UNPRECEDENTED CHALLENGES: THE COMPLEX TASK OF COORDINATING CONTRACTS AMID THE CHAOS AND THE REBUILDING OF IRAQ

HEARINGS

BEFORE THE

COMMITTEE ON GOVERNMENT REFORM

HOUSE OF REPRESENTATIVES

ONE HUNDRED EIGHTH CONGRESS

SECOND SESSION

MARCH 11, JUNE 15, AND JULY 22, 2004

Serial No. 108–213

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THE COMPLEX TASK OF COORDINATING CONTRACTS AMID CHAOS: THE CHALLENGES OF REBUILDING A BROKEN IRAQ

THURSDAY, MARCH 11, 2004

HOUSE OF REPRESENTATIVES,
COMMITTEE ON GOVERNMENT REFORM,
Washington, DC.

The committee met, pursuant to notice, at 2 p.m., in room 2154, Rayburn House Office Building, Hon. Tom Davis (chairman of the committee) presiding.

Present: Representatives Tom Davis, Burton, Ros-Lehtinen, McHugh, Mica, LaTourette, Ose, Jo Ann Davis, Platts, Turner, Carter, Tiberi, Waxman, Lantos, Kanjorski, Maloney, Tierney, Clay, Watson, Lynch, Van Hollen, Ruppersberger and Norton.

Staff present: Melissa Wojciak, staff director; David Marin, deputy staff director, director of communications; Keith Ausbrook, chief counsel; Ellen Brown, legislative director and senior policy counsel; David Young, counsel; Robert Borden, counsel/parliamentarian; Drew Crockett, deputy director of communications; John Cuaderes, senior professional staff member; Edward Kidd, professional staff member; Ken Feng, investigator/GAO detailee; Teresa Austin, chief clerk; Brien Beattie, deputy clerk; Allyson Blandford, office manager; Phil Barnett, minority staff director; Kristin Amerling, minority deputy chief counsel; Karen Lightfoot, minority communications director/senior policy advisor; Anna Laitin, minority communications and policy assistant; Jeff Baran and David Rapallo, minority counsels; Mark Stephenson, minority professional staff member; Earley Green, minority chief clerk; Jean Gosa, minority assistant clerk; Cecelia Morton, minority office manager; and Naomi Seiler, minority staff assistant.

Chairman TOM DAVIS. Good afternoon. We are going to go through two opening statements before we get to our witnesses, so take your time getting to your seats, the witnesses.

A quorum being present, the committee will come to order.

We meet today to look into the complex task of coordinating contracts amid the chaos and challenges of rebuilding Iraq.

Even before the conclusion of major military actions, there were plans for a major effort to rebuild Iraq's infrastructure and government. Emergency supplemental appropriations bills for both fiscal year 2003 and fiscal year 2004 have provided more than $20 billion to rebuild postwar Iraq. Many Federal departments and agencies have already awarded or soon will award contracts for the sustainment and reconstruction efforts.

The rebuilding of Iraq is a monumental task. Saddam Hussein spent decades frittering away his nation's vast wealth on himself and his Baath party cronies, while little to nothing was spent to meet the urgent needs of the Iraqi people. Decades of neglect and inaction have turned this once great nation into a country where the majority of people live in poverty and despair.

However, with Saddam's ouster, we are witnessing a rebirth of Iraq. Freedom and liberation have brought a new sense of urgency to the Iraqi people. They understand what is at stake; and we, as part of the coalition of the willing, must do our part to sustain freedom by rebuilding their nation.

Twenty days ago, I, along with other members of this committee, returned from Iraq where we witnessed the enormity of the reconstruction effort. This was my second trip, and in the 6 months since my last visit to the region I saw significant progress in our reconstruction efforts.

The task at hand is enormous. It will be years before we are able to get Iraq running on its own. Yet each day Iraqis are getting a better life, thanks to the dedicated American soldiers and civilians working there. Our reconstruction efforts are being completed under even life-threatening conditions. Our military is nothing short of superb. Besides ensuring the safety of the country, they have become master builders and diplomats. The use of funds from the Commanders Emergency Relief Program paves the way for local and regional stabilization by allowing for small rebuilding projects that have an immediate impact on the local population.

For example, we recently met with General Odierno, Commander of the 4th Infantry Division, who told us how he used his CERP funds to build a water treatment facility in Tikrit and a sewage treatment facility in Baji. In many ways, the Commanders Emergency Relief Program is meeting the immediate needs until our larger construction projects are completed.

The positive offshoots of the Iraqi rebuilding effort are beginning to take shape. Entrepreneurialism is sprouting; and unemployment, which was once a major problem, is coming under control. Our efforts are paying off. Reconstruction, together with an interim constitution, locally elected leaders and a functioning, better-trained security force all add up to a stable and more peaceful Iraq.

Today we meet to specifically discuss the complexity of coordinating our rebuilding of Iraq, primarily as it pertains to the larger construction projects and sustainment efforts. Currently, there are many U.S. Government agencies working to improve conditions in Iraq. For example, the Department of Defense, including the U.S. Army of Corps of Engineers and the U.S. Agency for International Development, are both working to rebuild Iraq. Both DOD and USAID have their own procurement shop, their own management team, and their own audit mechanisms. The committee is interested in the efforts made by each agency to manage and coordinate acquisition activities to ensure that taxpayer money is spent both effectively and efficiently.

In addition, enormous amounts of money have already or are about to be expended in the efforts to rebuild Iraq. We need to make sure that acquisition rules are being followed. Congress has spent years streamlining complex government rules and regula-

tions to make it easier for businesses to sell to the Federal Government, but did so in a way that carefully balances affordability, accountability, and accessibility to make sure taxpayer dollars are protected. It's our job to make sure that these things are happening in Iraq.

We hope to learn today how our acquisition system and the professionals who run it have responded to the challenges raised in Iraq. No one doubts that the circumstances are extremely difficult. I've seen the chaos on the ground there. The security situation is tenuous at best. Our servicemen and women are being killed and wounded. A number of contractor employees have also been killed and wounded.

Large-scale procurements are complex and difficult to understand in and of themselves. When it comes to procurement, if you're not confused, you're not paying attention.

Add in the urgency and inherent dangers of contracting in a war zone, and the challenge of acquiring urgently needed goods and services becomes quite daunting. Through this hearing we hope to separate fact from fiction, truth from rhetoric, and in turn help make sure we are coordinating contract processes in Iraq in a way that ensures success and safety.

Fortunately, our acquisition laws have been carefully crafted by Congress to provide enough flexibility for the government to quickly get the goods and services it needs in emergency situations. There are provisions in the acquisition laws that allow for carefully circumscribed exceptions to our standard for full and open competition to provide for a more limited, less time-consuming award of contracts for urgently needed supplies and services. I frankly cannot think of a situation that would better fit within these flexibilities than what we faced on the ground when we came into Iraq. Sometimes we just don't have time to take our time.

I find it ironic that those who are complaining that the government doesn't have sufficient people on the ground to oversee and administer the current contracts in Iraq would foster contracting strategies that would increase substantially the need for contract administration. For every complex problem, there is a simple solution that doesn't work.

I recognize that there have been mistakes. The contract oversight process is not always pretty, and the decisions made under the pressures of combat are not as always as lucid as those made under less-threatening conditions.

I commend my ranking member and others who have raised some important questions pertaining to the reconstruction process. Today I hope we can differentiate between real issues worthy of serious inquiry and those with little or no basis in fact that are raised solely to create a whiff of scandal.

There are some who have disagreements with contractors overpayments, and it should come as no surprise to anybody who's familiar with the administration of complex contracts in difficult circumstances. These difficulties should be viewed within the context of the wartime environment in Iraq.

Many of the disputes that have been made public show that the contract oversight process is indeed working. This hearing is part and parcel of a functioning oversight process.

Make no mistake, I have no patience for fraud or abuse. I expect that any such instances that are proven will result in harsh punishment for the perpetrators. I also expect that, as the conditions on the ground improve, the next generation of contracts will be awarded and administered in accordance with our standard acquisition procedures. Emergency procedures are for emergencies only.

This is a monumental task, and there is no room for error. Nor is there room for partisan sniping aimed merely at undermining the overall reconstruction efforts. We are interested in the truth, not rhetorical calisthenics. We are interested in helping coordinate the many important contracts in place today or planned for the future. In short, we are interested in moving forward with a contracting framework that benefits our reconstruction goals. We are not interested in simply repeating disingenuous sound bites.

Now, pursuant to committee rule 14, following the witnesses' opening statements, the ranking minority member and I shall each control 20 minutes in order to permit some important but complex lines of questioning and allow adequate time for full responses. Following the 40-minute questions, we will continue under the 5-minute rule.

Mr. Waxman and I have agreed that we don't expect any votes today at this point.

He has asked—requested of us that a number of documents be released from this committee. I understand that DOD has gone on their own volition and that these documents have been released.

We are also joining with him in a request for more documentation from the Department of Defense reiterating an earlier request for some of these documents, and we join him in this. If when we get the responses back, they are not adequate, we will then address what further avenues we may wish to pursue.

In the interests of time and given the 20-minute block agreement I have made with Mr. Waxman, we are limiting opening statements to the ranking member and myself. But statements will be included in the record, and you will have 10 calendar days to do so.

I also want to thank all of our witnesses for appearing before the committee, and I look forward to their testimony. I also want to recognize a new member of the committee, the gentleman from Ohio, Mr. Tiberi. We have had a couple of vacancies on this committee, and we are very happy to have him here. We understand he is going to be here for the entire hearing, and we appreciate it. Thank you.

At this time, I will yield for Mr. Waxman's opening statement.

[The prepared statement of Chairman Tom Davis follows:]

Opening Statement of Chairman Tom Davis
Government Reform Committee Hearing
The Complex Task of Coordinating Contracts Amid Chaos:
The Challenges of Rebuilding a Broken Iraq
March 11, 2004

We meet today to look into the complex task of coordinating contracts amid the chaos and challenges of rebuilding Iraq.

Even before the conclusion of major military actions there were plans for a major effort to rebuild Iraq's infrastructure and government. Emergency supplemental appropriations bills for both FY03 and FY04 have provided more than $20 billion to rebuild postwar Iraq. Many federal departments and agencies have already awarded or will soon award contracts for the sustainment and reconstruction efforts.

The rebuilding of Iraq is a monumental task. Saddam Hussein spent decades frittering away his nation's vast wealth on himself and his Baath party cronies, while little to nothing was spent to meet the urgent needs of the Iraqi people. Decades of neglect and inaction have turned this once great nation into a country where the majority of people live in poverty and despair.
However, with Saddam's ouster, we are witnessing a rebirth of Iraq. Freedom and liberation have brought a new sense of urgency to the Iraqi people; they understand what is at stake and we, as part of the coalition of the willing, must do our part to sustain freedom by rebuilding their nation.

Twenty days ago, I, along with other members of this committee returned from Iraq, where we witnessed the enormity of the reconstruction effort. This was my second trip, and in the six months since my last visit to the region, I saw significant progress in our reconstruction efforts.

The task at hand is enormous; it will be years before we are able to truly get Iraq running on its own. Yet each day Iraqis are getting a better life thanks to the dedicated American soldiers and civilians working there. Our reconstruction efforts are being completed, even under life threatening conditions. Our military is nothing short of superb. Besides ensuring the safety of the country, they have become master builders and diplomats. The use of funds from the Commanders Emergency Relief Program (CERP) paves the way for local and regional stabilization by allowing for small rebuilding projects that have an immediate impact on the local population.

For example, we recently met with General Odierno, Commander of the 4th Infantry Division, who told us how he used his CERP funds to build a water treatment facility in Tikrit and a sewage treatment facility in Baji. In many ways, the Commander's Emergency Relief Program is meeting the immediate needs until our larger construction projects are completed.

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Today we meet to specifically discuss the complexity of coordinating our rebuilding of Iraq, primarily as it pertains to the larger construction projects and sustainment efforts. Currently, there are many U.S. government agencies working to improve conditions in Iraq. For example, the Department of Defense, including the U.S. Army Corps of Engineers, and the U.S. Agency for International Development are both working to "rebuild" Iraq. Both DOD and USAID have their own procurement shop, their own management team, and their own audit mechanisms. The Committee is interested in the efforts made by each agency to manage and coordinate acquisition activities to ensure that taxpayer money is being spent effectively and efficiently.

In addition, enormous amounts of money have already or are about to be expended in our efforts to rebuild Iraq. We need to make sure that acquisition rules are being followed. Congress has spent years streamlining complex government rules and regulations to make it easier for businesses to sell to the federal government, but did so in a way that carefully balances affordability, accountability, and accessibility to make sure taxpayer dollars are protected. It's our job to make sure that is happening in Iraq.

We hope to learn today how our acquisition system and the professionals who run it have responded to the challenges raised in Iraq. No one doubts that the circumstances are extremely difficult. I've seen the chaos on the ground there. The security situation is tenuous at best. Our service men and woman are being killed and wounded. A number of contractor employees also have been killed or wounded.

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Fortunately our acquisition laws have been carefully crafted by Congress to provide enough flexibility for the government to quickly get the goods and services it needs in emergency situations. There are provisions in the acquisition laws that allow for carefully circumscribed exceptions to our standard for full and open competition to provide for a more limited, less time consuming award of contracts for urgently needed supplies and services. I frankly cannot think of a situation that would better fit within these flexibilities than what we are now facing on the ground in Iraq. Sometimes we just don't have the time to take our time.

I find it ironic that those who are complaining that the government does not have sufficient people on the ground to oversee and administer the current contracts in Iraq would foster contracting strategies that would increase substantially the need for contract administration. For every complex problem, there's a simple solution that doesn't work.

I recognize that there have been mistakes. The contract oversight process is not always pretty, and decisions made under the pressure of combat are not always as lucid as those made under less threatening conditions.

I commend my Ranking Member and others who have raised some important questions pertaining to the reconstruction process. Today I hope we can differentiate between real issues worthy of serious inquiry and those with little or no basis in fact that are raised solely to create a whiff of scandal.

That there have been disagreements with contractors over payments should come as no surprise to anyone familiar with the administration of complex contracts in difficult circumstances. These difficulties should be viewed within the context of the wartime environment in Iraq.

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Mr. WAXMAN. Thank you very much, Mr. Chairman. I want to thank you for holding this hearing today.

The subject we are going to consider, contracting in Iraq, urgently needs congressional oversight. It is an issue that has crucial implications for the success of our efforts in Iraq and for U.S. taxpayers. Usually I keep my remarks short at committee hearings, but today I am going to speak at some length in this opening statement.

I have been investigating contracting in Iraq for many months and I believe few of my colleagues understand just how big a mess this administration has created. I want to explain to the members of this committee and the public what is going wrong and why.

The problem starts with the procurement strategy that the administration is using in Iraq. It is profoundly flawed.

I have a chart that I want to display. It is over there.

The chart shows two numbers, the first, 2,300; 2,300 is the number of discrete reconstruction projects that the coalition provisional authority is planning to do in Iraq. The second, zero, is the number of projects that will be subject to competitive bidding.

Instead of promoting competition, the administration is giving contractors monopolies over huge sectors of the reconstruction effort. One company, Halliburton, gets all work related to oil reconstruction in southern Iraq. Another company, Parsons, gets all work related to oil reconstruction in northern Iraq. And they never have to bid against each other for any specific project. The administration has a procurement strategy that intentionally shields contractors from competition.

Think about this: For nearly a year both Halliburton and Bechtel have had enormous operations in Iraq. Both companies can do virtually the same work. But never once have they had to compete against each other for a specific project. This is a great deal for Bechtel and Halliburton, but it is an absolutely horrendous deal for the taxpayers.

These problems are compounded by the fact that many of the contracts that are being issued are cost-plus contracts. Under a cost-plus contract, the more the contractor bills, the more money the contractor makes. That is why cost-plus contracts are notoriously prone to abuse.

In the absence of competition to discipline the process and to hold down prices, the taxpayer has to rely on contracting officers working for the Defense Department to keep prices reasonable. These officials are supposed to scrutinize the proposals submitted by Halliburton and other contractors and reject those that are loaded up with unnecessary expenses. But they are inexperienced and overworked.

Representative John Dingell and I asked GAO to investigate what kind of job the Defense Department is doing managing the largest contract in Iraq, Halliburton's LOGCAP contract. The contract alone is worth over $4 billion to Halliburton.

GAO told us that the Army Central Command in Kuwait has not made cost control a priority. GAO found that the Army does not have the expertise or the personnel in Kuwait needed to ensure that taxpayers are not being overcharged. According to the General Accounting Office, inexperienced reservists are being sent to Ku-

wait and given key oversight responsibilities. A 2-week training course on contract management is the only preparation they receive.

GAO told us that in one instance the Army approved a LOGCAP contract worth $587 million to Halliburton in just 10 minutes. The documentation for this mammoth contract was just six pages long. In essence, this administration's approach to contractors like Halliburton is "trust but don't verify."

Auditors like the Defense Contract Audit Agency and criminal investigators with the Inspector General and the Justice Department can try to catch waste, fraud and abuse after it occurs, but there are few mechanisms in place to prevent overcharges from occurring in the first place. We are now learning that the administration's approach is an enormous mistake.

This week, the committee received two recent audits of Halliburton by DCAA. At the appropriate time—well, I won't need to move to have the committee release these documents publicly because I understand that we have all agreed and the DCAA has agreed to make these documents public, so they will be available. These audits are a scathing indictment of Halliburton.

According to DCAA, Halliburton's cost accounting system has, "significant deficiencies" and the company has repeatedly violated Federal acquisition regulations. Well, anybody who has followed this issue has heard Halliburton say over and over again that any violations or overcharges are isolated occurrences. This is what it said when it was revealed that Halliburton sought fees for millions of meals it never served, and it is what Halliburton said when it disclosed that company procurement officials participated in a $6 million kickback scheme, and this is also what Halliburton said to the DCAA.

When the audit agency gave Halliburton a chance to respond to its preliminary findings, Halliburton wrote, "this issue is not a significant estimating system deficiency as stated in the DCAA reports. Rather, this was a unique situation."

The problem with Halliburton's response is that it is not true. According to the DCAA, "The estimating deficiency is not a one-time occurrence. It is systemic."

Now here is a stunning fact that is revealed in the DCAA audit documents. The DCAA brought these systemic problems to the attention of the Army Corps of Engineers on January 13. Three days later, on January 16, the Army Corps gave Halliburton another $1.2 billion contract. It was as if the decisionmakers simply didn't care.

Yesterday, I sent my colleagues a briefing memorandum that went through some of these issues in detail, and I'd like to ask unanimous consent that it be made part of the hearing record.

Chairman TOM DAVIS. Hearing no objection, I would note that there are parts of the briefing memorandum that we take issue with on the factual side, Mr. Waxman. We will get to that in our questions, but with that understanding, without objection, it will be entered into the record.

[The information referred to follows:]

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INDEPENDENT

MEMORANDUM

March 10, 2004

To: **Democratic Members of the House Government Reform Committee**

Fr: **Rep. Henry A. Waxman**

Re: **New Information about Halliburton Contracts**

We have recently received significant new information from the Defense Contract Audit Agency, the General Accounting Office, and the Defense Energy Support Center about Halliburton's work in Iraq. The purpose of this memorandum is to bring this new information to your attention prior to tomorrow's Committee hearing on Iraq reconstruction contracts.

Halliburton has the largest contracts with the federal government for work in Iraq. Its two principal contracts are a contract to provide logistical support for U.S. military forces in Iraq, also known as "LOGCAP," and a contract to restore and operate Iraq's oil infrastructure. To date, Halliburton has been given task orders for projects in Iraq worth at least $3.4 billion under LOGCAP[1] and more than $2.4 billion under the oil contract.[2]

The new information we have received includes a December 31, 2003, audit of Halliburton by DCAA; a January 13, 2004, memorandum from DCAA to the Army Corps of Engineers and other Defense Department agencies; a recent briefing from GAO on the preliminary results of its investigation of the LOGCAP contract; and new information from the Defense Energy Support Center about the costs of importing gasoline into Iraq. This new information reveals the following major points:

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[1] U.S. Army Field Support Command, *Media Spreadsheet: LOGCAP Contract* (Jan. 6, 2004).

[2] U.S. Army Corps of Engineers, *Frequently Asked Questions: March 2003 Contract Obligation Status* (Feb. 9, 2004).

- DCAA's December 31 audit, known as a "Flash Report," found "significant" and "systemic" deficiencies in the way Halliburton estimates and validates costs. According to the DCAA audit, Halliburton repeatedly violated the Federal Acquisition Regulation and submitted a $2.7 billion proposal that "did not contain current, accurate, and complete data regarding subcontract costs." For example, DCAA found that Halliburton "did not disclose the termination of two subcontracts ... [that] were the basis for over $1 billion of projected food service costs."

- DCAA's January 13 memorandum to the Army Corps of Engineers concluded that Halliburton's deficiencies "bring into question [Halliburton's] ability to consistently produce well-supported proposals that are acceptable as a basis for negotiation of fair and reasonable prices," and it urged the Corps to "contact us to ascertain the status of [Halliburton's] estimating system prior to entering into future negotiations." Despite this explicit warning, the Corps awarded Halliburton a new $1.2 billion contract on January 16. The Corps later claimed: "We have our own internal audit process [and] haven't turned up any serious wrongdoing or major problems."

- GAO reported that there is a $700 million discrepancy between the cost of the certified proposal that Halliburton submitted on October 8, 2003, for the largest task order under LOGCAP and the cost of a revised proposal that Halliburton submitted on December 23, 2003, for the very same task order.

- GAO reported that the Defense Department exercises ineffective oversight over Halliburton's work in Iraq under the LOGCAP contract. According to GAO, a military review board approved a six-month renewal contract with Halliburton worth $587 million in just ten minutes and based on only six pages of supporting documentation. In addition, "logistics support units" sent to the region to provide commanders with contracting advice included military reservists with no contract experience and no previous knowledge of LOGCAP.

- The Defense Energy Support Center prepared a breakdown of the costs it incurred to import gasoline from Kuwait to Iraq from August to December 2003. According to the Center, its fuel costs for this period were $0.96 per gallon and its transportation costs were $0.36 per gallon — for a total cost of $1.32 per gallon. In contrast, Halliburton charged U.S. taxpayers $1.17 per gallon for fuel, $1.21 per gallon for transportation, $0.24 per gallon for "markup," and $0.02 per gallon for "other" expenses — for a total cost of $2.64 per gallon, twice as much as the Defense Energy Support Center.

These new findings follow months of mounting evidence that Halliburton has routinely and systematically overcharged the U.S. government. In December, DCAA reported that Halliburton submitted an unjustified cost proposal for $67 million in food services and overcharged the government $61 million for gasoline imports.[3] In January, Halliburton admitted

[3] U.S. Department of Defense, *Media Availability on the Kellogg Brown & Root Contract* (Dec. 11, 2003).

that procurement officials took up to $6.3 million in kickbacks.[4] And in February, two former Halliburton procurement officials described a pattern of overcharging and an irresponsible corporate ethic of "Don't worry about price. It's cost plus."[5] The Defense Department Inspector General has now opened a criminal investigation into allegations of Halliburton fraud, and criminal investigators from the State Department Inspector General's office have been asked to join this effort.[6]

Together, the totality of this information demonstrates that the Administration's approach to contracting in Iraq is profoundly flawed. Halliburton's inability to estimate and validate costs, combined with a lack of sufficient oversight on the part of the Defense Department, has resulted in apparently widespread contract abuses and overcharging of the U.S. taxpayer.

Halliburton's "Significant Deficiencies"

On December 31, 2003, DCAA issued an audit report on Halliburton's cost estimating system under Task Order 59 of LOGCAP.[7] Task Order 59 is the largest task order under the LOGCAP contract. This is the task order under which Halliburton provides support services such as laundry, sanitation, and food to U.S. military forces in Iraq.

The audit report, known as a "Flash Report," found "significant deficiencies" in Halliburton's cost estimating practices. According to DCAA, these deficiencies "could adversely affect the organization's ability to propose subcontract costs in a manner consistent with applicable government contract laws and regulations."

According to the Flash Report, Halliburton submitted a $2.7 billion proposal that "did not contain current, accurate, and complete data regarding subcontractor costs." The auditors provided specific examples. For instance, the report found that that Halliburton "did not disclose the termination of two subcontracts ... [that] were the basis for over $1 billion of projected food service costs." In other words, Halliburton provided government auditors an estimate for $1 billion worth of food services, but did not inform them that the estimate was based on subcontracts that had been terminated for cause. The report also noted that Halliburton submitted costs of $208.8 million for certain food services "without disclosing, referencing, or

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[4] *Halliburton Tells Pentagon Workers Took Kickbacks To Award Projects in Iraq*, Wall Street Journal (Jan. 23, 2004).

[5] Letter from Reps. Henry A. Waxman and John D. Dingell to William H. Reed, Director, Defense Contract Audit Agency (Feb. 12, 2004).

[6] Letter from Reps. Henry A. Waxman and John D. Dingell to Joseph E. Schmitz, Inspector General, Department of Defense (Feb. 24, 2004).

[7] Defense Contract Audit Agency, *Flash Report on Estimating System Deficiency Found in the Proposal for Contract No. DAAA09-02-D-007, Task Order 59* (Dec. 31, 2003) (Audit Report No. 3311-2004K24020001).

mentioning the fact that they had already issued subcontracts for these sites ... totaling $141.5 million."

The Flash Report also found that Halliburton's proposal did not comply with the Federal Acquisition Regulation. According to the Flash Report, among other violations, Halliburton (1) failed to submit cost and pricing data; (2) failed to provide data showing the degree of competition and reasonableness of price for subcontracts and procurements; and (3) failed to analyze the prices and costs of subcontractors. DCAA further noted that Halliburton did not even comply with its own Cost Estimating Manual, but provided "no valid reason for deviating from the manual."

Prior to finalizing the Flash Report, DCAA provided Halliburton a chance to respond to its preliminary audit findings. In a December 4, 2003, letter to DCAA, Halliburton argued:

> [T]his issue is not a "significant estimating system deficiency" as stated in the DCAA draft report. Rather, this was a unique situation due to the significant cost, amount of data and volume of effort that was associated with the TO 59 proposal.

DCAA categorically rejected Halliburton's contention in the final Flash Report. DCAA concluded: "the estimating deficiency is not a one time occurrence; it is systemic."

Halliburton's New $1.2 Billion Contract

Based on the Flash Report, DCAA sent a January 13, 2004, memorandum to the Army Corps of Engineers and other Defense Department offices warning that Halliburton could not adequately estimate its costs for work in Iraq.[8] The DCAA memorandum summarized the findings of the Flash Report and emphasized that Halliburton's systemic deficiencies "bring into question [Halliburton's] ability to consistently produce well-supported proposals that are acceptable as a basis for negotiation of fair and reasonable prices." The December 31 Flash Report was distributed with the memorandum as an attachment.

The January 13 memorandum concluded with the following explicit warning to the Corps:

> We recommend that you contact us to ascertain the status of [Halliburton's] estimating system prior to entering into future negotiations.

The Corps, however, appears to have ignored this warning. On January 16, just three days after DCAA sent out its memorandum, the Corps entered into a new $1.2 billion contract with Halliburton to restore the oil infrastructure in the southern half of Iraq.[9]

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[8] Defense Contract Audit Agency, *Status of Brown & Root Services (BRS) Estimating System Internal Controls* (Jan. 13, 2004).

[9] U. S. Army Corps of Engineers, *News Release: U. S. Army Corps of Engineers Awards Contracts for Repair of Iraq's Oil Infrastructure* (Jan. 16, 2004).

According to the Corps, this new award was based on four factors:

(1) past performance and experience;
(2) business/management approach;
(3) contract administration plan; and
(4) cost.[10]

The Corps has not explained how it reached its decision that Halliburton satisfied these four factors. The December 31 Flash Report and the January 13 memorandum demonstrate major deficiencies in Halliburton's past performance, one of the most important factors in the contract award. The documents also raise significant issues about Halliburton's management approach and its plans for contract administration, as well as its ability to accurately predict costs.

Based on the significant and systemic deficiencies reported in DCAA's December 31 Flash report and conveyed in DCAA's January 13 memo, the decision by the Corps to award Halliburton the new $1.2 billion contract just three days later is incomprehensible. In essence, it required the Corps to ignore DCAA's warnings. In explaining this decision, Army Corps spokesman Scott Saunders stated on February 1: "We have our own internal audit process [and we] haven't turned up any serious wrongdoing or major problems."[11]

The $700 Million Discrepancy

GAO's investigators also reported significant discrepancies in Halliburton's cost estimates under LOGCAP.

At a February 13, 2004, briefing for Committee staff, GAO reported that Halliburton submitted an "initial certified proposal" for Task Order 59 of $2.7 billion. This initial proposal was submitted to DCAA on October 8, 2003. According to GAO, this initial certified proposal was rejected by the Defense Department after DCAA's preliminary audit found significant problems. GAO reported that six weeks later, on December 23, 2003, Halliburton submitted a revised certified proposal to the Defense Department for the same task order. According to GAO, this revised proposal was approximately $700 million lower than the October submission.

This is an enormous discrepancy, and it remains largely unexplained. Although GAO has been in contact with Defense Department officials regarding the new estimate, GAO has reported that it was not able to obtain a breakdown of what portion of this discrepancy was due to an overstatement of costs and what portion was due to changing requirements.

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[10] U.S. Army Corps of Engineers, *Frequently Asked Questions: Engineer Support to Operation Iraqi Freedom* (Jan. 17, 2004).

[11] *Halliburton Contract Questions Dog White House,* Chicago Tribune (Feb. 1, 2004).

Moreover, the actual amount of the discrepancy may end up being even greater than $700 million. According to GAO, Halliburton withdrew its December 23 submission under continued criticism from DCAA. GAO does not expect another revised proposal until May 2004.

According to GAO, Halliburton's fee is based on a percentage of the certified proposal, regardless of the amount of actual costs incurred. The LOGCAP contract provides Halliburton with a guaranteed 1% fee with a potential additional fee of up to 2% based on performance. Thus, had Halliburton's initial $2.7 billion proposal been accepted, the company would have been entitled to a fee of $27 million to $81 million for Task Order 59, even if its actual costs were hundreds of millions of dollars less.

The Lack of Effective Pentagon Cost Controls

The GAO investigators also reported that government oversight for LOGCAP is deficient. According to GAO, Army Central Command in Kuwait has not made cost control a priority in its utilization of the LOGCAP contract.

For example, GAO reported that some members of "logistics support units" sent to the region to advise military commanders on the LOCGAP contract had no prior contract management experience. These units are supposed to prepare independent cost estimates that can be compared with Halliburton's estimates. Yet according to GAO, reservists who had never heard of LOGCAP were given only a two-week training course before being sent to the Middle East to provide contracting advice to commanders. GAO explained that, after all designated LOGCAP Support Unit reservists were tapped, inexperienced civilian reservists were called up to take on this advisory function.

GAO further reported that the Army's Combined Acquisition Review Board approved a six-month renewal contract with Halliburton worth $587 million in just ten minutes and based on only six pages of supporting documentation.

Halliburton's Inflated Gasoline Charges

New information from the Defense Energy Support Center raises further questions about Halliburton's inflated prices for gasoline imported from Kuwait into Iraq.

In November, the Army Corps of Engineers informed the minority staff that Halliburton charged an average price of $2.64 per gallon to import approximately 74 million gallons of gasoline from Kuwait into Iraq for civilian uses. Halliburton hired an obscure Kuwaiti subcontractor, Altanmia Commercial Marketing Company, which had no previous fuel procurement or transportation experience, to import gasoline from Kuwait. Halliburton paid Altanmia $1.17 per gallon to purchase the gasoline from the Kuwait Petroleum Company and $1.21 per gallon to transport the gasoline from Kuwait to Iraq by fuel truck. Halliburton then

received a $0.24 per gallon overhead "markup" as well as a $0.02 per gallon "other" charge, for a total cost of $2.64 per gallon.[12]

At the same time Halliburton was using Altanmia to import gasoline from Kuwait into Iraq for civilian uses, the Defense Energy Support Center was using private contractors to import gasoline from Kuwait into Iraq for military purposes. The Center has now made available its average gasoline prices from Kuwait for the five-month period from August to December. According to the Center, its average total price to import gasoline from Kuwait between August 5 and December 31, 2003, was $1.32 per gallon.[13] This is exactly half the $2.64 price charged by Halliburton. The Center's total price is composed of the cost of purchasing the gasoline and the cost of transporting it. There is no extra $0.26 per gallon markup like the one Halliburton charges.

Under its fuel contract, the Center paid an average of $0.96 per gallon for the gasoline itself. This average reflects a range of gasoline market prices, from low costs of $0.88 per gallon in September to high costs of $1.05 in December. At no time did the Defense Energy Support Center pay more than $1.05 for a gallon of gasoline.[14] Unlike Halliburton, the Center bought its gasoline directly from the Kuwait Petroleum Company, not through a middleman like Altanmia.[15] The Center's fuel contract was a "fixed price with escalation" contract. In other words, there was an established differential between the price charged by the Kuwait Petroleum Company and the published Platt's Arab Gulf "spot price." Every two weeks, the gasoline price would be adjusted to take into account changes in the market price.[16]

The Center's average transportation cost was just $0.36 per gallon during this period.[17] The Center relied on three contractors to transport the gasoline to Camp Cedar II, 150 miles

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[12] Letter from Reps. Henry A. Waxman and John D. Dingell to National Security Advisor Condoleezza Rice (Dec. 10, 2003).

[13] E-mail from Legislative Affairs, Defense Logistics Agency, to Minority Staff, Committee on Government Reform (Feb. 20, 2004).

[14] E-mail from Legislative Affairs, Defense Logistics Agency, to Minority Staff, Committee on Government Reform (Feb. 7, 2004).

[15] E-mail from Legislative Affairs, Defense Logistics Agency, to Minority Staff, Committee on Government Reform (Jan. 21, 2004).

[16] Telephone briefing by the Defense Energy Support Center for Minority Staff, Committee on Government Reform (Jan. 28, 2004).

[17] E-mail from Legislative Affairs, Defense Logistics Agency, *supra* note 13. According to the Defense Energy Support Center, the $0.36 average price for transportation is an approximate price that is based upon 30-day months, truck loads equaling 8,000 gallons, and a two and a half–day delivery period.

inside southern Iraq.[18] All three contracts were fixed-price contracts under which the contractor, rather than the U.S. government, "bears the risk of price fluctuations."[19] The Center's average transportation cost was a weighted average of the rates of three contractors: TriStar Transport, Mubarak & Sons Transport, and LeNouvelle General Trading and Contracting Co. The companies charged different rates for each fuel truck per day: $750 for TriStar, $1,175 for Mubarak, and $1,500 for LeNouvelle. To further reduce costs, the Defense Energy Support Center discontinued the use of LeNouvelle, the most expensive of the three contractors, on February 1.[20]

According to the Defense Department Inspector General, Halliburton's high fuel costs are now under criminal investigation.[21]

Conclusion

This new information has major implications for contracting in Iraq, the subject of tomorrow's hearing. It depicts a situation where costs are virtually uncontrolled and Halliburton can overcharge the taxpayer by phenomenal sums. Given our nation's mounting debt and the escalating costs in Iraq, all members of Congress should be extraordinarily concerned about this new evidence of waste, fraud, and abuse in contracting in Iraq.

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[18] Telephone briefing by the Defense Energy Support, *supra* note 16. The U.S. military handles the transportation of the gasoline from Camp Cedar II.

[19] E-mail from Legislative Affairs, Defense Logistics Agency, *supra* note 14.

[20] *Id.*

[21] *Pentagon Opens Criminal Inquiry of Halliburton Pricing,* New York Times (Feb. 24, 2004).

Mr. WAXMAN. It is not just the government auditors who are complaining about Halliburton's practices. Halliburton's own internal auditors have said that the company procedures are, "antiquated" and that it has, "weak internal controls."

Last month, my staff was contacted by two former Halliburton procurement officers. They described company practices that systematically overcharge the taxpayer on hundreds of routine requisitions every day. When they tried to protest, they were ignored. They said that the company's motto was "Don't worry about price. It's cost-plus."

Well, it's very hard to get details from the administration about the specific amounts Halliburton is charging for particular projects. The White House, Secretary of Defense, and the USAID all have an aversion to any form of oversight. When Representative Dingell and I wrote letters raising significant issues, they were almost always ignored. But we have been able to penetrate one particular contract, Halliburton's contract to import fuel from Kuwait into Iraq; and what we have learned is that Halliburton and its obscure subcontractor, Altanmia, have been gouging the taxpayer.

I have another chart, and I want to show this to everyone here.

Halliburton imports gasoline from Kuwait into Iraq for Iraqis to use. The Defense Energy Support Center imports gasoline from Kuwait into Iraq for the military to use. The chart simply compares the prices the government pays with those that Halliburton pays. The differences are astounding.

Gasoline in the Middle East is a commodity. Everyone should be able to get it at essentially the same price, but Halliburton is paying over 20 cents more per gallon than the Energy Support Center just to purchase the fuel. Both Halliburton and the Energy Support Center have to transport the fuel through dangerous conditions into Iraq, both entities are using private contractors to handle the transportation, and both entities receive, military protection for convoys. But it costs the Energy Support Center just 36 cents per gallon compared to $1.21 for Halliburton, and then Halliburton adds on a markup for itself of 24 cents per gallon and another category called "other" charge of 2 cents per gallon. The end result is that it costs the taxpayer twice as much when Halliburton imports the fuel as it would cost the government to do it.

Representative Dingell and I first raised this issue on October 15. Since then, all I have been hearing from the Army Corps of Engineers, which is the agency responsible for the fuel contract, is a string of denials and platitudes. As recently as February 1, the Corps spokesman said, "We have our own internal audit process, and we haven't turned up any serious wrongdoing or major problems."

When you get to the bottom of this, that is the real problem. The policymakers in this administration don't seem to care about the pattern of waste, fraud and abuse that is coming to light.

Fifty years ago, the CEO of General Motors said, what is good for the country is good for General Motors and what is good for General Motors is good for America. Well, I have a message to this administration: What is good for Halliburton is not always good for America. Iraq is a dangerous country. All of us in Congress want to do whatever is necessary to make sure our troops have the

equipment and protection they need, and Americans are a generous people. They are willing to spend billions to help Iraqis rebuild their nation and establish democracy. But gouging and profiteering is heinous and should never be tolerated.

I firmly believe that Congress has an important oversight roll to play in ensuring the wise expenditure of taxpayers' dollars. Part of the problems that we are experiencing can be attributed to the lack of vigorous congressional oversight. But I'm encouraged by the recent steps that Chairman Davis has taken. He has joined me in requesting the DCAA audit documents. He scheduled this hearing, and he has promised to hold another hearing hopefully by the end of April. This is not easy for him to do, and I am sure it will alienate many in the administration, but I commend him for the steps that he is taking, even as I will be pressing him to take more.

In closing, let me say that I look forward to today's hearing and the opportunity to hear from and question the distinguished witnesses before us.

Thank you, Mr. Chairman.

[The prepared statement of Hon. Henry A. Waxman follows:]

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BERNARD SANDERS, VERMONT,
INDEPENDENT

Statement of Rep. Henry A. Waxman, Ranking Minority Member
Committee on Government Reform
Hearing on
The Complex Task of Coordinating Contracts Amid Chaos: The Challenges of Rebuilding a Broken Iraq

March 11, 2004

Mr. Chairman, I want to thank you for holding this hearing today. The subject we are going to consider — contracting in Iraq — urgently needs congressional oversight. It is an issue that has crucial implications for the success of our efforts in Iraq and for the U.S. taxpayer, yet it is being badly mismanaged.

Usually, I keep my remarks short at Committee hearings. But today, I am going to speak at some length. I have been investigating contracting in Iraq for many months, and I believe few of my colleagues understand just how big a mess this Administration has created. I want to explain to the members of this Committee — and to the public — what is going wrong and why.

The problems start with the procurement strategy that the Administration is using in Iraq. It is profoundly flawed.

I have a chart that I want to display. It shows two numbers. The first — 2,300 — is the number of discrete reconstruction projects that the Coalition Provisional Authority is planning to do in Iraq. The second — 0 — is the number of projects that will be subject to competitive bidding.

Instead of promoting competition, the Administration is giving contractors monopolies over huge sectors of the reconstruction effort. One company — Halliburton — gets all work related to oil reconstruction in southern Iraq, and another company — Parsons — gets all work related to oil reconstruction in northern Iraq. And they never have to bid against each other for any specific project.

The Administration has a procurement strategy that intentionally shields contractors from competition.

Think about this. For nearly a year, both Halliburton and Bechtel have had enormous operations in Iraq. Both companies can do virtually the same work. But never once have they had to compete against each other for a specific project.

This is a great deal for Halliburton and Bechtel, but it's an absolutely horrendous arrangement for the taxpayer.

These problems are compounded by the fact that many of the contracts that are being issued are "cost-plus" contracts. Under a cost-plus contract, the more the contractor bills, the more money the contractor makes. That's why cost-plus contracts are notoriously prone to abuse.

In the absence of competition to discipline prices, the taxpayer has to rely on contracting officers working for the Defense Department to keep prices reasonable. These officials are supposed to scrutinize the proposals submitted by Halliburton and the other contractors and reject those that are loaded up with unnecessary expenses.

But they are inexperienced and overwhelmed.

Rep. John Dingell and I asked GAO to investigate what kind of job the Defense Department is doing managing the largest contract in Iraq: Halliburton's LOGCAP contract. This contract alone is worth over $4 billion to Halliburton.

GAO told us that Army Central Command in Kuwait has not made cost control a priority. GAO found that the Army does not have the expertise or the personnel in Kuwait needed to ensure that taxpayers are not overcharged. According to GAO, inexperienced reservists are being sent to Kuwait and given key oversight responsibilities. A two-week training course on contract management is the only preparation they receive.

GAO told us that in one instance, the Army approved a LOGCAP contract worth $587 million to Halliburton in just ten minutes. The documentation for this mammoth contract was just six pages long.

In essence, this Administration's approach to contractors like Halliburton is "trust but don't verify." Auditors like the Defense Contract Audit Agency and criminal investigators with the Inspector General and the Justice Department can try to catch waste, fraud, and abuse after it occurs. But there are few mechanisms in place to prevent overcharges from occurring in the first place.

We are now learning that the Administration's approach is an enormous mistake. This week, the Committee received two recent audits of Halliburton by DCAA. At the appropriate time, I will move that the Committee release these documents publicly.

These audits are a scathing indictment of Halliburton. According to DCAA, Halliburton's cost accounting system has "significant deficiencies," and the company has repeatedly violated federal acquisition regulations.

Anybody who has followed this issue has heard Halliburton say over and over again that any violations or overcharges are isolated occurrences. This is what it said when it was revealed that Halliburton sought fees for millions of meals it never served. And this is what Halliburton said when it disclosed that company procurement officials participated in a $6 million kickback scheme.

This is also what Halliburton said to DCAA. When the audit agency gave Halliburton a chance to respond to its preliminary findings, Halliburton wrote: "This issue is not a 'significant estimating system deficiency' as stated in the DCAA draft report. Rather, this was a unique situation."

The problem with Halliburton's response is that it's not true. According to DCAA — and I quote — "the estimating deficiency is not a one time occurrence; it is systemic."

Here's a stunning fact that is revealed in the DCAA audit documents. DCAA brought these systemic problems to the attention of the Army Corps of Engineers on January 13. Three days later — on January 16 — the Army Corps gave Halliburton another $1.2 billion contract. It was as if the decisionmakers simply didn't care.

Yesterday, I sent my colleagues a briefing memorandum that went through some of these issues in detail. I ask unanimous consent that it be made part of this hearing record.

It is not just the government auditors who are complaining about Halliburton's practices. Halliburton's own internal auditors have said that the company's procedures are "antiquated" and that it has "weak internal controls."

And last month, my staff was contacted by two former Halliburton procurement officers. They described company practices that systematically overcharged the taxpayer on hundreds of routine requisitions every day. When they tried to protest, they were ignored. They said that the company's motto was "Don't worry about price. It's cost-plus."

It's very hard to get details from the Administration about the specific amounts Halliburton is charging for particular projects. The White House, the Secretary of Defense, and U.S. AID all have an aversion to any form of oversight. When Rep. Dingell and I write letters raising significant issues, they are almost always ignored.

But we have been able to penetrate one particular contract: Halliburton's contract to import fuel from Kuwait to Iraq. And what we have learned is that Halliburton and its obscure subcontractor Altanmia have been gouging the taxpayer.

I have another chart I want to show. Halliburton imports gasoline from Kuwait into Iraq for Iraqis to use. The Defense Energy Support Center imports gasoline from Kuwait into Iraq for the military to use. The chart simply compares the prices the government pays with those that Halliburton pays.

The differences are astounding. Gasoline in the Mideast is a commodity. Everyone should be able to get it at essentially the same price. But Halliburton is paying over 20 cents more per gallon than the Energy Support Center just to purchase the fuel.

Both Halliburton and the Energy Support Center have to transport the fuel through dangerous conditions into Iraq. Both entities are using private contractors to handle the transportation. And both entities receive protection from military convoys. But it costs the Energy Support Center just $0.36 per gallon, compared to $1.21 for Halliburton.

And then Halliburton adds on a "markup" for itself of 24 cents per gallon and an "other" charge of 2 cents per gallon.

The end result is that it costs the taxpayer twice as much when Halliburton imports fuel as it costs when the government does.

Rep. Dingell and I first raised this issue on October 15. Since then, all I've been hearing from the Army Corps of Engineers, which is the agency responsible for the fuel contract, is a string of denials and platitudes. As recently as February 1, the Corps spokesman said: "We have our own internal audit process [and we] haven't turned up any serious wrongdoing or major problems."

And when you get to the bottom of this, that's the real problem. The policymakers in this Administration don't seem to care about the pattern of waste, fraud, and abuse that is coming to light. Fifty years ago, the CEO of General Motors said, "What is good for the country is good for General Motors, and what is good for General Motors is good for America."

Well, I have a message to this Administration, "What's good for Halliburton is not always good for America."

Iraq is a dangerous country. All of us in Congress want to do whatever is necessary to make sure our troops have the equipment and protection they need. And Americans are a generous people. They are willing to spend billions to help Iraqis rebuild their nation and establish democracy. But gouging and profiteering is heinous and should never be tolerated.

I firmly believe that Congress has an important oversight role to play in ensuring the wise expenditure of taxpayer dollars. Part of the problems that we are experiencing can be attributed to the lack of vigorous congressional oversight. But I am encouraged by recent steps that Chairman Davis has taken. He joined with me in requesting the DCAA audit documents. He scheduled this hearing. And he has promised to hold another hearing in April or May,

This is not easy for him to do, and I am sure it will alienate many in the Administration. But I commend him for the steps that he is taking — even as I will be pressing him to do more.

In closing, let me say that I look forward to today's hearing and the opportunity to hear from and question the distinguished witnesses before us.

Chairman TOM DAVIS. Thank you very much, Mr. Waxman.

We have our panel today. We have Major General Carl Strock, who is the Director of Civil Works, Army Corps of Engineers; General Paul Kern, Commanding General, U.S. Army Materiel Command, Department of Defense; Major General Wade McManus, Commanding General of the U.S. Army Field Support Command; Ms. Tina Ballard, the Deputy Assistant Secretary of the Army for Policy and Procurement, U.S. Department of Defense; Lewis Lucke, Deputy Assistant Administrator, USAID; Honorable Dov Zakheim, the Under Secretary of Defense, Comptroller, and Chief Financial Officer, Department of Defense. We have Mr. William Reed, the Director of the Defense Contract Audit Agency [DCAA]; and Rear Admiral David Nash, the director of Iraq Program Management Office, Coalition Provisional Authority.

It is our committee's policy that all witnesses be sworn before you testify. So if you would rise with me.

[Witnesses sworn.]

Chairman TOM DAVIS. I think I went over with everybody that we try to keep a 5-minute rule. Mr. Waxman and I didn't observe it. So we understand. Your total statement will be in the record. Obviously, there are a lot of allegations and things going out there. We want to give you adequate time to make your statements.

We have a distinguished panel that I think for most of you are career military or civil servants, served under administrations of both parties. We appreciate your taking the time to be here.

I am going to start with General Strock and work our way down.

General STROCK. Thank you, Mr. Chairman.

Chairman TOM DAVIS. I also need to recognize that Dr. Zakheim will be retiring on April 15. I want to extend my gratitude for your many years of service to our country and best wishes as you move forward and thank you for being with us today.

Mr. ZAKHEIM. Thank you, Mr. Chairman.

Chairman TOM DAVIS. The others will be here for our next hearing, but this may be our last bite at you.

Dr. Zakheim do you want to start off.

Mr. ZAKHEIM. I think if you would like to go in that order, just in terms of the flow, of how this is all seen in terms of oversight, then probably starting with General Strock is the right way to go. I will be talking specifically about contract performance oversight, and to start there is almost like starting a story in the middle. So with your permission I think we will start at——

Chairman TOM DAVIS. We will then thank you.

Again General Strock, thank you for being with us.

