S. installations. The civil reconstruction of Iraq has largely been accomplished by contractors. Our reporting on reconstruction contracts has demonstrated significant shortfalls in most aspects of contractor oversight: there are simply not enough qualified contracting and program personnel available to secure the government's interests even at the prime contractor level.

A second policy that increases oversight risk is specifying that local contractors receive priority consideration for contracts. The Iraqi First program, developed by DoD in 2006 to stimulate and expand Iraqi employment and skills, encouraged the use of Iraqi contractors and personnel and resulted in greater subcontracting. DoD reported that during fiscal year 2008 it awarded more than \$2.34 billion in contracts to Iraqi vendors, an increase of \$300 million over fiscal year 2007. As of March 2010, DoD reported about 4,400 contractors were participating in the program.

Contracting with host-country firms has several benefits: it creates jobs, stimulates the local economy, and supports counterinsurgency efforts. However, in Iraq and other countries where there are no reliable databases with information on contractors, the vetting process presents a very real and difficult problem, especially at the subcontractor level. Often, records on personnel and companies either do not exist or are very limited. Therefore, oversight risks increase because it is difficult to determine the reliability, integrity, and allegiance of companies and individuals. I believe there needs to be a thorough examination of the policy implications of using contractors, especially from the host country and from third countries.

² [*Applying Iraq's Hard Lesson to the Reform of Stabilization and Reconstruction Operations, 2/2010.*](#)

It should be noted that government activities sometimes work at cross-purposes for reasons that may be totally unrelated to the fact that some activities may be contracted. For example, the DoD's Commander's Emergency Response Program (CERP) and the Department of State/U.S. Agency for International Development's (USAID) Economic Support Fund programs in the Iraqi countryside too often negated one another's effects; but this had little to do with the contracted elements and everything to do with the government's inability to achieve unity of effort.

TRANSPARENCY IN CONTRACTS CAN BE DIFFICULT TO ACHIEVE

The FAR provides contracting agencies with considerable flexibility in requiring prime contractors to identify subcontractors and their qualifications to perform on the contract. However, the need or desire for greater information on subcontractors must be balanced with the reality that the information may not be available in all cases and that such information comes at a cost. Moreover, the desire for more specificity in contracts to hold contractors accountable for their actions must be balanced against the reality that the government may have little practical recourse when faced with poor performance by a contractor in a combat zone.

SIGIR believes that the provision of more information on contractors and subcontractors would provide greater transparency in contracts and could give agencies the opportunity to determine the acceptability of subcontractors. However, even prime contractors may have difficulty identifying all of their subcontractors.

For example, in July 2007 SIGIR issued a report that discussed the difficulties in identifying subcontractors involved in Iraq reconstruction work.³ The study looked at USAID's Phase II design-build construction contract awarded to Bechtel. The contract was awarded for \$680 million on April 17, 2003, but was later modified and increased to approximately \$1.03 billion. The contract ended on February 28, 2006.

The Bechtel Phase II contract was geared toward the use of subcontractors according to its USAID-approved subcontracting plan, which stated that Bechtel would subcontract approximately 90% of the direct reconstruction costs. Bechtel awarded 66 subcontracts—64 fixed-price and 2 cost-plus fixed-fee. Of the 66 subcontractors, 11 further subcontracted to 102 lower-tier subcontractors. Thus, we were able to identify a total of 168 subcontractors. Bechtel officials also told us that there were probably other subcontractors that were not specifically identified. This lack of information creates oversight risks for the U.S. government.

The FAR also provides agencies considerable flexibility to incorporate requirements into contracts that "flow down" from prime contractors to their subcontractors. Greater specificity in contract requirements achieves a number of objectives such as putting subcontractors on notice of government requirements, providing contract managers with firm criteria to evaluate

³ [Review of Bechtel's Spending under Its Phase II Iraq Reconstruction Contract \(SIGIR-07-009\), 7/24/2007.](#)

contractor performance, and providing the government a sound basis to pursue adverse actions against contractors who do not perform to those requirements.

I believe a Contingency FAR would better position agencies to identify requirements that should be incorporated in contracts. To help ensure that contractors and subcontractors do not undermine national policy, the Contingency FAR could require appropriate terms along these lines in contracts. I also believe there is a necessary balance that needs to be struck between the need and desire for greater transparency about subcontractors with the lack of reliable information about them, in some cases.