STATEMENTS OF MAJOR GENERAL CARL A. STROCK, DIRECTOR OF CIVIL WORKS, U.S. ARMY CORPS OF ENGINEERS, U.S. DEPARTMENT OF DEFENSE; GENERAL PAUL J. KERN, COMMANDING GENERAL, U.S. ARMY MATERIEL COMMAND, U.S. DEPARTMENT OF DEFENSE; MAJOR GENERAL WADE H. McMANUS, JR., COMMANDING GENERAL, U.S. ARMY FIELD SUPPORT COMMAND, U.S. DEPARTMENT OF DEFENSE; TINA BALLARD, DEPUTY ASSISTANT SECRETARY OF THE ARMY (POLICY AND PROCUREMENT), U.S. DEPARTMENT OF DEFENSE; LEWIS LUCKE, DEPUTY ASSISTANT ADMINISTRATOR, U.S. AGENCY FOR INTERNATIONAL DEVELOPMENT; DOV S. ZAKHEIM, UNDER SECRETARY OF DEFENSE (COMPTROLLER) AND CHIEF FINANCIAL OFFICER, U.S. DEPARTMENT OF DEFENSE; WILLIAM H. REED, DIRECTOR, DEFENSE CONTRACT AUDIT AGENCY, U.S. DEPARTMENT OF DEFENSE; AND REAR ADMIRAL DAVID NASH, USN (RET.), DIRECTOR, IRAQ PROGRAM MANAGEMENT OFFICE, COALITION PROVISIONAL AUTHORITY

General STROCK. Mr. Chairman and members of the committee, thank you for allowing us to testify today. It really is an honor to be here to tell you a bit about what we faced in Iraq.

As you mentioned, I am the Director of Civil Works for the U.S. Army Corps of Engineers, but from March to September I served with ORHA and later CPA in a number of capacities, culminating as the Deputy Director for Infrastructure in the CPA. What I would like to do today is give you a limited description of the operating environment that was faced by coalition military forces and civil authorities as we went into Baghdad.

Sir, ORHA was established in January 2003—that's the Office of Reconstruction and Humanitarian Assistance—and we deployed to Kuwait on March 15, 2003. ORHA consisted of three pillars: reconstruction, led by the U.S. Agency for International Development [USAID]; civil administration, led by the Department of Defense; humanitarian assistance, led by the Department of State; and three regional coordinators for north, central and south Iraq headed by two retired general officers and one former Ambassador.

The priority of effort for ORHA initially was the planning for an expected humanitarian crisis. Significant effort went into planning for food, water, shelter and medical support. The reconstruction focus was to repair damaged infrastructure to prewar conditions. We understood that the future of Iraq relied on the integrity of the infrastructure, so careful efforts were made to use precision weapons to minimize impacts on infrastructure. The ground forces were also sensitive to the need to limit damage to infrastructure. The U.S. Agency for International Development was given a $680 million effort to apply to all sectors of infrastructure, and oil was handled separately through a contract under a task force to restore Iraqi oil from the Corps of Engineers that reported directly to coalition forces land component commander.

The third element of ORHA was civil administration, and that was aimed at the reestablishment of government functions in the liberated country. This consisted of senior advisors for each of the 23 ministries in teams from one to five. We expected that the lead-

ership would flee but that ministry work force and facilities would be intact on our arrival.

Lieutenant General Gardner and his leadership really concentrated on creation of a guiding coalition for the future of Iraq. The first elements deployed to the port of Umm Qasr in late March, shortly after the commencement of the hostilities, and the main body began deployment to Baghdad in mid-April. When we arrived, we found a country roughly the size of California in terms of population and geography where virtually every element of government did not exist.

There was relatively little damage due to combat operations, with the exception of the communications infrastructure which was deliberately targeted. We anticipated some looting but not as significant as it turned out to be. It was extremely difficult for our forces to control, and it was especially bad in government facilities. We also anticipated some level of sabotage, but again this exceeded our expectations, not as much as expected in the oil infrastructure, where very few fires were set, but much more in other elements of infrastructure. Virtually every public building was burned, with its records, its equipment and supplies all destroyed.

The most challenging aspect we found in the infrastructure was really not about the damage caused by the war and its aftermath but by 30 years of neglect under the Saddam regime. We found an infrastructure that was fragile and antiquated, that was really on its last legs. It was only to the credit of the Iraqi public servants that this infrastructure worked at all, largely as we understand it through threat that they produce for the country. Saddam also used basic services and infrastructure to reward those who favored him and to punish those who did not.

In the electricity sector, there was no generation of electricity when it arrived in Baghdad, a tremendous challenge. There was no water treatment. There was no sewage flowing. All the irrigation in the country had ceased. Fuel supplies were far more limited than we anticipated. The hospitals were in darkness and closed down. Schools were not operating. The work force will be expected to take advantage of.

As expected, the key leaders were absent. They either fled or had been removed from debaathification. But the remaining civil servants we found were competent, committed and courageous. However, they really lacked a sense of initiative that is so important in a self-performing government and virtually had to be told to do everything that was necessary. They also lacked facilities, tools, and equipment and supplies and money to get their job done.

Finally, the security situation that all of us faced was a tremendous challenge for everyone.

I might add that ORHA, those civil servants who went in with General Gardner, faced exactly the same living conditions as the Iraqis—no food, no fuel, no power, no transportation, everything the same.

Sir, when we got on the ground we first established a regional presence through our regional coordinators to include Baghdad. We relied very heavily on the military forces in the early stages. Their civil affairs and line units really carried the weight of the recon-

struction and establishment of government, utilizing seized and invested assets and their own capabilities.

General McKiernan, who commanded the Combined Forces Land Component Command, recognized the need early on to get electricity flowing in the country, so he convened a task force called "fajr," which is first light in Arabic. It's a multidisciplinary task force led by Brigadier Steve Hawkins that went into Baghdad right behind the military forces with a priority to establish electricity, to first furnish it to hospitals, then water supply, then sewage treatment, and finally to domestic needs of the Iraqi people.

We also found a flooding situation on our hands, as all the reservoirs had been abandoned and they were operated at free flow. Working with the Iraqi public servants we were able to find, we brought the rivers under control, and we started up the power plants and began to establish the electrical grid and began to treat water and get hospitals back on line. Eventually Task Force Fajr expanded their scope to a national level.

Another task force that was established was Task Force Restore Iraqi Hope—Iraqi Oil. On February 13, the Army was designated as executive agent for restoration of oil infrastructure, and that authority was passed on to the U.S. Army Corps of Engineers, which further delegated authority to Brigadier General Bob Creer from the Southwestern Division to pull together a task force and accomplish that mission.

The immediate mission was to fight anticipated fires and to safely shut down the oil fields in Kirkuk and Rumaila and then to bring the refineries, pipelines and export facilities back into operation. We used LOGCAP to reposition the firefighting forces that we needed for the immediate aftermath of the fighting, and after careful analysis decided to go to sole source with Kellogg, Brown and Root services to accomplish, the reconstruction of the oil infrastructure.

There was far less sabotage than expected. We quickly brought the fires under control with the assistance of the Kuwaitis and, working with the Iraqi Oil Ministry, have made remarkable progress. We are now at prewar oil production levels of 2.5 million barrels per day. We are exporting 1.5 million barrels per day and refining about 500,000 barrels per day for domestic consumption. The expected earnings are $1.5 to $2 billion a month; and so far, to date, we have returned $8 billion to the DFI for use by the Iraqi people.

Task force RIO also picked up an additional responsibility to provide domestic fuel for all the people of Iraq. This is not just gasoline. It included diesel, kerosene and LPG, which they used for cooking and heating.

Sir, our final task was Task Force Restore Iraqi Electricity. In August, General Abizaid was very concerned about the progress of reconstruction. He was concerned that we were losing the consent of the Iraqi people, and frequently you heard from these people that this is the Nation that put a man on the moon but we can't get the lights on in Baghdad. Out of frustration, General Abizaid convened a conference in which he wanted to look at what we were doing with the electricity, the oil and refined fuel and the security situation that cared for all that infrastructure.

One of the outcomes of that conference was the need for a FEMA-like capability similar to our domestic disaster response where teams of experts with flexible contracting tools and the necessary resources to fix problems as they encountered them could flow into Iraq. We deployed this task force within 2 weeks. We pulled General Steve Hawkins back, not to the fight and put him ashore, and since that time we've contributed in many ways to the restoration of electricity working under the leadership of USAID and the CPA.

We accomplished the first mission of 4,400 megawatts of productivity in October, and we are well on the way to achieving the 6,000 megawatt target by May. The task force really focused on temporary generation, distribution controls and logistics, while USAID focused on the longer-term aspects of electrical generation and distribution. To do this, we employed four competitively bid projects much like the IDIQs used by LOGCAP and Task Force RIO, and so far our efforts have been tremendously successful.

My written includes far more detail, but I again appreciate the opportunity to lay out for you the situation we faced and some of the mechanisms we employed to address.

Chairman TOM DAVIS. Thank you very much. As I noted before, your entire statements are in the record; and questions will be based on the entire statement.

[The prepared statement of General Strock follows:]

STATEMENT BY

MAJOR GENERAL CARL STROCK
DIRECTOR OF CIVIL WORKS, U.S. ARMY CORPS OF ENGINEERS

BEFORE THE

COMMITTEE ON GOVERNMENT REFORM
UNITED STATES HOUSE OF REPRESENTATIVES

SECOND SESSION, 108TH CONGRESS

ON CONTRACTING IN IRAQ

MARCH 11, 2004

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INTRODUCTION:

Mr. Chairman and members of the Committee, I am Major General Carl Strock, Director of Civil Works for the U.S. Army Corps of Engineers and I am honored to appear before you today to testify on the work of the United States, in concert with our Coalition and Iraqi partners, to repair and rebuild Iraq. I returned last September from six months in Kuwait and Iraq where I served with the Office of Reconstruction and Humanitarian Assistance (ORHA) and the Coalition Provisional Authority (CPA). I held a number of positions culminating with service as the Deputy Director for Operations and Infrastructure for the CPA.

PLANNING PRIOR TO THE WAR

As is usual in military operations, planning for reconstruction was conducted simultaneously with planning for war. These plans included extensive use of contractors to supplement military and governmental capacity. Our original expectations were that we would have to repair the damage caused by military action, deal with the humanitarian crisis we were expecting to encounter, and set the stage for the new Iraqi government to oversee reconstruction. In fact, we worked closely with all elements of the Joint and Combined Command in assessing potential effects of US and Coalition munitions on critical Iraqi infrastructure.

ORHA was an interagency and international organization consisting of three "pillars": Reconstruction, led by the US Agency for International Development (USAID); Civil Administration, led by the Department of Defense (DoD); and Humanitarian Assistance, led by the Department of State (DoS). With the expectation of large numbers of displaced people, shortages of food, water, and shelter, and the potential for widespread disease, humanitarian assistance was the priority effort. Reconstruction was focused on returning the country's infrastructure to pre-war conditions and assistance in governance. s early effort approximately $1.5 Billion was allocated to reconstruction, the majority set

aside for construction contracts. Civil Administration was focused on assisting the 23 Iraqi ministries in reestablishing control in their respective sectors. We anticipated that the senior leadership would be absent but the ministries and their staffs would largely be intact and capable of running operations with the assistance of a small cadre of coalition advisors – in some case as few as one or two people per ministry.

Knowing that much of this infrastructure would be critical to the future of a free Iraq, the war planners, employing precision munitions, deliberately attempted to minimize damage wherever possible. An even greater concern going into the war was that Saddam Hussein's regime would repeat their actions of the Gulf War, where they set ablaze and crippled a large portion of the Kuwaiti oil infrastructure. Understanding that the flow of oil was the essential lifeblood of the future, free Iraqi economy, the Acting Secretary of the Army designated the US Army Corps of Engineers as the executive agent for Iraq Oil Infrastructure Reconstruction, and we formed Task Force Restore Iraqi Oil (RIO) under the superb leadership of Brigadier General Robert Crear to exert command and control over this important mission.

WHAT WE ENCOUNTERED

When we entered Iraq, we encountered relatively little war damage, but instead an infrastructure crippled by a combination of long-term neglect, recent looting, and sabotage. The country's infrastructure, while experiencing some damage from the war, was sagging under the weight of 30 years of neglect, misrule, and mismanagement. There was no electricity, very limited public water supply, no sewage treatment, no communication system except what we brought with us, no railroads in operation and limited other modes of transportation, and basically very little means for the new Iraqi government to do its work. Water was not being controlled at the reservoirs on the Tigris, Euphrates and other rivers, so irrigation systems were disrupted and there was major risk of flooding. Virtually all public buildings and their contents – records, equipment, supplies – were destroyed by looters and saboteurs, making it almost impossible to reestablish government and provide basic services. Furthermore, the

experts on the country's infrastructure were Ba'ath Party members who had fled or had been removed. Under the Hussein regime public servants did only what they were told by their supervisors, so there was no tradition of individual initiative. Our relatively small cadre of advisors faced considerable challenges dealing with this catastrophic situation.

I want to stress that we found very little actual war damage. This was in large measure due to precision targeting and effects-based weapons employment. The Iraqi transportation and utility systems, although in near complete disarray, were little damaged by war. The one sector of Iraq's infrastructure that did suffer unavoidable harm during the war was the communications network. The Coalition had necessarily targeted key communications nodes to prevent Saddam Hussein from effectively commanding and controlling his forces. This caused communications difficulties that we struggled to overcome early in our reconstruction efforts.

Moreover, the humanitarian crisis – the threat of mass starvation and disease – that we feared might occur during the war's aftermath did not come to pass, although we quickly had to rebuild the water supply in many locations to help minimize these threats. Creating even greater difficulties for reconstruction, many of the local Iraqis with expertise necessary to restore and operate critical infrastructure were either unavailable or fearful of working with the Coalition.

During this period early in the reconstruction, the effects of widespread sabotage and looting were constantly undermining our efforts. Because we had anticipated and planned for operations in just such a difficult and dangerous environment, one of our immediate and major efforts in the early days was to secure critical facilities. The damage resulting from the actions of saboteurs and looters, however, still turned out to be significant. As an example, it is estimated that fewer than 50 high voltage electricity transmission towers were toppled or significantly damaged as result of the war. At the peak of sabotage and looting, this number grew to more than 700 as criminal elements scavenged copper from the high voltage wires.

The greatest problem we faced, however, was dealing with an infrastructure that had been neglected and mismanaged for 30 years as the Saddam Hussein regime used such basic utilities as water and electric supplies to reward his friends and punish his enemies. The country suffered from a lack of capital investment as Saddam chose to purchase weapons and build palaces instead of power plants and water treatment facilities. International sanctions also contributed to the lack of maintenance. It is a tribute to Iraqi engineers that the country's systems were able to function at all, and that we were able to assist in restoring them as quickly as we did.

It should be noted that those of us who were part of the ORHA team initially suffered many of the same hardships as the Iraqi people. Like them, we did not have basic services such as reliable food, water, power, and sewage; nor did we have an adequate work area. Also like them, we were greatly hampered by the lack of reliable communications in the area. In fact, we often had no communications at all.

WHAT WE DID

In rebuilding Iraq's infrastructure, we faced an enormous and monumental task. A country similar in size and population to California's, Iraq was not going to be successfully rebuilt without a significant effort. In order to do this, we assembled a team consisting of representatives from the following agencies: United States Agency for International Development (USAID); Department of State; Department of Transportation; Department of Health and Human Services; Department of Agriculture; Department of Commerce; the Corps of Engineers; United Nations agencies such as UNICEF, UNESCO and UNDP; Iraqi Ministries; non-government organizations such as the International Committee of the Red Cross and CARE; and the private sector. We also knew going in—and this was part of our planning—that Iraq's successful reconstruction would require considerable contractor involvement.

My initial involvement was as a member of the ORHA. I arrived soon after Baghdad had been secured, and was part of the group tasked with the initial responsibility for reconstruction. As we began to establish operations, the LOGCAP contractor was essential in providing basic services such as food, water, power and electricity. The LOGCAP contractor also provided transportation and security services for ORHA. The contractor provided these services to ORHA just as it did to military units across the country.

The military units on the ground accomplished the very earliest reconstruction, restoration, and relief efforts. They were restoring electricity, water, sewage and other basic services all across the country. They helped rebuild schools and often provided employment opportunities to many Iraqi citizens. Throughout Iraq, these military units were the coalition presence, setting up local governments and reestablishing safety and security in their areas. From the earliest days, as we worked to get the infrastructure of Iraq back on its feet, it was often a coalition military unit working directly with the local Iraqi citizens doing the work.

Within the ORHA, we provided advisors to many of the Iraqi ministries. We assumed these advisors would deal with "decapitated" ministries--ministries where the Ba'ath leadership was absent but with facilities and workforce largely intact. What we found, though, were ministries that were non-functional. Their facilities were destroyed or incapacitated due to a combination of war-fighting, sabotage, looting, and long-term neglect, with no communications, and no equipment. Workers were fearful for their personal safety, and influence of the Ba'ath party, whose members had to be removed, reached deeper than we had anticipated. Even when provided a place to work, many members of these ministries were either unwilling or unable to return to these vital public service agencies. Soon after arrival, therefore, we quickly went to work assisting in the performance of initial, rudimentary repairs to their workplaces, providing a secure work environment, and offering our communications systems to assist them in the day-to-day operations of a country struggling to restore its society and culture and establish a new democracy. The advisors we assigned to these ministries provided both technical

expertise and assistance in setting up models of governance and public service that would work in a democracy, as opposed to the old models designed to support a totalitarian regime.

We knew from the beginning that identifying and engaging Iraqi's who had the expertise in Iraq's infrastructure would be critical. Due to the initial enormity of the tasks, even with the valiant efforts of the military units, we knew that this group of Iraqi specialists would be essential to the rapid restoration of basic services. Once again, however, we found the lack of a basic communications system, such as telephones, hindered this effort. All meetings had to be face-to-face. For example, we scheduled regular meetings with the Iraq Ministry of electricity. During one of these meetings, I was introduced to an expert in another utility area. I arranged a meeting at an appointed place and time, but I was unable to make the appointment due to security and transportation difficulties. Without a functioning phone system or any other means of communication, I had to wait until the next regularly scheduled meeting to arrange another appointment, and hope we would both be able to meet at the agreed upon time and place. Despite these challenges, we quickly identified essential Iraqi citizens who often "bridged-the-gap" between efforts of the military units and efforts of the contractors provided by ORHA and later, the CPA.

Soon after Coalition forces initially secured Baghdad, we established Task Force Fajr, which translates to "dawn" or "first light." Task Force Fajr consisted of approximately 20 people – mostly from the Corps of Engineers – led by Brigadier General Steve Hawkins, commander of our Great Lakes and Ohio River Division. The initial mission of Task Force Fajr was to initiate the restoration of power and potable water, first in Baghdad, then throughout Iraq, to assist in the hydrology and watershed management, and provide assistance in reestablishing hospitals in Baghdad.

One of the early challenges facing Task Force Fajr was potential flooding in the Tigris and Euphrates River basins. Rivers were rising and the Iraqis who understood and operated the system had fled. Employing "reach-back" techniques – Corps satellite video teleconferencing kits - we were able to place engineers on the ground at key reservoirs

and link them via satellite with technical experts in our Mobile District. The Mobile District used this and other information to construct a hydraulic model of the entire Euphrates and Tigris River Basins. The Mobile District then linked back to Task Force Fajr Engineers at key reservoirs, and working with local Iraqis used these reservoirs to regulate flow and avoid potentially catastrophic flooding.

In reestablishing a normal life for Iraqis, our first priority was to restore electrical power. Upon arrival in Baghdad, one of our first challenges was to find the "wiring diagram" for the national electrical grid. We soon discovered that the Saddam Hussein Regime restricted this information to very few loyal Ba'ath party members. In fact, electrical power was used as a tool of punishment and reward, with loyalists in the "Sunni Triangle" receiving ample power and the southern Shi'a and northern Kurds receiving little. Because of this strict, centralized control, few copies of the plans for the national grid existed and had been destroyed before we secured Baghdad. The first schematic of the entire Iraqi electrical grid was actually drawn by a lieutenant in the Corps of Engineers 249th Prime Power Battalion.

As we began to restore power, we found that the system was more like a string of old fashioned Christmas lights than a modern national power grid. When one key facility went out, the entire system failed. After years of operating as part of a totalitarian regime, power plants now fell under the control of local governments in their area. Having local government control pieces of the national power grid was not the most effective or efficient method for meeting the country's energy needs. Early on, for example, a number of power plants were forced by local governments to put power on the local grid and drop off the national grid. As a result, the remaining plants on the national grid were asked to provide more power than they had available to meet the national demand. The power plants still on the national grid were shut down to prevent overload, and soon, the entire grid shut down. Whenever this happened, we were forced to begin the laborious process of getting all of the stations back up and running, applying power back to the national grid. Accomplishing this, we might experience a failure at a different power plant due to lack of maintenance or damage from looting and sabotage.

Without an effective national communications network and with antiquated control systems, we were sometimes unable to react in time and were required to go through the entire process of shutting down and restarting all over again. Over time, we educated individual plant operators, negotiated operating schedules with local governments, provided military communications systems to assist in operations and control, and began providing reliable power across the country.

The combination of military units and local Iraqi people allowed us to restore and stabilize basic life support functions. As planned, we also began using contractors from numerous agencies, to include USAID and the Corps of Engineers to provide more long term, permanent solutions.

EARLY CORPS OF ENGINEERS INVOLVEMENT

To illustrate the use of contractor's in the reconstruction efforts, I will highlight two from the Corps of Engineers that assisted me in my role overseeing the reconstruction of a portion of the infrastructure. I must emphasize that these were only a few of the many contractors that provided essential life support, security, and construction services across Iraq.

To accomplish the mission of getting Iraq's oil production running again, we established Task Force RIO (Restore Iraqi Oil). In Central Command's planning for the Operation Iraqi Freedom, safety and security of the oil fields was considered paramount to the overall success of the operation. During the Gulf War, Saddam Hussein had demonstrated a callous disregard for human health and the environment, as he set the oil fields of Kuwait ablaze. Task Force RIO's immediate mission was to secure the oil fields, put out the fires, and get the oil flowing to provide refined fuel products for domestic use and ultimately oil for export. With more than 12,000 wells in the southern Iraq Oil Fields alone, the potential for disaster was enormous. We knew that this effort would require extensive contractor involvement and the short notice, requirements for secrecy, and essential nature of the mission limited our contracting flexibility.

Task Force RIO operated in two main areas – Rumaila and Kirkuk. The Task Force achieved tremendous early success. There were fewer than 10 significant fires, which we fought in a cooperative effort with Kuwaitis. What we did encounter was extensive damage caused as looters stole various components of the system. Terrorists and saboteurs continually targeted the oil pipelines that cross Iraq. They recognized that disrupting the flow of crude oil and refined petroleum products could delay efforts to restore peace. Before the war, we estimated it would take 12 weeks to reopen the fields. Due in large part to the hard work of Task Force RIO, its contractors, and especially the Iraqi experts in oil production, however, it took only about three weeks to get the oil flowing again. Despite the fact that terrorist attacks against the infrastructure continue today, Iraq is now producing about 2.5 million barrels per day of crude oil and is ahead of schedule in restoring production to pre-war levels. Additionally, Iraq is now exporting more than 1.5 million barrels of oil per day. These exports are pumping much needed funds back into the Iraqi economy, much of which is being used to restore infrastructure.

After initial restoration and stabilization efforts, electricity production leveled off during the late summer at a peak production capability of approximately 3,000 mega-Watts. By this time, responsibility for reconstruction had transitioned to the Program Management Office (PMO) of the CPA The PMO had the lead and was working an excellent plan using USAID and its contractor, Bechtel, to provide large scale generating, transmission, and control projects. What was needed though was an immediate, short-term solution that would give a much-needed boost to the availability of electricity across Iraq.

In September, the Corps of Engineers was asked by Central Command to look at the electrical situation in Iraq again and see if there was anything we could do to provide immediate assistance in order to allow USAID to focus on more long-term solutions. We did this with Task Force RIE (Restore Iraqi Electricity). Using our well-honed domestic emergency management skills, within two weeks we had a team of more than 30 Corps of Engineers employees in Iraq working under the leadership of the PMO. Working closely with the PMO and Iraqi Ministry of Electricity, Task Force RIE initially was assigned 26

projects that included new generation, generator rehabilitation, and restoring transmission lines and control systems. Just as we do in domestic emergency management situations such as recovery from Hurricane Isabel, we used existing, competitively bid contracts to accomplish this work. At the peak of activity, more than 2,000 contractors were on the Task Force RIE team. The initial efforts of Task Force RIE placed more than 500 mega-Watts of power back onto the Iraq electrical grids, but more importantly, helped ensure the reliable distribution of that power.

CONCLUSION

From the beginning of planning through current efforts, we have recognized the enormity of the tasks facing us required extensive contractor involvement on the Corps and Coalition teams. This need was not unique to either our prior wartime experience or our day-to-day operations at home and abroad. The contractors involved in the reconstruction effort brought extraordinary technical expertise, dedication and commitment to the team. I believe we would not have enjoyed the success we experienced without their contributions.

I am intensely proud that I had the opportunity to work alongside the extraordinary professionals in the US, Coalition and new Iraqi government. Thank you for allowing me to spend time with you today, and once the other members of this panel have made their statements I will be happy to take your questions

Chairman TOM DAVIS. General Kern, thanks for being with us.

General KERN. Thank you, Mr. Chairman and members of the committee. I appreciate the opportunity today to speak to you about the Army's Logistics Civilian Augmentation Program, referred to as LOGCAP by the members and in our current testimony.

My command, the Army Materiel Command's mission is to support our warfighters, and that includes all of our services as well as Ambassador Bremer's CPA, the Polish Multinational Division and other organizations in this theater.

I have just returned from talking to members of the CJTF Command, General Sanchez in our area, and I would report that it's remarkable that it's been less than a year since the conditions which General Strock just described have been turned into a country which has been restoring itself into an economy and we hope to a democracy. We work each day to improve our support in the theater, and the observations that we have made show great success in that area as well as the areas that we need to improve. Part of the purpose of my visit there was to find those areas we need to improve so that we get direct feedback from our customers in their requests.

LOGCAP provides to us the vital support for our forces in peace and in war. It gives us today the ability of an entire division of soldiers that can be returned to the fighting force and support through LOGCAP contracting. It provides us agility, flexibility, and fulfills critical, time-sensitive needs, and that is the critical part of a contingency-type contract where time is essential. It provides the means for our warfighters and our Nation to execute national security missions.

These contracts are around the world, not just in Iraq, and they provide us extensive capability in each area we use them. When our forces go in as General Strock has described, they carry with them everything that they have for life support. The food, the water, the tents and the laundry they hope will not be far behind.

LOGCAP has provided us the capability to change their conditions in which the soldiers and the support structure lives, from lying on the ground and eating MREs to one to being able to have shelter, sleep on cots, and have hot food prepared. If they wanted to shower when they arrived in Iraq last year, they used a bucket of water. Today, they have facilities to shower in. If they wanted a clean uniform, they used the same bucket of water; and today they have laundries that they can use. As many of the soldiers have reported to us, LOGCAP has changed the way that they can live and survive in that theater.

Today force provider has provided transportable shelters, it has provided dining facilities, it has provided maintenance facilities, it manages large pieces of our general support for parts, and it is providing a new quality of life in the country.

The stories are similar throughout. There are 61 base camps and today 79 dining facilities, which are supporting more than 180,000 soldiers. It is time critical, and so it is a contingency type contract which allows us to go in based on requirements and work through a process of definitizing the contract requirements and coming to an equitable adjustment. Frequently in these austere places, sup-

port is not what we would expect, and our contingencies allow us to both plan for that early and then react as requirements develop. Again, timing is critical and key in all of these.

The contractors also—and I would like to correct my written statement, since three additional contractors were killed just yesterday, has resulted today in eight killed from any accident and two killed in accidents. So they are exposed to the same dangers that our soldiers and others in Ambassador Bremer's organization are exposed. We don't know precisely where we are going to be in our security arrangements, and this has given us the flexibility to respond.

We also believe in fiscal responsibility. So our process, which I will ask General McManus to describe in some more detail, allows for that fiscal responsibility. It is a process of defining requirements, making sure that they fit within the scope of our contracting efforts and then following up with audits and defense contract management administrative contracting officers to ensure that everything is done in accordance to our Federal acquisition regulations.

The point is, we do plan and we do followup and we are fiscally and legally responsible for the actions that we do take.

I believe that LOGCAP and our soldiers are doing a remarkable job. We aren't perfect. It is a war zone, and we are correcting the mistakes as we find them. I believe you will find that we have corrected more than we have found by the basis of just eliminating and working together both with our supporting requirements and our audit agencies. The soldiers have done a remarkable job, and they have been supported by the LOGCAP contract admirably.

We look forward to your questions and I appreciate the opportunity on our behalf to testify.

Chairman TOM DAVIS. Thank you very much.

[The prepared statement of General Kern follows:]

RECORD VERSION

STATEMENT BY

General Paul J. Kern
Commanding General
U.S. Army Materiel Command

BEFORE THE

COMMITTEE ON GOVERNMENT REFORM
UNITED STATES HOUSE OF REPRESENTATIVES

SECOND SESSION, 108TH CONGRESS

ON CONTRACTING IN IRAQ

MARCH 11, 2004

NOT FOR PUBLICATION
UNTIL RELEASED
BY THE COMMITTEE
ON GOVERNMENT REFORM

STATEMENT BY
General Paul J. Kern
Commanding General
U.S. Army Materiel Command
ON CONTRACTING IN IRAQ

INTRODUCTION

Mr. Chairman and distinguished members of the Committee, thank you for this opportunity to report to you on the Logistics Civil Augmentation Program.

The Logistics Civil Augmentation Program (LOGCAP) provides vital support to our forces both in peace and war. It increases the efficiency and warfighting capability of the Armed Forces, immediately improves the quality of life for soldiers and forces on the ground, and actually allows fewer soldiers to accomplish a larger mission. While this specific program and the capability it provides has been in existence for over a decade supporting American forces in contingency operations around the world, the role of private enterprise and contractors on the battlefield is as old as our nation.

LOGCAP I covered the period 1991 to 1996. The contract was competitively awarded to Brown and Root Company, and managed by the Corps of Engineers. During this period, support was provided for the Southwest Asia pipeline and principally to contingency operations in Somalia and the Balkans.

LOGCAP II covered the period 1997 to 2001. The contract was competitively awarded to DynCorps and managed by the U.S. Army Materiel Command (AMC) and supported contingency operations in East Timor, Colombia and the Philippines.

The latest contract, LOGCAP III covers the period from 2002 to present. Again, this contract was competitively awarded to the company now known as Kellogg, Brown and Root Services, Inc with continued management by the U.S. Army Materiel Command. As of today, LOGCAP III provides support to contingency operations in Iraq,

Kuwait, Afghanistan, Djibouti, Republic of Georgia and Uzbekistan while planning for contingency operations in other locations depending on our national security needs.

Through LOGCAP, the Army plans for contractor logistics support for existing operational and contingency plans and conducts exercises and training events. More to the point, LOGCAP provides contingency support wherever and whenever required.

The LOGCAP umbrella contract statement of work (SOW) specifies the support, which *may* be provided by the LOGCAP prime contractor divided into three broad categories: supply operations, field services, and operations and services. The flexible nature of the umbrella contract allows the commander in the field to call on contractors to overcome the logistics shortfalls as the situation on the ground evolves.

As I mentioned, LOGCAP is about providing support to our troops and this support covers the full logistics spectrum. Some of the more critical functions include laundry and bath, facilities and billeting, clothing exchange and repair, waste and sanitation, food service, mortuary affairs, supply support, maintenance, transportation and distribution, and power generation and distribution to list but a few. The more austere the operating environment, the more difficult it becomes for the Army to insert theses critical services for our troops. The current environments in Iraq and Afghanistan are among the most difficult and challenging in which we have had to operate on a sustained basis.

Although contract support is essential throughout the Army's operations, here at home as well as overseas, exercising the option of LOGCAP is not automatic. The initial choice to use LOGCAP is a careful and deliberate analysis of all available support options in terms of adequacy and time. Combatant commander requirements may be supported by U.S. Active, Reserve and National Guard support units; allied military arrangements such as the North Atlantic Treaty Organization; host and other foreign nation support; and, organic, in-theater contracting capabilities. LOGCAP program

managers assist the supported force with planners to review all support options available.

The LOGCAP III umbrella contract was competitively awarded to Brown & Root Services, Inc. (BRS) of Houston, Texas, now known as Kellogg, Brown and Root, December 14, 2001. The Army Materiel Command awarded this contract following a competitive procurement, using best value source selection techniques. Best value allows the Army to access tradeoffs among cost and non-cost factors and accept the most advantageous proposal. Two other major defense contractors submitted proposals during this competition. We evaluated the companies on their management plan, technical plan, past performance, financial capability and proposed cost structure. We awarded the contract, without protest, to the company determined to provide the Best Value to the U.S. Army considering cost and all other factors.

The contract is an indefinite delivery, indefinite quantity (ID/IQ) contract. This allows the government to immediately set requirements within the scope of the contract without further competition. Requirements are placed against the basic contract as separate task orders. Task orders under the contract may be priced on a cost-plus-award-fee, firm-fixed-price, or cost-plus–fixed-fee basis. Cost–plus-award-fee contracts are appropriate for contingency operations in which the performance parameters of the contract, such as the size, location and field conditions of the supported force, are not known with precision and are subject to change. The Army pays only for work performed. No funds are applied solely for having the contract awarded to a company.

Timing is key to all military operations. A LOGCAP contract is designed to allow the warfghter the ability to place task orders on contract rapidly, to support evolving, dynamic operations to provide critical and essential life support to our forces operating in harsh environments where host nation assets are unavailable or do not satisfy the support requirement. LOGCAP contracts provide a means to respond to a wide range of needs while retaining checks and balances to ensure effective management of tax dollars.

Combatant commanders, or other supported customers such as the Coalition Provisional Authority or the Iraqi Survey Group, develop requirements for support based upon operational plans. The customer examines the possible alternatives for satisfying that requirement which including organic support, reserve component units, host nation support, or LOGCAP.

After the customer determines that LOGCAP is the only viable capability to provide the support, normally within compressed timelines due to operational realities and exigencies, the customer writes a scope of work with the assistance of Army LOGCAP planners. This scope of work is forwarded through channels to the Army's Deputy Chief of Staff, Logistics, or G4, and then to the U.S. Army Field Support Command's LOGCAP contracting office. The AFSC is AMC's subordinate command responsible for executing the LOGCAP program.

Following reviews for legal and contractual compliance, the procuring contracting officer, or PCO, sends the scope of work to the contractor and requests a rough order of magnitude (ROM) estimate of the cost of performance and a technical execution plan. The contractor develops this estimate and plan and provides them to the PCO and the customer. After the customer accepts this estimated cost and execution plan, and funds are received, the PCO issues a notice to proceed to the contractor who initiates action to satisfy the warfighter or customer requirement. In urgent circumstances this process can be completed in 72 hours following receipt of a scope of work. The ability to meet urgent requirements in such an expedited time frame is one of the major advantages and benefits of the LOGCAP contract.

At this point the government and the contractor have entered into an unpriced contractual action, on a cost-plus-award-fee basis. The rough order of magnitude estimate of the cost of performance has become a ceiling, or "not-to–exceed" value for the contract. The estimated cost of the action, against which the award fee will be calculated, has to be "definitized," the negotiated details of specific deliverables and

costs associated with resolution of a previously undefined task order. The contractor will provide the PCO a proposed estimated cost for completing the work under the task order. The Defense Contract Audit Agency (DCAA) audits this proposal and provides the results to the PCO. The PCO negotiates the cost estimate with the contractor and modifies the task order to establish the definitized estimated cost base.

The first task order to support operations in Southwest Asia awarded under LOGCAP III was for an update of the Worldwide Management and Staffing Plan in January 2002 at a price of $853,000. The first task order to support base camp operations was awarded in April 2002 for Karshi-Khandabad, Uzbekistan, at a price of $17 million. The Army currently has identified 76 task orders against the LOGCAP III contract. Of these, 16 directly support Operation Enduring Freedom (OEF) and 38 support Operation Iraqi Freedom (OIF).

Two of the task orders that we executed under the LOGCAP contract for OIF involved planning and preparation for the need to immediately restore the Iraqi oil fields following hostilities. Following receipt of funds and a scope of work from the Department of Defense, we issued a task order for development of an oil field restoration plan in November of 2002. With hostilities imminent, OSD requested an additional task order be issued in February 2003 to pre-position personnel and equipment for a restoration effort. Following this effort, the Army Corps of Engineers assumed total responsibility for the program called "Restore Iraqi Oil," and issued a contract to Kellogg, Brown and Root.

LOGCAP is currently supporting America's Global War on Terrorism contingency operations in seven countries. The program also assists with the planning, training and deployment of forces in the United States.

Not only is Kellogg, Brown and Root performing in Iraq, Kuwait and Afghanistan, but also in support of contingency operations in Uzbekistan, the Republic of Georgia, and Djibouti as well as continuing to support planning requirements and missions in the

continental United States. Over 20,000 employees and subcontractor employees are deployed to augment U.S. forces. To date, Kellogg, Brown and Root has suffered a total of 29 casualties, of which five Americans were killed and 12 wounded as a result of hostile fire while performing these services in support of U.S. military operations. The environment in which we are applying the skills and services of our LOGCAP contractors is not only harsh, but continues to be highly dangerous.

At this time the LOGCAP contractor is responding to further changes in requirements due to the current troop rotation in support of OIF. There are pending missions to support the Department of State when they assume the CPA function in July and to support other agency projects in Iraq.

The Government has a contract administration program in place to oversee performance of the contract and manage costs. The PCO has authorized Kellogg, Brown and Root to requisition material from the government supply system and to order material off of General Services Administration supply schedules. The PCO also delegated authority to the Defense Contract Management Agency (DCMA) to provide on site administrative contracting officers (ACO). DCMA is a critical strategic partner in the overall management and execution of this process.

The DCMA ACOs are located at numerous sites to provide daily contract compliance oversight, review and approve all requisitions over $2,500, evaluate and manage quality assurance, and monitor the use and control of government property acquired under the contract. The ACO team performs technical reviews of contractor cost proposals that support the negotiation of the contract cost base.

The Defense Contract Audit Agency (DCAA) also plays a key role on the government's contract management team. DCAA auditors perform audits on the contractor's cost proposals. They review and approve the contractor's cost estimating and accounting systems. DCAA reviews and approves the contractor's payment vouchers, prior to sending them to the Defense Finance and Accounting Service

(DFAS) for payment. DCAA audits all costs incurred to support the government contracting officer's final determination of which costs are allocable, allowable and reasonably incurred under the contract. Any cost not found allocable, allowable and reasonably incurred under the contract will not be paid by the government.

Kellogg, Brown and Root Services, Inc is also a critical, strategic partner in this effort. In order to properly manage costs, the contractor must account for those costs in accordance with both federal cost accounting standards and generally accepted accounting practices. The contractor is required to maintain adequate accounting systems, purchasing systems and invoicing systems. The corporate ACO periodically reviews these systems.

In addition to the incentive to incur costs in a reasonable manner, the contractor has two other incentives to exercise prudent cost control. Controlling costs is evaluated by the PCO and becomes a part of the contractor's performance record. This record, in turn, is used as an evaluation criterion when the contractor competes for future government business. Contractors who have a record of proven cost control will be better positioned to win additional contracts. Finally, the contractor's performance on cost control is one of the evaluation factors, which determines the award fee.

In these first phases of supporting our troops, the focus and priority has been on responsiveness, but all within the framework established by the Federal Acquisition Regulation (FAR). The process of definitizing task orders has taken longer than we would like and certainly much longer than we expected or even planned for. The speed and volume of task orders placed and the numerous valid changes to the customer's requirements have been major factors. The changing nature of operations in Southwest Asia has impacted the contractor's ability to submit valid cost proposals in a timely fashion and certainly has impacted our collective ability to satisfy the 180-day requirement of the FAR to definitize undefined contractual actions. The pace of setting new requirements and changes to current requirements has greatly exceeded the original plans of both the contractor and the government.

Finally, the harsh operating environment of Iraq and Afghanistan, the non-linear and non-contiguous operating area, and major infrastructure shortfalls have hindered the implementation of robust business management systems. Both the contractor and the government have recently made substantial progress in augmenting personnel and systems support. A firm timeline to establish final requirements and costs has been established along with metrics and standards to measure the performance of all agencies involved in this process. This primarily includes the PCO, DCAA, DCMA, and KBR. Progress has already been made, as we have negotiated three task orders for definitization and have a commitment from KBR to accelerate the schedule of the next few task orders. These include the two contract actions that supported OSD for planning and preparation to restore the Iraqi oil fields.

The negotiated estimated cost will be the base against which the award fee is calculated. The fee structure of the LOGCAP contract was proposed by Kellogg, Brown and Root Services Inc as a maximum of 3 percent, which comprises KBR's projected profit on this contract. One percent is the base fee and a maximum of 2 percent is the award fee. The award fee is determined by the government, following an evaluation of the contractor's performance in terms of timeliness of technical performance to include timeliness of response, quality of response, quality of work, cost control and overall management. In the event we cannot satisfy the established timelines for definitization, or we are unable to agree, the Army is prepared to unilaterally definitize the task orders.

When we enter into a cost-plus-award-fee contract, we realize that the management of costs incurred under the contract is an important responsibility. This instrument enables the contractor to control costs throughout the process as they use their own capital to satisfy our requirements prior to payment. The government only pays for goods and services that meet certain criteria. DCAA audits all costs incurred under the LOGCAP contract, as part of the definitization process and as a final audit prior to the government determining the amount of final payment.

I think it is also important to address the LOGCAP funding process. Army LOGCAP funding starts at the Department of the Army level and is passed down to Forces Command (FORSCOM). FORSCOM in turn allocates funds to their subordinate levels (i.e., Combined Forces Land Component Command or CFLCC). CFLCC issues funding authority to the various OEF/OIF task forces (i.e., CJTF7, CJTF180 and CFLCC Forward). The task forces furnish funds to the Army Field Support Command, AFSC, Resource Manager who validates the accounting data and initiates acceptance.

Upon acceptance, funds are released to the AFSC contracting office to create the task order for fulfillment of an approved requirement. This task order gives the contractor authority to incur cost against the LOGCAP contract. A copy of the task order is made available to the LOGCAP customer for recording of the obligations and disbursements in their own accounting system to meet their financial reporting requirements.

Coalition Provisional Authority and Iraqi Survey Group funds flow is slightly different. Funds are allocated through AMC to AFSC from DA. AFSC establishes the accounting record in the AFSC accounting system. The funds are certified and then released to the AFSC contracting office for generation of the task orders. All accounting for these funds are recorded within the AFSC accounting system and certified at the end of the fiscal year. CPA and ISG funds account for approximately 10% of the LOGCAP funds received at the AFSC.

Over the next 12 months, the LOGCAP government team will work with the combatant commander in theater to continue to improve the process and control costs. The focus is on the requirements process to refine and improve the total LOGCAP process through internal process improvement teams and meetings between government representatives and KBR. We will aggressively definitize completed task orders and stay on task with KBR on the agreed to plan of action. Additionally, we will develop a strategy to determine the most effective method of transition from

contingency contract operations to sustainment contract operations. As needs are definitized, we will seek to transition from cost-based to performance-based, fixed price task orders, whenever possible, to provide maximum incentive for the contractor to perform work in the most efficient and effective manner possible.

The role of the LOGCAP program is recognized and valued by the supported combatant commander and our troops. I believe that it has met its original intended goals and has proven to that it has even greater potential than originally expected of a contingency contracting instrument.

It provides a flexible, viable alternative for supporting our logistics requirements and providing augmentation to our support units for early entry of our forces, as well as long term sustainment needs that would otherwise place great strains on our warfighters. We have seen an unprecedented level of contractors on the battlefield, with more than a division's worth of contractors working side-by-side with our soldiers. They too are our troops and we need to ensure that the policies and systems are in place to support and take care of our total force, which includes our contractors

We are committed to supporting current operations and transform simultaneously. Supporting our soldiers remains our number one priority and ensuring they get the very best quality of life and other logistic support is one way that the people of AMC do that. As I have described to you earlier, LOGCAP contracting is a process we need to constantly review and improve if we are to improve the Army's tooth to tail ratio. We will improve and continue to improve our management of this program. Thank you for your support of America's armed forces and our efforts to support them.

Chairman TOM DAVIS. Can we go now to Ms. Ballard.

Ms. BALLARD. Mr. Chairman and distinguished members of the committee, thank you for this opportunity to report to you on the U.S. Army's role in contracting in Iraq.

It is my privilege to represent——

Chairman TOM DAVIS. Could you pull the mic just a little closer there?

Ms. BALLARD. Is that better, sir?

Chairman TOM DAVIS. It's better.

Ms. BALLARD. It is my privilege to represent the Army leadership and the military and civilian members of the Army's contracting work force who are at the forefront in the reconstruction and restoration of Iraq's infrastructure. We are very proud of these dedicated men and women because of their extraordinary efforts to help create a stable and successful Iraq, especially in light of the dangers they face every day.

This is a time of tremendous change, and we are most grateful for the committee' wisdom, guidance and strong support. Over the last year, our Army has met the demands of the global war on terrorism with more than 330,000 troops deployed around the world in more than 120 countries. They are doing what our country needs them to do in Bosnia, Kosovo, in the Sinai, in Korea, in Afghanistan and in Iraq. The U.S. Army—well-trained, well-led and well-equipped—is an important part of our globally engaged joint force. Our Army was instrumental in the defeat of Saddam Hussein and the subsequent liberation of more than 46 million people from oppression and despair. Our Army remains a central and critical participant in Operation Iraqi Freedom.

On May 21, 2003, the Deputy Secretary of Defense designated the Secretary of the Army as the Executive Agent for the Office of Reconstruction and Humanitarian Assistance, later to become the Coalition Provisional Authority [CPA], in Iraq. On January 14, 2004, the Deputy Secretary of Defense further assigned responsibility for Acquisition and Program Management Support for CPA to the Secretary of the Army. The Army is the lead service, helping Iraqi people build a stable and democratic society.

Our job is enormous, but we continue to make progress in an extremely difficult situation. I would like to reiterate the widespread neglect of basic services that Deputy Secretary of Defense Paul Wolfowitz reported to the Senate Foreign Relations Committee on May 22, 2003. He said:

Before the war, large numbers of Iraq's children under 5 years old suffered from malnutrition.

Only 60 percent of the Iraqi people had access to safe drinking water.

Ten of Basrah's 21 potable water treatment facilities were not functional.

Seventy percent of Iraq's sewage treatment plants needed repair. According to UNICEF reports, some 500,000 metric tons of raw or partially treated sewage was dumped into the Tigris or Euphrates rivers, which are Iraq's main source of water.

Eighty percent of Iraq's 25,000 schools were in poor condition. In some cases, as many as 180 students occupied one classroom—with an average of one book per six students—while at the same time every one of the first 100 or so schools we inspected in southern Iraq had been used as military command posts and arms storage sites.

Iraq's electrical power system operated at half its capacity.

Iraq's agriculture production had dropped significantly.

Iraq's oil infrastructure was neglected."

It will take time to reverse these desperate conditions, but we are making steady progress.

The Army, as Executive Agent, is providing contracting and program management support both in Iraq and in the United States. We are charged with procuring all nonconstruction items and services to meet the humanitarian needs—the basic needs—of the Iraqi people as well as the economic reconstruction and repair of Iraq's infrastructure. To date, in total, more than 1,500 contracts valued at more than $9.7 billion have been awarded. Of that total, more than 1,300 contracts totaling $1.3 billion have been awarded by our contracting office in Iraq. These contracts were awarded for the repair and renovation of schools, banks, railway stations, clinics, mosques, a human rights building, a teacher training institute, a women's rights building, and water treatment plants. These contracts were awarded to provide police and firefighters with uniforms and equipment, hospitals with badly needed supplies, electrical power system equipment, rescue equipment and buses. In addition, our contract awards are helping to build playgrounds, youth centers, emergency housing, roads, sewers and irrigation systems.

Again, of the overall total of more than $9.7 billion, contracts awarded within the United States total $2.5 billion for more than 200 contracts that are restoring Iraqi oil, shutting down and repairing oil wells, firefighting, explosive ordinance demolition, restoring Iraqi electricity, radio installation throughout Iraq, laptops, and emergency medical personnel in each of Iraq's 18 governates.

Led by Admiral David Nash, U.S. Navy retired, the Program Management Office for rebuilding Iraq is located in Baghdad with a support office located in the Pentagon. As the requirement focal point for all Iraq reconstruction contracting, the PMO is responsible for oversight and implementation of the $18.4 billion appropriated by the U.S. Congress to support the reconstruction of Iraq's infrastructure. The construction sectors are oil, electricity, public works and water, security and justice, transportation and communications, buildings, education and health.

Over $12.6 billion will be spent toward actual construction over the next few years, and $5.8 billion will be spent on nonconstruction. Some of the funds will go toward democracy, which is not covered by supplies. Computers are needed to monitor and control electrical and water systems; vehicles are needed to transport materials or to support system maintenance; uniforms and supplies are needed to support the police and civil defense corps; and supplies are needed to support schools.

On January 6, 2004, the Army released seven design/build construction solicitations. Proposals were received in February and are under evaluation for project awards in March of this year. These seven solicitations will result in 10 contracts in support of electrical, public works and water, water resources, transportation, communication, security projects and buildings. Contracts will be awarded using best value valuation methodology based on technical, management, past performance and cost factors.

Our contracting personnel on the ground in Iraq are courageous, dedicated volunteers. Since June 2003, when our first person arrived, we have been operating in Iraq. We now have a total of 28 individuals. They are multi-service and civilian: 3 Army, 4 Navy,

1 Marine, 11 Air Force and 9 civilians working in small, jam-packed work spaces. They are doing a phenomenal job under very tough and dangerous conditions.

Let me illustrate my point. Army Colonel Elias George Nimmer, a Medical Service Corps Officer and a member of the acquisition work force assigned to the Office of Assistant Secretary of the Army for Acquisition, Logistics and Technology was deployed in late June 2003, as part of a team supporting CPA's work with Iraq's Ministry of Health. In the early morning of October 26, 2003, a barrage of rockets hit the al-Rashid Hotel where he was staying, and a rocket impacted directly inside his room. Colonel Nimmer was hit with shrapnel in the spine and unable to move. Following three surgeries, he is doing remarkably well and recently returned to duty within the Office of the Assistant Secretary of the Army.

Currently, the General Accounting Office, in response to requests from Congress, is reviewing Iraqi essential services contracts to perform that the Army has followed proper procedures. We are working closely with the GAO auditors to ensure that they have all the information necessary to complete their work.

I have a deep and growing appreciation for the courage, competence, dedication and efforts of our contracting personnel. Thanks to their hard work and extreme dedication, the U.S. Army leads the way in providing contracting support to CPA and to the people of Iraq. The work has been—and will continue to be—performed in accordance with proper procedures by military and civilian volunteers who are concerned and committed to accomplishing their work under the toughest and most austere conditions. We are proud of our role in helping to create and rebuild a stable and successful Iraq. Our accomplishments are helping the citizens of Iraq move toward governing themselves and sustaining, operating and maintaining their own infrastructure which, in turn, will help our soldiers, sailors, airmen and Marines to return home sooner.

Thank you, Mr. Chairman.

Chairman TOM DAVIS. Thank you.

[The prepared statement of Ms. Ballard follows:]

RECORD VERSION

STATEMENT BY

MS. TINA BALLARD
DEPUTY ASSISTANT SECRETARY OF THE ARMY
(POLICY AND PROCUREMENT)

BEFORE THE

COMMITTEE ON GOVERNMENT REFORM
UNITED STATES HOUSE OF REPRESENTATIVES

SECOND SESSION, 108TH CONGRESS

ON CONTRACTING IN IRAQ

MARCH 11, 2004

NOT FOR PUBLICATION
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STATEMENT BY
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DEPUTY ASSISTANT SECRETARY OF THE ARMY
(POLICY AND PROCUREMENT)

ON CONTRACTING IN IRAQ

INTRODUCTION

Mr. Chairman and distinguished members of the Committee, thank you for this opportunity to report to you on the United States Army's role in Contracting in Iraq. It is my privilege to represent the Army leadership and the military and civilian members of the Army's contracting workforce who are at the forefront in the reconstruction and restoration of Iraq's infrastructure. We are very proud of these dedicated men and women because of their extraordinary efforts to help create a stable and successful Iraq, especially in light of the dangers they face every day.

This is a time of tremendous change, and we are most grateful for the Committee's wisdom, guidance, and strong support. Over the last year, our Army has met the demands of the Global War on Terrorism, with more than 330,000 troops deployed around the world in more than 120 countries. They are doing what our country needs them to do in Bosnia and Kosovo, in the Sinai, in Korea, in Afghanistan, and in Iraq. The United States Army – well-trained, well-led, and well-equipped – is an important part of our globally engaged Joint force. Our Army was instrumental in the defeat of Saddam Hussein and the subsequent liberation of more than 46 million people from oppression and despair. Our Army remains a central and critical participant in Operation Iraqi Freedom.

THE ARMY AS EXECUTIVE AGENT

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Our job is enormous, but we continue to make progress in an extremely difficult situation. I would like to reiterate the widespread neglect of basic services that Deputy Secretary of Defense Paul Wolfowitz reported to the Senate Foreign Relations Committee on May 22, 2003. He said, "Before the war:

- Large numbers of Iraq's children under five years old suffered from malnutrition;
- Only 60% of the Iraqi people had access to safe drinking water;
- 10 of Basrah's 21 potable water treatment facilities were not functional;
- 70% of Iraq's sewage treatment plants needed repair. According to UNICEF reports, some 500,000 metric tons of raw or partially treated sewage was dumped into the Tigris or Euphrates rivers, which are Iraq's main source of water;
- 80% of Iraq's 25,000 schools were in poor condition; in some cases as many as 180 students occupied one classroom – with an average of one book per six students – while at the same time every one of the first 100 or so schools we inspected in Southern Iraq had been used as military command posts and arms storage sites;
- Iraq's electrical power system operated at half its capacity;
- Iraq's agriculture production had dropped significantly;
- Iraq's oil infrastructure was neglected."

It will take time to reverse these desperate conditions, but we are making steady progress.

The Army, as Executive Agent, is providing contracting and program management support both in Iraq and in the United States. We are charged with procuring all non-construction items and services to meet the humanitarian needs – the basic needs – of the Iraqi people as well as the economic reconstruction and repair of Iraq's infrastructure. To date in total, more than 1,500 contracts valued at more than $9.7 billion have been awarded. Of that total, more than 1,300 contracts totaling $1.3 billion have been awarded by our contracting office in Iraq. These contracts were awarded for the repair and renovation of schools, banks, railway stations, clinics, mosques, a human rights building, a teacher training institute, a woman's rights building, and water treatment plants. These contracts were awarded to provide police and fire fighters with uniforms and equipment; hospitals with badly needed supplies; electrical power system equipment; rescue equipment, and buses. In addition, our contract awards are helping to build playgrounds, youth centers, emergency housing, and roads, sewer and irrigation systems.

Again, of the overall total of more than $9.7 billion, contracts awarded within the United States total $2.5 billion for more than 200 contractors that are restoring Iraqi Oil, shutting down and repairing oil wells, fire fighting, explosive ordnance demolition; restoring Iraqi electricity; radio installation throughout Iraq; laptops; and emergency medical personnel in each of Iraq's 18 governorates.

PROGRAM MANAGEMENT OFFICE

Led by Admiral (Retired) David Nash, the Program Management Office (PMO) for rebuilding Iraq is located in Baghdad with a support office located in the Pentagon. As the requirement focal point for all Iraqi reconstruction contracting, the PMO is responsible for oversight and implementation of the $18.4 billion appropriated by the U.S. Congress to support the reconstruction of Iraq's infrastructure. The construction sectors are oil, electricity, public works and water, security and justice, transportation and communications, buildings, education and health.

Overall, $12.6 billion will be spent towards actual construction over the next few years, and $5.8 billion will be spent on non-construction [some of the funds will go towards democracy, etc., which is no covered by supplies, etc. reference in your description.]. Computers are needed to monitor and control electrical and water systems; vehicles are needed to transport materials or to support system maintenance; uniforms and supplies are needed to support the police and civil defense corps; and supplies are needed to support schools.

On January 6, 2004, the Army released seven design/build construction solicitations. Proposals were received in February and are under evaluation for projected awards in March 2004. These seven solicitations will result in 10 contracts in support of electrical, public works and water, water resources, transportation, communications, security projects, and buildings. Contracts will be awarded using best value evaluation methodology based on technical, management, past performance, and cost factors.

A TOUGH JOB UNDER VERY DANGEROUS CONDITIONS

Our contracting personnel on the ground in Iraq are courageous, dedicated volunteers. Since June 2003, when our first person arrived, we have been operating in Iraq. We now have a total of 28 individuals. They are multi-Service and civilian: three Army; four Navy; one Marine; 11 Air Force; and nine civilians working in small, jam-packed work spaces.

They are doing a phenomenal job under very tough, dangerous conditions. Let me illustrate my point. Army Colonel Elias George Nimmer, a Medical Service Corps Officer and a member of the acquisition workforce assigned to the Office of the Assistant Secretary of the Army (Acquisition, Logistics and Technology) (OASA(ALT)) was deployed in late June 2003 as part of a team supporting CPA's work with Iraq's Ministry of Health. In the early morning of October 26, 2003, a barrage of rockets hit the al-Rashid Hotel where he was staying and a rocket impacted directly inside his room. Colonel Nimmer was hit with shrapnel in the spine and unable to move. Following three

surgeries, he is doing remarkably well and recently returned to duty within OASA(ALT).

PROPER PROCEDURES

Currently, the General Accounting Office (GAO), in response to a request from Congress, is reviewing Iraq essential services contracts to confirm that the Army has followed proper procedures. We are working closely with GAO auditors to ensure that they have all the information necessary to complete their work.

CONCLUSION

I have a deep and growing appreciation for the courage, competence, dedication, and efforts of our contracting personnel. Thanks to their hard work and extreme dedication, the United States Army leads the way in providing contracting support to CPA and the people of Iraq. The work has been – and will continue to be – performed in accordance with proper procedures, by military and civilian volunteers who are concerned and committed to accomplishing their work under the toughest, most austere conditions. We are proud of our role in helping to create and rebuild a stable and successful Iraq. Our accomplishments are helping the citizens of Iraq move toward governing themselves and sustaining, operating, and maintaining their own infrastructure which, in turn, will help our Soldiers, Sailors, Airmen and Marines to return home sooner.

Chairman TOM DAVIS. Let's move to Mr. Lucke. Again, your total statement is in the record, so try to keep it within 5 minutes.

General McManus is here for questions, and Mr. Reed is here for questions. That is why they are sitting up there, but they don't have to give opening statements. Thanks.

Mr. LUCKE. Mr. Chairman and distinguished members of the committee, I welcome the opportunity to testify on the U.S. Agency for International Development's participation in Iraq reconstruction.

USAID began contingency planning for possible humanitarian and reconstruction efforts in post-conflict Iraq in late 2002. As part of this process, we mobilized significant resources and technical expertise to support both potential humanitarian as well as reconstruction requirements. I arrived in the region in November 2002, moved to Baghdad in April 2003, and remained as USAID mission director until last month.

Working with CPA to improve the lives of Iraqis, USAID is working throughout Iraq to restore critical infrastructure, support the delivery of health care and education services, expand economic opportunity and improve governance. With a staff of some 160 ex-patriots and Iraqis, we are managing some $3.8 billion in projects to date. The USAID contractors and grantees now number some 800 ex-patriots, 3,000 Iraqis with a presence in every province of Iraq.

Starting from zero, we're now fully mobilized and producing results, and we have moved fast. Our infrastructure contract alone has obligated over $1 billion in power, water and other work since the contract was awarded in March of last year. In coordination first with ORHA and then CPA, USAID was tasked with managing some $2.1 billion of the first April 2003 supplemental appropriation.

We have many partners in Iraq within CPA: the Corps of Engineers for infrastructure supervision, the U.S. Army for the power sector, and the State Department in various sectors, especially governance.

Our role in post-conflict Iraq has been twofold: first, to avoid a humanitarian crisis, which didn't happen; and, second, to lay the foundation for long-term reconstruction, where we are well on the way to helping CPA accomplish this goal.

Our specific accomplishments in Iraq are significant.

In infrastructure, we have repaired and are repairing power systems, the port of Umm Qasr water and sanitation systems, airports, telecommunications facilities, schools, health clinics, railways and irrigation systems.

In social services, we've immunized millions of children, strengthened the health care system, printed and distributed millions of new textbooks, distributed school and student kits to millions of students, and trained teachers.

In the area of economic opportunity, we have implemented key reforms in economic governance related to the regulatory environment, banking, taxation, replacement of the old currency, and begun work in the key agriculture sector.

In governance, we have helped establish local councils throughout Iraq, awarded rapid response grants to provide essential local services, begun civic education programs, helped reestablish func-

tioning government ministries, established hundreds of community associations, and we're helping CPA lay the groundwork for a democratic and sovereign Iraq.

We have accomplished this work under the initial 2003 supplement by awarding nine contracts for port administration, airport administration, logistic support, infrastructure repair, architecture and engineering services for infrastructure, health, education, economic recovery and reform and agriculture.

Additionally, we have significant grants to five U.S. NGO's for community development throughout Iraq, grants to the World Health Organization, UNICEF and UNESCO for health, water sanitation and replacement of math and science books respectively, and grants to five U.S. universities to partner with Iraqi universities.

Under the second Iraq supplemental, USAID was the first agency to make an award in support of the continuing efforts in Iraq with a $1.8 billion infrastructure contract utilizing full and open competition. It's anticipated that this contract will primarily provide additional work in the power and water sectors.

Although proud of our efforts in Iraq, our work takes place in the context of considerable security and logistical challenges associated with standing up the largest U.S. reconstruction program since the Marshall plan. USAID has remained as open and transparent as possible in our procurement process. We have made serious efforts to make available virtually every procurement document we legally can on our Web site.

Steven Schooner of the George Washington University Law School recently wrote at a Government Contracts Year in Review conference that USAID, "has endeavored, for the most part successfully, to provide information related to its contracting activities on its Web page." He goes on to say, "I believe that USAID has set a new standard for transparency and public procurement."

We will continue to expand our efforts to meet the very high standards that we have set for ourselves. We are also doing everything we can to ensure that the taxpayers receive value for their dollar, that includes posting U.S. direct-hire staff to Iraq, including to three regional offices to oversee these contracts, as well as hiring senior contracting officials to help administer these awards.

We are co-located in Baghdad with the USAID Inspector General's Office and receive audit support from the Defense Contract Audit Agency to ensure funds are spent appropriately and are accounted for. And we take this accountability responsibility seriously.

USAID is determined to successfully help CPA lay the foundation for governmental and economic transformation in Iraq. We are successfully managing an enormous sum of public funds to an ambitious but focused reconstruction program, and we are prepared to continue this effort for the duration of the construction period.

Thank you, Mr. Chairman.

[The prepared statement of Mr. Lucke follows:]

Prepared Statement
of
Lewis Lucke
Deputy Assistant Administrator
Bureau for Asia and the Near East
United States Agency for International Development
before the
House Government Reform Committee
Thursday, March 11, 2004

Introduction

Through the provision of expert policy and technical assistance, the Agency for International Development (USAID) is helping to promote U.S. foreign policy goals in the reconstruction of Iraq. USAID activities in Iraq are fully coordinated with the Coalition Provisional Authority and its Administrator, Ambassador Jerry Bremer.

Currently, USAID has 16 long-term, direct hire staff, 64 contract staff, and 60 Iraqi staff in Iraq. Ten of these direct hire staff are located in regional offices outside of Baghdad. Contractors and grantees funded by USAID have over 700 expatriate and 3,000 Iraqi staff, and have a presence in every province.

USAID had staff on the ground in Kuwait from just prior to the assault, and entered Iraq behind our troops to begin programs on **March 31**, 2003 under the Office of Reconstruction and Humanitarian Assistance (ORHA). Thus far, USAID has been assigned management of $3.8 billion in projects to date, ranging from economic reform and local governance to education and electricity. Our initial contractors deployed during April 2003, and have been effective in their programs for nearly a year.

USAID's role in the Iraq Reconstruction

USAID participated in the contingency planning that occurred in Spring 2003 that led to USAID's being tasked by the Administration to manage $2.1 billion of the April 2003 Supplemental appropriation. USAID is currently coordinating with CPA on planning activities it will manage with the FY 2004 supplemental funding. Presently, the CPA has directed $1.7 billion of these new resources to USAID. USAID is coordinating closely with CPA on how to implement

these funds and on the issue of whether USAID will receive and manage further funds from the FY 2004 supplemental.

USAID has eleven contracts for reconstruction through April, but will be scaling back to nine contracts over the summer. (The airport and seaport management contracts will not be renewed, as Iraqi ministries take over operation of the ports.) We have grants to the United Nations (UNICEF, WHO, UNESCO, and WFP), to five U.S. universities, and nine international non-governmental organizations. As conditions improve in Iraq, CPA and USAID would like to see a greater number of non-governmental organizations become active with U.S. funding. Through USAID contractors and grantees, USAID has provided financial support to over 600 Iraqi nongovernmental organizations.

The First Year's Assistance

Reform programs in conflict areas require special handling, and USAID brings years of experience from numerous countries: El Salvador, southern Mexico, Guatemala, Colombia, Peru, Bolivia, Angola, Sudan, Congo, Afghanistan, Philippines, Nepal, West Bank, Sri Lanka, Bosnia and Kosovo.

Five common themes link these experiences, and these themes are applicable to Iraq:

1. **Avoid a humanitarian disaster.** The United States has done that in Iraq.

2. **Reactivate food production and markets.** We are assisting the Ministry of Trade to maintain the public ration distribution system, smoothing the importation of food, and working with the Ministry of Agriculture on grain and other food production. Private food markets are functioning.

3. **Involve the private sector early on.** Economic growth is good for the poor, and agricultural growth is even better for them.

4. **Link economic development with democratic governance.** Good economic governance boosts economic growth. We are reforming the legal and regulatory framework and promoting a transparent tax system.

5. Transparency in government finance and procurements. Successful introduction of democracy will require the confidence in the probity of public officials and faith in the equity of public investment.

The USAID role in the first months in the immediate post-conflict environment in Iraq was to work closely with military civil affairs units, doing triage to ensure the greatest civil and governmental stability possible. We were part of ORHA at that point, and our programs aimed at creating conditions that would facilitate the transition from military to civilian governance. In July, ORHA was replaced by the Coalition Provisional Authority.

In large part due to the swiftness and precision of the military campaign, there was little displacement of the population and no humanitarian crisis occurred. During the six months immediately following the war, USAID strongly supported public health activities and emergency food delivery to avoid a potential humanitarian disaster. For example, USAID assisted the World Food Program to deliver 516,000 tons of grain to ensure that the population was fed, and enough medical supplies and equipment for 1 million persons.

The Second Supplemental and the PMO

As it became evident that a longer reconstruction period would be appropriate, CPA and USAID contemplated a change in strategy. Leaving the immediate post-conflict period, CPA and USAID looked towards the economic and governmental reforms that would be necessary to solidify the emerging Iraqi state. These reforms, which we call transitional development, are seen as key in foreign assistance programs in a wide range of countries large and small. We see these economic and governmental reforms as a significant part of the exit strategy for our soldiers as a provisional Iraqi government is increasingly able to manage its own affairs.

With the establishment of the Coalition Provisional Authority in July 2003, USAID prepared a two-year program to extend the reconstruction program beyond post-conflict triage. The CPA in Baghdad is the lead in planning and directing the reconstruction. Presently, USAID-managed activities are approved by CPA and then funded by the

Project Management Office (PMO). USAID is presently working in four areas of concentration:

- Infrastructure repair: We have worked in partnership with civil affairs troops, as well as with the Army Corps of Engineers and CJTF-7.
  - Commerce was restored as three major bridges linking the country's highways were repaired.
  - Electricity was restored to pre-conflict levels in six months.
  - Wired telephone service was restored.
  - The country's deep-water port at Umm Qasr now has 50 ocean-going ships a month docking with grain and other goods after USAID had the port dredged and removed shipwrecks left since the 1980-1988 Iran-Iraq War.
  -

Education and health. USAID worked with CPA officials to maintain these important sectors:

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- 8.7 million math and science textbooks in Arabic and Kurdish have been distributed.
  - 32,000 teachers have been trained to teach children to think instead of merely memorize.
  - 2,300 schools have been renovaeted
  - Health teams now vaccinate 40,000 children per month.

- Governance: USAID has worked with State Department officials and a wide array of CPA staff in laying the foundations for Iraq governance.
  - USAID assisted civil affairs troops and CPA officials to quickly set up Local governments in Iraq's cities and its 18 governorates. Generally seen by citizens as legitimate, the men, women, clerics, businessmen and others on the councils learned to work together, compromise and spend small budgets on traffic, street lights, clinics, schools, police, computers, trash and other local issues.
  - Ministries were quickly up and running despite post-war looting. The Agency's Office of Transition Initiatives provided "ministries in a box" and set up 100 officials in each ministry with desks, chairs, and computers.
  - Women's rights have been helped and women's centers are being opened. Women voters and candidates were escorted to the local council elections. War widows

and women's unemployment are being addressed.

Economic growth: USAID continues to work with both State Department and Treasury officials in economic reform maintain financial stability was created.

- USAID assisted CPA's program to replace the Iraqi dinar with Saddam's portrait with new dinars that brought the country together.
- The central bank was put back on its feet with a financial management information system that will help the IMF and World Bank to begin programs in 2004.
- The public food distribution system was kept operating so there was no hunger. USAID sent 516,000 tons of grain and provided logisticians to help CPA keep the system moving.

Project Management and Oversight

Under the initial Emergency War-time Supplemental in FY 2003, USAID obligated approximately $2.1 billion of the $2.475 billion appropriated for the Iraq Relief and Reconstruction Fund in support of U.S. efforts to rebuild Iraq after the war.

During this initial period, USAID awarded contracts for personnel support, airports, seaports, reconstruction, education, health, local governance, economic growth and agriculture. Based on the need to act quickly following the end of active hostilities, we chose to do a limited competition for most of the initial awards. Although the vast majority of USAID's procurements are conducted using fully competitive procedures, the federal acquisition regulations grant the Administrator the authority to waive normal contracting procedures by making a written determination "that compliance with full and open competitive procedures would impair foreign assistance objectives, and would be inconsistent with the fulfillment of foreign assistance programs."

Under the second Iraq supplemental, USAID was the first agency to make an award in support of the continuing efforts in Iraq, with a $1.8 billion contract to Bechtel for infrastructure support utilizing full and open competition. The award was made under ideal contracting circumstances in that the highest technical scored proposal also was the lowest cost proposal submitted.

Although very proud of our efforts in supporting U.S. goals in Iraq, these efforts have not been accomplished without some difficulties. The urgency of these actions made for difficult and challenging circumstances. We have been very creative in trying to meet the personnel requirements that would normally be needed for this large an undertaking. However, a review of the numerous audits performed by our Inspector General's (IG) Office will show that USAID followed federal procurement rules and regulations in the award of these contracts, with minor exceptions. The IG audit report also pointed out things we could have done better to strengthen our procurements, particularly in the area of additional documentation. Many of the suggestions have already been implemented. USAID's Office of Procurement and the Bureau for Asia and the Near East have a good working relationship with the Office of Inspector General and will continue to work closely with this office to ensure compliance with all relevant regulations.

USAID has remained as open and transparent as possible in our procurement process. We have made very serious efforts to make available virtually everything we legally can on our web site. Steven L. Schooner, Associate Professor of Law at George Washington University Law School, recently wrote at a Government Contracts Year in Review conference that USAID "…has endeavored (for the most part successfully) to provide information relating to its contracting activities on its web page." He goes on to say that, "…I believe that USAID has set a new standard for transparency in public procurement." This is exactly the kind of open and transparent agency USAID is striving to be. We will continue to expand our efforts to meet the very high standard we have set for ourselves.

Given the large increases in our budget with Iraq (and Afghanistan) and beginning in FY 2004, USAID has gone from an annual obligation of just over $6 billion in 2001 to approximately $12 billion in 2003. While we have been very successful in making the critical awards, we are also doing everything we can to assure that the taxpayers of this country are receiving value for their expenditures. This includes moving U.S. direct-hire staff to Iraq to oversee the contracts as well as hiring senior contracting talent to help administer these awards. We are also requesting support from the IG's office and audit support from the Defense Contract Audit Agency to make sure that funds are

being spent appropriately and accounted for properly. As such, this is an area that we will want to monitor very closely over the coming months and years.

Conclusion

USAID has proven itself up to the demanding task of supporting the gains made by our troops in Iraq and laying a foundation for governmental and economic transformation. We have successfully managed an enormous sum of public funds in a broad range of politically and socially activities. Our assistance programs have been timely in initiation and technically apt to the evolving demands of situation. We are prepared to continue this level of effort through the duration of the reconstruction period.

Chairman TOM DAVIS. Thank you very much.

Dr. Zakheim, thank you.

Mr. ZAKHEIM. Thank you, Mr. Chairman, Representative Waxman, members of the committee.

I want to focus on Department of Defense oversight of contracts related to military operations and reconstruction in Iraq. With me on my left is Mr. Bill Reed, who has been serving as Director of DCAA, the Contract Audit Agency, for 16 years and is a respected professional in his field.

DOD considers the oversight of contracts an essential responsibility. We have a number of strong organizations, policies and regulations to fulfill this responsibility. Our task is not only to identify contract issues, but also to prevent future occurrences of problems we identify, recover any excess charges and take appropriate action against any contractor wrongdoing.

As the Under Secretary of Defense Comptroller and also the Department's Chief Financial Officer, I am responsible for ensuring the adequate financial management of funds spent on the reconstruction of Iraq. My involvement in DOD contract performance oversight comes primarily from my office's responsibility for the Defense Contract Audit Agency. Bill Reed reports to me.

DCAA's mission is provide all contract audit and financial advisory services related to DOD acquisition of goods and services. Other DOD organizations that are not within my office, such as the Defense Contract Management Agency and the DOD Inspector General, also play important oversight roles in terms of managing—of watching contracts—and work closely with DCAA. My colleague, the Under Secretary of Defense for Acquisition, is responsible for the contract policies to help ensure the Department obtains the best value when acquiring equipment and services and also is responsible for oversight of the Defense Contract Management Agency.

The Army and DCAA are strategic partners in the oversight of contracts through performance. The Army, as the executive agent for all Department reconstruction requirements in Iraq, is responsible for contract and program management activities there.

DCAA, which is co-located with Army personnel in Baghdad, evaluates all contractor proposals and reviews all billing paperwork for primes and subcontractors.

My office's financial management activities in Iraq began at the end of major combat operations there. I created and had in place by late April 2003 a 20 member forward cell that included representatives not only from DCAA but also from the DOD Inspector General, from the Office of Management and Budget, from the Defense Contract Management Agency, from the Joint Staff, from USAID and from the General Accounting Office. This team and its supporting rear cell at the Pentagon were especially critical to getting the Coalition Provisional Authority fully operational and capable of undertaking its enormous reconstruction tasks.

DOD contract performance oversight is now being supported by DCAA's Iraq branch office under Branch Manager Dan Altemus. The office now has 25 auditors. I met all 25 of them when I was in Iraq 2 weeks ago, the office it will increase to 31 auditors by the end of May.

Complementing this in-country support, DCAA has auditors that also provide contract oversight at stateside locations that have major contracts in Iraq.

Let me talk briefly about some of our findings and actions. DOD oversight of contract performance in Iraq has uncovered a number of problems. A resulting action has ranged from recommending changes in processes to rejection of unsupported proposal costs to reductions in billed costs for potentially unreasonable expenditures, to referral of our findings to the DOD Inspector General for possible legal action against the contractor.

Contractor performance in Iraq has not been perfect, but it has not been terrible. Iraq presents a difficult security environment for contractors, as you have heard. A number have already been killed, many wounded. Many contractors that have not had problems in performing their domestic DOD contracts are having difficulties in adjusting to the unique environment in Iraq and to their own firm's influx of new business.

We believe that contractor financial and internal control problems will resolve themselves. In the meantime, we will take whatever actions are necessary to protect the government's financial interest. DOD has enforced and will continue to enforce the highest standards for contracts in Iraq and anywhere else. Halliburton, mainly through its Kellogg, Brown and Root subsidiary, is the largest contractor operating in Iraq with contract ceilings that approach $18 billion. We are not surprised that the largest contractor has the bulk of the contract problems we found.

KBR has been responsive to the reported contract findings and has agreed to work on improving its contract performance. Contract problems reported to date generally have been caused by contractor deficiencies, not by problems with contract policies or the DOD organizations managing these contracts. The process works.

Still, to mitigate only process problems, the Department has taken action to ensure that its contract processes are integrated, effective and efficient. Especially significant has been the creation of the CPA's Program Management Office, led by Admiral Dave Nash who is here. I should also mention, new CPA Inspector General.

My statement for the record provides details on DOD oversight of Iraq contracts and the major issues we have identified. I will only highlight a very few of them orally.

Estimating practices: DCAA has identified significant deficiencies in KBR's estimating practices relating to the award of subcontract costs. Earlier this year, after consultation with the contracting officer, DCAA returned two major task order proposals worth more than $3 billion to KBR because they were inadequate for the purposes of negotiating a fair and reasonable price.

KBR later resubmitted one of the task orders for $700 million less than the original proposal. Even this resubmitted proposal was later withdrawn by KBR due to continuing pricing issues.

It was DCAA that found that $700 million problem. These issues included proposal subcontract costs that were significantly different from previously negotiated actual subcontract amounts and KBR's use of proposal estimates instead of more than $290 million of actual costs already incurred. Both issues were disclosed during the DCAA audit.

On January 13, 2004, DCAA notified the appropriate government contracting officials that KBR's subcontracting estimating process and procedures were considered inadequate and recommended that DCAA be advised before the negotiation of any future contract awards. KBR's deficiency in estimating some contracts was the catalyst of DCAA's review of potential gasoline overpricing under the Restore Iraqi Oil [RIO], contract.

The review found significant issues related to KBR's pricing and award of subcontract costs. It disclosed potential overpricing on gasoline of $61 million through September 2003. During DCAA's review, the auditors came across other information that led them to make a referral to the DOD Inspector General, which recently launched an investigation of this potential overpricing of gasoline.

KBR and dining facilities subcontract costs: DCAA has identified inadequate support for billed dining facilities costs. In DCAA's opinion, the billed number of meals appears to exceed significantly the actual meals served.

DCAA and KBR have agreed on the withholding of $176.5 million, of which it voluntarily withheld $140.7 million from future billings while KBR prepares a response to issues reported by DCAA.

Then there is the violation of the "Anti-kickback" Act. KBR itself has voluntarily disclosed a possible violation of the "Anti-kickback" Act by two of its employees. KBR has already reimbursed the government for the estimated impact of $6.3 million. DCAA has requested supporting data from KBR to validate that sum. DCAA has helped identify contracting issues that stem from the fact that major contracts in Iraq have been slow to get definitized, and by definitized, I mean to get a definite contract price negotiated.

DCAA found that KBR was not observing the 85 percent limit in the reimbursement vouchers it submitted for its undefinitized LOGCAP task orders. In late February, DCAA told KBR that it should apply that 85 percent limit to its vouchers, in other words, not charging the additional 15 percent. The Army's contracting officer has received KBR's response to the DCAA recommendation and is currently evaluating it.

There are other contract issues that go beyond KBR, and it is important to mention a few of these.

Titan Corp.: Recent DCAA audits disclosed deficiencies in Titan's labor distribution system, which records costs to Titan employees. DCAA also found that Titan lacked procedures for adequate tracking of hours worked by foreign national consultants. Based on these findings, the Defense Contract Management Agency contracting officer implemented a 10 percent withhold on all of Titan's labor and consulting costs until all identified deficiencies are corrected and bills to the government are based on adequate internal controls.

Restore Iraqi Electricity: In January and February of this year, DCAA auditors evaluated proposal costs exceeding $900 million from the three prime contractors for the RIE program, Fluor Federal systems, Perini Corp. and Washington Group International. As a result of these proposal reviews, DCAA reported to the Army Corps of Engineers that all three contractors had substantial subcontract pricing issues.

DCAA will continue to perform oversight of the subcontract estimating and billed costs. It will work closely with the prime contractors and the Corps of Engineers to ensure that future subcontract estimates are adequate. In addition, it will evaluate each voucher submitted by the prime contractors to ensure that contract costs, including subcontract costs, are properly billed and paid.

In closing, I first want to underscore the context in which all of this is taking place. You have heard the details of how the country of Iraq has been completely transformed in less than a year. After the war, we have opened hospitals; we have opened medical clinics; we have restored Iraqi oil to prewar levels; courts are back in operation and are probably functioning a bit better than the previous 30 years; a new currency in circulation; 170 newspapers are being published; students sit in rehabilitated classrooms with new textbooks whose contents probably are true for the first time in many years; and a Governing Council that ratified a Bill of Rights.

That is the context in which we have all operated. Beyond that, I want to underscore that we in the Department of Defense are absolutely committed to an integrated, well-managed process in Iraq. We will not tolerate the billing of costs that are not properly documented and supported. If internal controlled systems are deficient, we will continue to use protections, such as contract withholdings, to safeguard the people's interests. And we will provide whatever personnel and budget resources are needed to enforce integrity in DOD contracts.

My comptroller organization will continue to work with other organizations within and outside the Department to assist those organizations and to share our findings. From the beginning, DCAA and my office have coordinated closely not only with the DOD Inspector General but with the General Accounting Office and now with the CPA Inspector General, since its creation.

We have regularly provided these organizations with information on our activities. And this has included DCAA detailed briefings to the GAO on June 23 and November 7 of last year. And this past January 7, DCAA Director Bill Reed and I personally briefed David Walker, the Comptroller General and Gene Reardon, the Deputy Inspector General of DOD, on DCAA's contract audit support of Iraq reconstruction.

DCAA and my office are the primary source of information on Iraq oversight for both the GAO and the DOD Inspector General. I repeat, we are the primary source. GAO and the DOD IG have been supportive of our work in Iraq and have allowed DCAA to continue its programmed audits without attempting to duplicate their work.

In sum, I believe the Department's contract oversight has been vigilant, and we will ensure that it continues to be vigilant. I look forward to addressing any questions or comments you have on this matter.

[The prepared statement of Mr. Zakheim follows:]

Statement for the Record of Dr. Dov S. Zakheim
Under Secretary of Defense (Comptroller)
House Committee on Government Reform
11 March 2004

Mr. Chairman, members of the committee, my statement for this hearing will focus on Department of Defense (DoD) oversight of contracts related to military operations and reconstruction in Iraq.

DoD Contract Performance Oversight Responsibilities

The Department of Defense considers the oversight of contracts an essential responsibility. We have a number of strong organizations, policies, and regulations to fulfill this responsibility. DoD's task is not only to identify contract issues, but also to prevent future occurrences of problems we identify, recover any excess charges, and take appropriate action against any contractor wrongdoing.

As the Under Secretary of Defense (Comptroller) and the Department's Chief Financial Officer, I am responsible for ensuring adequate financial management of funds spent on the reconstruction of Iraq. My involvement in DoD contract performance oversight comes primarily from my office's responsibility for the Defense Contract Audit Agency (DCAA). DCAA's mission is to provide all contract audit and financial advisory services related to DoD acquisition of goods and services. Other DoD organizations not within my office -- such as the Defense Contract Management Agency (DCMA) and DoD Inspector General (DoDIG) -- also play important contract oversight roles and work closely with DCAA. The Under Secretary of Defense (Acquisition, Technology and Logistics) is responsible for the contract policies that help ensure the Department obtains the best value when acquiring equipment and services and is also responsible for DCMA.

The Army and DCAA are strategic partners in the oversight of contractor performance. The Army, as the executive agent for all Department reconstruction requirements in Iraq, is responsible for contract and program management activities there. DCAA, which is collocated with Army personnel in Baghdad, evaluates all contractor proposals and reviews all billing paperwork for primes and subs.

My office's financial management activities in Iraq began at the end of major combat operations there. I created and had in place by late April 2003 a 20-member forward cell that included representatives from the DCAA, DoDIG, Office of Management and Budget (OMB), DCMA, Joint Staff, U.S. Agency for International Development (USAID), and General Accounting Office (GAO). This team and its supporting rear cell at the Pentagon were especially critical to getting the Coalition Provisional Authority fully operational and capable of undertaking its enormously complex reconstruction tasks.

DoD contract performance oversight is now being supported by DCAA's Iraq Branch Office under Branch Manager Dan Altemus. The Office now has 25 auditors, and will increase to 31 auditors by the end of May. Complementing this in-country support, DCAA has auditors that

also provide contract oversight of U.S. firms at stateside locations that have major contracts in Iraq.

Summary of Findings and Actions

DoD oversight of contract performance in Iraq has uncovered a number of problems. Our resulting action has ranged from recommending changes in processes, to rejection of unsupported proposal costs, to reductions in billed costs for potentially unreasonable expenditures, to referral of our findings to the DoD Inspector General for possible legal action against a contractor.

Contractor performance in Iraq has been neither perfect, nor terrible. Iraq presents a difficult security environment for contractors. Many contractors that have not had problems in performing their domestic DoD contracts are having difficulties in adjusting to the unique environment in Iraq and to their own firms' influx of new business. We believe that contractor financial and internal control problems will resolve themselves, but in the meantime, we will take whatever actions are necessary to protect the Government's financial interests. DoD has enforced and will continue to enforce the highest standards for contracts in Iraq and anywhere else.

Halliburton, mainly through its Kellogg, Brown and Root (KBR) subsidiary, is the largest contractor operating in Iraq – with contract ceilings approaching $18 billion. We are not surprised that the largest contractor has the bulk of the contract problems we have found. KBR has been responsive to reported contract findings and has agreed to work on improving its contract performance.

Contract problems reported to date generally have been caused by contractor deficiencies, not by problems with contract policies or the DoD organizations managing these contracts. Still, to mitigate this latter possibility, the Department has taken action to ensure that its contract processes are integrated, effective, and efficient. Especially significant has been creation of the CPA's Program Management Office and Inspector General.

I will now provide details on DoD oversight of Iraq contracts and the major issues we have identified.

DCAA Staffing and Actions

Since April 2003, DCAA has worked with all Iraq-based U.S. procurement organizations to determine the need for audit support. These organizations include the CPA, Army Materiel Command, Army Corps of Engineers, USAID, and State Department. This coordination has enabled DCAA to build a universe of all Iraq-related auditable contracts, which is a significant step towards ensuring that needed audit procedures are comprehensive, and performed effectively and efficiently. DCAA has established a contract audit universe (for cost-type incurred cost, internal control, and contract payment audits) that presently includes more than 60 prime contracts with contract ceiling amounts of $24.9 billion and funding/awards to-date under those contracts of about $9.7 billion.

DCAA's services include professional advice to customers in Iraq – most notably the U.S. Army and USAID -- on accounting and financial matters to assist them in the negotiation, award, administration, repricing, and settlement of contracts. Especially important has been DCAA's in-country testing of contractor timekeeping, subcontract management, and cash disbursement procedures. DCAA's real-time audits are critical to ensuring that contractor internal control systems are adequate and costs are properly charged to Government contracts.

During FY 2004 DCAA has already issued over 180 audit reports related to contractors involved in Iraq reconstruction. These reports address forward pricing proposals, costs directly incurred on existing contracts, and contractor policies and internal controls.

Contract Issues for Halliburton – KBR

KBR has been awarded Iraq Reconstruction contracts with ceilings totaling $17.6 billion under two major programs: $9.4 billion under the Logistics Civil Augmentation Program (LOGCAP III) contract; and $8.2 billion under the Restore Iraqi Oil (RIO) contract. DCAA has been providing continuous contract audit oversight on both programs.

The U.S. Army Materiel Command competitively awarded the LOGCAP III contract to the company now known as KBR on December 14, 2001. Today, under LOGCAP III, KBR supports U.S. operations in Afghanistan, Kuwait, Djibouti, Republic of Georgia, Uzbekistan, and Iraq.

Estimating practices. DCAA has identified significant deficiencies in KBR's estimating practices related to the award of subcontract costs. Earlier this year after consultation with the contracting officer, DCAA returned two major task order proposals (worth more than $3 billion) to KBR because they were inadequate for the purposes of negotiating a fair and reasonable price. KBR later resubmitted one of the task orders for $700 million less than the original proposal. Even this resubmitted proposal was later withdrawn by KBR due to continuing pricing issues. These issues included proposal subcontract costs that were significantly different from previously negotiated actual subcontract amounts and the use of proposal estimates instead of more than $290 million of actual costs already incurred – both disclosed during the DCAA audit.

On January 13, 2004, DCAA notified the appropriate Government contracting officials that KBR's subcontracting estimating process and procedures were considered inadequate and recommended that DCAA be advised before the negotiation of any future contract awards.

KBR's deficiencies in estimating subcontracts were the catalyst for DCAA's review of potential gasoline overpricing under the Restore Iraqi Oil contract. The review found significant issues related to KBR's pricing and award of subcontract costs. It disclosed potential overpricing on gasoline of $61 million through September of 2003. During DCAA's review, the auditors came across other information that led them to make a referral to the DoD Inspector General, which recently launched an investigation of this potential overpricing of gasoline.

Dining Facility Subcontract Costs. DCAA has identified inadequate support for billed dining facility costs. In DCAA's opinion the billed number of meals appears to exceed significantly the actual meals served. DCAA and KBR have agreed on a withholding of $176.5 million ($140.7 million that KBR voluntarily withheld from future billings and

$35.8 million that DCAA suspended on current billings), while KBR prepares a response to issues reported by DCAA.

Violation of the Anti-Kickback Act. KBR has voluntarily disclosed a possible violation of the Anti-Kickback Act by two of its employees. KBR has already reimbursed the Government for the estimated impact of $6.3 million. DCAA has requested supporting data from KBR to validate the $6.3 million.

Application of Federal Acquisition Regulations (FAR). DCAA has helped identify contracting issues that stem from the fact that major contracts in Iraq have been slow to get definitized, that is to get a definite contract price negotiated. The FAR allows the government to award a letter contract when there is insufficient time to negotiate a well-defined contract with a specified price – insufficient time because of pressing requirements that contract would meet. However, in those situations it is important to negotiate prices as soon as practical after award to avoid negotiating a price after most or all the costs have been incurred by the contractor. The use of letter contracts in Iraq stems from the rapidly changing situation there, which often causes changes in contract requirements – for example, for services and equipment. Federal Acquisition Regulations limit contract reimbursement to a maximum of 85 percent of allowable costs until a contract is definitized.

DCAA found that KBR was not observing this 85 percent limit in the reimbursement vouchers it submitted for its undefinitized LOGCAP task orders. In late February DCAA told KBR that it should apply the 85 percent limit to its vouchers. The Army's contracting officer has received KBR's response to the DCAA recommendation and is evaluating it. If the required 15 percent withhold is applied to all costs billed under undefinitized LOGCAP task orders, the total withhold would be about $200 million. After these task orders are definitized, this withheld amount would be available for reimbursement if otherwise allowable per DCAA audit.

Other Contract Issues

Titan Corporation. In 1999, Titan was awarded an Indefinite Delivery/Indefinite Quantity contract with a current ceiling amount of $294 million to provide linguist and translator services to the U.S. Government. The majority of the current contract costs center on Iraq support. Recent DCAA audits disclosed deficiencies in Titan's labor distribution system, which records costs for Titan employees. DCAA also found that Titan lacked procedures for adequate tracking of hours worked by foreign national consultants. Based on these findings, the DCMA contracting officer implemented a 10 percent withhold on all of Titan's labor and consultant costs until all identified deficiencies are corrected and bills to the Government are based on adequate internal controls. The resulting withhold amount could be as much as $4.9 million on future billings depending on the timeliness of the needed improvements.

Restore Iraq Electricity (RIE). In January and February of 2004, DCAA auditors evaluated proposal costs exceeding $900 million from the three prime contractors for the REI program: Fluor Federal Systems, Perini Corporation, and Washington Group International. As a result of these proposal reviews, DCAA reported to the Army Corps of Engineers that all three contractors had substantial subcontract pricing issues. Examples included an absence of any

documentation for selection of a specific subcontractor, and the absence of cost and pricing data to establish fair and reasonable prices.

DCAA will continue to perform oversight of the subcontract estimating and billed costs. DCAA will work closely with the prime contractors and the Army Corps of Engineers to ensure that future subcontract estimates are adequate. In addition, DCAA will evaluate each voucher submitted by the prime contractors to ensure that contract costs (including subcontract costs) are properly billed and paid.

Closing

In closing, I want to underscore that we in the Department of Defense are absolutely committed to an integrated, well-managed contracting process in Iraq. We will not tolerate the billing of costs that are not properly documented and supported. If internal control systems are deficient, we will continue to use protections, such as contact withholdings, to safeguard our interests. And we will provide whatever personnel and budget resources are needed to enforce integrity in DoD contracts.

My Comptroller organization will continue to work with other organizations within and outside the Department to assist those organizations and share our findings. From the beginning, DCAA and my office have coordinated closely with the GAO and DoDIG, and with the CPA IG once it was created. We have regularly provided these organizations with information on our activities. This included detailed briefings by DCAA to the GAO on June 23 and November 7, 2003. This past January 7, DCAA Director Bill Reed and I personally briefed Comptroller General David Walker and the Deputy DoD Inspector General Gene Reardon on DCAA's contract audit support of Iraq reconstruction. DCAA and my office are the primary source of information on Iraq contract oversight for the GAO and DoDIG. They have been supportive of our work in Iraq and allowed DCAA to continue its programmed audits without attempting to duplicate their work.

In sum I believe that the Department's contract oversight has been vigilant, and we will ensure that it continues. I look forward to addressing whatever questions or comments you have on this oversight. Thank you.

Chairman TOM DAVIS. Thank you very much.

Admiral Nash, clean up here.

Admiral NASH. Thank you and good afternoon, Mr. Chairman and members of the committee.

I will submit my written remarks for the record and I would like to summarize them very quickly. I really appreciate this opportunity to offer a field perspective on the reconstruction in Iraq based on my 8 months of experience there. It is an honor to appear before you and to bring the information that I have.

The Program Management Office is a living example, in my opinion, of how a total can be greater than the sum of its parts. I am proud to represent that team today that is dedicated. Speaking in the broadest of terms, the Public Management Office is responsible for managing and executing the U.S.-funded reconstruction of Iraq's infrastructure and essential services. As the Office's Director, I report to the Coalition Provisional Authority's Administrator, Ambassador Bremer. I also report to Acting Secretary of the Army—Brownlee—for Acquisition and Program Management Support.

Our goals are simple: To properly execute the supplemental work; to build the capacity for Iraq to do large program management for their own future; to build the capacity of Iraq construction and construction support industry; and finally and most important, is to win the peace in Iraq.

Most of you have seen the statistics about electricity and water and telephone and other infrastructure elements in Iraq. Having lived in Iraq for 8 months, I can attest to the severity of these challenges. As you know, Saddam Hussein's government paid little attention to maintaining the country's infrastructure. Before the war, the electrical grid left more than one-third of the Iraqi citizenry without power; 40 percent of their citizens lacked access to safe, reliable water supplies, with only 6 percent of the population linked to a sewage treatment system, and telephones limited to only a handful of homes. In summary, facilities and services across the country ran until they were broken and then abandoned.

Rebuilding the Iraqi infrastructure is a key part of the overall strategy to assist Iraq in becoming a free and democratic country. You all did your part by providing the $18.4 billion to help rebuild Iraq. The $12.6 billion will be focused on construction and approximately $5.8 billion on nonconstruction. Our emphasis is creating security through stability that will ultimately accelerate the pace at which Iraqi sovereignty will lead to all of our troops returning home permanently.

Lieutenant General Sanchez and I agree wholeheartedly on this principle, and we are committed to working together. Moreover, we are firmly committed to the concept that time is of the essence, and we must work as fast as possible to rebuild Iraq infrastructure. And to ensure accountability for the funds allocated under fiscal year 2004 supplemental appropriations bill for the reconstruction of Iraq, a coordinated body was necessary.

The Coalition Provisional Authority and Ambassador Bremer created the Program Management Office designed to direct, coordinate and oversee the contracting organizations for this endeavor. U.S. Government organizations and agencies, such as USAID and the

Army Corps of Engineers, will serve as executive agents in contracting on our behalf.

We established an approach and reconstruction efforts that follow four basic tenets: First, financial and contractual authority will follow a clear chain of responsibility; second, program management will follow an innovative and highly leveraged approach that relies heavily on the private-sector participation; third, contracting the work will follow a strategy of full and open competition and comply with the Federal acquisition regulations in the supplemental bill; and finally, we will have maximum transparency in everything we do.

Our approach leverages the private sector for construction and program management support while maintaining a layer of government oversight protecting the American taxpayer. This concept of operations is inherently agile and allows us to evaluate and adjust each stage based on performance. The result is the greatest value at the least cost.

The assistance you have provided in response to the President's emergency supplemental request is vast and speaks well for the generosity of the American people. It will lay a solid foundation for the future in Iraq.

As we move forward, we are organized for success and have the people, technology and processes to do the job. We are at work today on the following: The supplemental funds for reconstruction are being committed in accordance with the 5 January 2007 report to Congress. Each contract contains explicit incentives for hiring Iraqi citizens. And finally, we are emphasizing transparency of operations by using off-the-shelf management information systems for real-time reporting, visible on the Program Management Office Web site.

I said earlier that our actions were open, competitive and transparent. To assure that they remain so, the following auditors, including others, will oversee and review our work: The Defense Contracting Auditing Agency has already joined us. The Coalition Provisional Inspector General has already stood up, and I have already spoken to the General Accounting Office and the Comptroller General.

Continuing audits, in my experience, are a normal part of the acquisition cycle and not only serve the classic functions of preventing waste, fraud and abuse but also will serve as a running tutorial for the Iraqi Government and business community.

I am confident that we have made a solid start to the task ahead. However, no effort of this size or scope has ever been flawless. We will work hard to continually evaluate ourselves, improve and ask the auditors to help us do so.

Mr. Chairman on June 30, a sovereign Iraqi Government assumes power. However, the mission to rebuild the infrastructure of Iraq will continue. Rebuilding power plants, water treatment facilities, telecommunications facilities, schools, security facilities, public buildings, this all will take time. In my 8 months in Iraq, I have met hundreds of Iraqis. Their message has been consistent. They want nothing more than what we enjoy here, reliable electricity, clean water, functioning sewage systems, an educational infrastruc-

ture and better health care. Beyond that, they expect the United States will make good on its promises, and we shall.

Thank you very much.

[The prepared statement of Admiral Nash follows:]

Testimony before the House Government Reform Committee by Rear Admiral David Nash (Ret.) Director, Program Management Office Coalition Provisional Authority March 11, 2004

Introduction

Thank you and good afternoon, Mr. Chairman and members of the committee. I appreciate this opportunity to offer a field perspective on the reconstruction of Iraq based on my 8 months of experience in Iraq. It is an honor to appear before you and members of the committee today. The Program Management Office is a living example of how the total can be greater than the sum of its parts. I am proud to represent this team of dedicated professionals here today.

Background

Speaking in the broadest of terms, the Program Management Office is responsible for managing and executing the U.S.-funded reconstruction of Iraq's infrastructure and essential services.

As the Office's Director, I report to Coalition Provision Authority Administrator, L. Paul Bremer III. I also report to the Acting Secretary of the Army for acquisition and program management support.