ACCOUNTABILITY CANNOT ALWAYS BE ENSURED

Government agencies need to hold contractors accountable for the satisfactory performance of their contracts and for their actions in the performance of that work. However, again, there is a need to balance carefully risks against benefits. There are instances where the ability to perform oversight is reduced due to security concerns or the nature of the program being implemented. Those factors need to be considered in the government's plans, and they were not considered, or were inadequately considered, in the case of Iraq's reconstruction.

SIGIR's work has identified a number of factors that have affected government oversight and accountability with respect to reconstruction efforts in Iraq. One of our 2008 reports summarizes the key issues.⁴ For example, we state that staffing issues—not having enough people with the right skills and the rapid turnover of personnel—reduced the U.S. government's ability to effectively manage contracts and programs and contributed to a perception that government officials were inexperienced. We cite a specific contract where the contractor estimated it was overseen by 17 different contracting officers between March 2004 and April 2006, the two years of the contract.

With regard to security concerns, the same report states that the U.S. government did not fully anticipate or plan for working in the unstable security environment that confronted U.S. managers.

Programs involving host-country companies and direct payments to local nationals also can present accountability challenges. While evidence of problems with such programs is not widespread, SIGIR and the USAID Inspector General have identified several instances of problems in this area.

In an audit currently being conducted by SIGIR, preliminary findings show accountability problems with the MNF-I Sons of Iraq program. The Sons of Iraq were local nongovernmental security forces that worked with the MNF-I and, in some cases, the Iraqi government, to protect their local communities.

⁴ [Key Recurring Management Issues Identified in Audits of Iraq Reconstruction Efforts, SIGIR 08-020, 7/27/2008.](#)

SIGIR's preliminary work has identified accountability problems. Some of the problems include ghost employees and poor controls over the distribution of cash payments to local leaders who were responsible for paying their men. No rosters or receipts were provided to the U.S. military's fund managers.

The vulnerability of these types of programs was demonstrated when Captain Michael Dung Nguyen pled guilty in December 2009 to the crimes of theft of government property and structuring financial transactions. Nguyen admitted that while deployed to Iraq, he stole approximately \$690,000 in currency from the CERP program, which funded both the Sons of Iraq program and local relief and reconstruction. Nguyen gained access to the currency in his capacity as a project purchasing officer.

In March 2008, the USAID Inspector General reported that funds from its Community Stabilization Program (CSP) were "being extorted by at least one known militia leader," with adverse consequences for U.S. military personnel.⁵ USAID's CSP program is a \$544 million program intended to complement military security efforts and civilian local government development with economic and social stabilization efforts such as community cleanup campaigns and trash collection, rehabilitation of roads and schools, and larger-scale engineering projects to improve water and sewage services.

In this instance, USAID received a letter from a USAID Provincial Reconstruction Team representative embedded with the U.S. military stating that there were "compelling indications" that funds from CSP projects in his area were being extorted. In response, the USAID Inspector General gathered detailed evidence concerning the extortion of funds from CSP projects and their possible diversion to militia activities.

The major factors contributing to the program's vulnerability to fraud were the lack of regular, independent site monitoring and the inadequate vetting of CSP contractors. Estimates of potential fraud in this case ranged from \$6.7 to \$8.4 million. Evidence in USAID's report suggested that similar problems may exist elsewhere in Iraq.

In summary, I have presented a need to reach a balance between achieving program objectives and fulfilling the responsibility to safeguard taxpayer funds that arises when using contractors in a combat zone. To address concerns raised about current practices, I believe a Contingency FAR would be useful in the short term to help agencies identify requirements that should be incorporated in contracts. I also believe there is a longer-term need for a thorough examination of the policy implications of using contractors, especially local or third-country firms and

⁵ [Audit of USAID/Iraq's Community Stabilization Program, USAID-E-267-08-001, 3/18/2008.](#)

employees. Lastly, and most importantly, I believe that a new integrated office to manage stabilization and reconstruction operations could significantly enhance the U.S. government's ability to plan and execute these operations, including the use and oversight of contractors.

That concludes my testimony. Thank you for your attention, and I am happy to answer any questions you may have.