Our goals are to:

- Properly execute the supplemental work
- Build the capacity for Iraq to do large program management for their own future

- Build the capacity of Iraqi construction and construction support industry; and,
- Win the peace in Iraq

Most of you have seen the statistics about the electricity, water, telephone and other infrastructure elements in Iraq. Having lived in Iraq for 8 months, I can attest to the severity of the challenges.

As you know Saddam Hussein's government paid little or no attention to maintaining the country's infrastructure. Before the war, the electrical grid left more than one-third of Iraq's citizenry without power. Forty percent of the citizens lacked access to safe reliable water supplies - with only 6% of the population linked to a sewage treatment system. And telephones were limited to only a handful of homes.

In summary, facilities and services across the country ran until they were broke and then left in place to decay and scar the landscape and countryside.

Making all of this work - rebuilding the Iraqi infrastructure – is a key part to the overall strategy to assist Iraq in becoming a free, democratic country.

How are we going to do it?

Our Approach: Improved Security Through Infrastructure

Congress did its part by providing $18.4 billion to help rebuild Iraq - $12.6 billion will be focused on construction and $5.8 billion for non-construction. We are contributing to the restoration of a secure and sovereign Iraq through our Reconstruction efforts. Our emphasis is on creating security through stability that will ultimately accelerate the pace at which Iraqi sovereignty will lead to all of our troops returning home permanently. Lieutenant General Sanchez and I

agree wholeheartedly on this principle and we are committed to working together. Moreover we are firmly committed to the concept that time is of the essence and that we must begin working as fast as possible to rebuild Iraq's infrastructure.

To ensure accountability for the funds allocated under the FY04 Supplemental Appropriations Bill for the reconstruction of Iraq a coordinating body was necessary. The Coalition Provisional Authority and Ambassador Bremer created the Program Management Office - designed to direct, coordinate and oversee the contracting organizations for this endeavor. These US government organizations and agencies, such as USAID and the Army Corps of Engineers, serve as "executive agents" contracting on our behalf.

We established an approach to the reconstruction efforts that follows four basic tenets:

- First, financial and contract authority will follow a clear chain of responsibility;
- Second, program management will follow an innovative and highly leveraged approach that relies heavily on private sector participation;
- Third, contracting the work will follow a strategy of full and open competition and comply with the Federal Acquisition Regulations and the Supplemental Bill; and,
- Finally, we will have maximum transparency in everything we do.

We will use a multi-layered concept of operations that has been successfully implemented with large-scale construction efforts in the United States. The approach leverages the private sector for construction and program management support, while maintaining a small layer of government oversight protecting the American taxpayer. This concept of operations is inherently agile and allows us to evaluate and adjust at each stage based on performance. The result is the greatest value at the least cost.

The assistance you have provided in response to the President's emergency supplemental request is vast and speaks well for the generosity of the American people, it will lay a solid foundation for the future.

While not a directly assigned responsibility, we obviously must also coordinate our efforts with the international donor community and the Government of Iraq -- not only the current government, which functions under the sovereignty exercised by CPA, but the sovereign government which will take office on June 30. I mention the international donor community because they are an important part of this transition to sovereignty. As an example, The Madrid Donors Conference in October 2003 resulted at least $13 billion in pledges from other countries and international financial institutions to assist in the reconstruction effort. And recently we participated at the Abu Dhabi conference on international donor coordination to identify projects that can be accomplished by other donor nations.

Protecting Taxpayer Funds Through Transparency

As we move forward, we are organized for success and have the people, technology and processes to do the job. We are at work today on the following:

- The supplemental funds for reconstruction are being committed in accordance with the 5 January 2207 report to Congress.
- Each contract contains explicit incentives for hiring Iraqi citizens. The provision for hiring Iraqi citizens accomplishes two important objectives:

  (1) First, to generate employment, which helps the economy and has its own stabilizing effect; and

  (2) Second, to train the workforce so that we leave behind more than just $18.4 billion in bricks and mortar – we leave behind the human capital necessary for sustaining a modern society.

These are important outcomes that contribute to our goals for the Iraqi people to continue to build their future. Right now 4,000 Iraqis are at work on our construction projects. In addition, thousands more will be created as the reconstruction continues; and,

- Emphasizing transparency of operations by using off-the-shelf management information systems for real-time reporting visible on the Program Management Office web site – www.rebuilding-iraq.net.

I said earlier that our actions were open, competitive and transparent. To assure that they remain so, the following auditors, including others, will oversee and review our work.

- The Defense Contracting Audit Agency;
- The Coalition Provisional Authority Inspector General; and,
- The General Accounting Office.

These continuing audits are a normal part of the acquisition cycle and not only serve the classic functions of preventing waste, fraud and abuse, but will also serve as a running tutorial for Iraqi government and business on the programmatic and economic benefits of competitive procurement.

The Path Forward: Measuring Success

I am confident that we have made a solid start to the tasks ahead and that we have clear and understandable procedures in place. Nevertheless we realize that we will have to make adjustments and improvements. No effort of this size and scope has ever been flawless. We will work hard to continually evaluate ourselves and ask the auditors to help us do so. Auditors and inspectors are a normal component of the acquisition cycle. They are a necessary element in helping us measure success and identify a lessons learned program - we

welcome this involvement. It is essential to maintaining a fair and open contracting process.

We are also creating a new regulatory environment. As an integral part of our efforts, we have worked with two Iraqi ministries to create national construction and environmental standards that will create design and construction procedures, consistency of practices, and ensure quality requirements for the building and construction sectors.

Additionally, we have procured a national site license for construction management software. That software becomes part of the economic infrastructure we will leave behind. The construction management software and the experience Iraqis will gain from working on the construction projects will allow Iraq to develop the inherent capacity to manage large programs in the future. Long after we leave, the Iraqi government will have an embedded capacity to oversee and operate large construction as well as inventory projects and contractor performance.

As essential services become increasingly available, the Iraqi economy will generate jobs unrelated to construction. Increased employment, in turn, lessens public dissatisfaction and contributes to security and political progress.

Mr. Chairman, on June 30 a sovereign Iraqi government assumes power. However, the mission to rebuild the infrastructure of Iraq will continue. Rebuilding power plants, water treatment facilities, telecommunications facilities, schools, security facilities, and public buildings will take time.
I am confident Iraq's new government will be a proactive and productive partner. In my eight months in Iraq I have met with hundreds of Iraqis ranging from government and religious leaders to the average citizen. Their message has been consistent. They want nothing more than we enjoy here: reliable

electricity, clean water, functioning sewage systems, educational infrastructure and better health care as soon as possible.

Beyond that, they expect that the United States will make good on its promises. And we shall.

Thank you, Mr. Chairman.

Chairman TOM DAVIS. Thank you all very much.

Let me start the questioning. This really goes to everybody on here. I am going to ask a three part question, but I want to get this on the record, and everybody is under oath. Have you or anyone in your office ever discussed with the Vice President or with his office the award of a contract for Iraqi reconstruction prior to any contract being awarded?

General STROCK. No, I have not.

General KERN. No, sir, I have not.

General MCMANUS. No, sir, I have not.

Ms. BALLARD. No, sir, I have not.

Mr. LUCKE. No, sir, I have not.

Mr. ZAKHEIM. No, sir, I have not.

Mr. REED. No, sir, I have not.

Admiral NASH. No, sir, I have not.

Chairman TOM DAVIS. Did the fact that the Vice President was a former officer, CEO, of Halliburton influence the selection of Halliburton and KBR in any way?

General STROCK. No, sir, it did not.

General KERN. No, sir, it did not.

General MCMANUS. No, sir, it did not.

Ms. BALLARD. No, sir, it did not.

Mr. LUCKE. We have no contractual arrangement with Halliburton.

Mr. ZAKHEIM. We oversee, but I have no knowledge of any of this.

Mr. REED. No, I have no knowledge.

Admiral NASH. No, sir, I have not.

Chairman TOM DAVIS. Have you or anyone in your office been pressured by any political appointee or high official in the administration to make an award to a particular firm or go easy on any contractor in carrying out contract oversight activities?

General STROCK. Not to my knowledge.

General KERN. No, sir, not in my office.

General MCMANUS. No, sir, not in my command.

Ms. BALLARD. No, sir.

Mr. LUCKE. No, sir, not to my knowledge.

Mr. ZAKHEIM. No, sir.

Mr. REED. No.

Admiral NASH. No.

Chairman TOM DAVIS. Thank you.

An issue was raised, given the conditions on the ground in Iraq, do you think it would have been practical to have used multiple award task order contracts for sustainment or reconstruction services?

There was a chart put up by the ranking member on a number of discrete projects and the number of discrete projects subject to competition. Is there any chance you would have been able to conduct competition for any of these task orders? Let me start with you, General McManus.

Admiral Nash, you now are current. Maybe as the situation changes, could we do a better job?

General MCMANUS. It is important to note that the LOGCAP contract provides us a flexibility and agility to respond to unknown

requirements over unknown timelines in uncertain conditions. As we began to prosecute this campaign—and remember, we were operating in Iraq as well as Afghanistan and Kuwait with forces employed to include bringing in the additional support for ORHA and CPA, the Iraqi Survey Group, and now the multinational division—the timelines against which we execute the warfighter's requirements or the customer's requirements are often very, very tight.

In the course of normal competition, we wouldn't be nowhere near where we are today in terms of life support, distribution logistics support, if we had to do that. Time really becomes the biggest enemy, sir.

Chairman TOM DAVIS. I understand that, but LOGCAP is given to one company.

General MCMANUS. That is correct.

Chairman TOM DAVIS. So, basically, when you go out to them, nobody can say, "I can do it cheaper or better," on any number of tasks, isn't that right?

General MCMANUS. That is correct. It's also important to note that LOGCAP, as a former program, we have been using as an institution for a decade. This is competition in which we select competitively a contractor to support contingency operations.

Chairman TOM DAVIS. Admiral Nash, did you want to add anything to do that?

Admiral NASH. When you use multiple award contracts, it requires that you have a lot of contractors mobilized onsite. It works very well in the United States where you have lots of contractors.

But when you don't have lots of contractors, then you end up with the additional costs of mobilizing many. As we get many contractors mobilized in Iraq in the future, it will be something we will look at, because we will be looking for ways to become more efficient.

Chairman TOM DAVIS. Since the contractors had to be there, there was no—there wasn't a lot of people knocking on the door to send people over?

Admiral NASH. No, sir, to my knowledge.

Chairman TOM DAVIS. Mr. Lucke, do you have any comments?

Mr. LUCKE. We began planning in November 2002, and we were able to use limited competition for eight of our nine grants. The one that we did not use limited competition on was for personnel, and that was a sole source that we absolutely needed in order to have personnel present in order to implement the programs.

Chairman TOM DAVIS. Let me ask Mr. Reed, you are head of the Defense Contract Audit Agency. How many years have you been in the business of looking at government contracts?

Mr. REED. Thirty-nine years.

Chairman TOM DAVIS. You served under a lot of different administrations and seen—you have seen a lot of contracts go awry during that time?

Mr. REED. Yes.

Chairman TOM DAVIS. The ranking member made a comment that cost-plus contracts are notoriously open for abuse. Let me ask about the reliance on cost-plus contracts in this particular circumstance.

Obviously, there are some cases where there are better vehicles than others. As you look at this from your perspective having to audit these, were there better ways to do this, or was this the most efficient way to accomplish the mission?

Mr. REED. The selection of the contract type is usually a balancing of risk between the government and the contractor. Firm-fixed contracts shift most of the risk to the contractor. Obviously, cost reimbursement is more of a balanced risk.

There's no question that, when you are dealing with a contingency operation, that it will be very difficult to get any contractor to bid firm-fixed price for the scope of some of these efforts, which the requirements are very fluid, quite frankly. So I believe that the contracting vehicle selection is appropriate in my judgment.

Chairman TOM DAVIS. And when you talk about cost-plus, there is an award fee with that, too, that goes to your ability to manage the contracts and bring costs down?

Mr. REED. That is correct, and that is a classic vehicle used by contracting officials to ensure contract performance.

Chairman TOM DAVIS. You have seen, obviously, a lot of cost-plus contracts in your time. In this situation, there have been allegations that one of the contractors, Halliburton in particular, would send in invoices for meals that weren't served. Is this a common practice, when you're not sure what logistics are going to be and what is our catch to catch this and make sure there are corrections made as this goes through the process?

Mr. REED. DCAA certainly is not an expert in restaurant services, but just from a common sense standpoint and what we have been advising to the contracting officer that we would expect to see, just common sense, is a reimbursement based on actual meals served plus a small margin for unexpected surplus based on some pattern of history. So, you know, if the average is 3,000 meals a day, 1 day only 2,900 show up and we have a small margin for the contractor to be covered because he estimated based on history to serve 3,000 meals.

Chairman TOM DAVIS. So it is not uncommon for them to come in with an invoice for more or less than they actually served, based on historical——

Mr. REED. That should be a condition of the contract. The contract should spell that out. And DCAA will audit to whatever the terms of the contract are.

Chairman TOM DAVIS. Do you have any comments on that?

General MCMANUS. No, sir.

Chairman TOM DAVIS. Ms. Ballard.

Ms. BALLARD. No, sir.

Chairman TOM DAVIS. As I understand it, the allegation here is that there were meals not served, and there were billings coming in. But ordinarily, on an audit, it would be reconciled?

Mr. ZAKHEIM. That is exactly right.

Chairman TOM DAVIS. The process is set up that it would not be uncommon for someone to come in slightly over or under and on audit, you pick those up and reconcile?

Mr. ZAKHEIM. Exactly.

Chairman TOM DAVIS. That is not necessarily evidence of fraud, that's just the way it works in the normal scheme of things?

Mr. REED. That's right.

Chairman TOM DAVIS. Why is any gasoline being imported from Kuwait under Halliburton's IO contract? Why are they such high prices? Ms. Ballard, can you explain that to us, because you have the chart that was up there and the chart leaps out at you?

Ms. BALLARD. Mr. Chairman, first, the oil is being imported from Kuwait because of safety issues for our soldiers. Initially, when we began to import oil from Kuwait, it was a few days after the hostilities had ceased in Iraq. There were lines miles long, two to three cars wide. This gave openings to riots, to civil unrest, which created threats to our soldiers. The crowds became cover upon which the insurgents could use it to attack our soldiers. So our first and primary objective was to obtain fuel so we could disburse crowds and eliminate the civil unrest.

Strategically, we need to be able to obtain fuel from the north and south. If a border is shut down in the north and we are only receiving north fuel, then we have returned to the situation where we have created opportunities for civil unrest and threats to our soldiers.

And third, sir, in obtaining fuel from Kuwait, Jordan and Turkey, we are just making the requirements for fuel in the region, and it is a principal requirement to maintain fuel supplies in the region.

Chairman TOM DAVIS. Who within the Defense Department would decide what that reasonable price for fuel would be on that? Tina, do you know why $1.32 might be normal in some cases and $2.64 would be normal under other circumstances?

General STROCK. Sir, if I could take that on, sir. Again Carl Strock from the Army Corps of Engineers.

This is a very complex question to resolve and answer. The prices you see here have a lot of variables in them. As Ms. Ballard mentioned, at the time that we entered into our first contract for delivery of fuel, it was early May, and, sir, I was in Baghdad the day that a U.S. soldier from the 3rd Infantry Division was assassinated in a gasoline line trying to keep order. We were told to get fuel moving now.

Sir, we worked with our contractor to do that. The contractor secured three prices on May 4th and, on May 5th, made an award to the lowest price. That price was as reflected on the board here.

Sir, that price has three components, one is the cost of the fuel. The other is transportation and other costs associated with that. The transportation costs were $1.2 a gallon. They are significantly different from the lower one because the distance was three times further Camp Cedar versus Baghdad. So the distance, considerably longer. And the turnaround time on that distance is considerably longer as well. About a 2-day turnaround to Camp Cedar is 6 to 10 days to get in and out of Baghdad.

Chairman TOM DAVIS. So this is really not apples to apples?

General STROCK. No, sir, it is not. There is a time span here as well. The contract on the top was awarded on May 5th. The other was awarded later in August. Our contractor, when we approached him, said, "Give me time. I can negotiate a better price." We said, "There is no time. Do the best you can, and this is it."

The additional costs there, sir, the 24 sentences of other costs, has to do with the capability of Iraqi infrastructure to download the fuel we delivered. Iraq does not routinely import fuel. They move fuel around the country by pipelines, and the storage places take fuel from the tanks to trucks. They are not set up to take fuel from trucks to tanks. We had to create those conditions through our contractor, and there was a cost associated with that, sir. So the 24 cents has to do with those kinds of expenses and difficulties.

And finally, sir, the 2 percent represents, as I am told, the markup from the contractor for the management of this contract. It is the normal cost of doing business.

I would also like to add, sir, that the cost of fuel from Turkey has averaged $1.20 to $1.30 per gallon. We import about two-thirds of the fuel from Turkey and about one-third from Kuwait, and we do that for the reasons Ms. Ballard has cited.

We need to keep it flowing from two different directions. We could not use Turkey exclusively because, for example, at one point, when we were negotiating with the Kuwaitis, the border of Turkey was closed for 4 days, and the fuel was shut off. So the uncertainties of the situation required that. And further, the Turkish drivers would not take fuel into Baghdad, but the Kuwaiti drivers were willing to do so.

Today, sir, we are paying 39 cents less per gallon than we did with that first task order, as we have negotiated with the supplier, who has agreed to work a spot market price for our fuel, still accelerated because we buy on spot market. We have not been willing and able to enter into contracts longer than 30 days duration.

I can't speak to the DESC contract and how that's structured, but I know ours was deemed to be fair and reasonable.

Chairman TOM DAVIS. What was the justification for selling this gas inside Iraq for 4 to 15 cents a gallon in some cases?

General STROCK. We worked on that with the Iraqi Ministry of Oil and State Oil Marketing Organization. They have a responsibility for the provision of domestic fuel to their people. They were concerned about the level of strategic reserves and they were also willing to do what it took to get fuel to the pump. They chose not to transfer the cost of this fuel to the Iraqi people because of the impact it would have had on the economy in Iraq.

I would also like to point out that it doesn't really matter where this money comes from. We must use it in a responsible way. But of the $1.4 plus billion we spent on the importation of fuel, 95 percent of that money has been from the development fund for Iraq and only about 5 percent, or $72 million, has come from U.S. taxpayers.

Chairman TOM DAVIS. Most of this was in dinars and was from the Development Fund?

General STROCK. Yes. It is from the $8 billion worth of revenue from the oil market as well as the $1 billion that the U.N. put in. Again, I want to emphasize, that is not a reason to not demand the lowest possible price, but——

Mr. OSE. Would the gentleman yield?

One point that gets lost here, over the past decade or 15 years, the average price of gasoline in Iraq has been around 8 cents a gallon. So to go into Iraq and all of a sudden start charging a dollar

a gallon, you are going to have massive disruptions. And I think that is the point that General Strock is trying to make.

General STROCK. This applied to all types of fuel. LPG and kerosene, they use for cooking and heating. If we had charged the actual cost that we paid——

Chairman TOM DAVIS. There would have been a riot in Iraq and reconstruction would have been over before it started. I appreciate—who first raised the issue of the potential overpricing by Halliburton under this task order? Was it DCAA, the contracting people?

Mr. ZAKHEIM. DCAA raised it first. Bill will give you some details on that.

Mr. REED. We were doing our normal activities, in terms of auditing these various task orders. This was one of the larger task orders, and we were doing a review of how KBR was administering its subcontracts for fuel and found that they were very deficient in documenting the basis of the awards. Much of the information you just heard from General Strock, unfortunately, was not documented by KBR in their subcontract files.

Chairman TOM DAVIS. No reason to believe it was inaccurate, just undocumented?

Mr. REED. Just undocumented, and the haste was their reason, people were turning over and they were just a little sloppy.

Chairman TOM DAVIS. OK. I think that puts it into perspective. Mr. Ose.

Mr. OSE. Mr. Chairman, could we get the DESC to buy gasoline and ship it to California? I don't know who has this information. I am looking at a piece of paper, background information, U.S. support for Iraq reconstruction efforts, that lists the appropriation expenditures together with five separate contracts that were awarded as of January 2004. Do you have this paper down there, any of you? It came in this packet that I got.

Chairman TOM DAVIS. I think that was for committee members.

Mr. OSE. There are five contracts listed at the bottom of that. There is one to USAID, three to the Corps and another to AID. One is $1.8 billion to Bechtel, $1.6 billion to KBR, another $1.2 to KBR and another billion for Bechtel and $800 million to Parsons. And then above—I think they need this form down in front of them.

Chairman TOM DAVIS. Mr. Waxman raised an issue in his opening testimony about the northern part being—going to Parsons in the RIO contract exclusively and the southern part of the country going to Halliburton, and that we don't bid tasks off between the two of them. Would that make any sense?

Ms. BALLARD. Mr. Chairman, when the acquisition strategy was developed for the Restore Iraqi Oil solicitation, we found that Iraq's existing infrastructure had a northern and a southern oil company. Based on this, the procurement specialist determined that to best integrate with the existing Iraq infrastructure we should also have contractors in the north and the south. There were also some technicalities with regard to the different type of fuels that were generated in the north and the south.

Sir, the issue of multiple awards, IDIQ contracts, has been raised. The Federal Acquisition Regulations specifies that—when we are not to use that type of contract. The circumstances specified

in the regulation exist here. For example, we must determine that the benefits of structuring the contract as we did outweigh the benefits of competing the contract as Congressman Waxman has suggested. Those circumstances do exist, because our objective is to then transfer these capabilities to the northern and southern Iraqis. To maintain stability in the region, we structured our contracts to match the infrastructure that existed in Iraq when we arrived.

Chairman TOM DAVIS. I think that puts all of this in a much different perspective than we have heard. But my time is up, and I now yield 20 minutes to Mr. Waxman.

Mr. WAXMAN. Thank you, Mr. Chairman.

Earlier Chairman Davis asked each of you whether anybody was under political pressure to award contracts to particular companies, and you all answered no. He also asked whether you are aware of any political pressure on administration officials, and again, you all answered no.

I want to draw your attention to a December 15 Wall Street Journal article. The article refers to two letters by an Army Corps contracting officer, Mary Robertson. Ms. Robertson indicated that she was under political pressure to direct Halliburton to negotiate exclusively with Altanmia, an obscure and inexperienced Kuwaiti firm. Ms. Robertson wrote, "Since the U.S. Government is paying for these services, I will not succumb to the political pressures from the Government of Kuwait or the U.S. embassy to go against my integrity and pay a higher price for fuel than necessary." She wrote that to her superiors, but then Halliburton went ahead and contracted with Altanmia.

She is not the only one who claims political pressure. Thomas Crum, a senior Halliburton official, stated, "The concern that the embassy had was expressed clearly, and it was the same as the Government of Kuwait, that we weren't buying enough gasoline from Kuwait." How do you respond to these two statements from U.S. Government employees that they were under political pressure?

Mr. ZAKHEIM. In the first place, Congressman, half of what you are discussing is the Government of Kuwait, not the Government of the United States.

Mr. WAXMAN. I am discussing the U.S. embassy, and they work for us.

Mr. ZAKHEIM. Well, yes, but that is a different agency and so at least——

Mr. WAXMAN. Let me ask General Strock because this woman works for him.

Were you aware—and maybe she even contacted you—that she was under pressure from someone to tell—to have Halliburton contract with Altanmia, and she urged them not to because she didn't feel she could give in to that political pressure and charge the higher price as a result?

General STROCK. Sir, at the risk of sounding evasive, she did not work for me. I work for the CPA, and I was on loan to CPA, and I happened to be an Army Corps of Engineers officer there.

She worked for Brigadier General Robert Crear in the Task Force RIO, and I am not aware of anything surrounding that allegation, sir.

Mr. WAXMAN. I see. We are going to have another hearing, and maybe we can get to the bottom of that. But I would indicate that maybe none of you are aware of political pressure, but there were two people working for the government that did feel they were under political pressure.

Mr. Reed, I want to ask you about the audit that was done, what is known as the Flash Report. So I want to get some questions answered about it. This Flash Report found significant deficiencies in Halliburton's cost estimating practices, is that correct?

Mr. REED. That's correct.

Mr. WAXMAN. Can you explain what these deficiencies were?

Mr. REED. Well, the largest deficiency was the inadequate support for their subcontract estimates. They simply were not following what we considered reasonable business procedures to solicit bids, evaluate bids and justify the fair and reasonable price of the subcontracts being awarded. At least we couldn't tell that was being done by the documentation in their files. That was certainly very significant.

Generally, there was—I would characterize the general deficiency as a real problem supplying current, accurate and complete data in support of all of their proposed costs, not just subcontract estimates, but subcontracts were by far the most material part of the proposal.

Mr. WAXMAN. The Flash Report also found that Halliburton repeatedly violated the Federal Acquisition Regulations. Is that right?

Mr. REED. There is a guideline in the Federal Acquisition Regulations prescribing what the contractor should submit in its proposal to support its proposed costs. They failed to follow those guidelines, particularly in the case of subcontracts.

Mr. WAXMAN. The report found that Halliburton even violated its own cost estimating manual. Is that right?

Mr. REED. That's correct. Their own manual very closely followed the FAR guidelines.

Mr. WAXMAN. In a statement yesterday, Halliburton claimed they had no opportunity to respond to your findings. They said, "We have not been given a chance to respond to accusations before they were released publicly." Did Halliburton have an opportunity to review DCAA's Flash Report before it was issued?

Mr. REED. Yes, sir. Our standard practice is to provide a draft report to the contractor for written comments. In this case, we did that; written comments were received. In fact, they are attached to our Flash Report.

Mr. WAXMAN. You even mention in your report that they had a chance to review it, and they responded?

Mr. REED. That's correct.

Mr. WAXMAN. Let's turn to one of Halliburton's responses to your audit. You said DCAA found significant deficiencies in Halliburton's estimating system. Did Halliburton agree that these deficiencies were significant?

Mr. REED. While agreeing to the deficiencies, they argued that they were not significant.

Mr. WAXMAN. And what did DCAA think about Halliburton's claims that these deficiencies were insignificant?

Mr. REED. We disagreed and stated that to the contracting officer in our report.

Mr. WAXMAN. You thought there were serious problems, and DCAA explicitly concluded the estimating deficiency was not a one-time occurrence, but it was systemic?

Mr. REED. That's correct.

Mr. WAXMAN. These cost estimate proposals are very important. Once approved, the cost proposals are the basis for Halliburton's fees, aren't they?

Mr. REED. There are many factors that go into the fee setting, but certainly cost is a consideration in setting the fee.

Mr. WAXMAN. DCAA found that Halliburton submitted a $2.7 billion proposal that, "did not contain current, accurate and complete data regarding subcontractor costs." Is that correct?

Mr. REED. That's correct.

Mr. WAXMAN. If Halliburton's estimate is too high and is accepted, then Halliburton gets profits for work it has never completed. Is that right?

Mr. REED. That's a possibility.

Mr. WAXMAN. GAO told us that there were enormous discrepancies between the first proposal that Halliburton submitted in October and the second proposal that Halliburton submitted in December after DCAA rejected their first proposal. According to GAO, the first proposal was $700 million higher than the second proposal. Is that correct?

Mr. REED. That's correct. And actually, it was DCAA who identified that and briefed it to the GAO.

Mr. WAXMAN. Now, is this normal to have that kind of $700 million deficiency?

Mr. REED. Certainly the materiality of that issue is not normal, no, sir.

Mr. WAXMAN. In fact, I understand there still has not been a final proposal submitted. GAO told us that DCAA continued to have doubts about the validity of the second proposal, and as a result, Halliburton withdrew this proposal also. Is that correct?

Mr. REED. Yes, sir. That is correct. The company is taking these rejections very seriously. I have had the highest level of commitments from the company officials that they are going to get these problems solved, and they are hesitant to submit additional proposals until they can submit current, accurate and complete data. We are urging them to do so expeditiously.

Mr. WAXMAN. On January 13, DCAA sent its December audit to the Army Corps and other Defense agencies overseeing major Halliburton contracts. The January 13 cover memo from DCAA highlighted the serious nature of the audit findings and concluded with the final explicit warning to the Corps and others, "We recommend that you contact us to ascertain the status of Halliburton's estimating system prior to entering into future negotiations."

Nonetheless, 3 days later, the Corps issued a new $1.2 billion contract to Halliburton.

Mr. Reed, your January 13 memo asked the Corps to contact you before it entered into any further contracts with Halliburton. Do you have a recollection of anyone from the Corps contacting you about this matter before it signed the new contract with Halliburton?

Mr. REED. No, sir, I have no knowledge of being contacted.

Mr. WAXMAN. Were you surprised when you learned that Halliburton just received this contract worth $1.2 billion?

Mr. REED. I wouldn't say I was surprised, sir. There are circumstances where contracting officers do have other ways of evaluating price and cost data. We are giving them our advice so we can explain to them what we saw as the risk in the contractor's proposals. If they had read our report and considered those risks and considered as well other data they may have had, I can't say that they did not have a sufficient basis to award the contract.

Mr. WAXMAN. But they never talked to you about it?

Mr. REED. No, they did not.

Mr. WAXMAN. General Strock, Mr. Reed says the Army Corps never contacted DCAA about its audit findings before giving Halliburton another $1.2 billion contract. Do you have any information to contradict this?

General STROCK. No, sir, I do not. I know the contracting officer did have the DCAA January 13 memo in his hands when he made this and considered it and documented the reasons for his decision.

Mr. WAXMAN. Why didn't the Corps followup with DCAA?

General STROCK. I can't answer that. I was not in the process.

Mr. WAXMAN. I can't understand how the Corps can operate this way. The government auditors have just found enormous problems with Halliburton's performance, and these are just ignored. We are talking about a contract that will cost the taxpayers $1.2 billion, yet it doesn't seem like the Corps even bothered to contact the DCAA before issuing the contract.

General Strock, your Web site says when the Corps was deciding who to award this contract to, one of the key factors was past performance. Other key factors were Halliburton's management approach and its contract administration plan. I want to ask you how you could possibly have found there were no problems with Halliburton's past performance or its management approach or its contract administration plan. The DCAA audit in its warning said that the company can't accurately predict its costs. It also found significant deficiencies and systemic problems. That is not a good sign of past performance or good contract management, is it?

General STROCK. I can't comment on the basis for the decision. I do know the contracting officer had that information available to him. And generally, the position is, we make decisions based on substantiated claims, not purely on allegations.

Mr. WAXMAN. At the briefing with my staff, we asked you to be able to answer these questions. Are you able to answer them? You don't have the contracting officer here. Did you contact the contracting officer, anticipating that you were going to be asked these questions?

General STROCK. I did speak with the contracting officer about whether or not they had possession of the 13 January memorandum and whether they considered that in their decision, and that

was the answer I got. It was considered and reviewed and found to be an appropriate outcome.

Mr. WAXMAN. And that satisfied you?

General STROCK. Yes, sir.

Mr. WAXMAN. At the time the new contract was awarded, Representative Dingell and I had been bringing information to the Corps for months that showed Halliburton was charging twice as much for gasoline as it should. DCAA validated these concerns in December. I don't know how these overcharges figured into the assessment of Halliburton's past performance.

The day before the contract was awarded, Halliburton, in fact, told the Defense Department that its procurement officers had been involved in a $6 million kickback scheme. Do you know if this was factored into the evaluation of Halliburton's past performance?

General STROCK. No, sir, I do not.

Mr. WAXMAN. Well, does anybody know that?

Mr. ZAKHEIM. I can't speak to the evaluation. What I can say, however, is that, in fact, it was Halliburton that informed us of this, and therefore, we are taking appropriate action as a result. So they came forward. It certainly doesn't seem to me to be to the detriment of KBR that they reported on their own people.

Mr. WAXMAN. Well, let's look at this thing. They report to you that their own employees were getting kickbacks of $6 million. Your own audit people were telling you that there were systemic problems with Halliburton's handling of this whole business. You have this whole system of problems with Halliburton in the past, and so the next day, they are given a $1.2 billion contract, and the claim is they are given a $1.2 billion contract because they had good past performance. How could they reach that conclusion?

Mr. ZAKHEIM. Congressman, in the first place, Halliburton identified two people out of I believe 19,000 that are working for KBR right now around the world. So I hardly think that means that the other 18,998 are in the same boat. They found the people themselves. They reported that.

As General Strock said, certainly, I don't have visibility into how the Army Corps of Engineers makes a decision. But clearly, the fact that they identified these people, and we have taken appropriate action doesn't seem to me like being to their detriment.

Mr. WAXMAN. We had the $6 million in kickbacks. We also heard about millions of dollars in meals that were being charged, but had not been served. We had an obscure Kuwaiti subcontractor given the gasoline contract. And one of the Army Corps Officials thought that was beyond her integrity to have that done. We had a systematic deficiency in accounting practices.

They are under investigation by the Pentagon Inspector General, and we now also know they are under investigation by the Justice Department. Now those investigations by the Justice Department and the Inspector General and the State Department Inspector General, that is not just for overcharging the government. These are criminal investigations.

That means there is something really wrong, fraud or criminal action not just Halliburton overcharging.

Mr. ZAKHEIM. Not necessarily. Let me take your points one by one. In terms of the meals, as Bill Reed has already indicated,

there is a disagreement. KBR is within its rights to make its case, and that is still being evaluated.

Isn't that right, Bill?

Mr. REED. That's correct.

Mr. ZAKHEIM. The issue and the outcome have not been settled.

As for the officer, I told you earlier, I wasn't personally familiar with the so-called pressure. However, once we did become familiar with her letter, that was part of the reason that we referred this whole oil—$61 million—to the Inspector General. So we were the ones who referred it in part on the basis of something that we didn't have visibility into.

Finally, in terms of your talking about investigations, of course, an investigation is simply that. It doesn't necessarily mean that someone is guilty. Very often—the Inspector General of DOD has told me this on several occasions—an investigation is undertaken just to clear someone's name. It is not at all clear that just because an investigation has been undertaken those people are guilty.

Mr. WAXMAN. Let me ask you a question because you just raised an interesting thought in my mind. A minute ago I asked you if you knew about that letter from Mary Robertson, and you said you didn't know about it. And then you testified, on the basis of that letter, that you referred it to the Justice Department Criminal Division.

Mr. ZAKHEIM. I understood your question—perhaps I misunderstood you, Congressman—I understood your question to be whether I was aware of the pressures outlined in that letter, and I was not. Was I aware of letter? Yes, of course.

Mr. WAXMAN. Chairman Davis asked you if you were aware of any charges of political pressure by anybody involved in this contracting issue. And here we have a letter that you have seen from someone working for the Army Corps of Engineers saying that it would violate her integrity to pay more than necessary and she is under political pressure but she doesn't want to give into it.

Mr. ZAKHEIM. I understood the question of whether I was aware of political pressure. The letter does not necessarily convey to me that there was pressure. There was an allegation of pressure, and it was referred to the Inspector General to see whether the allegation is valid or not.

Mr. WAXMAN. I know that before anybody is convicted of a crime, it has to be proved beyond a reasonable doubt. But I don't think it should be the job of this administration to give Halliburton the benefit of the doubt in every case when they have a long record of charging for millions of meals that they didn't deliver, overpaying for gasoline they were bringing in, systemic deficiencies in their cost estimating system and your own auditors telling us there are big problems with the way they are handling their contracts in Iraq.

I just want to ask one very clear question. When there are criminal charges being investigated, doesn't that indicate to you that it is not just an instance of poor judgment?

Mr. ZAKHEIM. Again, I can't speak to an investigation. On the other hand, what I can speak to is what I have seen in Iraq since I have been out there twice, most recently 2 weeks ago. I did see services provided, and I did see clean toilets, and I did eat decent

food, and I didn't hear complaints from anyone about how they were being supported.

It seems to me, in the larger context of what is going on with a massive tax that is taxing one of the larger companies in this country, it seems to me—and I have said this on the record before, that they are not doing a great job, but they are not doing a terrible job.

Mr. WAXMAN. Well, you have pointed out that they are already at the budget ceiling of $18 billion, which is more than we realized they were getting in Iraq. That is a lot of money for you to have a clean toilet and a good meal in Iraq and for them to do the job they need to do. They need to do the job they are paid to do. We need you and them to protect the taxpayers in this country from overpaying. And we are worried whether we are getting that kind of service from people in this administration.

Mr. ZAKHEIM. Congressman, we are the ones that have found the discrepancies. We are the ones that referred them to the Inspector General. We have 25 auditors risking their lives out there. We are carrying out our responsibility.

Mr. WAXMAN. But you are the ones who are also ignoring all the evidence including the report from your own audit team that the taxpayers are overpaying and that Halliburton is contracting with subcontractors and paying those subcontractors more than they should be paying.

Mr. ZAKHEIM. On the contrary, Congressman. With respect, I have to differ. If, indeed, it is proved that there is overcharging taking place, that money will be restored. That has already happened in several cases. In those cases where there is a dispute, it has to be resolved. But any money that is identified as having been overpaid is indeed being restored.

Mr. WAXMAN. Do you think it was appropriate to issue the $1.2 billion contract without the Corps talking to DCAA when they sent an audit saying, "Please talk to us first?"

Mr. ZAKHEIM. I believe General Strock answered that.

Chairman TOM DAVIS. Let me make a comment. How many criminal investigations are being undertaken now by the IG's office? Any idea.

Mr. ZAKHEIM. I don't know if they're all criminal. There are four investigations all told.

Chairman TOM DAVIS. Well, I mean ongoing.

Mr. REED. For the whole Federal Government?

Chairman TOM DAVIS. For the whole Federal Government, right.

Mr. ZAKHEIM. I have no idea. We'd have to get you that for the record.

Chairman TOM DAVIS. But it's a lot, isn't it?

Mr. ZAKHEIM. It's more than four.

Chairman TOM DAVIS. It's more than a dozen, isn't it?

Mr. ZAKHEIM. I will have to get that for you for the record.

Chairman TOM DAVIS. Absolutely.

How many IGs are there?

Mr. ZAKHEIM. Quite a few. We'll get you that for the record.

Chairman TOM DAVIS. Exactly. I mean all of us who have been in government contracts know that whenever you see anything suspicious—Mr. Reed, isn't that right, that you would refer to this?

Mr. REED. Yes. DCAA has made up to hundreds of referrals a year.

Chairman TOM DAVIS. Thank you. That's what I'm trying to establish here. This isn't so out of bounds, particularly when the contractor himself comes to you and says, we think we have allegations with some of our employees. And they want to use that and blacklist them?

We went through this. We had votes in the House on this issue before about blacklisting contractors over some allegation or some investigation before there's an adjudication, and this House voted opposite where Mr. Waxman is on that.

Mr. WAXMAN. Would the gentleman yield?

Chairman TOM DAVIS. I'd be happy to.

Mr. WAXMAN. The House and the Senate faced supplemental bills and one the Senate had a provision saying there ought to be criminal penalties for war profiteering. The conference met and took that provision out.

Chairman TOM DAVIS. That may be, but that wasn't the vote I'm talking about, the blacklisting regulations that were promulgated by the previous administration. And we've had votes on this and what——

Mr. WAXMAN. No one is calling for a blacklist. What we're calling for is scrutiny——

Chairman TOM DAVIS. Reclaiming my time, I——

Mr. WAXMAN. Are you on your time?

Chairman TOM DAVIS. I'm on my time.

All I'm trying to say, Mr. Waxman, is—and I understand you are raising some important points here as we go through, but that's not a mark of past performance when an employer comes forward and says, look, we may have a problem with some employees, we may have a problem with the government that's trying to extort and make us go to one contractor, and they come forward to the government and disclose this. They shouldn't be punished for it. This is what you want contractors to do when they have problems like that.

Am I right on that, Mr. Reed? Isn't that how you want a contractor to act?

Mr. REED. That's true. The DOD Inspector General has promoted this voluntary disclosure program for that very purpose, to encourage company management to take responsibility for enforcing its own internal controls.

Chairman TOM DAVIS. Let me ask you this. Documentation in a war zone is sometimes a little more difficult to undertake, isn't it, than if you're sitting back in an office somewhere? Is that fair it to say?

Mr. REED. That would certainly be my expectation. You would not necessarily see the same type of documentation you would in an environment in the States.

Chairman TOM DAVIS. And is Halliburton—since you let them know the standard of documentation you're now expecting in a war zone, are they shaping up, are they coming forward with better documentation?

Mr. REED. I wouldn't want to comment on this point. That's still a work in process. But they——

Chairman TOM DAVIS. OK. They don't get paid unless they provide the documentation; isn't that correct?

Mr. REED. Well, we obviously in certain cases feel we have enough basis to suspend costs, which we have done in the case of the—the dining facilities. The company, though, has, I think, shown the right response in terms of stating to us what actions they are planning to take; and we're going to make sure they take those actions in a timely way.

Chairman TOM DAVIS. Let me just get back—the reason you have a cost-plus fee, an award fee, fixed fee, whatever in some cases is—who fronts the cost in a contract of that type?

Mr. REED. Contractor—I may defer to Ms. Ballard.

Chairman TOM DAVIS. Ms. Ballard, doesn't the contractor front the costs?

Ms. BALLARD. Yes, he does.

Chairman TOM DAVIS. So in this case, the contractor, whoever it is—Bechtel, Halliburton, whoever—fronts the costs and then they submit reimbursements from what they have already upfronted; is that correct?

Ms. BALLARD. That is correct. And if the costs that they submit are not fair and reasonable, allowable or allocable, we do not pay those costs to the contractor.

Chairman TOM DAVIS. Theoretically, they end up costing them money if they don't clear DCAA in their scrutiny and they don't clear your shop; is that fair to say?

Ms. BALLARD. Yes, that is correct.

Chairman TOM DAVIS. And so there's no taxpayer money invested up front. It comes in the reimbursements and that's when the auditors come in; is that correct?

Ms. BALLARD. That is correct.

Chairman TOM DAVIS. What a deal. It seems to me, under those circumstances, that's a pretty good vehicle for the government. We're not having the taxpayers upfront money, putting money at risk, until we see the audits and it's cleared. And it's not uncommon, from my 20 years of experience in government contracting, to see contractors come forward with costs and have them thrown right back at you from alert, trained auditors that are used to this and you argue about it from there. Is that your experience?

Ms. BALLARD. That is correct and that does happen.

Chairman TOM DAVIS. I just want to put all of this in an appropriate framework for this. This is a war zone and things go on.

I think Mr. Waxman has raised some important points. One thing he's talked about is the contracting officer that decided not to notify DCAA before they went ahead. I mean, we'd like to talk to that officer, like to have that officer come before the committee, but to find out what they weighed.

And, General Strock, if you could make that available to us.

Mr. WAXMAN. Just a correction. It's my understanding that Ms. Robertson did contact the contracting officer, her superiors, and urged them not to go forward and be pressured into the subcontract with Altanmia.

Chairman TOM DAVIS. Let's find out. I think we need to get—and that can be a subject; we just need to find out what went into this.

Obviously, whenever you have allegations of the type that are coming forward here, favoritism or something, given this, then we want to get to the bottom of it and see. I don't see that it's happened, but we still have some threads we have to follow through on.

I think it's pretty clear from your testimony that there's no obvious evidence of this. From what I understand from Mr. Waxman's questions, the political pressure was on using a company in Kuwait, and I don't know under what circumstances they would have told us—the embassy or anybody else would have said, we have to use a certain oil company in Kuwait. But am I wrong? Aren't the Kuwaitis doing their own investigation on that?

Mr. ZAKHEIM. You're absolutely right. The Kuwaitis are investigating, and that just shows that there is a concern both here and there. I mean, we are investigating. There is a concern.

Chairman TOM DAVIS. Not to cast aspersions, but isn't corruption not uncommon in that part of the world?

Mr. ZAKHEIM. I don't want to cast aspersions, Mr. Chairman.

Mr. MCHUGH. Mr. Chairman, would you yield to a question from me?

Chairman TOM DAVIS. I'd be happy to.

Mr. MCHUGH. I get a little confused sometimes in my old age, but wasn't your question to the panel that Mr. Waxman has referred to, did they receive any political pressure from the administration to award the contract to Halliburton?

Chairman TOM DAVIS. That's correct.

Mr. MCHUGH. Now, did Halliburton, where this lady was employed, receive pressure to award it to a Kuwaiti firm, correct?

Chairman TOM DAVIS. That's correct. I didn't ask that question.

Mr. MCHUGH. I thought so and——

Mr. ZAKHEIM. To be clear, the contract officer was working for the government, but our answer was, that we were not aware of political pressure. She has made an allegation, and that is part of an overall referral to the inspector general precisely to get to the bottom of this.

Mr. MCHUGH. She was working with Halliburton, but Halliburton already had the contract was the point. It was not so the administration was trying to enrich——

Mr. ZAKHEIM. No. Absolutely not.

That's correct, Mr. McHugh.

Mr. MCHUGH. But that was the suggestion that was made.

Chairman TOM DAVIS. That's fine. Mr. Waxman, you have 5 minutes.

Mrs. Maloney, you're recognized for 5 minutes. Thanks for bearing with us.

Mrs. MALONEY. Thank you, Chairman Davis and Ranking Member Waxman.

I just want to state that I've been fortunate enough to visit Iraq twice with Chairman Davis, in August and in February, and to meet with the troops and review the contracts; and the troops are really doing a remarkable job under very severe conditions, and we are thankful for their service and to your service.

I would like to go back to Ms. Ballard, when you testified earlier that when a decision is made to give a monopoly contract, a sole-source contract, you make a determination.

Was a determination made in the case of the sole-source monopoly contracts in Iraq? Was that procedure followed in the letting of those contracts.

Ms. BALLARD. Congresswoman, I need to be sure I understand your question. Are you speaking of the sole-source award to Halliburton, or are you speaking of the Parsons award in the north and the KBR award in the south?

Mrs. MALONEY. I'm speaking to all three.

You said that when you make a decision to let a no-bid, sole-source contract, you make a determination that is appropriate to do that as opposed to having a competitive bid. That was part of your testimony that was part of the procedures that if you don't have a competitive bid, you make a determination that it's important for whatever reason, an emergency or whatever, to follow the other course; and my question was, was that determination made in all three contracts?

Ms. BALLARD. In the case of the Restore Iraqi Oil contract, a determination was made under the Competition in the Contracting Act that unacceptable delays existed and therefore a sole-source award was appropriate.

Mrs. MALONEY. Could we have an example or could we have a copy of the written determination, all three cases?

Ms. BALLARD. The LOGCAP contract is the one sole source and, yes, ma'am, there is a determination that we can make available.

In the case of the Parsons award in the north and the KBR award in the south, those were not sole-source contracts. Those contracts were competed and, in fact, there were six offerers who competed for those awards.

Mrs. MALONEY. And I would like to see a copy of the determination and the types that you provided with a no-bid contract.

Admiral Nash, when we were in Iraq——

Chairman TOM DAVIS. There's no problem with supplying that is there?

Ms. BALLARD. No.

Chairman TOM DAVIS. I just wanted to get that on the record. I just wanted make sure there's no problem with supplying that. They said there's not.

Mrs. MALONEY. And we had this conversation when we were in Iraq, and I asked and I believe the chairman also asked why we were not allowing Halliburton and Bechtel to compete for specific projects. At one point, you said we had to let these contracts because you had to get the people over there.

Now they're both over there. Why couldn't we let these two companies compete? Would that not save taxpayer dollars?

Mr. NASH. Some of the contracts under which they're working are not full and open, so therefore I can't use them in some cases. In fact, KBR, Halliburton is the contractor for the oil in the south. It was full and open competition; and they will in fact be doing the work down there.

We will look at the opportunity, whether we can do some competition, but the goal is to be able to implement this work effi-

ciently and effectively. So I guess the answer is, we can and we can't for those contracts that are not correctly—were not done in a way that the supplemental laid out. We won't be able to use them. So we'll take a look at that.

Mrs. MALONEY. I think that could save taxpayers' money.

And General Strock, didn't the Army Corps recently award a construction contract for the Central Command to 10 different companies?

General STROCK. Yes, ma'am, we did, out of our Transatlantic Center in Winchester, VA.

Mrs. MALONEY. So, Admiral Nash, why did the administration choose to deviate from this practice?

Admiral NASH. I'm sorry. I don't understand. We are using some of those 10 contracts right now to do work in Iraq with the supplemental money, because they were full and open competition.

Mrs. MALONEY. And now that Parsons and Halliburton have monopolies in the south and in the north, what's wrong with having these two groups compete, as opposed to cost-plus contracts in which there is really no incentive to save taxpayers' money?

Admiral NASH. Well, if I may, all of these contracts have mechanisms so that we have tasks and those tasks are negotiated. So it's not the true cost-plus that they just send us a bill after they're done and we pay whatever it is.

If I understand your question, why can they not compete for all of the oil work, whether they are working the north or the south—and that's what I said we would take a look at now that we have those in place—it depends on what the contract—what the contract clause is saying.

And I will take a look at that, ma'am.

Mrs. MALONEY. When I arrived in Iraq on the very first—we actually were in Kuwait. The headline in the Kuwaiti paper was that Altanmia was being investigated by the Kuwaiti Government, by a unanimous vote of their parliament, over allegations that Altanmia was making profits of over $800,000 a day; and that's extremely troubling.

Chairman TOM DAVIS. The gentlelady's time has expired.

Mrs. MALONEY. I just want to say, if I could, Mr. Chairman, that I truly I do believe that the American taxpayer owes a great deal of debt to Mr. Waxman and yourself for your diligent overview of taxpayers' money in these contracts.

Chairman TOM DAVIS. Thank you very much. This isn't our last hearing, but we appreciate that.

The gentleman from New York.

Mr. MCHUGH. Thank you, Mr. Chairman. I'm getting confused again. I've been on the Armed Services Committee for 12 years. I serve as the chairman of the Total Force Subcommittee.

I thought I understood LOGCAP. I heard the gentlelady from New York say "sole-source," "exclusive," "no-bid," and other such colorful adjectives, "contracts." Isn't the purpose and hasn't the purpose of LOGCAP always been to, after a competitive process, which happened here, and after the winner is announced, which was Halliburton in this case, you make use of those in extreme situations just as we did when I visited Haiti with General Sullivan, just as they did when I was with the Chief of Staff of the Army

when I was in Bosnia, just as I did when I visited a K–2 in Uzbekistan, or the twice I've been to Iraq, or 10 days ago when I was in Afghanistan for 2 days.

Am I correct on that or am I really badly confused?

General MCMANUS. You're correct, sir.

General KERN. Congressman, if I can elaborate on the LOGCAP contract, we're on LOGCAP 3 right now, which gives you an indication that this isn't the first time in this—as mentioned earlier, we've been doing this for 10 years and it has been competitively awarded.

Mr. MCHUGH. Let me ask you that because you raised a point. This one was competitively awarded. I seem to recall about the time I went to Bosnia in 1997, there was a competitive award process run. DynCorp won that under the previous administration. The previous administration rejected that competition and thereafter awarded a true sole-source contract to Halliburton. Is my memory correct there?

General KERN. DynCorp had the previous LOGCAP contract; that is correct. It was competed in 2001.

Mr. MCHUGH. It was competed later, but in Bosnia, Halliburton was kept on the ground; is that not correct?

General KERN. This is another confusing issue. There was a sustainment contract awarded in Europe for Bosnia. That was competed separately. That was different than the——

Mr. MCHUGH. And who——

General KERN. LOGCAP contract that we're talking about.

Mr. MCHUGH. Who held that?

General KERN. DynCorp held it previously, but the pieces of it were then recompeted.

Mr. MCHUGH. And who held it for Bosnia?

General KERN. I will have to make sure——

General MCMANUS. Congressman, I think this is important because LOGCAP won—that was a 5-year contract 1992 to 1996, Corps managed. Brown & Root Services won that competition then. There were four other companies that competed.

During the period of time of that contract, we supported operations in southwest Asia, in Somalia and we began to work in the Balkans. That's an important thought because I'm going to come back to that in a second.

Then on the LOGCAP, which you were talking about, the second iteration, LOGCAP 2, was the period 1997 to 2001. That again was competitively awarded, then to DynCorp; and there were three other defense contractors in that competition during this time period between the operations. And this is what we try to do: We go into an area with a contingency contract, when the requirements are unknown here, duration, and this gives us the flexibility and agility to deal with those changing requirements in the battle space.

After about 2 to 3 years, with experience in the Balkans, you, sir, then made the decision to compete for sustainment purposes the continuation of that mission in the Balkans, which is separate from LOGCAP today, sir.

Does that——

Mr. MCHUGH. It does, but the point remains the same. There was a unique treatment in the Balkans that I suspect, if it were done today under the current administration, would somehow be characterized as special treatment because Halliburton was already there and obviously participated to advantage in that contract.

General MCMANUS. Yes, sir.

Mr. MCHUGH. And that's the answer I could have gotten 3 minutes ago. I appreciate it. But that is the key point.

Now let me ask you another question. The cost-plus contract today, it's a 1 to 3 percent; is that correct? What was it under the previous administration.

General MCMANUS. Sir, let me—let me go back to LOGCAP 2, sir, if I may.

Under LOGCAP 2——

Mr. MCHUGH. I enjoy our travels.

General MCMANUS [continuing]. Lessons learned off of the—each time we do this because you cannot compare each contingency we support. They're unique in their own right.

Mr. MCHUGH. General, I'm not asking you to justify it. I'd just like you to answer what the cap is today.

General MCMANUS. It's 3 percent. It's a 1 percent base fee, 2 percent award fee, which they compete for, that we've not gotten to yet.

It was 8 percent in LOGCAP 2, so we drew——

Mr. MCHUGH. Eight percent. So if you're concerned about the percentage, then actually Halliburton is receiving less under this administration than they did under the previous. And by the way, I think those charges, if anybody would make them, are ludicrous. I supported that initiative back then and I support it now, and in all those places, I've seen good work being done by men and women in uniform I couldn't be more proud of.

And that doesn't suggest that Dov Zakheim and others don't have a lot of work to do on any contract, they do, but we have been there trying to work these out to the benefit of the American people. Somehow to suggest that an embassy who conveys the issues with the country, that they work to any corporate interest of America that is in that corporation is somehow criminal, then I'll tell you what we ought to do is go back, get Ben Franklin and everybody to Secretary Albright because they'd all be in jail.

So I just think we ought to understand what the realities are today. These are not clear-cut issues whether you're dishing out meals or cleaning toilets, as—having clean toilets, as the ranking member said. This is incredibly difficult work, and you folks have difficult work, and I feel confident that at the end of the day you're going to make sure the taxpayers get what they deserve while we're taking care of our men and women in uniform.

Thank you, Mr. Chairman.

Chairman TOM DAVIS. Thank you. The gentleman's time has expired.

The gentleman from Massachusetts, Mr. Tierney.

Mr. TIERNEY. Thank you.

Recently two former Halliburton employees who worked for Halliburton's LOGCAP procurement office in Kuwait came forward with, I think, some disturbing information about a culture of over-

charging. According to these whistleblowers, Halliburton officials frequently told employees that high prices charged by vendors were not a problem because the U.S. Government would reimburse Halliburton's cost and then pay Halliburton an additional fee. They referred to an informal Halliburton motto, "Don't worry about the price, it's cost-plus."

Examining the situation from a different angle, the GAO is reporting the same indifference to cost.

Dr. Zakheim, if these accounts are accurate, would you agree with me that this is a completely unacceptable attitude?

Mr. ZAKHEIM. If they're accurate. And what we have done is taken this account and treated it as a hotline referral; and as you know, a hotline referral goes to the inspector general precisely to investigate this.

One other point that I think is very important to make: We know that the courts have continually held that you cannot deny a contractor award on the basis of allegations. An investigation looks into allegations. You've got two guys here——

Mr. TIERNEY. I don't want to interrupt you, but I don't think I said anything about denying contracts. I was simply asking you a question.

Let me followup, because I understand that Mr. Reed immediately sent it over to the inspector general on a hotline referral, but what troubles me is, the inspector general is apparently doing nothing to followup on this.

The minority staff contacted one of the whistleblowers yesterday—his name is Henry Bunting—and he said that no one from the inspector general's office has contacted him.

Mr. Zakheim, how do you explain this? The allegations of the whistleblowers are serious; you've admitted that. Where is the followup?

Mr. ZAKHEIM. There will certainly be followup. They're very methodical. Their approach, as I understand it, and obviously I'm not working with the inspector general's office, but as I understand it, they are very careful, they assemble their facts, they interview people. I guarantee those two gentlemen are going to be interviewed.

Mr. TIERNEY. Well, both Mr. Dingell and Mr. Waxman sent a letter explaining all of this in significant detail over a month ago—over a month ago.

The whistleblowers also say that Halliburton employees deliberately keep purchase orders below $2,500 so they can avoid the requirement to solicit more than one quote, in other words, to avoid having vendors compete to supply the company with goods.

They say that Halliburton's supervisors encouraged them to use a list of preferred Kuwaiti vendors even though many of these firms were unreliable or charged outrageous prices. Now, this letter is over a month ago and we've seen nothing come back.

Mr. Bunting testified before the Senate Democratic Policy Committee last month. The same day, or virtually the same day, GAO investigators contacted the minority staff to ask for more information on how to contact Mr. Bunting and the other whistleblower. That's what I would think an investigator would do if they were serious about this, but no one from the inspector general's office has ever contacted Mr. Waxman or his staff to learn how to get in

touch with these whistleblowers, and apparently no one has contacted Mr. Bunting despite the fact that they were put on notice over a month ago.

Mr. REED. Mr. Congressman, could I tell you one additional thing that is being done? I'm not sure where it stands with the IG, but in addition to the regular conduct that might have been suspected from the letters, we took it as an issue, as well, of normal contracting for DCAA to followup on this.

So I have sent that letter to my audit office in Iraq. We have been looking—working with the Defense Contract Management Agency, that is responsible for administering the contracts and for approving these $2,500 awards. They have to sign off on every single one of them. So we have brought these very serious allegations to their attention, and we are working together with DCMA to see if we can validate and correct these situations.

Mr. TIERNEY. I appreciate that, Mr. Reed. And I appreciate, Mr. Reed, your immediate referral to the inspector general's office. I think that was the appropriate action to take, and I think you should be commended for that.

Will you be getting back in touch with the attorney—the inspector general to find out why this lapse has occurred or what's going on?

Mr. REED. We do normally receive periodic updates from hotline referrals. And, yes, sir, we will do that.

Mr. TIERNEY. I thank you for that. I yield back.

Mr. LATOURETTE [presiding]. I'm going to recognize myself for 5 minutes.

I didn't have the opportunity to go with the chairman on his trip, but I did have the chance to be in Iraq in January with the Transportation and Infrastructure Committee to look at civil works projects. And before I ask a couple of questions, I want to just relay a story.

There was a young lieutenant from Toledo, OH, who talked to me about the 2,000 civil works projects that had gone on in Iraq, and some of them have been mentioned—redoing schools, Operation Chalkboard, reopening hospitals, making sure hospitals were up and running, giving people running water that had never had running water in their life. I think the chairman in his opening statement talked about a wastewater treatment plan by General Odierno in the Sunni Triangle. And I made the observation to the lieutenant, I said, you know, lieutenant, I watch a lot of television, as I think we all do in my job; and I can tell you, back home when we do something swell, we as politicians have a band and a ribbon, and we all cut it with scissors, and we take the scissors home or the shovel home after the groundbreaking. How come I've never seen any of this on television? Why have you never had a ceremony?

And the lieutenant said, we've had a ceremony for every one of those successfully completed civil works projects.

I said, how come you think I'm not watching it back on television?

He said, Congressman, we watch a lot of CNN and Fox here, because we've got it in Baghdad, and we've never seen it on television either; and our feeling is that the broadcast media waits by the

scanner for one of our buddies to be injured and you'll see that on the news at night, but you'll not see our successes. So when you go home, it would be nice if you could tell people about the successes.

So I'm keeping my promise today to the lieutenant from Toledo.

You are doing an amazing amount of work in Iraq, and you know, I saw a guy on TV when I was there and he said, under Saddam Hussein I had electricity 24 hours a day and now I only have it 16 hours a day.

And I asked the lieutenant, why is that?

He said, because he's from Tikrit. Everybody in Tikrit had electricity 24 hours a day, but the guy in the next town had it zero hours a day, and so through our redundancy efforts, we're going to make sure that everybody's treated the same and everybody has it 16 hours a day.

Now to my question. When the ranking member, Mr. Waxman, was making his opening remarks—and if I misquote him, I apologize and I'll be certain to yield to him—but talking about contractors' officers, and I think he said that reservists are going over and are being given a 2-week crash course in contract management, words to that effect.

And, Ms. Ballard, I heard you talk about the contract officers that are in station. Is there a 2-week sort of correspondence crash course on how to administer these contracts? Are these contracts being administered by people on the ground in Iraq by professionals or the Keystone Kops?

Ms. BALLARD. Congressman, I have no knowledge of 2-week training crash courses to go over and be contracting officers in theater. In my experience, the reservists who come to work for us are usually put in positions where they have experience from their commercial occupations or from their military service. On the ground, our professionals come from the Defense Contract Management Agency, an agency I'm proud to have worked for, and I can say clearly that they do have professionals on the ground that administer these contracts and provide oversight to us.

Mr. LATOURETTE. Thank you very much.

And Admiral——

General KERN. Congressman, could I add—I think I'd like to clarify——

Mr. LATOURETTE. Sure.

General KERN. There is a Reserve unit called the LOGCAP Support Unit, which I believe is what Congressman Waxman was referring to. It was the first time we had employed that unit, starting with operations primarily in Afghanistan, when we began the buildup of the LOGCAP work. That organization is comprised, however, of the professionals that was referred to, of DCMA auditors as well.

I just met with them in Baghdad. They are on their second iteration of it. It's a multiservice, multicomponent unit composed of professionals. The professional PCOs are part of General McManus's office that oversees the contract. The ACOs, the administrative contracting officers, in theater, are professionals as part of DCMA.

I'd let McManus describe it in more detail.

General MCMANUS. Sir, the LOGCAP Support Unit concept is a new edition, based again on lessons learned, because as we have to leverage this capability, we have to train our folks. We provide these planners to go into the theater, out to the base camps, to the units, if you will, 4th division, to the brigades and so forth. So as requirements are generated, these are the folks who work together to create the scopes of work.

And so prior to their deployment, this is a case of having a new organization. We wanted to bring them up as currently as we could, because this is a case of forming, organizing and deploying, and have the support and get your skills at the same time. So this was an attempt to bring it up to speed.

This is a new organization, new capability we're trying now to build for future operations, because it's making a huge difference for us as we work the requirements through this whole process from—from origin through completion.

Mr. LATOURETTE. Well, General—either general—let me ask you this: Do you have confidence that these men and women know what they're doing? Are they watching the American taxpayers' buck on these contracts?

General KERN. Yes, they are. And we have taken that from the previous lessons provided by GAO and others on how to improve the process. And that's why this unit exists today and that's why the training that we are using with them. The task order process we are using also breaks it down into further detail, and it is a complex process, to ensure that we have oversight of the entire operation.

Mr. LATOURETTE. Thank you very much. I believe the gentleman from Massachusetts is recognized, Mr. Lynch, 5 minutes.

Mr. LYNCH. Thank you, Mr. Chairman.

I want to thank Chairman Davis and also Ranking Member Waxman for their good work in putting this together. I also want to thank the members of the panel for coming before us and helping us in our inquiry.

I also had a chance to go into Iraq. I was actually part of the first delegation to go into Baghdad after the invasion. And I've got about 20 years in construction management, managing contracts.

And a couple of things I know about no-bid and cost-plus contracts. No. 1, since there is no or very little competition, it's basically a guarantee for whatever contractor is anointed. The second thing, on a cost-plus contract, the profits are guaranteed and there really are no restraints on how much a project will cost. There are no internal restraints on the part of the contractor. So I think Mr. Zakheim would agree that the auditing function here, and Mr. Reed would agree, the auditing function is extremely important, because the more the company spends or the contractor spends, the more they're going to make on their percentage. So the auditing function is extremely important.

Is that correct, Mr. Zakheim?

Mr. ZAKHEIM. Absolutely, sir. I agree.

Mr. LYNCH. In this case we have an auditing function where our—the DCAA wrote a recommendation to the Army Corps of Engineers and said—and I'm going to pull it right from the letter. It said, "They have identified systemic problems with Halliburton's

accounting, and it urged "the DOD not to award further contracts to Halliburton without talking to the DCAA about Halliburton's accounting problems."

And the problem that I have is, this is the way the system is supposed to work, that the auditor is supposed to oversee what's going on and that the contracting authority is supposed to listen. But that didn't happen here.

That didn't happen here, and another $1.2 billion went out to Halliburton and, in other cases, Brown & Root. Despite some problems that have been found in their operation, they continue to work without any correction or any restraints at this point.

General Kern, I'd like to bring your attention to a couple of reports regarding several Halliburton employees who were caught taking kickbacks. They took them from a Kuwaiti company in exchange for steering contracts of that company; and as I understand it, Halliburton caught the officials engaged in these activities and reported them to the Defense Department; is that correct?

General KERN. That's correct, Congressman.

Mr. LYNCH. Last week, General, your staff met with our committee staff in preparing for this hearing and our staff asked for the identity of those two individuals. Your staff at that time reported that they didn't have the information then, but they'd get back to the committee with the information.

Unfortunately, we have been waiting and that has not happened, to my knowledge. Is that forthcoming or——

General KERN. I was away last week, Mr. Congressman, so I don't know—have the precise answer. I promise you, I will get back to you, and if there is no legal reason why I cannot provide that, it will be provided.

Mr. LYNCH. I've got to tell you, I'm one of the Democrats who actually supported the action in Iraq, and I supported the money for our troops and for reconstruction, and I've got to tell you, I'm concerned right now. I'm concerned. I'm not somebody who has criticized the military or been reluctant to support you, but I've got to tell you, it's our responsibility, all of us, to protect the American taxpayer.

General KERN. I agree with your concern.

Mr. LYNCH. I'm concerned.

General KERN. And we are—I will promise you, and I have spoken a number of times with my command counsel about this specific incident, and it is going to be thoroughly investigated; and we will bring those concerns to the forefront for you.

Mr. LYNCH. Well, more than concerns brought to the forefront. I'd like to have an opportunity to talk to those individuals and find out how senior are those individuals who accepted the bribes from this Kuwaiti company. Do we have at least an indication of how senior those Halliburton officials are?

General KERN. I do not have any indication of that. I know that it was brought forward. I know that it is under investigation, and I know that they have provided us compensation for what they believe was the amount of the bribe that was taken. But that is what we are going to ensure is investigated thoroughly.

Mr. LYNCH. I will conclude, Mr. Chairman.

I keep hearing this: that the price is overcharged and then the penalty is to give the money back that we caught you stealing. That's just not going to get it. That's just not adequate.

General KERN. Congressman, we agree with you 100 percent and that is, in fact, what is happening, that we are——

Mr. LYNCH. There've got to be more serious consequences than just, oh, we caught you stealing, give the money back. This is millions and millions of dollars of the taxpayers' money, and we have to have a better standard than that. And I'm just going to conclude with these remarks.

I don't understand how you couldn't know the rank and the identity of these officials. These officials were at the very top of the procurement ladder. These people were handing out millions of dollars in taxpayers' money in the form of contracts.

We know who these people are. That's why I say, my confidence has been shaken on this point, and we ought to put a lot of sunlight on this process, find out who these people were, find out how many contracts they oversaw, find out who the Kuwaiti contractors were that were bribing them. And are those subcontractors who provided the bribes doing other contract work in the country as well? We need some accountability here. That's all I'm asking.

Chairman TOM DAVIS [presiding]. The gentleman's time has expired.

But just to clarify, it was the—Halliburton came forward and said, we suspect bribery. Right? You wouldn't have known about it had they not come forward and said, We think there are employees—am I correct on that?

General KERN. I would hope that our audit would have picked it up, as well.

Chairman TOM DAVIS. Eventually, maybe.

General KERN. Yes.

Chairman TOM DAVIS. OK. The gentleman from California is recognized for 5 minutes.

Mr. OSE. Thank you, Mr. Chairman.

General Strock, your stars are confirmed by the Senate, are they not?

Mr. STROCK. Yes, they are.

Mr. OSE. General Kern, the same? Your stars are confirmed by the Senate?

General KERN. That's correct, sir.

Mr. OSE. General McManus.

General MCMANUS. Sir, that's correct.

Mr. OSE. Ms. Ballard, are you subject to Senate confirmation?

Ms. BALLARD. No.

Mr. OSE. Are you a political appointee?

Ms. BALLARD. No, I am not.

Mr. OSE. You're a civilian——

Ms. BALLARD. A career civil servant.

Mr. OSE. OK. Long-term?

Ms. BALLARD. Twenty-nine years.

Mr. OSE. You're almost permanent then, aren't you?

Mr. Lucke.

Mr. LUCKE. I'm a career foreign service officer, not subject to Senate approval.

Mr. OSE. Dr Zakheim.

Mr. ZAKHEIM. I was confirmed by the Senate.

Mr. OSE. OK. Mr. Reed.

Mr. REED. I'm a career civil servant.

Admiral NASH. I'm a private citizen back on duty here.

Mr. OSE. As an admiral, you were confirmed by the Senate were you not?

Admiral NASH. That's true.

Mr. OSE. All right. I've always enjoyed sandcastles here. Let me just—I want to make sure I've got this correct here.

Halliburton, it's been alleged, has some nefarious scheme going to pick the pocket of taxpayers. Now, if I understand, what you all have done is, they have submitted something for $2.7 billion, some contract here; you told them, well, it doesn't quite meet our expectations. So they came back at $2 billion, saving the taxpayers $700 million. But that wasn't satisfactory either.

Now, as I understand it, you've got to be nominated—who nominated you General Strock, to be a general?

Mr. STROCK. Sir, the President nominated me.

Mr. OSE. The President——

Mr. STROCK. Of the United States.

Mr. OSE. President Bush?

Mr. STROCK. I'm sorry, President Clinton.

Mr. OSE. President Clinton nominated you to be a Brigadier? How about a Major—for your second star, did you go to President Bush?

Mr. STROCK. President Bush, yes, sir.

Mr. OSE. General Kern, your fourth star was from President Bush?

General KERN. That's correct, sir.

Mr. OSE. General McManus.

General MCMANUS. Yes, sir. My second star was President Bush. I've been a general officer about 6 years now.

Mr. OSE. All right. Let's see.

Dr. Zakheim, you were nominated by the Bush-Cheney administration and confirmed by the Senate?

Mr. ZAKHEIM. Yes, sir.

Mr. OSE. Admiral Nash, your stripes?

Admiral NASH. President Clinton did both of my stars.

Mr. OSE. So let me make sure I've got this right. The people—the Bush-Cheney administration, who nominated some or all of you for your stars or for your positions, under the sandcastle scenario, is doing all this heavy lifting for Halliburton, but then all you people are sitting there telling Halliburton they can't have the contracts that they otherwise are submitting? You're saying the contracts aren't specific enough or they aren't clean enough or they don't meet our requirements under FAR.

Now, the sandcastle I'm trying to understand, as described by certain members on the other side, exactly how does Halliburton benefit when you guys return their contracts to them, when you say their contracts aren't good enough?

General Kern, you're the four-star here. Tell me how that works. I'm missing some picture here.

General KERN. Congressman, we take an oath to obey the laws of the President of the United States in orders from him and from the Constitution of the United States, and we are responsible to the American public to make sure that all of those things happen. So as our commander in chief, we follow the law and the orders of our administration, and we ensure that all the regulations that have come forth, such as the Federal Acquisition Regulation, provided by this Congress, and oversight are also met.

So we will continue to make sure that both the taxpayers' money is well spent and the security of our Nation is met.

Mr. OSE. General, I have actually gotten great comfort from the testimony here. It's the sandcastle allegations I'm trying to address.

Dr. Zakheim, you're a political appointee. You ought to be looking out for, under the scenario of the sandcastles, the interests of a certain individual, but your department is sending the contracts back for further review. You're costing these people money. I mean, exactly what are you up to?

Mr. ZAKHEIM. Well, my understanding is, I support the President of the United States and the American people by looking after the taxpayers' dollar, and the only pressure that I'm aware of is the pressure that I put on poor Bill Reed here to keep going after anybody or anything that's untoward or might rip off the taxpayer.

Mr. OSE. Which brings me to my point.

Now, Mr. Reed, there have been allegations that things weren't forwarded to the IG or that the IG is supposed to report to you on their activities. If I understand correctly, any illegal behavior that you suspected, you have, in fact, forwarded to the IG; is that correct?

Mr. REED. Yes, sir, that's correct.

Mr. OSE. Now once it's forwarded to the IG, is it within your domain to prosecute?

Mr. REED. No, sir.

Mr. OSE. That's somebody else's job?

Mr. REED. That's correct, sir.

Mr. OSE. Does the IG report to you?

Mr. REED. No, sir.

Mr. OSE. So the IG is supposed to pick up the burden at that point and carry on?

Mr. REED. That is correct, sir.

Mr. OSE. Are you aware of a contract that's been introduced or that the Corps entered into for recent——

Chairman TOM DAVIS. The gentleman's time has expired.

Mr. Ruppersberger.

Mr. RUPPERSBERGER. Yes, thank you.

First thing, there's a lot of testimony about Halliburton and other issues which are very important and need to be addressed. I'm more concerned about where we're going now and in the future, because our men and women are at risk. We have other people there. We're trying to rehabilitate a country, and I think it's very important that we take the lessons learned and go forward.

Now, I'm very concerned about—and I'm going to review a case right now, a contract, and I'm going to ask your comments on that,

because I'm concerned about this contract because it affects what is happening now and in the future.

Let me get into this issue. Major General Charles H. Swannack, Commander of the Army's 82nd Airborne Division, criticized the failure of U.S. Coalition Provisional Authority in Iraq to deliver equipment needed by newly formed Iraqi security forces.

And by the way, I was just in Iraq a couple of weeks ago. You know that part of the insurgents' plan is not only going after our men and women, but after the men and women in Iraq, especially security, that are working with their country. So it's a very important issue.

Now, Swannack said his division has successfully trained more than 10,000 Iraqis to be police security and border guards in the volatile regions stretching from Falluja to the Syrian border, but he said the forces lack the equipment needed to fight insurgents, which I assume was ammunition and guns and things of that nature, to protect the vast Iraqi border. Swannack voiced frustration because lack of equipment had hampered Iraqi efforts to secure the region.

Now, the equipment was to be delivered under a controversial $327 million contract that the Pentagon canceled last week, a month—that could delay the process for months. That concerns me. These people are at risk right now.

The contract had been awarded to a small Virginia firm with no history of arms dealing, and it is alleged that the company Nour, N-o-u-r, USA—and the President is A. Huda Farouki, F-a-r-o-u-k-i, has close ties with Chalabi, a member of the Iraqi Governing Council and a close ally of some Pentagon officials. Again, that's alleged and I'm not asking you to comment on that.

The contract was canceled after protests by competing companies that found Nour had claimed to be partners with high-profile companies, an individual who said in interviews they had no links to the firm.

Now, this was a quote that was made by the General, "Not only are the security forces bravely leading the fight against terrorists; they are in some cases insisting on doing it alone." And I know that those of us who were over there saw the will of those Iraqi individuals who want to take control their own country. And the only way we can get our men and women out of that country is to get them to secure their own country, build the infrastructure that is necessary.

But, anyhow, they are in some cases insisting on not doing it alone, not depending on coalition forces.

Swannack said this: "if we had the equipment for these brave young men, we would be much further along." That concerns me. Pentagon officials blaming—this is alleged—irregularities in the contracting process for the cancellation and saying they were rushing to finalize a new contract, but they predicted it would take 60 to 90 days before a new supplier was selected. That concerns me. And that is an issue we need to look at, we need to evaluate it so that it doesn't happen.

Here's what I would like: First thing, how was that contract put out to begin with, No. 1? How was the contract given to this company that really had no expertise? Who was involved with that?

Where—and I'd like to ask, really—I guess, Mr. Zakheim, you're getting a lot of the heat today, but I'd like to ask, who was responsible for this type of contract?

The men and women of Iraq are relying on us, our leadership, to provide them the resources that are necessary. Not only was this contract a bad contract, but we've got 60 to 90 days where we have a general saying that these Iraqi individuals—I mean, these Iraqi security people cannot do their job. That's what I'm concerned about.

We are going to deal with the Halliburton issues and all that; that will be around, and investigations will be done. But what about the future? That's very serious.

And the other issue I want to ask, because I'm concerned—my time is going to be up and I want to lay it out. I think the Iraqi Governing Council—I'd like to know how much money is given to them, if at all, that allows them to negotiate contracts using American dollars? I think that's an important issue. Using American dollars, how much influence do they have? Are they given any authority to contract with anyone with our American dollars?

I also supported the $87 billion because I believe we have to finish what we started. Whether you are for or against the war, we're there and we have men and women that are doing a good job there; and it's a hard job and we understand that.

So if you could address those issues—I think we need to have lessons learned, but let's deal with these kinds of situations. When you are affecting the security of these Iraqi security people and our men and women, that's serious.

Mr. ZAKHEIM. Congressman, let me address the question about what about the future. I think one of my colleagues can talk to you a little bit about the Nour contract, and I'm sure Admiral Nash can talk about how the Iraqis properly get involved in the contracting process.

Regarding the future, we are as concerned, as you rightly are, that we can't just wait around for the process to play itself out. And frankly, we're caught here because, on the one hand, we want to have the proper procedures, the proper competition, all the things we've been hearing about, in order to protect the American taxpayer; and that takes time. On the other hand, you've got commanders in the field and our young men and women who are being shot at, and we've got to help them out immediately, and we have to keep finding that delicate balance.

In this case, the one you raised, we are looking at alternative sources of financing, possibly out of the Development Fund for Iraq, that might help acquire some of this material, since the DFI, as it's called, is purely for the Iraqi people and this is for Iraqi security forces; and that, of course, we could implement much more quickly.

So we are indeed trying to do exactly what concerns you. Let me turn to my colleagues——

Mr. RUPPERSBERGER. But my question was, how did this occur? How was that——

Chairman TOM DAVIS. We're way over the time. I want to give him a chance to answer. I want to get——

Mr. RUPPERSBERGER. And don't forget the Chalabi issue, too.

Ms. BALLARD. Congressman, I'd like to say, first, that we have awarded over 1,300 contracts in Iraq, valued at $1.3 billion, of which approximately 1 percent is appropriated dollars. The competition rate on those actions is 99 percent, and 65 percent of the awards have gone to Iraqi businesses as primes. And we've generated over 21,000 jobs. We've done this with currently 28 personnel on the ground in Iraq facing significant challenges in austere circumstances.

By way of comparison, in 2002, the Robert Morris Center had roughly $2 billion in contracting actions and 305 people who worked those actions.

The contracting process, we strive every day for greater excellence in that process. Clearly, our staff in Iraq, faced with challenges in austere circumstances, is making significant contributions to the rebuilding of Iraq.

In those circumstances, with 1,300 contracts awarded, we have found the circumstance where offerers did identify concerns. The contracting process worked as it should; those circumstances were evaluated. We determined that action needed to be taken, and we took action. And the GAO, satisfied with our course of action, dismissed the protest.

In response to your question with regard to what we will do to support the soldiers, as Dr. Zakheim has indicated——

Mr. RUPPERSBERGER. Let me stop you here because you're not answering my question.

Mr. Chairman, I'm trying to get them to answer the question about the Nour contract.

Chairman TOM DAVIS. I know. I know. And we've got time. We've got to move on. Let me try to get it in the rebuttal at the end. We've got 20 minutes aside at the end——

Mr. RUPPERSBERGER. I've got to take off. So if somebody could follow through with that. It's just the Nour contract and Chalabi.

Chairman TOM DAVIS. OK. Thank you very much.

The gentleman from Texas.

Mr. CARTER. Thank you, Mr. Chairman. I just got back here a little while ago from going over there with the chairman, and I want to say that I think that I saw miraculous things happening in Iraq, and I was very impressed with everything that I saw. And there's no better group of fighting men and women on the face of the Earth than the ones I got to talk with and have supper with, and I'm very proud to be associated with them.

I've been hearing a lot of stuff here, and my background makes me listen for the magic words. And I hear words like so and so—it has been found that so and so "took a bribe." It has been found that such and such, so and so—I'm asking—my first question is, are there any actual people who are supposed to be finders of fact who actually found that this happened, or—it sounds more like this should be said: Someone has alleged that these things are taking place. Is that a better use of the description than a finding?

It may be as clear as it could be, but nobody has actually made a finding that would say that bad behavior has taken place. There were allegations that have taken place.

Mr. ZAKHEIM. I think in the main that's absolutely correct, and we've tried to stress that, that even an investigation is simply to look into what really went on.

It's an investigation of allegations; you're absolutely right. With respect to the so-called "kickbacks," that was presented to us by KBR and even that's being investigated, so——

Mr. CARTER. And it rightfully should be investigated before anybody is punished. I have never seen anybody in prison because somebody alleged that somebody did something. We generally went out and found out—had a finder of fact make a finding that they actually did that, like a jury or a judge or whatever procedures there may be in the Federal Government.

Mr. ZAKHEIM. Due process is part of our process.

Mr. CARTER. All of these things that we've heard about here today, including a question that was raised just a few minutes ago about an allegation that someone said that you're supposed to—don't worry about the cost because it's a cost-plus contract. That's being looked into is that correct?

Mr. ZAKHEIM. That's correct, sir.

Mr. CARTER. And, in fact, all the other allegations that have been raised here today, all those are turned over to the proper authorities to be investigated?

Mr. ZAKHEIM. Absolutely.

Mr. CARTER. And is anyone at the table here in charge of those investigations?

Mr. ZAKHEIM. In some cases, yes. When we're doing audit investigations, Bill Reed here does that. The inspector general is not at this table, but he certainly takes over those, as well.

Mr. CARTER. Right. But those then, as to the audit investigation, which there is someone at this table responsible for, would you say that's being sandbagged or is that a current investigation being carried on as we speak?

Mr. REED. The audit process is alive and well and being pursued vigorously with the support of all the contracting officers involved in these contracts.

Mr. CARTER. So we're doing the job—you are the only ones that can speak for this investigation, and we're doing the job that we're supposed to do. We're currently looking into the allegations that relate to the audit investigation.

Mr. REED. All of the contract audit issues are being pursued aggressively.

Mr. CARTER. So we're doing the job on that?

Mr. REED. Yes, sir.

Mr. CARTER. We've turned the others over to the proper authorities to be looked into.

Does anyone have knowledge that these proper authorities are not looking into these allegations?

Mr. ZAKHEIM. No.

Mr. CARTER. So does everybody agree that, as far as you know, they are currently investigating these things on a reasonable timetable to investigate these kinds of allegations?

Mr. ZAKHEIM. That's correct.

Mr. CARTER. That's kind of what I assumed was right, but the sounds that were going around here didn't make it sound that way.

Mr. Ruppersberger's contract question that he was talking about, that's a concern to me, too, because I was over there. I met those troops, and I was told the same thing, as soon as we get these guys geared up like we are, these guys are going to get out in the field and they're going to do a good job. So I also agree with Mr. Ruppersberger that we need to get those people supplied.

And the kind of contract—and I don't know the particulars of that contract, but when we start talking about the first initial contracts that are involved over there in Iraq, basically the military says we have a theater, a dangerous theater, that has a lot of contingencies that we can't predict exactly what those contingencies are; and that's why we go through this type of contracting process, which we're calling a cost-plus contract. And if I'm wrong, correct me, because I sure can be.

Is that right.

General MCMANUS. Sir, for contingency planning purposes we have a LOGCAP contract in region for those unknowns as they evolve.

Mr. CARTER. Right. And this is one of those unknowns that have evolved. So what can we do to make this an emergency situation to get these supplies to these troops that we've been training over there?

Mr. ZAKHEIM. Well, as I said, Congressman, we are looking at alternative sources of funding so that we can get the money more quickly, because the contracting process takes what it takes, and it's got to be done properly or else we will be answering questions as to why it was not done properly.

But there are alternative sources and we are looking carefully at that to get the money so that we can get the equipment to those Iraqis. Because you're absolutely right; they're being shot at every bit as much as our people, if not more.

Mr. CARTER. I guess what I'm saying is, this wouldn't be a real smart idea to just let this out for bid for the next 6 months to try to figure out who gets the highest bid. We've got an emergency. We've got to deal with it.

Mr. ZAKHEIM. And we're going to move on that.

General KERN. Congress, I met with General Sanchez on that specifically this week on how we're going to get through that. We are going to move out.

Mr. CARTER. Thank you.

Chairman TOM DAVIS. Thank you. Ms. Watson is recognized for 5 minutes.

Ms. WATSON. Thank you so much, Mr. Chairman, for this hearing.

I guess I will address this to Major General Strock, and just say yes or no. The Army Corps of Engineers awarded an initial no-bid contract to restore and operate Iraqi's infrastructure currently valued at $2.44 billion to Halliburton and its subsidiary, Kellogg Brown and Root.

General STROCK. The capacity of that contract was $7 billion, but that's correct.

Ms. WATSON. And almost $1.4 billion has been obligated for fuel importation into Iraq?

General STROCK. Yes, ma'am.

Ms. WATSON. More recently, the Corps split the oil work into two competitive contracts, one for the north and one for the south. And the Corps awarded Halliburton the new $1.2 billion contract to operate Iraq's oil industry in the southern half of the country?

General STROCK. Yes, ma'am.

Ms. WATSON. The Army Materiel Command has obligated over $4 billion for logistic support in Iraq under Halliburton's logistical civilian augmentation program?

General KERN. Yes, ma'am.

Ms. WATSON. And then I am very supportive of what all of you in the military and those assigned to build the infrastructure of Iraq and continue whatever we have to do militarilywise in Iraq. I did not support the war, but I support our troops, and I support our obligation.

I am concerned about reports that we are hearing, and we heard them from Halliburton, which got the contract, that there were kickbacks, and as I understand, and I want someone out there to correct me, that the persons involved must have been at the highest level because they were in control of millions of dollars, maybe billions of dollars of government procurement. And so I would request that with all due speed that we weed out these wrongdoers. My job is to protect my constituency and their tax money, billions of dollars that are being spent 10,000 miles away, and we have infrastructure problems right here. I am going to ask you with all due diligence to weed out—I don't care if it is 2 or 18,000. We need to know. Apparently goes way up high, because the decisionmakers make decisions over millions to billions of dollars.

And so to do the job in Iraq, it is costly. We understand that, and we support you. But I do not support the wrongdoers, I am suspicious because why Halliburton, no-bid contract, before we knew the people were on the ground, and you can trace an association to someone high up in the administration. Just the appearance of impropriety should not exist, but it happened, and we need to move on. But I would like the overseers, whoever is responsible, to immediately get back to us what steps are being taken, because it makes all of us look bad. And those who have the oversight and the auditing and so on, you look like you are not doing your job and you are not being responsible.

So let's dig them up and identify them if they exist, and let's clean them up, and let's see that every dollar of taxpayers' money is used effectively and efficiently and in the best interest of America and Iraq.

Thank you, and I yield back the rest of my time.

Mr. ZAKHEIM. I make one exception to one part of your statement, the part about the auditors, about not really being on top of it.

Ms. WATSON. Let me tell you what I meant. I want with all due speed for all of those—the buck stops here. I don't know who has the final oversight and who is going to do this investigation. It has not been cleared or clarified in what I have heard, so whoever is responsible. I am not blaming one person or the other. Dig out the wrongdoers, bring them to justice, and let's move on.

Mr. ZAKHEIM. We certainly could agree on that.

Chairman TOM DAVIS. Mr. Van Hollen, 5 minutes.

Mr. VAN HOLLEN. Thank you, Mr. Chairman. And I want to thank all the witnesses for being here as well. I want to thank the chairman of the committee for leading the bipartisan delegation to Iraq recently, and I was pleased to join him on that trip.

And, Admiral Nash, it was great to meet you there. And I want to thank you for doing hard work under very challenging circumstances. And we all agree, as we talked about today, that at the same time we want to make sure we protect the American taxpayer.

And I want to delve into some issues that Congressman Waxman raised, because he has raised some very important issues, and I want to focus specifically starting with DCAA and, Mr. Reed, the contract where you concluded that there were about $61 million on potential unaccounted for charges. And I understand that DCAA did that around December 11 of last year; is that right?

Mr. REED. If you are addressing the fuel issue on the restructuring?

Mr. VAN HOLLEN. The KBR fuel contract, $61 million.

Mr. REED. Yes.

Mr. VAN HOLLEN. And you recommended at that time that the contractor disallow those $61 million in costs; isn't that right?

Mr. REED. No, sir. What we did was we issued a draft report to the company to get their response to what we believed was some poorly documented costs that they were billing to us. At the time, based on some data that we had, we felt that the impact could be as high as $61 million, and we asked them to justify that cost.

Mr. VAN HOLLEN. You are saying they should justify that cost; is that right?

Mr. REED. That's correct.

Mr. VAN HOLLEN. And you were going to recommend to the contracting officer that they justify that cost; is that right?

Mr. REED. We were going to receive the company's response, evaluate it, and if they satisfied us, we would make no recommendation. If they did not satisfy us, we would recommend the cost be disallowed immediately.

Mr. VAN HOLLEN. Eight days after that, the Army Corps then filed a waiver, which essentially exempted KBR from providing that supporting documentation; is that right?

Mr. REED. That's right.

Mr. VAN HOLLEN. In your experience, have you ever heard of a waiver being granted in that way especially after auditors at DCAA had found overcharges and were in the process of reviewing the charges?

Mr. REED. Let me clarify my previous answer. What we were looking for was for Kellogg Brown and Root to show us how they determined that was a fair and reasonable price. That may or may not have called for the submission of cost or pricing data, which the waiver was granted for. Certainly there were facts or indicators that if indeed we were locked in with a sole-source supplier, that we should get cost and pricing data. That was one of the points that had not been pinned down as to whether we were locked in with a sole-source supplier, although there were certainly indications. I will let the Corps of Engineers address the waiver.

Mr. VAN HOLLEN. Let me ask you, are you satisfied as of today that $61 million should not be disallowed, that the American taxpayer has been treated fairly?

Mr. REED. No, I am not satisfied, and there is an investigation underway by the IG. And once their work is done, it is turned back to us, we will continue our audit work.

Mr. VAN HOLLEN. Let me turn to the Corps, General Strock. It seems to me that if we wanted to get to the bottom of this, we would tell KBR, look, you're charging this amount of money. It is your subcontractor. You should be providing the supporting documentation.

Why did we grant them a waiver.

General STROCK. A couple of factors. First of all, the chief of engineers as head of the contracting agencies is granted that waiver, and he was presented with the facts at the time he made the decision he thought was appropriate. The issue here is the cost and pricing data. We are informed that under Kuwaiti law, the subcontractors are not required to provide cost and pricing data, and we requested that, and that is the answer that we got, that the law disallows that.

Mr. VAN HOLLEN. Let me followup on that because, at least in my question, which is that we have independently tried to evaluate whether or not that is true, that amount equated to law, and Congressional Research Service, an independent agency here, has reached a different conclusion, and I am wondering if you could supply this committee, since the Army Corps reached that conclusion, with the specific provisions of Kuwaiti law that say they are prohibited—this subcontractor is prohibited. Have you seen that documentation yourself?

General STROCK. I have not seen the documentation. I have seen records of some of the conversations that went on from which we reached that conclusion.

Mr. VAN HOLLEN. If you could provide us with—because that was the primary rationale in disallowing this, and it seems to me it was reached very quickly. I understand Halliburton requested 1 day, and this waiver was granted the next. And I think that as important an issue as that, that the committee receive the legal support that was behind this decision. If that turns out not to be the case, that it is not barred by Kuwaiti law, would you review the waiver and ask KBR to provide the information?

General STROCK. Yes, sir.

Mr. WAXMAN. Will the gentleman yield to me?

The point is that we have asked for this information from the State Department and the Kuwaiti Embassy, and they have not been able to tell us about any Kuwaiti law that requires the contract to have been given out only to this one sole-source subcontractor.

Chairman TOM DAVIS. That is part of the criminal allegation. He has gone to the Congressional Research Service, and they can't find this in the law, and obviously we would like to get to the bottom of this. And I am sure it is going to be part of the criminal investigation as well, but anything you can get us on that will be helpful.

General STROCK. May I clarify, this was not a sole-source subcontract? The contractor got three quotes for the fuel, and this contractor was selected as the low bidder on that.

Chairman TOM DAVIS. I would hate to have seen the high bidder on that.

Mr. Kanjorski. Thank you for your patience.

Mr. KANJORSKI. Thank you, Mr. Chairman.

I am going to direct questions that may not be directly applicable to what the purpose of the hearing is, but over the last several months, I have had returnees from the Iraqi war, both National Guardsmen and Reservists, called me and asked to have meetings with me, and some of them were very disturbing. One sergeant came in and related that his Reserve unit was not capable of getting the boots that fit them, and for a period of 7 or 8 months while in Iraq never got the proper equipment, and he was firmly convinced that there is a prejudice between the real Army and the Reserve and National Guard forces that are over there in terms of getting material there like boots.

Having walked in the Army in my past life, boots are pretty important. And it would seem to me—I am all for, you know, building some of their waterworks over there, but can you find out why we can't give boots and shoes to the soldiers that are in combat zones?

And when you are doing that, I have at least 3 or 4 mothers and fathers who have contacted me over the last 9 months that they are literally buying protective vests for their sons and daughters that are in a combat zone because they are not available by the military. And these kids are getting shot at, injured, and in some instances killed because they lack this basic protective device. And it seems to me that somebody has to step up to the plate and ask some of the questions what's wrong.

And finally, you are awarding all these contracts over there, and I understand we have Humvees that were never anticipated to be used in insurgencies. Why it was not anticipated that they may be used in insurgency situations is beyond me, but they lack armor. Can't you guys award a contract real fast to Halliburton for a couple of billion dollars to put half-inch armor on the bottom of these things so we don't have any more legs, arms or heads blown off? Don't come back and tell us, well, we awarded a contract, we are going to bring these things back, and 18 months from now we are going to have armed Hummers. We have people over there, and they are dying, and most of them will tell you that these explosive devices that are being placed along the road, they are dying not because they couldn't be protected; because the vehicles they are driving aren't properly armored. And I am sure we could find some unemployed welders and people in Ohio, Michigan and Pennsylvania, and I can get you a lot of them and perfectly willing to go over and do this work.

Now, last, and probably you can't answer this, a disturbing news report about a month ago was talking about the extraordinary success that we are having with training policemen in the Iraqi services to provide security once we leave. And the whole story was about the fact that there were 600 recruits hired under contract of approximately $150 million to train over a period of 5 or 6 months, these recruits, half of which resigned within 3 weeks of showing

up. So they anticipated the graduating class would consist of about 300 police officers being trained by contract by the United States. And if you take the $150 million, I came to the conclusion that is $500,000 per police officer.

Now, you know, I got news for you. We have some police academies in Ohio, Pennsylvania and Michigan, and we have all kinds of aircraft going back and forth. If it costs us half a million dollars in Iraq to train a police officer, somebody is wacky. And if this contract is by Halliburton or by Bechtel, somebody ought to have the good sense to say half of a million dollars is ridiculous. We don't spend that amount to train a police officer in the United States, and there is no damn reason in the world we should throw taxpayers' money away to train them in Iraq.

Can anybody tell me whether there is any factual basis for those types of costs in training security and police officers in Iraq?

Mr. ZAKHEIM. You asked four questions. I will try to handle the first three, and Mr. Lucke will try to address your fourth.

On the boots issue, I have heard this before. I believe it is being taken care of, but I will get you an answer for the record because I don't know the exact specifics.

You asked about the body armor. We expect to have basically 175,000 kits in theater by the end of this month, that is to say March 2004, which will fully support the CENTCOM requirements. So it is not 18 months, it's this month.

On the up-armored Humvees, we are ramping up production. Current production is about 138 a month. We will ramp it up by more than 50 percent.

Mr. KANJORSKI. Where are you doing this? Here?

Mr. ZAKHEIM. Yes.

Mr. KANJORSKI. Welding isn't a tough thing.

General KERN. Could I answer that? Two points. One, every soldier today in Iraq has body armor. That was done by the end of January. The CENTCOM number goes beyond Iraq. It includes the people who are in Kuwait who would be transiting, and that is the number. So we have addressed that. General Schoomaker took that on as a personal issue. The Acting Secretary of the Army Mr. Brownlee took that on as a personal issue. And we reported to them every single day on the outfitting of those soldiers, boots, BCUs and the protective gear, and that has been done.

Mr. KANJORSKI. I hope it has been done, and if it has been done, congratulations. But, you know, what bothers us, where was the planning, where was the anticipation that there should have been enough body armor, there should be enough boots, there should be armored Humvees over there? Where was the planning behind this operation? There wasn't any? Nobody thought about this?

General KERN. The original planning gave the body armor to those soldiers who would be in direct contact, infantry armor, artillery soldiers. The secondary planning which went beyond that is everybody in theater, including our civilians who are working in the theater right now, and there is where we fell short in the original planning.

The other point on the Humvees, in addition to what Mr. Zakheim reported to you, we are producing armor kits in every depot. And I can't promise you that the one I have is producing it

in Pennsylvania, but it is doing it in Sierra, out in California. We are doing it in Alabama. Armored kits—in addition to the new production Humvees, in addition to the Humvees, those kits are also being put on the family of medium tactical vehicles and the heavy equipment transport.

So that is being done as quickly as we can from all sources we can, and we have gone to find those welders and sources of steel to make sure that does happen. We have taken that very seriously. We are not going to wait for the production.

Chairman TOM DAVIS. OK. Thank you very much. We were 3 minutes over. What I am going to do is move to summary at this point. Mr. Waxman is going to get up to 20 minutes for any additional questions, and I will summarize from there. And he can yield to any Members over there who still have questions under his time.

Anybody feel they need to take a break right now? I guess otherwise we will try to go ahead and get it done.

Mr. WAXMAN. I want to find out more about Altanmia. General Strock, you said that you agreed with the statement by Halliburton that this was an open and competitive process whereby they chose Altanmia as the subcontractor to provide the gasoline. Is that a fair statement of what your views are?

General STROCK. I have been informed that KBR solicited for quotes to three suppliers, and Altanmia was the lowest quote received.

Mr. WAXMAN. Well, the Army Corps sent to us on January 6 their justification for this claim that it was fair and reasonable, but in that justification it said Halliburton did not issue a public solicitation or a public request for quotations for the purchase of gasoline. Halliburton did not seek out all qualified bidders. Instead, Halliburton hand-picked three companies and telephoned them informally on May 4 to obtain quotes for the purchase of gasoline. And then on that same day, after they made these three calls, they chose Altanmia and requested the Corps' approval, which it received. Is that an inaccurate statement?

General STROCK. I think that's accurate, sir. We received three quotes and selected the smallest. I don't know the details. But I want to reiterate, the conditions at the time were long gas lines in Baghdad. Soldiers were getting attacked guarding those gas lines, and the contractor was told on May 3rd that they were to begin delivering fuel, and they did it in a very short and compressed period of time.

Mr. WAXMAN. According to your documents, Halliburton had three companies that they contacted. One was Altanmia, KAFCO and Monmar. The Defense Energy Support Center, which has been doing fuel purchases and transports in the Gulf for over 50 years, said they had no knowledge of doing business with any of these three companies. The Defense Energy Support Center also told us that it does do business with several other companies in Kuwait, including TriStar, Mubarak and LeNouvelle. But your records do not show that Halliburton called any of these companies. Do you know whether Halliburton even contacted the Defense Energy Support Center to find out who they would recommend in the region?

General STROCK. No, sir, I don't know.

Mr. WAXMAN. With a contract of this magnitude, a company's past performance and experience is clearly one of the most significant factors in the selection. What experience did Altanmia have in purchasing and transporting fuel?

General STROCK. I can't comment. I don't know.

Mr. WAXMAN. If Altanmia had no prior experience, as we understand the case to be, how would they know even to call them for a price quote? Does someone at Halliburton know someone at Altanmia? Do you know anything about that connection?

General STROCK. No, sir, I don't.

Mr. WAXMAN. Halliburton claims it was unable to locate any company in Kuwait that currently does fuel purchasing and transport for the U.S. Government, yet Halliburton was somehow able to find this other company, Altanmia, which had no experience and awarded a multimillion-dollar contract in less than 1 day. Does this process raise any eyebrows for you, General?

General STROCK. Certainly, sir, suggested that way, yes. May I just say, subsequent to that original award, the Kuwaiti Petroleum Co. refused to allow us to deal with anybody but Altanmia. And also the DESC traditionally deals directly with the Kuwait Petroleum Co., as I understand, and as the Kuwaitis prefer, so it was somewhat unusual that they would deal with a contractor, in this case KBR. So they prefer that the KBR not deal directly with the Kuwaiti Petroleum Co., but rather with the subcontractor.

Mr. WAXMAN. Do you know who owns Altanmia?

General STROCK. No, sir, I do not.

Mr. WAXMAN. Does anybody here know information about that? The record will indicate that no one responded.

I have heard multiple allegations that the brother of the Kuwaiti Oil Minister had some sort of financial interest in the company. Do you know whether that is true?

General STROCK. No, sir.

Mr. WAXMAN. Anybody else know whether it is true? Do you think it is important to know whether the Kuwaiti Oil Minister or his family had an interest in this company? Does anybody in the panel think it was important to know whether the Kuwaiti Oil Minister or his family had an interest in this company?

Mr. ZAKHEIM. I don't know if that would be the kind of question somebody would immediately ask. Certainly it wasn't the kind of thing that sprang to my mind when I looked at all this and passed it on and worked with Bill Reed on it, whether there was some family connection or something.

Mr. WAXMAN. I raised this issue in a letter dated January 15 to National Security Advisor Condoleezza Rice. I wrote that several sources had told us that Talal al-Sabah, the brother of the Kuwaiti Oil Minister, had financial ties to Altanmia. I wrote further that although this off-the-books arrangement appears to be undocumented, the sources claim that Mr. Al-Sabah is acting as a consultant for the company or as a hidden partner. I also said that some sources said that other members of the Kuwaiti royal family had ties to Altanmia. In response to my letter, Ms. Rice said this would be investigated by the Defense Department.

General Strock, what steps have you taken to investigate these allegations since then?

And, Mr. Zakheim, what steps have you taken?

Mr. ZAKHEIM. This is all part of the inspector general's investigation of this entire matter.

Mr. WAXMAN. General Strock, do you know about any steps?

General STROCK. I am not sure if my command has taken any either except, as Dr. Zakheim said, to refer it to the investigator.

Mr. WAXMAN. Another mystery has been why the Army Corps keeps saying Halliburton's gasoline prices are fair and reasonable in light of all the evidence to the contrary. On October 18, your spokesman Scott Saunders said that Halliburton was, "getting the best price possible."

Let me take one stark example. We know the Defense Energy Support Center buys gasoline from Kuwait for 96 cents a gallon. Is it just the gasoline and not the transportation? And according to your office, Halliburton charges the U.S. Government $1.17 per gallon. To be clear, we are talking about the same Kuwaiti source. Yet Halliburton charges 21 cents more per gallon to buy the fuel.

Explain to me why Halliburton prices are fair and reasonable in light of this large differential. Why isn't this an overcharge for the purchase of this commodity?

General STROCK. The support center purchases directly from the Kuwait Petroleum Co. We purchase from Altanmia, not the Kuwait Petroleum Co. I also understand that as our contractor suggested, they could get a better price if we could have a longer-term contract and more time to negotiate. The exigency of the situation prohibited that. It is my understanding that Altanmia buys on the spot market instead of buying futures in the fuel, and therefore that fuel is more expensive.

Mr. WAXMAN. Do you know whether the energy support center buys on the spot market or has a long-term contract?

General STROCK. I don't know. They buy directly from the Kuwait Petroleum Co., as I understand it.

Mr. WAXMAN. I am somewhat taken aback with the entire rationale for finding Halliburton's prices reasonable; hinges on the sham 1-day telephone competition in which Halliburton excluded more experienced companies from the bidding. General, let me——

Chairman TOM DAVIS. Could I ask the gentleman to yield?

Mr. WAXMAN. Not yet.

Chairman TOM DAVIS. I will wait.

Mr. WAXMAN. I am just trying to make sure I can get through these questions. Let me ask you to think of yourself not as a contract manager, but as a taxpayer for the moment. Doesn't there come a point where you have to say the U.S. taxpayer should not be forced to pay Halliburton far more than the U.S. Government pays for exactly the same product? Did you ever reach that point?

General STROCK. I am sorry. If you would repeat that, sir.

Mr. WAXMAN. Are you troubled that Halliburton pays more for the gasoline that the government in the energy support center is paying for the same gasoline in Kuwait?

Chairman TOM DAVIS. Let me ask a question. Mr. Reed, you are looking at that, aren't you? Doesn't DCAA look at the price they paid, and if you determine it is unreasonable, then you disallow, and they end up eating it?

Mr. REED. We were in the process of looking at this very issue and question when other matters came to our attention that resulted in us referring the whole matter to the DOD IG for investigation.

Mr. WAXMAN. Mr. Reed, weren't you prevented from looking at this issue of Altanmia's prices because of the waiver?

Mr. REED. No, I don't think that is the way I would state it. We never got to that point because other matters came to our attention, and we referred it for investigation.

Mr. WAXMAN. Let's step back for a minute. Halliburton says they are going to use Altanmia, and they did a bidding process, but it seemed like a sham bidding process. Now they are with Altanmia and overpaying compared to what others are paying for the same gasoline. And we would want the Defense Department to be examining this more carefully. But suddenly the Corps came in with this waiver that Mr. Van Hollen asked about, and the reason—there was a reason from the requirement to get the data from Altanmia about why they are charging these higher prices—was that Kuwaiti law required it. So we don't know that information because someone said Kuwaiti law required that they not give this information.

Now we have checked it out, and Mr. Van Hollen indicated that we can't find any evidence of Kuwaiti law that says you can't look at that point. I think we need a clarification of it, and I expect for the record we will find out what do you think—where you got the idea that Kuwaiti law prevents this information from being supplied. Since we're paying the bills, why do we have to go along with Kuwaiti law that says we have to pay whatever they charge and we can't explore why they are overcharging?

Now, it appears that the underlying premise for the waiver is false. You may not agree to that, but I believe it is a false statement.

The other premise that we had was that the Army Corps suggested that Altanmia was the only company the Kuwaiti Government would allow Halliburton to use to buy gasoline and transport it to Iraq. In addition, an Army Corps whistleblower claimed she was being pressured to negotiate future fuel contracts exclusively with Altanmia. Now, this morning's Wall Street Journal reports that the Kuwaitis sent a letter to Halliburton and to the Army Corps on January 25, 2004, recommending that you drop Altanmia and buy the gasoline directly from the Kuwait Petroleum Co. Yet it appears that the U.S. Government has continued to pay inflated prices for gasoline to Halliburton and Altanmia even though we didn't have to.

Why wasn't Altanmia dropped in January as the Kuwaitis recommended, General Strock?

General STROCK. Sir, we awarded a task order on that same contract on March 2nd. We received a copy of that letter dated January 26 on March 4th, 2 days later. When we received that letter, we immediately suspended deliveries of fuel under that contract. However, when the fuel supplies dropped in Iraq in 2 days, we purchased under that instrument an additional 7 days, which will expire 2 days from now. So we were forced by the situation we faced to go to the only source we have to provide this fuel for the Iraqi people.

Mr. WAXMAN. The journal reports the letter was sent by DHL to the Army Corps officials at Camp Doha. And the letter was faxed to Halliburton on the same day, so that would have been January 25, 2004. And there is a time-stamped receipt.

Have you gone back over your files to determine when you, in fact, received the letter?

General STROCK. I believe that has been done. And indirectly, I have heard that the letter was addressed to a contracting officer who had departed the command and therefore was not acted on by the people who followed. And it was only after it was brought to our attention on March 4th that we acted on it. It was also based upon the way in which it came to us and questioned the legitimacy of that letter. We confirmed just yesterday that, in fact, it was a legitimate letter, and we will comply with it, sir.

Mr. WAXMAN. So because the letter got in somebody else's hands, we have spent how many millions of dollars extra for this gasoline that might have been saved if we had gone to the Kuwaiti Petroleum Co.? What was the figure? $300 million because someone at Doha wasn't working there anymore for the Army Corps? Is that your explanation?

General STROCK. No, sir, I would not necessarily reach that conclusion.

Mr. WAXMAN. What is the current status of the Altanmia contract? Are we still paying them inflated prices as of today? And are we taking any steps to recoup the $300 million paid to Altanmia?

General STROCK. I can't answer the second part. We are still paying under that contract because of the circumstances in Kuwait. That delivery order we have out will expire 2 days from now. There is no other source.

Mr. WAXMAN. What bothers me about the gasoline contract is that again and again what the administration and Halliburton have said turns out to be wrong. The Corps and Halliburton told us the prices were fair because there was full and open competition. We now know there wasn't real competition. The contract was issued in 1 day, and none of the established companies in fuel transport got a chance even to bid. Halliburton told us that the reason the energy support center prices were so low is they used military transport vehicles, whereas Halliburton had to use private contractors. We now know this is wrong. The energy support center used private contractors just like Halliburton. They just used much cheaper ones.

We were told that the reason it was necessary to give Halliburton a waiver from providing cost and pricing data was that the Kuwaiti law prohibited Altanmia from providing this data. We now know, and you helped establish that you believed it, too, that this was false. We were told that the reason that Halliburton had to use Altanmia was that the Kuwaitis would not allow anyone else to have the contract. We now know that's not true.

I see a pattern here that I don't like. I have not said it is a cover-up, but it troubles me that the administration and Halliburton keep putting out false and misleading information. The whole affair does not smell right. We clearly need a full investigation. Do you agree with that?

General STROCK. Sir, I agree we need a complete investigation. I don't agree with everything you have said, no, sir.

Mr. WAXMAN. Who do you think ought to do that investigation? You think there ought to be an investigation. Who ought to do it?

General STROCK. I think it is in the hands of the IG at this time, and I understand the Justice Department has also been called in.

Mr. WAXMAN. I would like to yield to Mr. Van Hollen 2 minutes.

Mr. VAN HOLLEN. I just have a brief followup on the whole issue of granting the waiver, because as I understand it, the Corps has the discretion whether or not to grant the waiver. I have a very simple question, because we have been talking about the need to save the taxpayer money, and my question is, how did granting that waiver help protect the American taxpayer?

General STROCK. We followed an established process which does protect the American taxpayer. The situation in Iraq at the time when the chief engineer signed that waiver was felt to be urgent and compelling, that it had to be done, and this was the only source available. And again, I don't want to understate the importance of this decision, but the moneys applied to this contract are Iraqi moneys from the DFI, not American taxpayer money. And I understand that does not matter here, but this is not American taxpayer dollars.

Mr. VAN HOLLEN. Did the KBR say they would no longer be providing these services unless you granted the waiver?

General STROCK. I don't know the answer to that.

Mr. VAN HOLLEN. Why should the burden fall on the American taxpayer as opposed to KBR with respect to the decision of the Kuwaiti Government? I think it is clear there is a question about whether Kuwaiti law requires that they not disclose this information. I think it is clear that that may not be the case. Why should the burden fall on the American taxpayer as opposed to KBR as the prime contractor of what Kuwaiti law says?

General STROCK. I don't think this burden is falling on the American taxpayer. And second, as we indicated here, our process is to audit all of these proposals we get from the contractor. That has been initially done as irregularities have come forward. That will continue to be investigated. So in the end, I have confidence that the system will work as designed.

Mr. VAN HOLLEN. I agree we should continue to audit. That is why I am puzzled by the fact that you provided the waiver, because the waiver essentially said to KBR, did it not, that you don't have to provide the underlying documentation?

General STROCK. They did receive a waiver on cost and pricing data, which is permitted in the FAR, yes, sir.

Mr. REED. Notwithstanding the waiver, we would still expect KBR to justify how they determined the price to be fair and reasonable. Notwithstanding they didn't give us cost to pricing data, we would expect some other supporting data to establish the fairness of that price.

Mr. WAXMAN. I would yield 5 minutes to Mr. Lantos. But before I do, we didn't get to some questions on Bechtel, and perhaps if you will join us to get some of the answers to some of the questions we wanted to ask USAID about Bechtel.

Chairman TOM DAVIS. And we will leave the record open.

We will recognize the gentleman.

Mr. WAXMAN. Records and documents. We want both.

Chairman TOM DAVIS. Gentleman from California.

Mr. LANTOS. Thank you very much, Mr. Chairman. Let me first express my respect and admiration for all of our military working and fighting in Iraq. I had the privilege of visiting the Baghdad area and up in Mosul, and my respect and admiration is unbounded.

I would like to change the subject, if I may, to an entirely new area. Under Saddam Hussein one of the many restraints and restrictions of that despicable police state was on the rights of workers to organize and to be represented. I would be grateful if any of you, ladies and gentlemen, would tell me what we are doing with our contractors to ensure that in this new world, we are attempting to make sure workers' rights are respected and then enforced.

Mr. ZAKHEIM. Congressman, we will look into that. As you know, there are a number of programs that we are working in conjunction with our partners at AID and State that fall under the rubric of governance that have to do with everything from the rule of law to setting up courts and so on, and we will get you an answer for the record on that specific question.

Mr. LANTOS. I hope you can do better than that because you have been operating there now for over a year, and I would be deeply disturbed if my question would be the first time the question of labor rights emerged in the context of spending billions and billions of American taxpayers' dollars employing Iraqi employees.

You wanted to say something.

Mr. LUCKE. I can tell you that we are very concerned about the rights of citizens and the participation—the fuller participation of Iraqi citizens in their own governance. We have been involved—we have been financing a $167 million local governance contract.

Mr. LANTOS. I am not asking about governance. I am asking about workers' rights. One of the most objectionable aspects of a police state is that it does not accept the concept of workers' rights. Stalin did not accept it. Hitler didn't accept it. And Saddam Hussein did not accept it. He did not want to see the emergence of independent and viable labor unions that would represent an alternative source of power and influence in society.

Now we are attempting to bring about a metamorphosis of Iraqi society, which is a generational undertaking. You folks have been in charge of this now for about a year. Has the issue of labor rights, the right to unionize, the right to protect workers, been part of your discussion? Has it been part of your contracting with various contractors? When you deal with Bechtel or you deal with any of the others, do you discuss workers' rights? Do you discuss the right of Iraqi workers to unionize?

Mr. LUCKE. Workers' rights does not fall under any of the USAID contracts for now.

Mr. LANTOS. Under whom does it fall, since you are the one who signs the contract that gives the money to the contractors? Who else should deal with this?

Mr. LUCKE. There are many implementers of programs. My agency works only with appropriated dollars on contracts. CPA is an organization that works with ministries for the Provisional Govern-

ment of Iraq. There is a Ministry of Labor, and I am quite sure that CPA, if they were represented here, could tell you about some of those programs that may be implemented with other funds, with funds or seized assets. There are no programs that I know of that are being implemented with appropriated funds, and not through AID.

Mr. LANTOS. But your testimony is, that the funds—what is the amount of funds under your control?

Mr. LUCKE. We have about $3.8 billion that we will eventually—have been promised now under the first supplemental and the second supplemental together.

Mr. ZAKHEIM. Congressman, I am going to turn over to Admiral Dave Nash, who heads the CPA Program Management Office. But before I do, there is another aspect that goes beyond contracting, and that is we now have the new administrative law, the TAL it is called, and that does provide for basic human rights. And that is the first step to what you are discussing, but I would like to have Admiral Nash talk about it.

Admiral NASH. There is a Ministry of Labor, and there is a senior advisor to the Ministry of Labor, and we will get some information back to you. But I understand your question to be what are we doing about the contracts that we are letting. And I think the answer is, I will have to get back to you on that. They are being let just like the contracts are in this country, because all the contracts, at least the ones I am responsible for, are being awarded under the Federal acquisition regulation.

Mr. LANTOS. Our labor laws do not apply in Iraq.

Admiral NASH. That's correct.

Mr. LANTOS. So it is the responsibility of CPA to see to it that Iraqi labor is protected.

Admiral NASH. And I will carry that message back, sir.

Chairman TOM DAVIS. Mr. Lantos, thank you for being patient.

Mr. Waxman, thank you very much.

And we obviously have a lot of concerns as we take a look at the amount of expenditure. I want to thank this panel. A lot of tough questions, some within your purview, some without the purview, but I think it shows the seriousness we have in Congress about overseeing contracting there.

When you went over there, it was a mess. In fact, you have 150,000 troops you have to house and feed and worry about telephone calls, transporting them across a difficult country, making a lot of snap decisions. There are mistakes that get made. I feel a little more confident as we go up and find them. In many cases the contractors under these cost plus contracts front the money up front and then come back for reimbursements. That makes me feel a little better about it.

And, Mr. Reed, this is the first time I have had you before this committee, but having had contacts with the DCAA in my previous life, it is a pretty good organization. And if anything, we want you to take away from this, we want you to continue to do your job. We don't want any favoritism, and we are going to hold you accountable.

We are going to be coming back on this. You have a very difficult task. When you said in your opening comments—when you spelled

out the task for America in Iraq and getting that mission accomplished, you are doing the job. And along the way, you have to rely on contractors to do a lot of things, and by and large we have done a good job, but there are things that slip through. The whole Kuwaiti oil incident is something that if we don't watch contractors very closely, obviously if we could do this over again, this is something they should have come to you right away, and it would have been done differently.

As we move forward, I think the warning is we need to be even more careful. And we want to work with Mr. Waxman to get to the bottom of exactly what happened there. And I know the Kuwaiti Government has their ongoing investigation. My understanding is in that part of the world, that nobody can get the cost and pricing data from any Middle Eastern country. I don't know if there is a law. I don't know if they strong-arm us, but we are going to make an effort to try do to it. And if there is any way to do it, we would like to get it, because it looks to me just on its face that something went wrong here. And I don't know if Halliburton might have been the victim, but that would mean the American taxpayers would be the victims, and Iraqi citizens at the same point who are shouldering much of that burden.

It is a tough job, and I think as I have been over there on a couple of occasions now, see the job many of our contractors are doing. We didn't talk about some of the contractors that haven't gone too well besides one. It happens the Vice President was a past president of one company, and the focus has been on that, but every company doing business over there has their own concerns and their own problems, and some contracts have been terminated. Our focus doesn't need to be on everybody.

We know it is a tough job, but we are looking and watching you. And we are going to come back and do followup hearings and investigations in May, and we wish you to continue to do the job. But if anything, we want you to err on the side of being tough and making sure that we are getting our dollars' worth on this. And as the situation gets a little bit more manageable, we expect, I think, as Mr. Waxman and others have talked about, a little more competition as we get into these, on some of the task orders and everything else, looking at some of the contracting vehicles. I think it is a little too early to make any definite determination on charging practices on the part of any company because they are all under investigation. And I have been in this business a long time, and what you hear and what may look on the surface, after it goes back and forth, hopefully this can be resolved, but it looks like we want you to stay tough. I guess that is our message to you as we move forward.

I don't think I have any other questions at this point from our side, but we will have some followup requests for documents, and we may get some other written questions back and forth. And although Mr. Waxman and I don't agree on every aspect of this, I think every member of this committee wants to make sure that as we move forward, we learn from what has happened before. We proceed to get more efficient about the way that we contract, and we want to work together to that, and you are a critical part of

that. I thank you for the job you are doing, and I want to reiterate this. You are doing a great job over there.

Mr. WAXMAN. Mr. Chairman.

Mr. ZAKHEIM. Mr. Chairman, may I make one comment? And I think it is important so there be no misunderstanding. We are tough and, we do ask the tough questions, and you have seen that today. But there are an awful lot of dedicated contractor people, not just Halliburton and their 19,000, but all the contractors who are risking their lives as we speak, and we shouldn't minimize this. And, yes, we will get to the bottom of these issues, but we should be at the same time we look at it as being cognizant of the fact that these people are dedicated, that they are not deliberately trying to rip anybody off, least of all their fellow Americans, and they are sticking their necks out while we are sitting here.

Chairman TOM DAVIS. We met some of the contractors over there as well and talked to them. It is a tough breed of cat. They uproot themselves from their family and their children to go over there to help the war effort. And let's not lose sight that the vast, vast majority of not just our people in uniform, but our civil servants and our contractors are there to accomplish a mission. But things still go wrong under those circumstances, and that is when we get involved and you get involved. I am confident that working together that we can try to resolve some of these issues.

Mr. WAXMAN. I want to thank the members of this panel as well. We are doing our job when we have this kind of a hearing to try to raise these questions and get some answers. And I don't know that we got all the answers. I know we didn't get all the answers. We got only some. I think there needs to be a thorough investigation. And I look forward to working with the chairman in getting the answers we need.

But I must tell you this. When we are asking our young men and women to put their lives on the line in Iraq, I don't want to see anybody enrich themselves unfairly. This is a situation where our country's interest is at stake, and lives are at stake, and we ought to make sure that the taxpayers are being protected and someone along the line is not just getting rich and profiteering in this war while our young people are dying every single day. Thank you very much.

Chairman TOM DAVIS. I would just note that in terms of profiteering, this is just my perception coming off this, there might have been some decisions that could have been made differently downstream, but in the Kuwait situation, if there was a bribery there, no company was profiteering. You might have had an individual or two that has gone astray, might have paid too much for gas, but there was no profiteering on that. These were costs that were passed on. But as Mr. Waxman said, obviously, we all have an interest in making sure that doesn't happen.

The vast majority of contractors are there for the right reasons. I commend you for the job you are doing for this country, and we thank you for being here today.

This hearing is adjourned.

[Whereupon, at 5:50 p.m., the committee was adjourned.]

[The prepared statements of Hon. Carolyn B. Maloney, Hon. Wm. Lacy Clay, Hon. Jo Ann Davis, Hon. Ileana Ros-Lehtinen and additional information submitted for the hearing record follow:]

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Statement of Congresswoman Carolyn B. Maloney
Hearing: "The Complex Task of Coordinating Contracts Amid Chaos: The Challenges of Rebuilding a Broken Iraq"
March 11, 2004
Room 2154, Rayburn House Office Building

Thank you Chairman Davis and Ranking Member Waxman for holding this very important hearing today. Before I begin, I'd like to say that I have been fortunate enough to visit our troops in Iraq twice with Chairman Davis in August and again in February and that they are doing an extraordinary job under extremely adverse conditions. We are thankful for your service to our country and hope for your safe return.

While we were there in February, we heard about the bloody attack in Falluja where an Iraqi police station was attacked and at least 25 people were killed. It was clear from this attack that the Iraqi police force had not been trained properly, nor did they have the proper equipment. In fact, when we met with General Odierno, he mentioned that training the Iraqi police force was going too slowly and it a weak link.

As you know, last April, the State Department awarded DynCorp International a contract worth $145 million to train and supply a new Iraqi police force. This contract was awarded without full and open competition. A comparison of work being done by the military with the Iraq Civil Defense Corps (ICDC), versus the work of DynCorp is shocking:

ICDC required: 8,665
ICDC hired: 10,074
ICDC trained: 7,920

As you can see, the U.S. military has trained nearly 80% of the Iraq Civil Defense Corps.

Now, compare it to the DynCorp numbers:

Police required: 18,565
Police hired: 15,549
Police trained: 1,501

In almost a year, DynCorp has managed to train just 10% of the police force. I am very

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concerned that they while they have not done the job they were given $145 million to do, the State Department has actually extended their contract without competition...again. I also want to know, if we have to give no-bid contracts, why can't we at least let the American military compete to do the job? They have clearly succeeded in their job with the ICDC while DynCorp has failed miserably. This is wrong for the Iraqi people, wrong for our troops, and wrong for the American taxpayer.

I'd like to raise another issue of serious concern. When we arrived in Iraq, there was a huge story in the Kuwait Times about the Altanmia Commercial Marketing Company, an obscure Kuwaiti subcontractor hired by Halliburton that had no previous fuel procurement or transportation experience. They were hired by Halliburton to buy and import gasoline. The article noted that the Kuwaiti Parliament voted unanimously to establish a legislative panel to investigate an allegation that Altanmia made profits of **$800,000 a DAY**. Today, the ***LA Times*** is reporting that Halliburton is under investigation for overcharging the U.S. government by as much as $61 million for gasoline imported from Kuwait into Iraq as of September 30. I'd like to know why Halliburton was given a contract that charged the U.S. taxpayer $2.64 per gallon to import gasoline from Kuwait into Iraq when the Defense Energy Support Center, was importing gasoline from Kuwait into southern Iraq for military use at half the price, $1.32?

Finally, we were fortunate to have met with Admiral Nash where we discussed monopoly contracts. If we give these companies a monopoly, I want to know why can't we at least get the two major contractors, Halliburton and Bechtel, to compete against each other at a task order level? Why do we continue to allow no-bid contracting when we know that we are losing and the American taxpayer is being overcharged and underserved?

I hope that this hearing is one in a series of hearings as we review accountability and needed transparency in government contracting. I thank our witnesses today and hope to have the opportunity to ask some tough questions so that we all leave with a better grasp of what is being done to improve the current contracting system in Iraq.

Thank you.

Statement of the
Honorable William Lacy Clay
Before the
Government Reform Committee
Thursday, March 11, 2004

"The Complex Task of Coordinating Contracts Amid Chaos: The Challenges of Rebuilding a Broken Iraq"

Mr. Chairman, this long-overdue hearing presents us with an important opportunity to examine the extraordinary circumstances surrounding private contracts for the reconstruction of Iraq, and for the supply and maintenance of our troops and other personnel in Iraq and Kuwait.

It is beyond dispute that in the awarding of these contracts, favored treatment was given to the Halliburton Company, the company previously headed by Vice President Dick Cheney. Mr. Cheney's unexercised stock options and deferred salary constitute a "financial interest," according to an analysis provided by the Congressional Research Service.

Is it just a coincidence, that Vice President Cheney was the most outspoken advocate, in this Administration, of invading Iraq?

Mr. Cheney, as Secretary of Defense in the George H. W. Bush Administration, and then as CEO of Halliburton, has long argued for the benefits of outsourcing services for the military, to private contractors.

While he was Secretary of Defense, the Pentagon commissioned Halliburton to do a classified study of how

support functions for U.S. troops abroad could be turned over to a single private contractor. The Pentagon also paid Halliburton for a follow-up study, and then in 1992, Halliburton was selected by the Army Corps of Engineers to perform these support functions for the military. [Peter W. Singer, Corporate Warriors; cited in "Contract Sport," by Jane Mayer, The New Yorker, February 16-23, 2004.]

Mr. Chairman, the company which received such favored treatment for the contract provided needed supplies to our troops in the field, is today surrounded by an extraordinary number of scandals. I am sure we will hear a great deal today about investigations by the Department of Defense into Halliburton's fuel contracts, the DCAA audit of the Halliburton food-service contract, and so on.

There are a number of other investigations and inquiries in which Halliburton is, or has recently, been involved, including:

* On Feb. 9, Kuwait's Energy Minister asked that country's prosecutor-general to investigate overcharging and profiteering in the Halliburton fuel-supply contract for Iraq, and two days later, 23 Kuwaiti parliamentarians called for a separate parliamentary investigation.

* A French magistrate is investigating $180 million in alleged bribes paid by Halliburton and others in connection with a gas project in Nigeria, undertaken while Cheney headed Halliburton in the 1990s. Reports in the European press say that Cheney is a target of the investigation, and that he could be indicted for misuse of corporate assets. France's {Le Figaro} reported on March 2, that the French

magistrate will soon receive the results of investigations carried out in Switzerland and Monaco.

* In Britain, the Export Credit Guarantee Department of the Department of Trade and Industry's is also investigating the Nigeria bribery allegations.

* The Nigerian Economic and Financial Crimes Commission and the Nigerian House of Representatives have both announced that they are investigating the bribery allegations.

* Halliburton itself acknowledged on January 15, 2004 that it had made $2.4 million in improper payments in connection with the Nigeria contract. In a Feb. 6 SEC filing, Halliburton stated that the U.S. Justice Department and the SEC are reviewing the Nigeria matter, "in light of the US Foreign Corrupt Practices Act." The Justice Department's investigation is reportedly being conducted by the Fraud Section of its Criminal Division.

* CBS 60 Minutes" on January 25, 2004 reported how Halliburton and other U.S. companies have used foreign subsidiaries to do business with "rogue states" such as Iran and Syria; such trading is banned for U.S. companies. New York City Comptroller William Thompson was quoted as saying that Halliburton and other companies appear to have violated the spirit of the law" through such commercial activities. On February 11, Halliburton said it had received an inquiry from the U.S. Treasury Department concerning its dealings with Iran.

Finally, I look forward to hearing from today's witnesses and hope they will address some of these issues. I ask unanimous consent to submit my statement into the record.

NOTES:

1. Sen. Frank Lautenberg press release on CRS report, Sept. 25, 2003. Lautenberg Releases CRS Report that Confirms that Cheney Deferred Salary and Stock Options Constitute a "Financial Interest in Halliburton

2. Peter W. Singer, Corporate Warriors; cited in "Contract Sport," by Jane Mayer, The New Yorker February 16-23, 2004. See also, washingtonpost.com: Halliburton's Deals Greater Than Thought

3. "Kuwait ponders probe of Halliburton, Associated Press, in Toronto Star, Feb. 9, 2004.

4. The French investigation has been widely reported. Here are a few stories: washingtonpost.com: French Judge Probes Unit of Halliburton Cheney Faces Indictment in France

5. On the British investigation, see News (I have full text version) and summary of the various investigations FORWARD : News

6. See Newsweek online, Feb. 4, 2004 MSNBC - Another Halliburton Probe and Newsday, Feb. 5 "Halliburton tied to Fed query." And see Halliburton 8-K filing , cited in footnote #7, at page 17.

7. See The Forward article cited above, also Halliburton 8-K filing, Feb. 6, 2004. e8vk, at page 19.

Congresswoman Jo Ann Davis
Opening Statement
Government Reform Hearing on Rebuilding Iraq
March 11, 2004

Mr. Chairman,

Thank you for holding this important hearing today. I am glad that the Committee is taking time to look into the situation in Iraq; it is important to our national security and to the future of Iraq to make sure the reconstruction is done well.

Getting Iraq's infrastructure back up and running is the key to that country's success. Without communications, water, electricity, and sewer systems, it would be impossible to have a stable Iraq. I have been encouraged at everything that has been accomplished so far.

I am looking forward to hearing more about how our reconstruction efforts in Iraq are going, and what we can do to help.

Our Armed Forces won a tremendous victory by conquering Saddam's regime. Now, they are proving just as impressive at rebuilding the country.

I do want to stress the fact that I think the rebuilding in Iraq should be done in the most efficient and effective way so that we spend the taxpayers' money wisely – especially during a time when we are facing such tight budget constraints here at home.

I want to thank the witnesses for being here today and thank you also for your commitment to serving our country. I look forward to hearing your testimonies.

Thank you again, Mr. Chairman, for looking into these important issues and holding this hearing.

Statement by Hon. Ileana Ros-Lehtinen submitted for the record
Hearing on "The Complex Task of Coordinating Contracts Amid Chaos: The Challenges of Rebuilding a Broken Iraq"

Mr. Chairman, I would like to take this opportunity to commend you on your leadership concerning the issue we are here to address.

Your most recent trip to Iraq to observe reconstruction efforts, demonstrates your commitment to the successful reconstruction of a free Iraq, after decades of destructive, corrupt rule by Saddam Hussein's regime.

Where Saddam's evil regime once built castles and torture chambers, we are now in the process of building schools, bridges and wastewater plants.

With over $20 billion in appropriated funds to build a new and democratic Iraq, I look forward to the testimony of our esteemed witnesses today from the United States Agency for International Development, the Army Material Command, the Army Corps of Engineers-- welcome Col Strock-- the Comptrollers Office, Program Management office and of course the Coalition Provisional Authority.

Welcome to you all and thank you for your service and dedication.

You are responsible for a difficult and complex, yet challenging and rewarding mission, trying to balance U.S. national interests with efficiency and budget considerations, helping to ensure a future of prosperity and growth for Iraq.

There are those who object to and criticize the decision by the Administration to, initially, afford only U.S. and 62 other eligible partner countries, the opportunity to compete for prime contracts.

I must ask these critics: if the U.S. and our coalition partners were the ones who liberated Iraq and continue to defend and protect the Iraqi people; to support them as they rebuild politically and economically, why should American companies and the people of our Districts throughout the U.S., not be given some preference,

initially, in competing to work with our new friends and partners, the Iraqi people.

During this transitional period, businesses from the U.S. and coalition nations, should not be asked to take a back seat to foreign companies and countries that continued their lucrative dealings with the brutal, oppressive regime of Saddam Hussein.

However, the concerns I wish to raise today focus on Iraqi projects being awarded to foreign companies that are heavily invested in such pariah states as Iran and Syria-regimes that are facilitating terrorist attacks against coalition forces and the Iraqi people, and that are repeatedly cited by the Department of State for their state-sponsorship of terrorism worldwide.

Under the Iran-Libya Sanctions Act, for example, these foreign companies are subject to U.S. sanctions.

Thus, I must ask: Are we taking such foreign policy factors into consideration? Who has the ultimate say on what companies are awarded contracts? What role do Iraqi ministries and entities, such as SOMO, have in selecting contracts?

What mechanisms are in place to monitor commercial interest in Iraq reconstruction to ensure that companies seeking contracts, do not have ties to individual terrorists, terrorist groups, or state-sponsors of terrorism?

I understand that the purpose of this hearing is to learn about each agency's involvement with the planning and management of Iraqi reconstruction and sustainment contracts, and how each agency's acquisition strategy is integrated into the acquisition programs from the other participating government entities.

However, I believe it is equally important to help ensure that terrorist regimes and those who serve to prop them up-as many countries did with Saddam Hussein's regime-do not benefit directly or indirectly.

I look forward to hearing from you all today. Especially my new friend, General Strock. General Strock and I had a great conversation last week about my dear Miami River dredging project. I look forward to hearing from you regarding my letter and, more importantly, hope that an RFP is granted for the project.

Thank you for all your hard work!

Thank you Mr. Chairman.

UNITED STATES AGENCY FOR INTERNATIONAL DEVELOPMENT

IRAQ RECONSTRUCTION AND HUMANITARIAN RELIEF

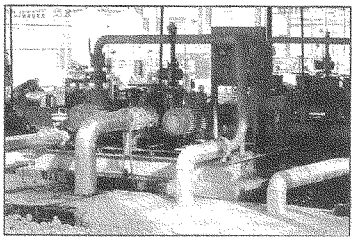
March 9, 2004
Weekly Update #22, Fiscal Year (FY) 2004

This fact sheet highlights overall accomplishments and some weekly activities from USAID's reconstruction efforts in Iraq. For more information on USAID's programs in Iraq please see: www.usaid.gov/iraq

USAID assists Iraqis in reconstructing their country by working within the Coalition Provisional Authority (CPA). USAID programs are implemented in coordination with the United Nations, World Bank, International Monetary Fund (IMF), Coalition country partners, nongovernmental organizations (NGOs), and private sector partners. The USAID Mission in Iraq carries out programs in education, health care, food security, infrastructure reconstruction, airport and seaport management, economic growth, community development, local governance, and transition initiatives.

The USAID Mission in Iraq implements programs in four strategic areas:

1. Restoring Essential Infrastructure
2. Supporting Essential Health and Education
3. Expanding Economic Opportunity
4. Improving Efficiency and Accountability of Government



Al Qudas power plant successfully started burning crude oil at Unit 1 on February 29. The unit is currently generating about 40 MW each day and is expected to be brought up to 100 MW this week. Conversion to crude oil will improve the plant's consistency, as crude oil is currently more abundant than the refined product.

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Program Descriptions and Updates

1. Restore Essential Infrastructure

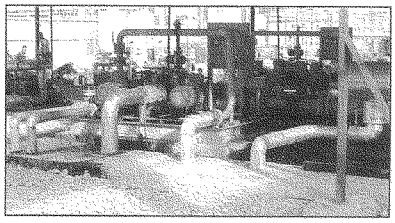
Electricity -- *Objectives include the emergency repair or rehabilitation of power generation facilities and electrical grids. Teams of engineers from the Ministry of Electricity, USAID, the U.S. Army Corps of Engineers, and the CPA have been working since May to restore capacity to Iraq's power system, which was dilapidated from decades of neglect, mismanagement, and looting.*

Accomplishments to Date:

- Generated 4,518 MW on October 6—surpassing the pre-war level of 4,400 MW. Average production over the last seven days was 3,978 MW. Production has increased as generators in scheduled maintenance come online and unscheduled outages decrease.
- Generated 98,917 MW hours on February 14—the highest since reconstruction began.
- Installed independent sources of power at Baghdad International Airport and Umm Qasr seaport.
- Collaborating with Bechtel, CPA, and Task Force Restore Iraqi Electricity on projects to repair thermal units, replace turbines, rehabilitate the transmission network, and install and restore generators.
  - Adding 907 MW of capacity by summer 2004 through maintenance and rehabilitation projects at nine gas turbine units and three diesel units.
  - Adding 1,636 MW of capacity by summer 2004 through new generation projects, including new gas turbine units being installed at 10 sites.
- Rehabilitating units 5 and 6 at Doura thermal power plant.
- Rehabilitating units 1, 2, 3, 4, and 6 of Bayji thermal power plant.
- Continuing reconstruction of the country's 400-kv transmission network by rebuilding 205 kilometers of Khor Az Zubayr-Nasiriyah 400-kv line.
- Installing new generating capacity at Kirkuk and South Baghdad power plants.

Highlights this Week:

- Al Qudas power plant successfully started burning crude oil at Unit 1 on February 29. The unit is currently generating about 40 MW and is expected to be brought up to 100 MW this week. Conversion to crude oil will improve the plant's consistency, as crude oil is currently more abundant than the refined product.
- USAID and Bechtel received a new 65 MW gas turbine power unit on February 25th at the site of a new power plant that will be started this July. The unit was trucked to the Kirkuk site from Turkey. The new power plant at Kirkuk will further the CPA's goal to bring average daily peak power to 6,000 MW by the summer.



Al Qudas power plant. crude oil transfer pump.

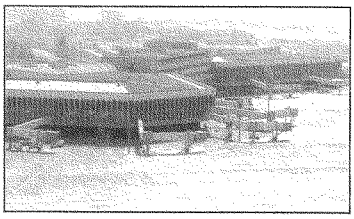
Airports -- *Objectives include: providing material and personnel for the timely repair of damaged airport facilities, rehabilitating airport terminals; facilitating humanitarian and commercial flights, and preparing the eventual handover of airport operations to the Iraqi Airport Commission Authority.*

Accomplishments to Date:

- Processing an average of 30 non-military arrivals and departures a day at Baghdad International Airport.
  - More than 5000 military and NGO flights have arrived and departed at Baghdad International Airport since July.
- Completed infrastructure work to prepare Baghdad International Airport for commercial air operations.
  - Repaired Terminal C and administration offices.

- Installed three X-ray machines.
- Installed very small aperture terminal (VSAT) communications systems and 6.5-MW power generators.
- Rehabilitated Iraqi customs office in the arrival hall.

- Substantially prepared Al Basrah International Airport for commercial operations. Ongoing projects include:
  - Repairing runway, taxiway, and apron striping.
  - Installing two baggage x-ray units.
  - Repairing passenger support facilities.
  - Installing VSAT satellite communications.
  - Installing security fence
  - Repairing airport water and sewage treatment plants.
- Completed evaluation of reconstruction requirements at Mosul Airport.



Baghdad International Airport Terminal was rehabilitated with support from USAID.

Bridges and Railroads -- *Objectives include: rehabilitating and repairing damaged transportation systems, especially the most economically critical networks.*

Accomplishments to Date:

Bridges:

- Demolished irreparable sections of three key bridges (Khazir, Tikrit, and Al Mat) and started reconstruction.
  - *Al Mat Bridge:* A key link on Highway 10 that carries over 3,000 trucks daily on the main route between Baghdad and Jordan.
    - Reopened the south span of the bridge for two-way traffic in mid-February. Complete repairs are expected in March 2004.
  - *Khazir Bridge*: Critical to the flow of fuel and agricultural products to the north.
    - Repaired the south span of the bridge and reopened it for two-way traffic on January 16. Complete repairs are expected by April 2004.
  - *Tikrit Bridge*: An important link for passengers and commerce over the Tigris River between Tikrit and Tuz Khurmatu.
    - On the upstream side of Pier 7, steel beams have been erected and dowels are installed. Work is expected to finish in May 2004.
- Repaired a floating bridge on the Tigris River in Al Kut, improving traffic for approximately 50,000 travelers a day.

Railroads:

- Iraqi Republican Railways (IRR) contributes equipment and labor, while USAID contributes project management, material, and parts. Work on the railways includes:
  - Repairing 16 km of track at the port of Umm Qasr and 56 km of track between the port and Shuiaba Junction near Basrah to facilitate cargo shipments including foodstocks from the seaport to mills.
  - Completed explosive ordinance disposal at all 53 sites of the rail line project near Shuiaba Junction (Al Basrah Governorate) in preparation for installation of new track.

Umm Qasr Seaport -- *Objectives include: managing port administration, coordinating transport from the seaport, and facilitating cargo-handling services such as warehousing, shipment tracking, and storage.*

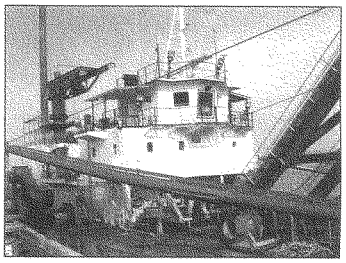
Accomplishments to Date:

- Reopened to commercial traffic June 17; completed first passenger vessel on July 16.
- Offloading cargo from more than 40 ships per month.

- Dredged the port to an average depth of 12.5 meters. Previously, the port was 9-10 meters deep, and limited cargo could arrive only during high tide. All 21 berths are now open to deep-draft ships.
  - An Iraqi dredger, which has been rehabilitated by USAID partner Bechtel, will assist in maintaining the harbor.
- Renovated grain-receiving facility, which can process up to 600 metric tons of grain an hour.
  - Over 200,000 tons of grain has been unloaded since the first bulk grain ship arrived in mid-November.
- Instituted interim port tariffs, which provide a revenue stream for financially sustainable port operations.
- Installed generators, energizing all three ring mains and restoring power to most parts of the port.
- Completed security fencing at the old and new ports and grain facility.
- Renovating the administration building, passenger terminal, customs hall building, and electrical substations.
- Employing 500 Iraqi staff, the majority of which are in the Marine Department of the Port Authority.

Highlights this Week:

- Restoration of the *Saif Saad* dredger is substantially complete and is expected to begin maintenance dredging at Umm Qasr port in early March. USAID partner Bechtel began rehabilitating the *Saif Saad* in August 2003. The 25-year-old dredger, which should go to dry dock for maintenance every two years, had not been used or maintained for more than ten years.



The Saif Saad Dredger after rehabilitation by USAID.

Telecommunications -- *Objectives include: installing switches to restore service to 240,000 telephone lines in Baghdad area; repairing the nation's fiber optic network from north of Mosul through Baghdad and Nasiriyah to Umm Qasr.*

Accomplishments to Date:

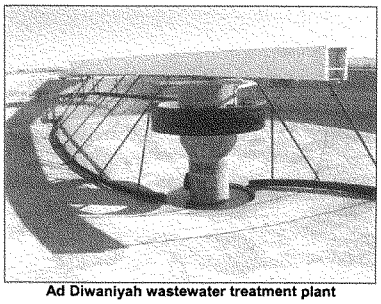
- Purchased tools, equipment, and parts to enable Iraqi engineers to restore the network.
  - Audited over 1,200 km of the fiber optic backbone network.
  - Repairing the national fiber optic network from Mosul to Umm Qasr, connecting 20 cities to Baghdad.
- Reconstituting Baghdad area phone service by installing switches with 240,000 lines of capacity. Installed new switches and main distribution frames at 12 sites and fully integrated them with the 14 existing switches. Over 190,000 individual subscriber lines have now been connected and 93,250 are active; work to allow final activation for all subscribers is underway.
    - Baghdad's largest exchange, Al Mamoun, opened on December 13.
  - The Ministry of Communications has brought in additional workers from outside Baghdad to expand the line-splicing workforce and accelerate progress.
- Completed installation of a satellite gateway system at Al Mamoun and restored international calling service to Iraq on December 30.
- Training Iraqi Telephone and Postal Company operators and engineers at Al Mamoun on telecommunications site operations, maintenance, and repairs.

Highlights this Week:

- In support of the CPA's objective to restore essential services, USAID officially handed over the Al Mamoun Telecommunications site to the Ministry of Communications on February 26. Twelve new telephone switches and an International Satellite Gateway have been integrated with fourteen Iraqi Telephone and Postal Company switches.

Water and Sanitation -- *Objectives include: rehabilitating and repairing essential water infrastructure to provide potable water and sanitation to communities and improve irrigation.*

Accomplishments to Date:


Ad Diwaniyah wastewater treatment plant

- *Nationwide:* Rehabilitating sewage treatment plants that are currently by-passing untreated sewage generated by millions of people into the Tigris and Euphrates Rivers.
  - Repairing and rehabilitating water systems throughout central and southern Iraq.
  - Repaired hundreds of critical breaks in Iraq's water network immediately after the war, significantly increasing water flow.
- *Baghdad*: Expanding one water plant and rehabilitating three sewage plants.
  - Rehabilitating and adding 45% capacity to Baghdad's Sharkh Dijlah water plant (previously named Saba Nissan water plant), adding an additional 225,000 cubic meters a day to the water supply by May 2004 mostly in the overpopulated eastern sections.
  - Installing back-up electrical generators at 39 Baghdad water facilities and pumping stations to ensure continuous water supply.
  - Rehabilitating Baghdad's sewage treatment plants—Rustimiyah North, Rustimiyah South, and Kerkh. The plants will be able to treat nearly 800 million liters of wastewater a day, benefiting 3.8 million people by October 2004.
  - Rehabilitated 70 of Baghdad's non-functioning waste pumping stations.
- *South Central:* Rehabilitating one water plant and four sewage plants.
  - Rehabilitating An Najaf municipal water treatment plant. The project will be completed by June 2004.
  - Rehabilitating Ad Diwaniyah and Karbala´ sewage treatment plants, which serve 200,000 residents and currently discharge untreated waste into the Euphrates River. These projects are expected to be completed by May 2004 and October 2004, respectively.
  - Rehabilitating An Najaf and Al Hillah sewage treatment plants to serve 194,000 residents. These projects are expected to be completed December 2004 and April 2004, respectively.
- *South:* Rehabilitating the entire Sweet Water Canal system, including the canal, its reservoirs, and 14 water treatment plants and pumping stations and the Safwan water system
  - The system provides drinking water to 1.75 million residents of Basrah City. It had been operating at less than half capacity.
  - Rehabilitated and removed 34,000 cubic meters of sand and silt from the west settling-reservoir of the Canal, allowing it to be refilled with clean water.
  - Began work on Sweet Water's 14 water treatment plants in January. By summer 2004, water quality and volume will surpass prewar levels.
  - Completed the restoration of the Safwan water system. All 40,000 residents now have access to potable drinking water.
- *North:* Rehabilitating two water plants and one solid waste collection system.
  - Constructing 400 solid waste collection points in Kirkuk (At Tamim Governorate) to improve sanitation.
  - Rehabilitating Mosul and Kirkuk water treatment facilities.

Highlights this Week:

- Civil engineering work at Al Hillah and Ad Diwaniyah wastewater treatment plants is complete. The civil work phase dealt with rehabilitating the entire plant except mechanical and electrical components. This

includes general site cleaning; site grading; cleaning of the process tanks, chambers, and connecting utility piping; structural restoration of site buildings; repair of concrete structures; and repair of structural steel and miscellaneous steel members.

2. Support Essential Health and Education

Health -- *Objectives include: supporting a reformed Iraqi Ministry of Health; delivering essential health services; funding medicines and supplemental nutrients; establishing a rapid referral and response system for the most serious cases; providing medical equipment and supplies; training and recruiting health staff; providing health education and information; and determining the specific needs of the health sector and of vulnerable populations such as women and children.*

Accomplishments to Date:

- Procured more than 30 million doses of vaccines since July with support from the Ministry of Health and UNICEF.
- Vaccinated three million children under the age of five through the Expanded Immunization Program since June. USAID will provide vaccines for a total of 4.2 million children under five and 700,000 pregnant women.
- Continuing a monthly immunization campaign with UNICEF and the Ministry of Health with 4,000 health workers and 124 supervisors.
- Awarding small grants to support Iraqi NGO healthcare efforts throughout Iraq.
- Developed a hospital and clinic facility database for the Ministry of Health on facility type, location, service distribution, cost information, and building condition.
- Renovated 52 primary health clinics and re-equipping over 600 to provide essential primary healthcare services including training staff in essential service delivery.
- Training more than 2,000 primary healthcare providers in maternal and child health services.
- Distributed high-protein supplementary food rations to more than 240,000 pregnant and nursing mothers and malnourished children.
- Evaluated 18 national and regional public health laboratories for equipment needs.
- Rehabilitated the National Polio Laboratory.
- Training more than 8,000 health workers to identify and treat acutely malnourished children.
- Working with the Iraqi Ministry of Health to develop a master plan to reduce child mortality and increase the level of preventative care available to the Iraqi people through assistance to their nine working groups which address: public health, health care delivery, health information systems, pharmaceuticals, medical supplies and equipment, health care finance, education and training, human resources, legislation and regulation, and licensing and accreditation.
- Working with the Ministry of Health to assist in the delegation of functions to other entities in the health sector such as NGOs, professional associations, community organizations, and businesses.

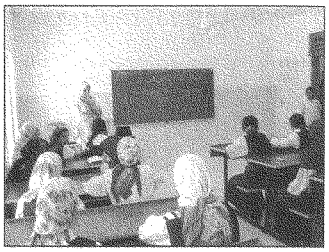
Highlights this Week:

- The renovation of the Central Blood Bank and Central Laboratory in Al Kut (Wasit Governorate) began in mid-January and is more than halfway complete. The Central Blood Bank is the only source providing blood to patients in Wasit Governorate.
- The Ministry of Health is finalizing plans to introduce a program to fortify wheat flour with iron and folic acid to reduce iron deficiency anemia and folic acid deficiency in women of childbearing age. This will help reduce neural tube birth defects and improve maternal and child health. This program is being supported by USAID in collaboration with the CPA.
- On February 22, the Iraqi Ministry of Health conducted a public health forum in Baghdad's Al Rassafa district. This is one of a series of forums providing information to the general public about the vision for health sector reform in Iraq. Surveys collected from forum participants will provide valuable information that will be used to shape reform strategy.

Education -- *Objectives include: increasing enrollment and improving the quality of primary and secondary education, ensuring that classrooms have sufficient materials, facilitating community involvement, training teachers, implementing accelerated learning programs, and establishing partnerships between U.S. and Iraqi colleges and universities.*

Accomplishments to Date:

- *Immediately After the Conflict*
  - Provided technical assistance for the resumption of the Ministry of Education functions.
  - Provided assistance for resumption of Ministry salaries.
  - Funded 5.5 million examinations for transitional grades, which ensured the smooth continuation of school.
  - Conducted a survey of secondary schools in all permissive areas in the country (3,300 schools total).
- *Facilities and Supplies*
  - Awarded 633 grants worth more than $6.1 million to rehabilitate schools and Directorates General.
  - Rehabilitated 2,339 schools countrywide for the first term of the 2003/04 school year.
  - Provided materials, equipment and supplies:
    - Distributed 1,495,283 secondary school kits that include pens, pencils, paper, math equipment, and other supplies.
    - Distributed 159,005 student desks, 26,437 teacher desks, 59,940 teacher chairs, 26,050 metal cabinets, 61,500 chalkboards and 58,500 teacher kits.
    - Delivered 808,000 primary student kits.
    - Delivered 81,735 primary teacher kits.
  - In consultation with the Iraqi Ministry of Education, reviewed 48 math and science textbooks for grades 1-12.
  - Printed and distributed 8,759,260 textbooks throughout Iraq.
- *Institutional Strengthening*
  - Trained 860 secondary school Master Trainers during September 2003-January 2004 nationwide.
  - Trained approximately 32,632 secondary school teachers and administration staff.
  - Conducting an accelerated learning program in Baghdad, Nasiriyah, Ad Diwaniyah, and Karbala'. An average of 600 students are participating in the program. In February, the students completed mid term exams.
- *Higher Education*
  - Returned the Fulbright Scholarship Program to Iraq after a 14-year absence. The program awarded at least 25 scholarships for Iraqis to study in the United States in 2004. USAID participated in the bi-national review committee for Iraq.
  - Launched Higher Education and Development Program. Awarded five grants worth an estimated $20.5 million for U.S.-Iraqi university partnerships:
    1) A consortium led by Research Foundation of the State University of New York at Stony Brook partnering with Baghdad University, Al Mustansiriyah University/Baghdad, and Mosul University in archeology and environmental research.
    2) The University of Hawaii College of Agriculture and Human Resources partnering with the University of Mosul Hamam Al-Alil for strengthening academic, research, and extension programs.
    3) The Human Rights Institute at DePaul University College of Law and the International Institute of Higher Studies in Criminal Sciences (Italy) partnering with University of Baghdad to reform legal education.



Girls studying in newly rehabilitated Rafah Secondary School for Girls. Photo: USAID

4) Jackson State University partnering with University of Mosul for public health and sanitation.
5) The University of Oklahoma partnering with Al Anbar University, Basrah University, and the University of Salah ad Din in higher education initiatives.

Highlights this Week:

- More than 8.7 million textbooks have been printed and distributed through USAID's Education Program in collaboration with UNESCO. Through this effort, 48 primary and secondary math and science textbook titles were reviewed and edited.
- More than 32,000 teachers have been trained in new school management and classroom teaching methods through a nationwide teacher education program, which concluded on February 16. The program began in autumn 2003 with 860 master trainers—57 in September and 803 in November. Selected graduates of the program conducted the nation-wide training in February 2004.

3. Expand Economic Opportunity

Economic Growth -- *Objectives include: currency conversion and development of economic statistics, small businesses credits, commercial legislation, a national employment program, micro-finance programs, a bank-to-bank payment system, a computerized financial management information system, tax policy and administration, budget planning, insurance ,telecommunications reform and electricity reform.*

Accomplishments to Date:

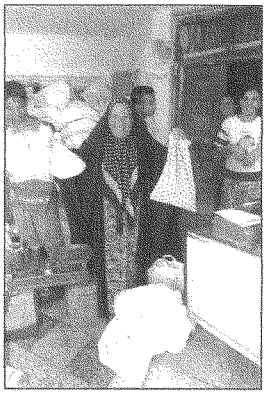
- Worked with the Ministry of Finance to introduce the new national currency.
  - The currency exchange began on October 15 and was completed on January 15.
  - All of the 6.36 trillion new Iraqi dinars are now in country, and 4.62 trillion Iraqi dinars are in circulation—106 percent of the original demand estimate of 4.36 trillion.
  - The overall management plan for the currency exchange operation was developed by BearingPoint, including security and logistics.
- Conducting a daily currency auction for banks to exchange dinars and dollars.
- Created more than 77,000 public works jobs through the National Employment Program.
- Provided technical assistance on the implementation of a bank-to-bank payment system that allows 80 banks to send and receive payment instructions.
- Assisted in developing, installing, and training staff to use the Financial Management Information System, a new accounting and reporting system that will eventually be used by all Iraqi treasury offices and ministries.
- Assisting CPA in managing a $21-million microcredit program.
- Supporting CPA's Oil for Food (OFF) Program in planning, program management, logistics, database applications, and communications to support the CPA OFF Coordination Center in the north and south.
- Evaluating and updating commercial laws pertaining to private sector and foreign investment; assisted in the development of the new Company Law.

Highlights this Week:

- USAID's Agriculture Reconstruction and Development Program for Iraq (ARDI) technical assistance team visited two Ministry of Agriculture organizations--the Agricultural Supplies Company (ASC) and the Veterinary Services Company (VSC) to explore increasing private sector participation in those activities.
- Administrator Paul Bremer signed CPA Order 54 this week, which imposes a 5 percent reconstruction levy on imports beginning April 1, 2004. USAID partner BearingPoint assisted in developing the reconstruction levy in collaboration with the Coalition Provisional Authority and the United Kingdom Customs Service. Since the levy was proposed in September 2003, USAID, BearingPoint, and the CPA have been working to train importers and businesses; customs and tax commissioners; border enforcement

officials; officials from the Ministries of Finance, Planning, and Foreign Affairs; and Central Bank officials.

Food Security -- *Objectives include: providing oversight support for the countrywide public distribution system, which provides basic food and non-food commodities to an estimated 25 million Iraqis; participating in the design of a monetary assistance program to replace the commodity-based distribution system to support local production and free-market infrastructure; and promoting comprehensive agriculture reform to optimize private participation in production and wholesale markets.*



Ration distribution through Iraq's Public Distribution System

Accomplishments to Date:

- Worked with the U.N. World Food Program (WFP) and Coalition Forces to re-establish Iraq's public distribution system in less than 30 days, avoiding a humanitarian food crisis and maintaining food security.
- Contributed cash and food aid in the amount of $425 million to WFP's emergency operations immediately following the conflict, making the U.S. the foremost contributor to WFP emergency operations in Iraq.
- Placed food specialists in Baghdad, Al Basrah, Al Hillah, and Arbil to support food operations immediately after the conflict.
- Provided ongoing support and technical assistance to WFP and local Iraqi authorities in the Ministry of Trade and the Kurdish Food Departments to ensure the smooth transition of public distribution system management tasks to the Iraqi government. Special attention was given to the transition phase in the northern governorates of Dahuk, Sulaymaniyah, and Arbil. The initial handover of responsibilities occurred on November 21 without significant problems.
- Played a role in negotiating a memorandum of understanding between the CPA, the Ministry of Trade, and the World Food Program that details WFP's areas of responsibility to include: capacity building and training, procurement of food commodities, the renegotiation of certain food contracts, shipment and overland transport of food commodities, and pipeline management. The World Food Program will continue to assist with supporting the public distribution system through June 2004 and will begin work immediately to assure continuation of food deliveries.
- Currently providing food aid expertise to CPA and Ministry of Trade in Baghdad and assisting with the CPA OFF Coordination Center as WFP and CPA and the Ministry continue to distribute food to all Iraqis.

Agriculture – *Objectives include: expanding agricultural productivity, restoring the capacity of agroenterprises to produce, process and market agricultural goods and services, nurturing access to rural financial services and improving land and water resource management.*

Accomplishments to Date:

Since October, USAID partner DAI has been implementing the Agricultural Reconstruction and Development Program for Iraq (ARDI) to formulate a long-term vision for the sector, while designing activities for quick impact, including:

- *Winter Crop Technology Demonstrations:* On 334 hectares in 15 governorates, 128 farm families are establishing plots with new crop varieties for extension field days.

Crops planted using conventional farming methods.

- *Kirkuk Veterinary Hospital Renovation:* Fifty communities will benefit from a $96,000 grant to renovate a hospital that serves more than 100,000 livestock in the area.
- *Taza and Rashad Veterinary Clinic Rehabilitation:* A $50,000 grant will be matched by supplies and equipment from the Ministry of Agriculture. These rural clinics are the two principal sources of vaccines and medicines for animals in 125 local communities.
- *Internet Connectivity and Repairs to a Student Union Building:* The Baghdad University School of Agriculture will receive a $75,000 grant that will benefit 4,509 students.
- Seven grants, totaling $394,000, were approved February 23 to build the capacity of Iraq's agriculture sector. The emphasis on veterinary programs allows an immediate, highly visible response to the challenges that face herders and farmers in the North and Central Regions.

Highlights this Week:

- In an effort to increase Iraq's economic production, 128 farm families are participating in ARDI's Winter Crop Technology Demonstration Program, which demonstrates new methods of cultivation to increase crop yields. The program supports USAID's goal to generate both income and employment by improving agricultural productivity.
- Under the direction of the Zakhu Agricultural Director, six villages in the vicinity of the city of Zakhu (Dahuk Governorate) will receive a sheep dipping tank with the assistance of a grant from USAID. Sheep dipping is used to keep animals clean of scabs, blowflies, ticks, keds, and lice, which damage the valuable wool and skin of the sheep.

Crops planted using new technologies recommended by the Crop Technology Demonstration Program.

Marshlands – *Objectives include: construct environmental, social and economic baselines for the remaining and former marshlands; assist marsh dwellers by creating economic opportunities and viable social institutions; improve the management of marshlands and expand restoration activities*

Program Goals:

- The $4-million Marshland Restoration and Management Program will promote wetlands restoration and provide social and economic assistance to marsh dwellers. Initiatives include:
  - Creating a hydraulic model of the marshes to improve water management.
  - Equipping a soil and water quality lab at the new Center for Iraq Marshlands Restoration.
  - Implementing pilot projects to improve treatment of waste and drinking water.
  - Providing social economic assistance through job- and income-generating activities in fisheries, aquaculture, livestock production, and date-palm reproduction.
  - Monitoring water quality in reflooded sites.
  - Extending healthcare services to marsh dwellers.
  - Building local capacity by partnering with Iraqi institutions such as the Ministry of Water Resources, the Ministry of the Environment, the University of Basrah College of Agriculture, the AMAR Charitable Trust, and the Iraq Foundation, and the governments of Canada, Italy, the United Kingdom, and Australia.

4. Improve Efficiency and Accountability of Government

Local Governance -- *Objectives include: promoting diverse and representative citizen participation in provincial, municipal and local councils; strengthening the management skills of city and provincial administrations, local interim representative bodies, and civic institutions to improve the delivery of essential*

municipal services; promoting effective advocacy and participation of civil society organizations; enhancing leadership skills; and serving as a recruiting tool for future leaders.

Accomplishments to Date:

- Implementing local governance activities in 18 governorates. More than 20 million Iraqis are engaging in local policy discourse through local government entities and civil society organizations to:
  - Enhance transparency and participation in local decision-making processes.
  - Restore basic services.
  - Improve the effectiveness and efficiency of local service delivery.
  - Establish, develop, and expand the number of civil society organizations that can interact with local government entities.
- Established 16 governorate councils, 66 district councils, 157 city and sub-district councils and 293 neighborhood councils.
- Awarded $13.4 million to local government agencies and civil society organizations to strengthen the capacity of municipal authorities to deliver core municipal services.
- Established the Iraqi Women in Local Governance Group in response to the challenge of women's gross under-representation in political processes across Iraq. The group will develop and guide program activities in order to expand women's participation at all levels.
- By working with local governance service departments to plan, budget, and manage their resources, and providing training on transparency and accountability in the use of those resources, the local governance team's assistance to officials in Dhi Qar resulted in more efficient delivery of public services to over 390,000 residents.
- Employed 868 Iraqi workers, of which more than half are senior and mid-level professionals.
- A civic education task force is implementing a nationwide campaign to educate Iraqis on democracy. The Civic Education Campaign conducts a range of activities including convening focus groups and town hall meetings and assisting in distribution of hand bills and posters.

Highlights this Week:

- The Maysan Woman's Conference on the Role of Women in Iraqi Society convened on February 18 in Al Amarah. Speakers included representatives from the Maysan Governorate Council, USAID's Local Governance Program and the Coalition Provisional Authority. Topics of discussion included the economic, social and political roles currently played by women and methods of increasing women's participation in Iraq's public life.
- USAID's is building the capacity of community NGOs in the city of Halabja, As Sulaymaniyah Governorate. The Kurdish city suffered greatly under Saddam Hussein's regime. In 1988, the Iraqi army bombed the city with chemical weapons, killing an estimated 12,000 people, 75% of whom were women and children; the region has never fully recovered.
- Al Basrah city government, USAID, and the local community are rehabilitating a city-owned slaughterhouse to supply wholesome meat to the city. The slaughterhouse is a significant health hazard in the community and was identified by the local government as a priority to improve public health.
- The Organization for the Defense of Farmer's Rights, a civil society organization in Diyala' Governorate with more than 60 members, will rehabilitate its building under a grant awarded by USAID's Local Governance Program on February 28. This project will assist the new organization in advocating for the improvement of government service delivery and improving its government partnerships for agricultural extension and educational services.
- The Local Governance Program is working in primary schools to instruct and gauge student understanding of basic democratic concepts.
- The Local Governance Program in Al Basrah is working with Iraqis to encourage the discussion of democracy issues. Specifically, they are providing training to Democracy Dialogue Activity facilitators who will further disseminate the democracy message to high school teachers and students, university students, and NGOs.

Transition Initiatives – *Objectives include: building and sustaining Iraqi confidence in the transition to a participatory, stable, and democratic Iraq. Working closely with the CPA, USAID's Iraq Transition Initiative assists Iraqi NGOs, national government institutions, and local governments to increase Iraqi support for the transition to sovereignty through quick-dispersing, high impact small grants.*

Accomplishments to Date:

- Awarded 645 small grants totaling more than $43 million for quick impact activities that support good governance, civil society, conflict management and mitigation, and human rights and transitional justice.
- Supporting initiatives crucial to the democratic transition, including civic education, civil society and media development, increased women's participation, conflict mitigation, and transitional justice. Groups targeted for assistance include women's and youth groups, professional associations, and human rights organizations.
- Met critical needs during the early transition period, by providing short-term employment, restoring basic government and community services, increasing Iraqi access to information and communication, and encouraging protection of human rights.
- Awarded two grants worth $475,000 to the Ministry of Human Rights for the rehabilitation of buildings to house the National Evidence Storage Facility (NESF). The NESF will serve as a venue to analyze recovered documents and store forensic evidence of mass graves and human rights abuses of the Ba'ath government. The facility is part of a larger effort to help build Iraq's capacity to investigate complex crimes and implement international law enforcement best practices.

Highlights this Week:

- The Kurdistan Civil Rights Organization has completed a series of 120 lectures for human rights activist training in northern Iraq's Dahuk Governorate under a grant from USAID.
- Six new grants were awarded to rehabilitate schools in the city of Balad, located in the highly conflictive area northwest of Baghdad in Salah ad Din Governorate. Repairing these schools will provide the children of Balad with a safe learning environment and demonstrate the benefits of a peaceful transition to the community. The grants, totaling $550,000, were awarded through USAID's Iraq Transition Initiative (ITI). quick impact grant program.
- USAID's Iraq Tranistion Initaive (ITI) is building the capacity of community NGOs in the city of Halabja, As Sulaymaniyah Governorate. The Kurdish city suffered greatly under Saddam Hussein's regime. Recent work in Halabja has included:
    - The Halabja Youth Freedom Organization received the first delivery of equipment, furniture and supplies under a USAID grant. This organization reaches out to youth by offering sports programs, music, computer, sewing, art and other classes.
    - The WADI Association for Crisis Assistance and Development Cooperation has established the area's first women's center. A USAID grant supplied furniture and equipment for the center, as well as training courses. The courses give women information on a variety of important issues, such as human rights; violence against women and the law; computer and literacy classes; and health and nutritional information.

Community Action Program -- *Objectives include promoting diverse, representative citizen participation in and among communities to identify, prioritize, and satisfy critical community needs, while utilizing local resources. CAP is implemented by five U.S. NGOs with offices in nine major Iraqi cities. Each concentrates on one region in Iraq: ACDI/VOCA (North), International Relief and Development--IRD (Baghdad), Cooperative Housing Foundation International--CHF (Southwest Central), Mercy Corps (Southeast Central), and Save the Children (South).*

Accomplishments to Date:

- Established over 600 Community Action Groups in 16 governorates. The projects undertaken by the Community Action Groups are part of a campaign targeting grassroots democratic development.
- CAP has committed $44.8 million for 1,317 community projects across Iraq; 666 projects have already been completed.
- Iraqi communities have contributed nearly $13 million to community projects. Contributions have included labor, land, buildings, and other in-kind assistance.
- Five U.S. NGOs each concentrate on a region: ACDI/VOCA (North), IRD (Baghdad), CHF (Southwest Central), Mercy Corps (Southeast Central), and Save the Children (South).
  - ACDI/VOCA focuses on the conflict prone areas of Mosul, Kirkuk, the area northwest of Baghdad, and the Iran-Iraq border. Their work bringing communities together has resulted in 126 completed projects and another 136 are in development. These include establishing a youth center in Huwija and establishing a new local water supply in Tikrit.
  - CHF has established a strong presence in the communities of the Shi'a holy cities of Najaf and Karbala, as well as Hillah by establishing very active community associations. An emphasis on critical infrastructure has provided these communities with access roads, sewage and water rehabilitation, school repairs, and swamp clean-up in addition to vital social infrastructure such as community centers and sports clubs. They have completed 82 projects.
  - IRD has completed 186 projects with a special emphasis on income generation. A marketplace that will serve 250,000 residents is being constructed, and crews are cleaning up medical waste dumps and educating medical personnel on proper disposal methods.
  - Mercy Corps has completed 54 projects and has 102 more in development. These projects focus on water, sewage, community clean-up, and school rehabilitation.
  - Save the Children has completed 239 projects through community action groups in the south, which include about 40 percent female membership. Projects have focused primarily on immediate community needs such as sewage clean up, water treatment and distribution, public health, and girls' access to education.

Highlights this Week:

- USAID provides assistance to Iraq's disabled citizens by developing social programs and rehabilitating facilities to meet the needs of the disabled. In this capacity, CAP is working on 13 projects nation-wide through its five U.S. NGO partners to improve the lives of Iraq's disabled citizens. These projects have provided assistance to associations for the handicapped and blind and physical therapy centers.

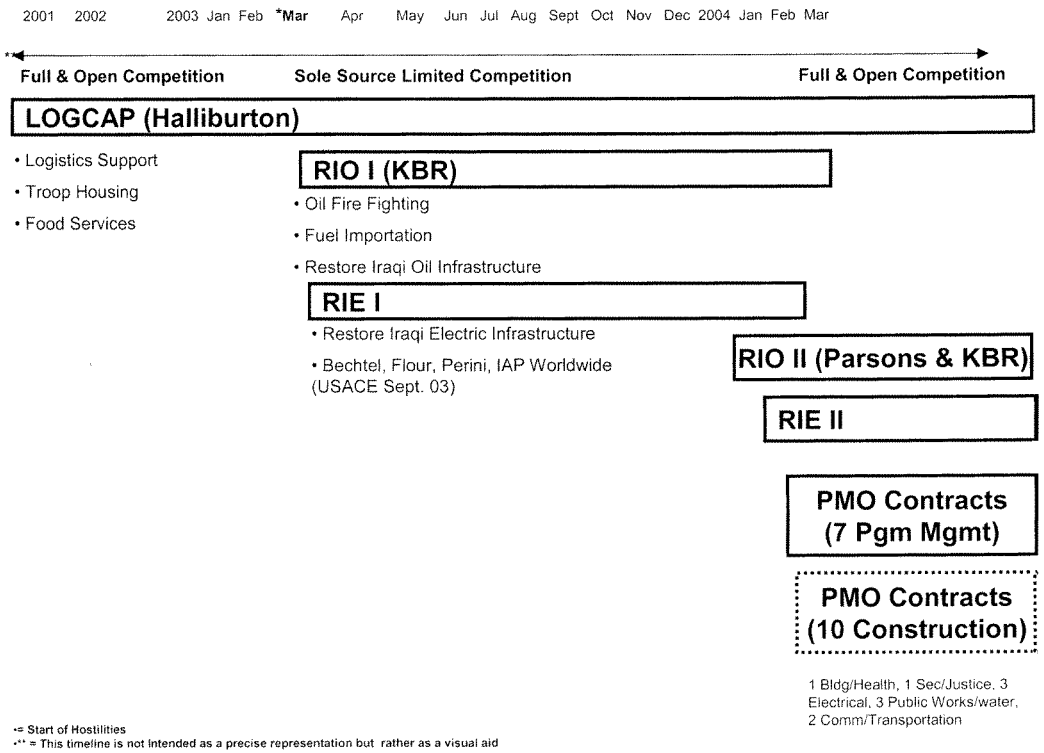
Agency	*Implementing Partner*	*Sector*	*Regions*	*Amount*
		FY 2003-2004*		
		RECONSTRUCTION		
USAID/ANE			**Subtotal:**	**$1,921,112,060**
	Abt Associates	Health	Countrywide	$20,995,000
	AFCAP	Logistics	Countrywide	$91,500,000
	Army Corps of Engineers	Architecture and Engineering services	Countrywide	$16,500,000
	BearingPoint	Economic Governance	Countrywide	$47,500,000
	Bechtel National	Airports, buildings, emergency communications, power, railroads, roads and bridges, Umm Qasr seaport, water and sanitation	Countrywide	$1,029,833,859
	Bechtel National	Infrastructure II: Airports, buildings, emergency communications, power, railroads, roads and bridges, Umm Qasr seaport, water and sanitation	Countrywide	$252,911,400
	Community Action	Development in impoverished	Countrywide	$70,000,000

	Program	communities		
	DAI	Marshlands	Countrywide	$4,000,000
	DAI	Agriculture	Countrywide	$5,000,000
	Fed Source	Personnel Support	Countrywide	$163,572
	IRG	Reconstruction Support	Countrywide	$29,087,094
	RTI	Local Governance	Countrywide	$155,611,000
	CAII	Education	Countrywide	$56,503,000
	UNICEF	Health, Water, and Sanitation	Countrywide	$36,700,000
	UNICEF	Education	Countrywide	$7,000,000
	UNESCO	Textbook Printing and Distribution: Math and Science	Countrywide	$10,000,000
	WHO	Strengthen Health System	Countrywide	$10,000,000
	SSA	Port Management	Umm Qasr	$14,318,985
	SkyLink	Airport Management	Baghdad Al Basrah Mosul	$27,200,000
	MSI	Monitoring and Evaluation	Countrywide	$5,500,000
	University Partners	Consortium led by the Research Foundation of the State University of New York (SUNY) at Stony Brook which includes Columbia University, Boston University and Oxford University (England), University of Hawaii, DePaul University College of Law and the International Institute of Higher Studies in Criminal Sciences in Siracusa, Italy; and Jackson State University and the Mississippi Consortium for International Development; and Oklahoma State University.	Baghdad University, Al Mustansiriyah University in Baghdad, Mosul University, Mosul University's College of Agriculture and Forestry in Hamam al-Alil, Basrah University, Al-Anbar University, and University of Salahaddin.	$20,730,000
	Yankee Group	Telecoms Planning	Countrywide	$58,150
	UNDP	Trust Fund Contribution	Countrywide	$5,000,000
	World Bank	Trust Fund Contribution	Countrywide	$5,000,000
		EMERGENCY RELIEF		
USAID/DCHA/OFDA				**$86,898,040**
	Administrative	Administrative Costs	Countrywide	$6,838,947
	AirServ	Logistics	Countrywide	$5,309,876
	ARC	Capacity building, Disaster support	Al Basrah	$537,746
	The Cuny Center	Research studies	Countrywide	$40,260
	GOAL	Coordination, Nutrition	Al Muthanna'	$1,507,900
	International Dispensary Association	Health	Countrywide	$1,284,972
	InterAction	Coordination	Kuwait City	$92,860
	IOM	IDP programs	Countrywide	$5,000,000

	Logistics	Commodities and DART support	Countrywide	$12,005,804
	UNICEF	Health, nutrition, water/sanitation	Countrywide	$4,000,000
	UN OCHA	Coordination and Information	Countrywide	$1,200,000
	USAID Amman	Support for emergency water activities	Countrywide	$500,000
	WFP	Logistics and pre-positioning of food	Countrywide	$5,000,000
	IMC	Food Security, Health, Nutrition, Water/Sanitation, Capacity building	Countrywide	$10,702,900
	IRC	Health, Water/Sanitation	Countrywide	$4,998,685
	Mercy Corps	Health, Non-Food Items, Shelter, Water/Sanitation	Countrywide	$7,000,000
	SCF/US	Food Security, Health, Shelter, Nutrition, Non-Food Items, Water/Sanitation, NGO Consortium	Countrywide	$6,883,131
	World Vision	Health, Logistics, Non-Food Items, Water/Sanitation	Countrywide	$4,994,959
	CARE	Quick-impact projects, Water/Sanitation, Health, Blankets	Countrywide	$9,000,000
USAID/DCHA/FFP				**$425,571,000**
	WFP	Operations	Countrywide	$45,000,000
	WFP	Emerson Trust – 81,500 MT	Countrywide	$40,337,000
	WFP	P.L. 480 Title II emergency food commodities – 163,820 MT	Countrywide	$140,234,000
	WFP	Regional Purchase – 330,000 MT	Countrywide	$200,000,000
USAID/DCHA/OTI				**$104,269,938**
	Administrative	Administrative Costs	Countrywide	$2,976,668
	IOM	Iraq Transition Initiative	Countrywide	$10,587,595
	DAI	Iraq Transition Initiative	Countrywide	$80,000,000
	Internews	Media	Countrywide	$160,359
	Radio SAWA	Media	Countrywide	$400,000
	NDI/IRI	National Governance	Countrywide	$400,000
	IFES	National Governance	Countrywide	$1,042,315
	Spa War**	Inter-Ministry Communications	Countrywide	$8,703,001
TOTAL USAID ASSISTANCE TO IRAQ IN FY 2003/2004				**$2,537,851,038**

* Figures in funding sheet are subject to change and do not represent a final official accounting of USG obligations.

** For accounting purposes, funding for this activity has been obligated by OFDA under an existing interagency agreement.


2001 2002 2003 Jan Feb *Mar Apr May Jun Jul Aug Sept Oct Nov Dec 2004 Jan Feb Mar
Full & Open Competition
Sole Source Limited Competition
Full & Open Competition
LOGCAP (Halliburton)
• Logistics Support
• Troop Housing
• Food Services
RIO I (KBR)
• Oil Fire Fighting
• Fuel Importation
• Restore Iraqi Oil Infrastructure
RIE I
• Restore Iraqi Electric Infrastructure
• Bechtel, Flour, Perini, IAP Worldwide (USACE Sept. 03)
RIO II (Parsons & KBR)
RIE II
PMO Contracts (7 Pgm Mgmt)
PMO Contracts (10 Construction)
1 Bldg/Health, 1 Sec/Justice, 3 Electrical, 3 Public Works/water, 2 Comm/Transportation
*= Start of Hostilities
*** = This timeline is not intended as a precise representation but rather as a visual aid

CHARRTS No.: HG-01-001
House Government Reform Committee
Hearing Date: March 11, 2004
Subject: The Complex Task of Coordinating Contracts Amid Chaos, the Challenges of Rebuilding a Broken Iraq
Congressman: Congressman Waxman
Witness: HON Zakheim
Question: #1

Question: Dr. Zakheim, how do Congress and the American people know exactly how much revenue from the sale of Iraqi crude oil is being collected and placed in the Development Fund for Iraq?

Answer: Revenues from sales of oil are deposited into the Development Fund for Iraq (DFI) pursuant to UN resolution 1483, which was strongly supported by the United States Government. At the behest of the CPA, the U.S. Federal Reserve Bank of New York (FRBNY) established the "Central Bank of Iraq-Development Fund for Iraq" account. The DFI is held on the books of the Central Bank of Iraq. The corpus of the DFI is held in the account at FRBNY for the Central Bank of Iraq. A portion of the fund has been transferred to Baghdad, Iraq and used to establish a DFI-Baghdad account at the Central Bank of Iraq, for the purpose of meeting cash payment requirements in country, for the benefit of the Iraqi people.

We have a strong incentive to insure that the sole beneficiary of sales of Iraqi oil is the Iraqi people. Oil revenues are a matter of public record and the Coalition Provisional Authority (CPA), working with the Iraqi Oil Minister, publishes the deposits and disbursements of oil revenue on the CPA website in accordance with Section 2215 of the Fiscal Year 2004 Emergency Supplemental Appropriations Act (Public Law 108-106).

We helped establish the International Advisory and Monitoring Board (IAMB) to insure that all funds in the DFI are used for the benefit of the Iraqi people. After years of corrupt practices by the previous regime in Iraq, it is time for oil proceeds to be used for the benefit of all Iraqis, not just a select few.

CHARRTS No.: HG-01-002
House Government Reform Committee
Hearing Date: March 11, 2004
Subject: The Complex Task of Coordinating Contracts Amid Chaos, the Challenges of Rebuilding a Broken Iraq
Congressman: Congressman Waxman
Witness: HON Zakheim
Question: #2

Question: Is there some sort of reporting requirement on CPA for the disclosure of precise revenue data?

Answer: In accordance with Section 2215 of the Fiscal Year 2004 Emergency Supplemental Appropriations Act (Public Law 108-106), the Coalition Provisional Authority is required to submit monthly reports regarding Iraqi crude oil production, oil revenues, and the use of those revenues.

CHARRTS No.: HG-01-003
House Government Reform Committee
Hearing Date: March 11, 2004
Subject: The Complex Task of Coordinating Contracts Amid Chaos, the Challenges of Rebuilding a Broken Iraq
Congressman: Congressman Waxman
Witness: HON Zakheim
Question: #3

Question: The descriptions of expenditures from the DFI have been very broad and vague to date. I understand more than a billion dollars has been spent on fuel imports. How have the remaining billions been spent? Can you provide a detailed breakdown of DFI expenditures?

Answer: The CPA IG report, dated March 30, 2004 includes a detailed list of sources and uses of DFI in Appendix F (attachment 1).

Details on estimated DFI revenue and expenditures in the 2004 Iraqi Budget are in appendix 1, Tables 4 through 10 (attachment 2). This appendix was also included in the quarterly report required by Section 2207 of the Emergency Appropriations Act for Defense and for the Reconstruction of Iraq and Afghanistan, FY 2004.

Appendix F - Development Fund for Iraq

This appendix outlines the sources and uses of Development Fund for Iraq (DFI) funds as of February 29, 2004.

The CPA-IG has not formally reviewed or audited the data.

ATTACHMENT 1

Development Fund for Iraq

The DFI will be audited by an independent public accounting firm selected by the International Advisory and Monitoring Board (IAMB). The IAMB consists of representatives of the International Monetary Fund, U.N., World Bank, and the Arab Fund for Economic and Social Development. The DFI's primary source of funds is the oil revenues of Iraq. While 95% of oil revenues go to the DFI, 5% is deposited in the Compensation Fund created by U.N. Resolution 687 (1991).

Development Fund For Iraq as of March 1, 2004		
Sources Amount Percentage		
U.N. Food Programs (Repatriation)	$5,912,364,574	44.63%
U.N. 1483 Repatriated Funds (See Table F-2)	751,095,285	5.67%
Deposits – Vested NY	15,310,389	0.12%
Oil Proceeds	5,986,010,312	45.18%
Collections Baghdad	536,861,843	4.05%
Investments, Other Deposits	46,422,989	0.35%
Sub-total – Sources – DFI	**$13,248,065,392**	
Uses Amount Percentage		
Electricity Infrastructure	$75,326,236	1.55%
Oil Infrastructure	409,521,678	8.40%
Oil For Food	663,660,270	13.62%
CERP And Regional Response Programs	349,673,925	7.18%
Currency Exchange Program	163,853,913	3.36%
Ministry Of Finance Budget	2,633,837,658	54.05%
Other Ministry Operations	6,266,124	0.13%
Infrastructure	38,545,234	0.79%
Misc.	62,582,392	1.28%
Letters Of Credit	469,890,251	9.64%
Sub-total – Uses – DFI	**$4,873,157,681**	

Table F-1: Sources and Uses of Funds for the Development Fund for Iraq. Data not formally reviewed or audited.

ATTACHMENT 1

Appendix 1
2004 Iraqi Budget

RESOURCES

Projected resources available for 2004 are expected to be $20096.9 million. This amount consists of opening financial capital (the opening balance of the Development Fund for Iraq), net capital inflows, plus revenues (primarily oil).

Table 1 - Total Resources	$ millions
Opening financial capital (1 Jan 2004)	5,410.8
plus Net Capital Inflows	200.0
plus Revenues	14,486.1
TOTAL RESOURCES	**20,096.9**

Opening Balance

On December 31st 2003 there was $ 5410.8 million remaining in the DFI account.

Projected net capital inflows for 2004

Net capital inflows are projected to be US$ 200 m. These consist to date of transfers of Iraqi assets from Jordan.

Table 2 - Capital inflows	$ millions
Capital Flows in	
Transfer of Iraqi assets from abroad	200.0
Less Capital Outflows	0.0
TOTAL NET CAPITAL INFLOWS	**200.0**

Projected revenues in 2004

Projected revenues for 2004 total US$ 14486.1 m. These revenues will come primarily from oil exports. A proposed Civil Service Pension Contribution and Reconstruction Levy to be implemented in April 2004 will also contribute to total revenues.

Oil revenues are estimated using a prudent assumption of a gradual fall in net oil prices from a high of $26 per barrel in January to $21 per barrel in June. Oil exports are assumed to reach 1.9 million barrels per day by the end of the year. If oil prices rise significantly or exports are greater than expected then there could be a very notable increase in net revenues - but for budgeting purposes CPA took a more cautious approach.

Table 3 - Revenues	$ millions
Oil Revenues	14,175.3
Interest Income	10.0
Reconstruction Levy	115.0
Personal Income Tax	5.0
Civil Service Pension Contribution	67.6
User Pay Charges	64.2
Other Taxes and Charges	49.0
TOTAL REVENUES*	**14,486.1**

ATTACHMENT 2

EXPENDITURES

Total Expenditures in 2004 are projected to be $ 19926.5 million.

Table 4 - Total expenditures	$ millions
Total Staff Expenditure	2,586.3
Total Operating Expenditure	1,974.5
Total Ministry Capital Projects	2,531.7
Total Transferred Expenditures	10,588.5
Total Foreign Obligations	1,448.6
Total Salaries and Retirement Rewards	797.0
TOTAL EXPENDITURES	**19,926.5**

Staff Expenditures

Table 5 - Staff expenditures	$ millions
Ministry Salaries (including reserve for new salary scale)	1,867.1
Centrally Funded Salaries	465.0
Hazardous Duty Pay	150.0
Facility Protection Service Guards	60.4
Iraqi Civil Defence Force Pay	43.8
TOTAL STAFF EXPENDITURES	**2,586.3**

Non-staff Operating Expenditures

Table 6 - Operating costs	$ millions
Normal Ministry Operating Expenditure	1,221.4
Railroad Security	*50.0*
Pharmaceuticals	*578.0*
TOTAL OPERATING COSTS*	**1,974.5**

**Listing does not include all line items, hence columns will not necessarily sum up to total operating costs.*

Ministry Capital Projects

Spending on capital projects by ministries is projected to be US$ 2531.7 m. This includes investments in infrastructure projects not included in the US Supplemental Appropriation.

Table 7 - Ministry capital projects	$ millions
Electricity Projects	900.0
Transportation Projects	150.0
Education Projects	150.0
Telecommunications Projects	130.0
Housing Projects	100.0
Oil Projects	200.0
TOTAL MINISTRY CAPITAL PROJECTS*	**2,531.7**

**Listing does not include all line items, hence columns will not necessarily sum up to total capital investment.*

ATTACHMENT 2

Transferred Expenditures

Projected transferred expenditures for 2004 are US$ 10588.5 m.

Transferred expenditures includes spending for national programs or items that will benefit the nation as a whole. The major spending items include the Public Distribution System, fuel imports, grants to regions, state owned enterprise support, additional security spending and agricultural subsidies.

Table 8 - Transferred expenditures	$ millions
Interest on Treasury Notes	213.0
Public Distribution System	2,400.0
Fuel Imports	2,100.0
Transfer Payments (was Contingency Fund)	1,670.8
Local/Regional Government Grants	830.8
Regional Development Projects	600.0
Commanders Emergency Response Program	70.0
Rapid Regional Response Programme Funds	225.0
State-Owned-Enterprise restructuring	381.3
State-Owned-Enterprise salary support	379.7
Economic Restructuring Programs	134.0
Agricultural Subsidies	200.0
Additional Security Spending	500.0
Oil Export Production Fee	85.2
Debt Negotiations Costs	50.0
Reconciliation of External Debt	4.0
Oil for Food Audit	3.0
Haj Subsidies	37.5
Other Measures	133.0
Nation Building	571.2
TOTAL TRANSFERRED EXP.	**10,588.5**

Foreign Obligations

Higher than projected oil revenues mean that Kuwaiti War Reparations are higher, as these are 5% of gross revenues. Funding for repayment of IMF and World Bank arrears has also been added. These combine to projected spending for 2004 by US$ 1448.6 m.

Table 9 - Foreign obligations	$ millions
Kuwaiti War Reparations	708.8
International Monetary Fund and World Bank Arrears	453.3
Oil for Food Contracts	269.5
Demining	17.0
TOTAL FOREIGN OBLIGATIONS	**1,448.6**

Salaries and Retirement Rewards

#REF!

Table 10 - Salary & retirement rewards	$ millions
Pensions and other transfer payments	547.0
Stipends to Demobilised Military	250.0
TOTAL SALARIES & RETIREMENT	**797.0**

ATTACHMENT 2

CHARRTS No.: HG-01-004
House Government Reform Committee
Hearing Date: March 11, 2004
Subject: The Complex Task of Coordinating Contracts Amid Chaos, the Challenges of Rebuilding a Broken Iraq
Congressman: Congressman Waxman
Witness: HON Zakheim
Question: #4

Question: When do you plan to make that information available to Congress?

Answer: The CPA IG report will be delivered to Congress on March 30, 2004. The most recent Section 2207 report will be delivered to Congress on April 5, 2004.

CHARRTS No.: HG-01-005
House Government Reform Committee
Hearing Date:
Subject: The Complex Task of Coordinating Contracts Amid Chaos, the Challenges of Rebuilding a Broken Iraq
Congressman: Congressman Waxman
Witness: HON Zakheim
Question: #5

Question: As Comptroller, please explain which Defense Department agency is in charge of conducting thorough, detailed, and rigorous audits over the expenditures of potentially $10 billion in oil proceeds?

Answer: A Defense Department agency is not in charge of auditing expenditure of Iraqi oil proceeds. The Departments of Defense, State, and Treasury negotiated with the International Advisory and Monitoring Board (IAMB) to ensure the DFI is used in a transparent manner. The IAMB is comprised of representatives from the United Nations, World Bank, International Monetary Fund, and the Arab Fund for Economic and Social Development. The IAMB recently approved KPMG as independent public accountants to audit the DFI and export sales of Iraqi petroleum, petroleum products, and natural gas. The results of the audit will be published and made available for review.

In addition, the CPA IG is responsible for engaging in audits, inspections, reviews, and investigations of the CPA's use of U.S. taxpayer, Iraqi, and other funds committed to the Iraq relief and reconstruction efforts.

CHARRTS No.: HG-01-006
House Government Reform Committee
Hearing Date:
Subject: The Complex Task of Coordinating Contracts Amid Chaos, the Challenges of Rebuilding a Broken Iraq
Congressman: Congressman Waxman
Witness: HON Zakheim
Question: #6

Question: Will GAO be given full access to all the information they need to audit how the DFI funds are being spent?

Answer: Yes. The CPA comptroller has already provided DFI procedures documentation and CPA Program Review Board files as requested by the GAO. The CPA comptroller will be responsive to any future requests by the GAO.

UNPRECEDENTED CHALLENGES: THE COMPLEX TASK OF COORDINATING CONTRACTS AMID THE CHAOS AND THE REBUILDING OF IRAQ

TUESDAY, JUNE 15, 2004

HOUSE OF REPRESENTATIVES,
COMMITTEE ON GOVERNMENT REFORM,
Washington, DC.

The committee met, pursuant to notice, at 11:20 a.m., in room 2154, Rayburn House Office Building, Hon. Tom Davis of Virginia (chairman of the committee) presiding.

Present: Representatives Tom Davis of Virginia, Shays, Mica, Souder, LaTourette, Ose, Lewis, Ms. Davis of Virginia, Platts, Cannon, Schrock, Duncan, Deal, Miller, Murphy, Turner, Carter, Blackburn, Tiberi, Harris, Waxman, Maloney, Cummings, Kucinich, Mr. Davis of Illinois, Tierney, Clay, Lynch, Van Hollen, Sanchez, Ruppersberger, Norton, Cooper, and McCollum.

Staff present: David Marin, deputy staff director/communications director; Keith Ausbrook, chief counsel; Ellen Brown, legislative director and senior policy counsel; Robert Borden, counsel/parliamentarian; Rob White, press secretary; Drew Crockett, deputy director of communications; John Cuaderes, senior professional staff member; John Brosnan, GAO detailee; Teresa Austin, chief clerk; Brien Beattie, deputy clerk; Robin Butler, financial administrator; Allyson Blandford, office manager; Corinne Zaccagnini, chief information officer; Leneal Scott, computer systems manager; Phil Barnett, minority staff director/chief counsel; Kristin Amerling, minority deputy chief counsel; Karen Lightfoot, minority senior policy advisor & communications director; Anna Laitin, minority communications & policy assistant; David Rapallo, Alexandria Teitz, and Jeff Baran, minority counsels; Mark Stephenson, Nancy Scola, and Adam Bordes, minority professional staff members; Cecelia Morton, minority office manager; Teresa Coufal, minority assistant clerk; Christopher Davis, minority investigator; Theresa Foote, minority special assistant; and James Temple and Lawrence Atkinson, minority interns.

Chairman TOM DAVIS. Good morning. I appreciate everyone's indulgence. The ranking member and myself have been trying to make this move as smoothly as we can for Members.

The committee will come to order. We meet here today to look into the challenges surrounding the complex task of coordinating and executing contracts amid the chaos of rebuilding Iraq.

Even before the conclusion of major military actions, there were plans for a massive effort to rebuild Iraq's infrastructure and government. Those responsible knew this endeavor would require an enormous amount of contractor support. Anticipating the worst, and recognizing the need for quick and decisive action, agency procurement professional properly invoked the carefully circumscribed statutory flexibilities designed to quickly provide urgently needed goods and services.

I am referring here to contracts that were let just prior to or soon after the conclusion of major military action. The urgency and difficult circumstances surrounding the anticipated scenarios justified the use of limited competition or, in a few cases, single source awards. Although I am an advocate for full and open competition, Congress, in anticipation of war and other emergency scenarios, provided our procurement professionals with these flexibilities to deal with emergencies just like we had in Iraq.

The rebuilding of Iraq is a very monumental task. Saddam Hussein spent decades frittering away his nation's vast wealth on himself and his Baath party cronies, while little or nothing was spent to meet the urgent needs of the Iraqi people. Decades of neglect and inaction turned this once great nation into one where the majority of people live in poverty and despair.

However, with Saddam's ouster, we are witnessing a rebirth of Iraq. Freedom and liberation have brought a new sense of urgency to the Iraqi people; they understand what is at stake and we need to do our part to sustain freedom by rebuilding their nation.

The task at hand is mammoth; it will be years before we are able to truly get Iraq running on its own. Yet, as each day passes, Iraqis are getting a better life thanks to the dedicated American soldiers and civilians working there. Our reconstruction efforts are well under way, even under life-threatening conditions.

Currently, there are many U.S. Government agencies working to improve conditions in Iraq. For example, the Department of Defense, the U.S. Army Corps of Engineers, and the U.S. Agency for International Development are all working to rebuild Iraq. There is no question that each of these entities is working in an extremely challenging environment. And although every day brings progress, we all recognize there are still major obstacles facing our military, government civilians and contractors.

There are serious security concerns as well, and the simple necessities of life like water and electricity are only sporadically available in many areas. So it is no surprise that our normal acquisition support and oversight resources are sorely stretched. The committee is interested in the efforts made to manage, oversee, and coordinate acquisition activities to ensure that taxpayer money is being spent as effectively and efficiently as possible in this difficult wartime atmosphere.

In addition to our ongoing work, the General Accounting Office has also been reviewing these efforts. A report on the challenges faced in awarding the contracts has just been issued. Another GAO report on the performance challenges faced by sustainment efforts is in the works.

Huge amounts of money have already been or are about to be expended in our reconstruction efforts. We need to make sure that ac-

quisition rules and the integrity of the processes are being followed. Congress has spent years streamlining complex government rules and regulations to make it easier for businesses to sell to the Federal Government, but did so in a way that carefully balances affordability, accountability, and accessibility to make sure taxpayer dollars are protected. It is our job, this committee's job, to make sure that is happening in Iraq.

We hope to learn today how our acquisition system and the professionals who run it have responded to the challenges faced in Iraq. No one doubts that the circumstances are exceptionally difficult. I have seen the chaos on the ground there. The security situation is tenuous at best. On a daily basis, our military, civilians and contractors come under hostile fire. Our service men and women are being killed and wounded. A great number of contractor employees have also been killed, captured, or wounded. It is a major understatement to say that this is a difficult place to conduct business, but we are doing just that and we are slowly accomplishing our goals.

Government contracting is difficult even under normal circumstances. Add in the urgency and the inherent dangers of a war zone and the challenge of acquiring urgently needed goods and services, and it becomes quite daunting. Through this hearing we hope to continue to separate fact from fiction, truth from rhetoric and, in turn, help make sure we are coordinating contract processes in Iraq in a way that ensures success and safety.

I recognize that there have been mistakes. That is why we are holding hearings. That is why we are requesting documents and getting briefed on a daily basis. The contracting process is not always pretty, and decisions made under the pressure of combat are not always as lucid as those made under less threatening conditions. Nevertheless, the vast majority of the new contract awards were done properly. While there were some difficulties, particularly in the issuance of task orders under existing contracts, it is my understanding that while the procedures used may have been flawed in some cases, the awards themselves could clearly have been accomplished under other authorities. Not surprisingly, it also seems that the management and oversight of contract performance remains a thorny challenge due to the evolving needs on the ground, staffing difficulties, and an intimidating security environment.

Many of the disputes that have been made public show that the contract oversight process is working. We need to let the give and take of contract oversight and management work. Make no mistake, overcharges cannot and will not be tolerated, and contractors need to establish systems and processes that protect the Government from waste and that maximize the reach of pressure taxpayer dollars. But we need to keep in mind the enormity of the effort involved and that it is being executed in a wartime environment where lives are at stake. This hearing is part and parcel of our functioning oversight process.

As chairman of the committee, I would like to move beyond the politics, honestly explore the challenges the military and contractors face, and figure out how to overcome them. I am not new to politics; I understand why others feel the need to say the word Halliburton as often as humanly possible, but we have more than just

one contractor in Iraq and lives are on the line. I would hope that our friends on the other side would agree and begin to move this debate in a more constructive direction, away from really what I would consider partisan politics that really serve the interest of a few.

For the record, we have spent months working together with the minority on these issues. We have set up joint witness interviews with DOD personnel; we have submitted joint document requests; we have had joint GAO briefings and my staff has participated in joint whistleblower interviews; and we are trying to conduct these in good, constructive, bipartisan faith with our friends.

On Sunday, Mr. Waxman sent a letter to the Vice President that included, in my judgment, unwarranted insinuations about improper contact between the Vice President's office and DOD contracting officials, something I am sure we will talk about today, allegedly based on a briefing by DOD officials. Just so we are clear, it was my staff, majority staff that set up and attended the briefing, and those who came over from DOD stated clearly that they had not experienced inappropriate influence from the Vice President or anyone in that office. We had no idea that the majority would send their own letter when we had been working together on these issues. It wasn't shared with us before it was released to the press, and we don't share that politically charged interpretation of what was said at the briefing. There are witnesses here today that can elaborate on that issue.

I completely understand what is going on here in the political context, but I find it distasteful from our role as an oversight committee to choose oversight by press release or by leaking draft reports and confidential briefings. This is a strategy that, as the majority, we will not pursue and, if we ever become the minority, I hope as long as I am the ranking member, would not pursue.

All you have to do is look back at the wide-ranging complex bipartisan oversight this committee has conducted over the past year and a half to understand why they have had to make, I think, some rather extreme statements to make their point that we don't think stands up for scrutiny, and we are not going to participate in that circus. We are going to continue to conduct responsible oversight, and I hope this hearing will serve as another step in that direction. I said this back in March at our last hearing on this issue, and it is worth repeating: I have no patience for fraud or abuse. I expect that any such instances that are proven will result in harsh punishment for the perpetrators. Since our last hearing, many of the limited competition contracts have been replaced by ones awarded through full and open competition. Emergency procedures are for emergencies only. When initial decisions were made, time was not our ally, but fortunately we anticipated this and were able to react in such a manner that assisted the war effort rather than hindering it. Our soldiers have benefited from this and lives have been spared because of this, and we need to keep that in mind as we conduct the oversight we are charged with conducting.

[The prepared statement of Chairman Tom Davis follows:]

Opening Statement of Chairman Tom Davis
Government Reform Committee Hearing
"Unprecedented Challenges: Contracting and the Rebuilding of Iraq"
June 15, 2004

Good morning. We meet today to look into the challenges surrounding the complex task of coordinating and executing contracts amid the chaos of rebuilding Iraq.

Even before the conclusion of major military actions, there were plans for a massive effort to rebuild Iraq's infrastructure and government. Those responsible knew this endeavor would require an enormous amount of contractor support. Anticipating the worst, and recognizing the need for quick and decisive action, agency procurement professionals properly invoked the carefully circumscribed statutory flexibilities designed to quickly provide urgently needed goods and services.

I am referring here to contracts let just prior to, or soon after the conclusion of major military action. The urgency and the difficult circumstances surrounding the anticipated scenarios justified the use of limited competition, or in a few cases, single source awards. Although I am an advocate of full and open competition, Congress, in anticipation of war and other emergency scenarios provided our procurement professionals with these flexibilities to deal with emergencies just like the Iraq war.

The rebuilding of Iraq is a monumental task. Saddam Hussein spent decades frittering away his nation's vast wealth on himself and his Baath party cronies, while little to nothing was spent to meet the urgent needs of the Iraqi people. Decades of neglect and inaction turned this once great nation into one where the majority of people live in poverty and despair.

However, with Saddam's ouster, we are witnessing a rebirth of Iraq. Freedom and liberation have brought a new sense of urgency to the Iraqi people; they understand what is at stake and we need to do our part to sustain freedom by rebuilding their nation.

The task at hand is mammoth; it will be years before we are able to truly get Iraq running on its own. Yet as each day passes Iraqis are getting a better life thanks to the dedicated American soldiers and civilians working there. Our reconstruction efforts are well under way, even under life threatening conditions.

Currently, there are many U.S. government agencies working to improve conditions in Iraq. For example, the Department of Defense, the U.S. Army Corps of Engineers and the U.S. Agency for International Development are all working to "rebuild" Iraq. There is no question that each of these entities is working in an extremely challenging environment. Although every day brings progress, we all recognize there are still major obstacles facing our military, government civilians and contractors.

There are serious security concerns, and the simple necessities of life like water and electricity are only sporadically available in many areas. So it is no surprise that our

normal acquisition support and oversight resources are sorely stretched. The Committee is interested in the efforts made to manage, oversee, and coordinate acquisition activities to ensure that taxpayer money is being spent as effectively and efficiently as possible in this difficult wartime atmosphere.

In addition to our ongoing work, the General Accounting Office (GAO) has also been reviewing these efforts. A report on the challenges faced in awarding the contracts has just been issued. Another GAO report on the performance challenges faced by the sustainment efforts is in the works.

Huge amounts of money have already been or are about to be expended in our reconstruction efforts. We need to make sure that acquisition rules and the integrity of the process are being followed. Congress has spent years streamlining complex government rules and regulations to make it easier for businesses to sell to the federal government, but did so in a way that carefully balances affordability, accountability, and accessibility to make sure taxpayer dollars are protected. It's our job to make sure that is happening in Iraq.

We hope to learn today how our acquisition system and the professionals who run it have responded to the challenges raised in Iraq. No one doubts that the circumstances are exceptionally difficult. I've seen the chaos on the ground there. The security situation is tenuous at best. On a daily basis our military, civilians and contractors come under hostile fire. Our service men and woman are being killed and wounded. A great number of contractor employees also have been killed or wounded. It is a major understatement to say that this is a difficult place to conduct business, but we are doing just that and we are slowly accomplishing our goals.

Government contracting is difficult enough under normal circumstances. Add in the urgency and inherent dangers of a war zone, and the challenge of acquiring urgently needed goods and services becomes quite daunting. Through this hearing we hope to continue to separate fact from fiction, truth from rhetoric – and, in turn, help make sure we're coordinating contract processes in Iraq in a way that ensures success and safety.

I recognize that there have been mistakes. That's why we're holding hearings, requesting documents, getting briefed on a daily basis. The contracting process is not always pretty, and decisions made under the pressure of combat are not always as lucid as those made under less threatening conditions. Nevertheless, the vast majority of the new contract awards were done properly. While there were some difficulties, particularly in the issuance of task orders under existing contracts, it is my understanding that while the procedures used may have been flawed, the awards themselves could clearly have been accomplished under other authorities. Not surprisingly, it also seems that the management and oversight of contract performance remains a thorny challenge due to evolving needs on the ground, staffing difficulties, and an intimidating security environment.

Many of the disputes that have been made public show that the contract oversight process is working. We need to let the give and take of contract oversight and management work. Make no mistake, overcharges cannot be tolerated, and contractors need to establish systems and processes that protect the government from waste and maximize the reach of precious taxpayer dollars. But we need to keep in mind the enormity of the effort involved and that it is being executed in a wartime environment where lives are at stake. This hearing is part and parcel of a functioning oversight process.

As Chairman of this Committee, I would like to move beyond the politics, honestly explore the challenges the military and contractors face, and figure out how to overcome them. I'm not new to politics; I understand why my Ranking Member and others feel the need to say the word *Halliburton* as often as humanly possible.

But we have more than just one contractor in Iraq, and lives are on the line. I would hope my friend, the Ranking Member, will agree with me and begin to move this debate in a more constructive direction, away from the blatantly partisan politics that serve the interest of only a few.

For the record, we've spent months working together with the minority on these issues. We've set up joint witness interviews with DOD personnel. We've submitted joint document requests. We've had joint GAO briefings and my staff has participated in joint whistleblower interviews. I was under the impression that we were conducting good, constructive, bi-partisan oversight on this difficult subject.

But my colleagues on the other side have chosen another path. On Sunday, Mr. Waxman sent a letter to the Vice President that included unwarranted insinuations about improper contact between the Vice President's office and DOD contracting officials, allegedly based on a briefing by DOD officials. Just so we're clear, it was my staff that set up and attended the briefing and those who came over from DOD stated clearly that they had not experienced inappropriate influence from the Vice President or anyone in that office. We had no idea the minority contemplated sending such an inflammatory letter. It was not shared with us before it was released to the press, and we do not share their politically charged interpretation of what was said at the briefing. There are witnesses here today who can elaborate on this issue.

Too many Democrats, for political reasons I completely understand but personally find distasteful, have chosen to practice oversight by press release, oversight by leaking draft reports and confidential briefings. This is a strategy being driven top down by House Democrat leadership. It's a component of their shopworn theme that Republicans aren't doing enough oversight. And all you have to do is look back at the wide-ranging, complex, nonpartisan oversight this committee has conducted over the past year and a half to understand why the Democrats have had to make some extremist statements to try to make their point: it just doesn't stand up to scrutiny.

I will not participate in such a circus. I will continue to conduct responsible oversight, and I hope this hearing will serve as another step in that direction. I said this back in March at our last hearing on this issue, and it is worth repeating: I have no patience for fraud or abuse. I expect that any such instances that are proven will result in harsh punishment for the perpetrators. Since our last hearing many of the limited competition contracts have been replaced by ones awarded through full and open competition. Emergency procedures are for emergencies only. When initial decisions were made, time was not our ally, but fortunately we anticipated this and were able to react in such a manner that assisted the war effort rather than hindering it. Our soldiers have benefited from this – lives have been spared because of this -- and we need to keep that in mind as we conduct the oversight we're charged with conducting.

Chairman TOM DAVIS. Mr. Waxman, your opening statement?

Mr. WAXMAN. Thank you, Mr. Chairman.

In early March, this committee held its first hearing on Iraq contracts. I spoke at length at that hearing about the fundamental flaws in the administration's procurement strategy and the enormous waste of taxpayer dollars that was occurring in Iraq. Today, more than 3 months later, none of these fundamental problems have been addressed. We know more today than we did 3 months ago about how the administration has mismanaged the contracts to reconstruct Iraq, and what we have learned shows that the problems are even worse than we thought.

The focus of today's hearing is the two largest Iraq contracts. One contract, called LOGCAP, was awarded to provide the military with logistical support, such as housing and dining facilities. The other contract, called RIO, was awarded to import fuel and restore Iraq's oilfields. Both of these contracts went to one well-connected company, Halliburton. In total, Halliburton has been awarded a phenomenal sum of money, over $7 billion, under these two contracts.

In the course of our investigation into the Halliburton contracts, we have tried to look at the contracts from three different perspectives. One is the boots on the grounds perspective of the employees who work for the company; one is the flyover perspective of Pentagon auditors who scrutinize Halliburton's books to ensure that the taxpayer is not being overcharged; and one is the 50,000 foot perspective of the General Accounting Office, which has examined whether the Federal Government has the necessary safeguards in place to prevent waste, fraud, and abuse. All three perspectives come to the same conclusion: Halliburton is gouging the taxpayer, and the Bush administration doesn't seem to care.

Yesterday I released the statements of five former employees of Halliburton. These individuals describe a company that acts like it is spending someone else's money, which is just what Halliburton is doing. Under the company's cost-plus contract, the more taxpayer money Halliburton spends, the more profit it makes. The examples of waste, fraud, and abuse provided by the former Halliburton employees are stunning. One former logistics specialist told us that Halliburton charged taxpayers $10,000 a day to house its employees in the five-star Kempinski Hotel in Kuwait. The same employees could have stayed in air conditioned tents like those used by our troops for less than $600 a day.

A former convoy commander told us that Halliburton removed the spare tires from its brand new $85,000 trucks, and if one of the trucks got a spare tire, Halliburton would abandon or torch the truck. Can you imagine that? Halliburton's approach to fixing a flat tire is to buy a new truck. Another truck driver, James Warren, tried to do something about the waste and theft he observed. He called Randy Harl, the president and CEO of KBR, the Halliburton subsidiary operating in Iraq. Instead of investigating Mr. Warren's allegation, KBR fired him.

The Pentagon auditors at the Defense Contract Audit Agency observed the same kind of problems that the whistleblowers report. In an audit that was completed last month, but withheld from Congress, DCAA found multiple deficiencies in Halliburton's billing

practices. In one example, DCAA found that Halliburton submitted "billings to the government for as much as three times the meals they actually served."

Well, last year, Representative John Dingell and I requested that the General Accounting Office review Halliburton's LOGCAP contract. Today we will hear GAO's testimony about the results of the investigation. GAO found widespread problems, including inadequate planning, little concern for costs, and poor contract management. Here is one example GAO told us about. Prior to the Iraq war, the military had a contract with a Kuwaiti company called Tamimi to provide meals to the U.S. troops in Kuwait. Before the war started, the Bush administration turned the contract over to Halliburton with the specific instructions that Halliburton subcontract with Tamimi to continue feeding the troops. According to GAO, a cost-conscious procurement official finally terminated the Halliburton contract this spring and they returned the contract to Tamimi. Well, when they finally got rid of Halliburton acting as a middleman, they cut the cost by over 40 percent. What purpose did Halliburton serve except to increase the cost that we were paying for the same meals being served by the same subcontractor who was doing it for 40 percent less?

Our own investigation has exposed other examples of astoundingly bad contract management. In the March hearing, I objected to the Bush administration giving the job of overseeing the reconstruction contracts to private contractors. When I investigated further, I learned that the companies hired to oversee the private contractors had significant conflicts of interest. Parsons, for example, was hired to oversee its business partner, Fluor, while CH2M HILL was hired to oversee its business partner, Washington Group International. When you are hired to oversee your business partner, there is a good reason to believe that you may not want to be as vigorous in making sure that your business partner doesn't overspend the money.

Well, these decisions have real consequences. Our troops have died in Iraq because they lack body armor and reinforced Humvees. We can't afford to throw away money on Halliburton when we don't have enough funds to adequately equip and protect our soldiers.

Now, GAO will tell us today that the Bush administration did not have contingency plans in place for feeding and housing the troops. But the administration did have detailed contingency plans for running Iraq's oilfields. In fact, Halliburton was given the secret contract in November 2002 to develop these plans. Now, here is the message that sends about this administration's priorities: protecting Iraq's oil came before protecting our own troops.

Many people have wanted to know what role the Vice President has played in all of this. For months he has denied any knowledge about Halliburton's contracts. He said, on television, and I want to quote him directly, this was on Meet the Press last September, "Since I left Halliburton to become George Bush's Vice President, I have severed all my ties with the company, and as Vice President I have absolutely no knowledge of, in any way, shape, or form, contracts let by the Corps of Engineers or anybody else. I deliberately stayed away from any information on that."

The administration has also consistently maintained that Halliburton was selected for the Iraqi contracts by career procurement officers. But we now know that simply was not true. Halliburton was selected for the oil contracts by political appointees in the Bush administration, not by procurement officials, and the Vice President's chief of staff, Scooter Libby, was personally briefed on the contracts before they were issued.

We don't know the full extent of the Vice President's involvement in the Halliburton contracts. All we know for sure is that what the Vice President has said so far is false.

Now, that has come, in part, from a briefing that both the minority and majority staffs participated in. It was not a confidential briefing, and that briefing gave information that contradicted the statements that Vice President Cheney, and this administration have been making over and over again, and it contradicts sworn testimony given to this committee in March, when we held our last hearing.

Americans cannot rely on the Bush administration to fix the contracting problems in Iraq. This administration is notorious for refusing to acknowledge mistakes or to hold officials accountable. In fact, as the Vice President's comments demonstrate, it is even hard to trust the administration to provide honest and full information. So it is really up to the Congress to look after the interest of the troops and the taxpayers, and the question I have is whether we are up to this challenge.

Chairman Davis has taken some commendable steps. We have had a conversation as a result of the letter that we sent him, and he has now agreed that we will hold a hearing in July to bring in the whistleblowers identified by the minority before the committee. We will discuss exactly who will participate in that hearing and that will be something that we will discuss together. He has also agreed that Halliburton's CEO, David Lesar, and KBR's CEO, Randy Harl, will receive formal written invitations to testify before the committee. I think Halliburton ought to testify before this committee. If they think that some of this information is inaccurate, they ought to be here to say so under oath and to be questioned about it.

Chairman Davis and I have discussed our concern about some other essential steps that I think we need to take. Three months ago, Chairman Davis and I wrote to Defense Secretary Rumsfeld and USAID Administrator Natsios to seek documents relating to the Halliburton and Bechtel contracts in Iraq. The administration failed to provide most of these documents. In fact, even when the administration finally did respond to portions of the request, it withheld key documents. I think we need to protect our rights to the documents and subpoena them, if necessary, so that we in this committee get those documents.

We cannot conduct effective oversight by consent. The test of what we investigate should be what we need to do in order to fulfill our oversight responsibilities, not what the administration agrees to let us see. If we are going to do our jobs, we need to be far more assertive than we have been so far.

George Will said something very wise in a recent column. He wrote, "Failures are multiplying because of choices for which no

one seems to be accountable." Although asking tough questions can be politically inconvenient, we will be doing the President no favor if we refuse to fulfill our Constitutional oversight responsibilities. Oversight can be painful at times, especially if you look at this whole issue from a partisan perspective. But it is an essential part of our system of checks and balances.

I look forward to the hearing today. I look forward to the hearing we will have in July, and I hope that it marks the beginning, not the end, of our committee's work on Iraq contract oversight.

Thank you very much, Mr. Chairman, for this chance to make the opening statement.

[The prepared statement of Hon. Henry A. Waxman follows:]

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Statement of Rep. Henry A. Waxman
June 15, 2004

In early March, this Committee held its first hearing on Iraq contracts. I spoke at length at that hearing about the fundamental flaws in the Administration's procurement strategy and the enormous waste of taxpayer dollars that was occurring in Iraq.

Today — more than three months later — none of these fundamental problems have been addressed.

We know more today than we did three months ago about how the Administration has mismanaged the contracts to reconstruct Iraq. And what we have learned shows that the problems are even worse than we thought.

The focus of today's hearing is the two largest Iraq contracts. One contract, called "LOGCAP," was awarded to provide the military with logistical support, such as housing and dining facilities. The other contract, called "RIO," was awarded to import fuel and restore Iraq's oil fields.

Both of these contracts went to one well-connected company: Halliburton.

In total, Halliburton has been awarded a phenomenal sum — over $7 billion — under these two contracts.

In the course of our investigation into the Halliburton contracts, we've tried to look at the contracts from three different perspectives. One is the "boots on the ground" perspective of employees who worked for the company. One is the "fly-over" perspective of Pentagon auditors who scrutinize Halliburton's books to ensure the taxpayer is not overcharged. And one is the "50,000 foot" perspective of the General Accounting Office, which has examined whether the federal government has the necessary safeguards in place to prevent waste, fraud, and abuse.

All three perspectives point to the same conclusion: Halliburton is gouging the taxpayer, and the Bush Administration doesn't seem to care.

Yesterday I released the statements of five former employees of Halliburton. These individuals describe a company that acts like it is spending someone else's money — which is

just what Halliburton is doing. Under the company's cost-plus contract, the more taxpayer money Halliburton spends, the more profit it makes.

The examples of waste, fraud, and abuse provided by the former Halliburton employees are stunning. One former logistics specialist told us that Halliburton charged the taxpayer $10,000 per day to house its employees in the five-star Kempinski Hotel in Kuwait. The same employees could have stayed in air-conditioned tents like those used by our troops for less than $600 per day.

A former "convoy commander" told us that Halliburton removed the spare tires from its brand-new $85,000 trucks. When one of the trucks got a flat tire, Halliburton would abandon or torch the truck.

Can you imagine that? Halliburton's approach to fixing a flat tire is to buy a new truck.

Another truck driver, James Warren, tried to do something about the waste and theft he observed. He called Randy Harl, the President and CEO of KBR, the Halliburton subsidiary operating in Iraq. Instead of investigating Mr. Warren's allegations, KBR fired him.

The Pentagon auditors at the Defense Contract Audit Agency observed the same kind of problems that the whistleblowers report. In an audit that was completed last month but withheld from Congress, DCAA found multiple deficiencies in Halliburton's billing practices. In one example, DCAA found that Halliburton submitted "billings to the Government for as much as three times the meals actually served."

Last year, Rep. John Dingell and I requested that the General Accounting Office review Halliburton's LOGCAP contract. Today, we will hear GAO testify about the results of the investigation. GAO found widespread problems, including inadequate planning, little concern for costs, and poor contract management.

Here's one example GAO told us about. Prior to the Iraq war, the military had a contract with a Kuwaiti company called Tamimi to provide meals to U.S. troops in Kuwait. Before the war started, the Bush Administration turned the contract over to Halliburton with the specific instructions that Halliburton subcontract with Tamimi to continue feeding the troops.

According to GAO, a cost-conscious procurement official finally terminated the Halliburton contract this spring and returned the contract to Tamimi. The result: eliminating Halliburton as a middleman cut costs by over 40%.

Our own investigation has exposed other examples of astoundingly bad contract management. In the March hearing, I objected to the Bush Administration giving the job of overseeing the reconstruction contracts to private contractors. When I investigated further, I learned that the companies hired to oversee the private contractors had significant conflicts of interest. Parsons, for example, was hired to oversee its business partner Fluor, while CH2M Hill was hired to oversee its business partner Washington Group International.

These decisions have real consequences. Our troops have died in Iraq because they lacked body armor and reinforced Humvees. We can't afford to throw away money on Halliburton when we don't have enough funds to adequately equip and protect our soldiers.

GAO will tell us today that the Bush Administration did not have contingency plans in place for feeding and housing the troops. But the Administration did have detailed contingency plans for running Iraq's oilfields. In fact, Halliburton was given the secret contract in November 2002 to develop these plans.

Here's the message this sends about this Administration's priorities: protecting Iraq's oil came before feeding the troops.

Many people have wanted to know what role the Vice President has played in all of this. For months, he has denied any knowledge about Halliburton's contracts. I'd like to play a tape of what Mr. Cheney said on *Meet the Press* last September:

> "Since I left Halliburton to become George Bush's vice president, I've severed all my ties with the company. ... And as vice president, I have absolutely no . . . knowledge of in any way, shape or form of contracts led by the Corps of Engineers or anybody else. . . . I deliberately stayed away from any information on that."

The Administration has also consistently maintained that Halliburton was selected for the Iraq contracts by career procurement officers.

But we now know that this is simply not true. Halliburton was selected for the oil contracts by political appointees in the Bush Administration — not by procurement officials. And the Vice President's chief of staff, Scooter Libby, was personally briefed on the contracts before they were issued.

We don't know the full extent of the Vice President's involvement in the Halliburton contracts. All we know for sure is that what the Vice President has said so far is false.

Americans cannot rely on the Bush Administration to fix the contracting problems in Iraq. This Administration is notorious for refusing to acknowledge mistakes or to hold officials accountable. In fact, as the Vice President's comments demonstrate, it's even hard to trust the Administration to provide honest information.

So it is really up to Congress to look after the interests of the troops and the taxpayers. And the question I have is whether we are up to this challenge.

Chairman Davis has taken some commendable steps. He has now agreed to bring the whistleblowers identified by the minority before the Committee. He has also agreed that Halliburton's CEO, David Lesar, and KBR's CEO, Randy Harl, will receive formal written invitations to testify before the Committee.

But Chairman Davis has failed to take other essential steps. Three months ago, Chairman Davis and I wrote to Defense Secretary Rumsfeld and USAID Administrator Natsios to seek documents relating to the Halliburton and Bechtel contracts in Iraq. The Administration failed to provide most of these documents. In fact, even when the Administration finally did respond to portions of the request, it withheld key documents. Despite this record, the Chairman has refused to subpoena the documents.

We cannot conduct effective oversight by consent. The test of what we investigate should be what we need to do in order to fulfill our oversight responsibilities — not what the Administration agrees to let us see. If we are going to do our jobs, we need to be far more assertive than we have been so far.

George Will said something very wise in a recent column. He wrote — and I quote — "failures are multiplying because of choices for which no one seems accountable." Although asking tough questions can be politically inconvenient, we will be doing the President no favors if we refuse to fulfill our constitutional oversight responsibilities. Oversight can be painful at times, but it is an essential part of our system of checks and balances.

I look forward to this hearing. And I hope that it marks the beginning — not the end — of our Committee's work on Iraq contract oversight.

Chairman TOM DAVIS. Thank you, Mr. Waxman. I think that we have Members here expecting you to put some motions. I am going to allow members to submit opening statements for the record, and during your 5 minutes of questions, if you prefer to use that time for statements, we will do that; otherwise, we will dispense with additional opening statements. And I understand you have some motions.

Mr. WAXMAN. Well, Mr. Chairman, before I do that, I want to welcome Representative Betty McCollum, who joins us today as the newest member of the Government Reform Committee. Throughout her career as a teacher, a city council member, and a member of the Minnesota House of Representatives, she has championed issues that are important to her constituents and to all Americans, and she has worked to ensure excellence in education, environmental protection, and health care access for all. And I am pleased she is joining us on this committee as a member of the Government Reform Committee, and she brings a wealth of experience and expertise to this committee, and I know all of us look forward to working with her.

Chairman TOM DAVIS. Well, thank you, Mr. Chairman. Let me just say for the majority we are happy to have her here and look forward to working with her.

Mr. Waxman.

Mr. WAXMAN. Mr. Chairman, I think that we need to subpoena documents in order to get those documents submitted to our committee. You and I have had a conversation prior to this meeting about these documents. Some of these documents involve matters that you and I have both requested from the administration, and with regard to those documents, we have requested them; some have been given to us, but not all of them. And I think it is appropriate to demand them and to subpoena them if we can't get them voluntarily. And I would like to yield to you.

Chairman TOM DAVIS. Thank you, Mr. Waxman. We still don't have a number of documents that we requested on March 26th. Some documents, which the minority was able to obtain anyway, I might add, actually post-dated March 26th and weren't included in that request. But what we don't have is the DOD cost estimate for Task Order 59; DOD reports on the Bechtel construction contract; determination to award a single, rather than multiple, award contract for oil infrastructure contract; various documents relating to the KBR contract for imported gasoline; and the aid reports on the Bechtel construction contract. By all right, the committee should have these.

What I will say today is I would like to give the Department until June 30th to get those documents before us. If there is a security reason why they can't do that, or logistical reason, we would like them to come up and at least give us the courtesy of meeting with Mr. Waxman and myself to see why these documents shouldn't be forthcoming. And if we don't hear by that time, it would be my intent, I think, to move ahead with subpoenas, but we want to give them an opportunity to move ahead with that or to at least give us a reason why they shouldn't, which they haven't to date.

Mr. WAXMAN. Well, Mr. Chairman, I want to put a list of some of these items in the record. We don't need to go through them now. You and I both requested the documents. You are suggesting that we give them until June 30th, and if they don't respond, either by coming forward and telling us why they can't respond or giving us the documents as we have requested, you will go forward with subpoenas, which you can issue on your own, without even convening a meeting of the committee, is that correct?

Chairman TOM DAVIS. That is correct.

Mr. WAXMAN. Well, under those circumstances, I don't see it necessary to offer a motion for the committee to vote on; I accept that is a reasonable course to fllow.

Chairman TOM DAVIS. Let me just say to our friends at the Department that we need these documents. We are entitled to them under law, and we ought to have them, and it has been a joint bipartisan request. And there were other documents, I might add, that Mr. Waxman wanted to add to this that we did not join him with that weren't in this list, but these were jointly agreed to.

Mr. WAXMAN. I have another motion for a subpoena that involves some other matters, if we can have them reported.

Chairman TOM DAVIS. Will the clerk designate?

Ms. AUSTIN. Which one would you be referring to?

Mr. WAXMAN. This is the one that involves the Vice President.

Ms. AUSTIN. Motion to subpoena Secretary of Defense Donald Rumsfeld for documents relating to DOD contacts with the Vice President's Office of the White House. Under House Rule 11(2)(k)(6), I move the committee issue a subpoena to a witness, Secretary of Defense Donald H. Rumsfeld, to appear before the Committee on Government Reform on July 6, 2004, to produce certain documents relating to contracting and the rebuilding of Iraq.

Mr. WAXMAN. Mr. Chairman, I ask unanimous consent that the motion be agreed to and considered as read.

Chairman TOM DAVIS. Without objection, so ordered and considered as read.

Mr. Waxman.

Mr. WAXMAN. Well, Mr. Chairman and my colleagues, we have the right to move for subpoenas to get this information, and there are documents that we are requesting that we think you would, on reflection, agree that we ought to have. But in our conversation before this hearing, you expressed to us you haven't had a chance to review all of our requests to see whether you would support them. And rather than put this to a vote, if you will afford us the opportunity to discuss these requests and join us jointly in requesting the information, where you feel it is appropriate, and not only make the request, but back it up with a subpoena if the request is not agreed to in an appropriate amount of time, I would find that an acceptable way for us to proceed together in comity on this second group.

Chairman TOM DAVIS. Well, Mr. Waxman, I always think we work better together as a bipartisan unit on these issues and try to take at least the partisan sting out of these. In addition to that, we have some disagreements on the documents, but in discussing this beforehand, I think there are some areas where we can agree

to move forward, and I would be happy to work with you in that regard, as we have in the past.

Mr. WAXMAN. Mr. Chairman, I think what you have suggested to us in good faith is helpful and constructive for us to proceed with together, and rather than put the committee to a vote that might well be partisan, and I so much don't want this to be partisan because it is our committee's responsibility on a bipartisan basis to do the investigation that is appropriate I will ask unanimous consent to withdraw my motion for a subpoena. We will discuss further the items. I want to make a case to you on each of the items and hope that I can get you to agree to jointly request them and back it up with a subpoena if the request is not honored.

Chairman TOM DAVIS. I thank the gentleman. If there is no objection, the request will be withdrawn.

Mr. WAXMAN. I have a third motion, and without offering that motion officially and withdrawing it, I do want to indicate to you that I would like to handle it in the same way we have handled the second one. It involves further request for Halliburton documents, and we would like to discuss them with you further, see if we can join together in a request for those documents, with the understanding that if we do request them jointly, and after an appropriate time if they are not forthcoming, that we will go to subpoena.

Chairman TOM DAVIS. I look forward to working with the gentleman on his request.

Mr. WAXMAN. Thank you.

Chairman TOM DAVIS. We have not had an opportunity to review all of these at this point, and we have some reservations about some of the things that have come up, but there are others I think we can find some area of closure, so I look forward to working with the gentleman.

Mr. WAXMAN. Well, I thank you very much, Mr. Chairman. I think that is the appropriate way for us to proceed, and I look forward to working with you. I want to make the case to you on each and every one of these, and hope I can get you to agree. That is all I can do, is make the case, and if you don't agree, you don't agree.

Chairman TOM DAVIS. We have the same opportunity on your witnesses, so we have a lot of things to talk about. I appreciate it.

Mr. WAXMAN. I appreciate it, and I do want to have you acknowledge that we are going to go ahead and have a meeting in July.

Chairman TOM DAVIS. That is correct, we will have a July hearing.

Mr. WAXMAN. Where we will have an opportunity for whistleblower testimony.

Chairman TOM DAVIS. Of course. As I had indicated in previous hearings, we will.

Mr. OSE. Mr. Chairman.

Chairman TOM DAVIS. Yes. Gentleman from California.

Mr. OSE. I have heard a lot of talk focused on a particular company, however, this contracting officer from our March 11th hearing was far larger than just one company. Am I to understand from your discussion that we are limiting our inquiries to one company?

Chairman TOM DAVIS. Not at all. Not at all. In fact, some of the inquiries and the documents we have requested do relate to other companies.

Mr. WAXMAN. If the gentleman would permit to yield to me, one of the documents we have requested involves Bechtel, which is the second largest contractor. We haven't received that information. It is impeding our investigation. But we are not just focused on Halliburton.

Chairman TOM DAVIS. There are others as well. If the gentleman has any suggestions, as I know he does, we would be happy to look at those as we.

Mr. OSE. Well, I am still waiting on answers to the questions we submitted through you and Mr. Waxman.

Chairman TOM DAVIS. From DOD. Well, we can add that to our request.

Mr. OSE. I would appreciate that.

Chairman TOM DAVIS. Thank you.

Is there any other discussion?

Mr. WAXMAN. We also had questions from our side. I remember Mr. Lynch asked some questions and had a promise he would get the information. So I hope we will get that as well.

Chairman TOM DAVIS. Well, why don't we make sure that staff includes that in our discussion, Mr. Waxman, as we move ahead and get it sent to the Department of Defense?

As I said before, Members will have 5 legislative days to submit opening statements.

We move forward to our first panel now. We are pleased to have the Honorable David M. Walker.

This means no votes, to committee members. You are certainly encouraged to stay here for the testimony and questions, but you won't be needed for a vote.

Thank you, Mr. Waxman.

The Honorable David M. Walker, Comptroller General of the United States, accompanied by Mr. William T. Woods, Director, Acquisition and Sourcing Management, U.S. General Accounting Office, and Mr. Neal Curtin, the Director of Defense Capabilities and Management, U.S. General Accounting Office.

As you know, it is our policy that we swear all witnesses.

Mr. OSE. Mr. Chairman, if I may.

Chairman TOM DAVIS. Yes, gentleman from California.

Mr. OSE. I noticed in the context of your conversation with Mr. Waxman that you were issuing invitations to the July hearing to the president of a couple of companies. Are those same invitations going to the leadership of the other companies who are engaged in contracting?

Chairman TOM DAVIS. Well, there are literally hundreds, if not thousands, of companies.

Mr. OSE. Well, I am particularly interested in the companies Parini, UBS, and Washington Group.

Chairman TOM DAVIS. Well, if the gentleman would work with us on that, we will see if we can accommodate his request. Would the gentleman agree to work with us on that?

Mr. OSE. I would be happy to work with you.

Chairman TOM DAVIS. All right, thank you.

[Witnesses sworn.]

Chairman TOM DAVIS. Mr. Walker, thanks for being with us and thanks for the good staff work you continue to do to shed some light on these issues. The issue of a report I know is sometimes subject to various interpretations, but we look to you here for guidance on these matters, and thanks for being with us.

STATEMENTS OF DAVID M. WALKER, COMPTROLLER GENERAL OF THE UNITED STATES, ACCOMPANIED BY WILLIAM T. WOODS, DIRECTOR, ACQUISITION AND SOURCING MANAGEMENT, U.S. GENERAL ACCOUNTING OFFICE, AND NEAL P. CURTIN, DIRECTOR, DEFENSE CAPABILITIES AND MANAGEMENT, U.S. GENERAL ACCOUNTING OFFICE

Mr. WALKER. Thank you, Mr. Chairman, Ranking Minority Member Waxman, other members of the committee. It is a pleasure to be back before you here to discuss various GAO activities dealing with operations and rebuilding efforts in Iraq.

I would like to summarize my statement. I believe all of you have been provided with the entire statement for the record, and hopefully all of you have also been provided a copy of the report that was released yesterday entitled, "Rebuilding Iraq: Fiscal Year 2003 Contract Award Procedures and Management Challenges." My testimony will address a summary of this report, as well as our work to date on various logistical support contracts on a global basis involving all four services.

Before I discuss our findings, I would like to briefly touch upon the scope of these two efforts. First, given the widespread congressional interest in ensuring that Iraq reconstruction efforts are awarded properly and administered effectively, we initiated this review under my authority, meaning the review that I am referring to here, the report that was issued yesterday. Specifically, we judgmentally selected 25 fiscal year 2003 contract actions. These 25 contract actions represented about 97 percent of the nearly $3.7 billion that have been obligated for Iraqi reconstruction through September 30, 2003. We are currently working on looking at 2004 contracting activity.

With regard to our work on the military's use of global logistic support contracts, this work was initiated at the request of Ranking Minority Member Waxman of this committee and the ranking minority member of the Energy and Commerce Committee, Mr. Dingell. It is one of a series of studies we have done on the military's use of private contractor support deployed forces on a global basis. Importantly, we looked at this on a global basis; we look at it for all the services, and we did not target any particular region or any particular company.

With regard of the award of fiscal 2003 Iraqi reconstruction contracts, we found that agencies generally complied with applicable laws and regulations governing competition when using sole-source or limited competition approaches to award new contracts. However, they did not always do so when issuing task orders under existing contracts. In several instances we found that contracting officers issued task orders for work that was not within the scope of the underlying contracts. The out-of-scope work under these orders should have been awarded using competitive procedures or, be-

cause of the circumstances involved, supported by justification for other than full and open competition in accordance with applicable legal requirements. In this regard, given the needs relating to and the challenges associated with the Iraqi reconstruction efforts, such justifications are likely possible, but needed to be made and documented in order to comply with the law and to protect taxpayer interest.

We made several recommendations to the Secretary of the Army and the Secretary of the Defense with regard to the lessons learned in this report, and I am pleased to say that DOD has generally concurred with our recommendations and plans to take actions based on our recommendations.

With regard to DOD's use of global logistic support contracts, we found mixed results in each of four critical areas that we reviewed, namely, planning, oversight, efficiency, and personnel matters. For example, we found that some DOD customers planned quite well for the use of contracts, following service institutions and including the contractor early in planning. Conversely, we found the use of the LOGCAP contract in Kuwait and Iraq was not adequately planned, nor was it planned in accordance with applicable Army guidance.

We also found that while oversight processes were in place and functioning well in some places, there were several areas needing improvement, such as reaching an agreement on terms, specifications, and prices of services to be delivered. This is especially critical in connection with cost-based contracts.

We also found that while some military commands actively looked for ways to save money, others exhibited little concern for cost considerations.

Finally, shortages in personnel trained in contract management and oversight is also an issue of critical importance that needs to be addressed. Our report will make a number of recommendations when it is issued later this summer in this regard.

In summary, Mr. Chairman, Ranking Member Waxman, and members of the committee, the United States, along with its coalition partners and various international organizations and donors, has undertaken an enormously complex, costly, and challenging effort to rebuild Iraq in an unstable security environment. At the early stage of these efforts, agency procurement officials were confronted with little advance warning on which to plan and execute competitive procurement actions. An urgent need existed to begin reconstruction efforts quickly, and the uncertainty as the magnitude in terms of the work required was evident.

Their actions in large part reflected proper use of the flexibilities provided under existing procurement laws and regulations to award new contracts using other than full and open competitive procedures. However, with respect to several task orders issued under existing contracts, some agency officials overstepped the latitude provided by competition laws by ordering work outside the scope of the underlying contracts. This work should have been separately competed or, alternatively, justified and approved at the required official level for performance by an existing contractor. Importantly, given the war in Iraq, the urgent need for reconstruction efforts, and the latitude allowed by the competition law, these task

orders reasonably could have been supported by justifications for other than full and open competition.

Logistic support contracts have developed into a useful tool for the military services to quickly obtain needed support for troops deployed to trouble spots around the world. Because of the nature of these contracts, however, that is, a cost-based contract arrangement, they require adequate planning and definitions of related requirements, as well as significant ongoing and active oversight by a variety of parties in order to make sure that they are meeting the needs of the forces in the most economic, efficient, and effective way possible under the circumstances.

While the military services are using how to use these contracts well, in many cases the services are still not achieving the most cost-effective performance and are not adequately learning and applying the lessons of previous deployments. Because of the military's continuing and growing alliance on these contract vehicles, it is important that improvements be made in the planning and execution of these arrangements, and that related oversight be strengthened.

I might note, Mr. Chairman, finally, that DOD contract management has been on GAO's high risk since 1992. There is a good reason for it: there are serious problems. They still exist. They are exacerbated in a wartime climate, and it is important that we continue to make progress to address these longstanding problems.

Thank you, Mr. Chairman.

[The prepared statement of Mr. Walker follows:]

United States General Accounting Office

GAO

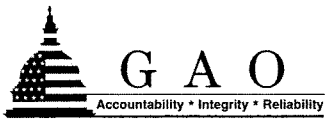
Testimony
Before the Committee on Government Reform, House of Representatives

For Release on Delivery
Expected at 11:00 a.m. EDT
June 15, 2004

CONTRACT MANAGEMENT

Contracting for Iraqi Reconstruction and for Global Logistics Support

Statement of David M. Walker
Comptroller General of the United States



GAO-04-869T

Chairman Davis, Ranking Member Waxman, and Members of the Committee:

I appreciate the opportunity to be with you today to discuss some of the work the General Accounting Office (GAO) is undertaking to address various operations and rebuilding efforts in Iraq. Specifically, GAO has a body of ongoing work looking at a range of issues involving Iraq, including Iraq's transitional administrative law, efforts to restore essential services to the Iraqi people, and the effectiveness of logistics activities during Operation Iraqi Freedom, among others. Importantly, given the challenging security environment in Iraq and the various other accountability organizations involved in the oversight process, we are attempting to coordinate our engagement planning and execution with other organizations as appropriate.

Today, I would like to discuss (1) our report that we released yesterday on the contract award procedures for contracts awarded in fiscal year 2003 to help rebuild Iraq[1] and (2) our preliminary findings on the military's use of global logistics support contracts. These support contracts have emerged as important tools in providing deployed military services with a wide range of logistics services.

Before I discuss our findings, I would like to briefly touch upon the scope of these two efforts. First, given the widespread congressional interest in ensuring that Iraq reconstruction contracts are awarded properly and administered effectively, we initiated a review under my authority that focused on reconstruction-related contract actions by the Department of Defense (DOD) (primarily the U.S. Army, including the Army Corps of Engineers), the U.S. Agency for International Development (USAID), and the Department of State. Specifically, we judgmentally selected 25 fiscal year 2003 contract actions, consisting of 14 new contracts awarded using other than full and open competition and 11 task orders issued under existing contracts. These 25 contract actions represented about 97 percent of the nearly $3.7 billion that had been obligated for Iraqi reconstruction through September 30, 2003. We conducted this work between May 2003 and April 2004 in accordance with generally accepted government auditing standards.

[1] See U.S. General Accounting Office, *Rebuilding Iraq: Fiscal Year 2003 Contract Award Procedures and Management Challenges*, GAO-04-605 (Washington, D.C.: June 1, 2004).

Second, our work on the military's use of global logistics support contracts, initiated at the request of the Ranking Members of this committee and the House Committee on Energy and Commerce, is one of a series of studies we have done on the military's use of private contractors to support deployed forces.[2] This work looks broadly across each of the services and includes four contracts: (1) the Army's Logistics Civil Augmentation Program (LOGCAP) contract; (2) the Air Force's Contract Augmentation Program (AFCAP) contract; (3) the U.S. Army, Europe's Balkan Support Contract (BSC); and (4) the Navy's Construction Capabilities (CONCAP) contract. We have completed our fieldwork and are now drafting our report, which we expect to publish this summer. In performing our work, we examined a wide range of contract documents and contracting guidance and met with contracting officers, contract customers, and the contractors to gain a comprehensive understanding of the contracts, the contract management process, and the issues related to using these contracts. We conducted this work between August 2003 and June 2004 in accordance with generally accepted government auditing standards.

Summary

With regard to the award of fiscal year 2003 Iraq reconstruction contracts, we found that agencies generally complied with applicable laws and regulations governing competition when using sole-source or limited competition approaches to award new contracts. However, they did not always do so when issuing task orders under existing contracts. In several instances, we found that contracting officers issued task orders for work that was not within the scope of the underlying contracts. The out-of-scope work under these orders should have been awarded using competitive procedures or, because of the exigent circumstances involved, supported by a justification for other than full and open competition in accordance with legal requirements. In this regard, given the needs relating to and the challenges associated with Iraq reconstruction efforts, such justifications were likely possible but needed to be made and documented to comply

[2] See, for example, U.S. General Accounting Office, *Contingency Operations: Opportunities to Improve the Logistics Civil Augmentation Program.* GAO/NSIAD-97-63 (Washington, D.C.: Feb. 11, 1997); U.S. General Accounting Office, *Contingency Operations: Army Should Do More to Control Contract Cost in the Balkans.* GAO/NSIAD-00-225 (Washington, D.C.: Sept. 29, 2000); and U.S. General Accounting Office, *Military Operations: Contractors Provide Vital Services to Deployed Forces But Are Not Adequately Addressed in DOD Plans,* GAO-03-695 (Washington, D.C.: June 24, 2003).

with the law and protect the taxpayer's interests. We made several recommendations to the Secretary of the Army, including reviewing out-of-scope task orders to address outstanding issues and take appropriate actions, as necessary. We also recommended that the Secretary of Defense evaluate the lessons learned in Iraq and develop a strategy for assuring that adequate acquisition staff and other resources can be made available in a timely manner. DOD generally concurred with our recommendations.

With regard to DOD's use of global logistics support contracts, we found mixed results in each of the four areas we reviewed: planning, oversight, efficiency, and personnel. For example, we found that some DOD customers planned quite well for the use of the contracts, following service instructions and including the contractor early in planning. Conversely, we found that the use of the LOGCAP contract in Kuwait and Iraq was not adequately planned, nor was it planned in accordance with applicable Army guidance. Given the lack of early and adequate planning and contractor involvement, two key ingredients needed to maximize LOGCAP support and minimize cost—a comprehensive statement of work and early contractor involvement—were missing. We also found that while oversight processes were in place and functioning well in some places, there were several areas needing improvement, such as in reaching agreement on terms, specifications and prices of services to be delivered. We also found that while some military commands actively looked for ways to save money, others exhibited little concern for cost considerations. Finally, shortages in personnel trained in contract management and oversight is also an issue that needs to be addressed. Our report will make a number of recommendations to address these shortcomings.

Compliance with Competition Requirements

We found that the agencies responsible for rebuilding Iraq generally complied with applicable requirements governing competition when awarding new reconstruction contracts in fiscal year 2003. While the Competition in Contracting Act of 1984 requires that federal contracts be awarded on the basis of full and open competition, the law and implementing regulations recognize that there may be circumstances under which full and open competition would be impracticable, such as when contracts need to be awarded quickly to respond to unforeseen and urgent needs or when there is only one

source for the required product or service. In such cases, agencies are given authority by law to award contracts under limited competition or on a sole-source basis, provided that the proposed actions are appropriately justified and approved.

We reviewed 14 new contracts that were awarded in fiscal year 2003 using other than full and open competition: a total of 5 sole-source contracts awarded by the Army Corps of Engineers, the Army Field Support Command, and USAID; and 9 limited competition contracts awarded by the Department of State, the Army Contracting Agency, and USAID. For 13 of these new contracts, agency officials adequately justified their decisions and complied with the statutory and regulatory competition requirements. For example, USAID officials awarded seven contracts under limited competition and two sole-source contracts citing an exception to the competition requirements that was provided for under the Federal Property and Administrative Services Act.[3] USIAD concluded that the use of standard competitive procedures would not enable it to put in place foreign aid programs and activities for Iraq in a timely manner. We found that USAID's justification and approval documentation supporting the award of these contracts complied with applicable requirements. As I will shortly discuss in more detail, we also found that the Army Corps of Engineers properly justified the award of a sole-source contract to restore Iraq's oil infrastructure. In one case, however, the Department of State justified and approved the use of limited competition under a unique authority that, in our opinion, may not be a recognized exception to the competition requirements. At the same time, State took steps to obtain some competition by inviting offers from four firms. In addition, it is likely that State could have justified and approved its limited competition under recognized exceptions to the competition requirements.

With respect to issuing a task order under an existing contract, the competition law does not require competition beyond that obtained for the initial contract award,[4] provided the task order does not increase the scope of the work, period of performance, or maximum value of the contract under which the order is issued. The scope, period, or maximum value may be increased only by modification of the contract, and competitive procedures

[3] The Act's authority for waiving competitive contracting procedures that would impair foreign aid programs was recently recodified and enacted into positive law (40 U.S.C. § 113(e)).
[4] If more than one contractor was awarded a contract, however, then all the contractors are required to be provided a fair opportunity to be considered for the task order.

are required to be used for any such increase unless an authorized exception applies. As we noted in our report released yesterday, determining whether work is within the scope of an existing task order contract is primarily an issue of contract interpretation and judgment by the contracting officer.

We found several compliance problems when agencies issued task orders under existing contracts. Specifically, of the 11 task orders we reviewed, 7 were, in whole or part, not within scope. For example, the Defense Contracting Command-Washington (DCC-W)[5] improperly used a General Services Administration (GSA) schedule contract to issue two task orders to the Science Applications International Corporation with a combined value of over $107 million for work that was outside the scope of the schedule contract. One order involved developing a news media capability—including radio and television programming and broadcasting—in Iraq. The other required the contractor to recruit people identified by DOD as subject matter experts, enter into subcontracts with them, and provide them with travel and logistical support within the United States and Iraq. The GSA schedule contract, however, was for management, organizational, and business improvement services for federal agencies. In our view, the statements of work for both task orders were outside the scope of the schedule contract.

Another example of an agency issuing a task order that was outside the scope of the underlying contract involved the Army Field Support Command's $1.9 million task order for contingency planning for the Iraqi oil infrastructure mission under the LOGCAP contract with Kellogg Brown & Root.[6] This task order, issued in November 2002, required the contractor to develop a plan to repair and restore Iraq's oil infrastructure should Iraqi forces damage or destroy it. Because the contractor was knowledgeable about the U.S. Central Command's planning for conducting military operations, DOD officials determined that the contractor was uniquely positioned to develop the contingency support plan. DOD also determined that developing the contingency plan was within the scope of the overall LOGCAP contract. We have concluded, however, that preparation of the contingency support plan for this specific mission (i.e. restoring Iraq's

[5] DCC-W, a division within the office of the Administrative Assistant to the Secretary of the Army, provides administrative support, including contracting support, to DOD components located in the National Capital Region.
[6] The LOGCAP contract, which was competitively awarded in 2001, requires the contractor to provide the Army and other entities with planning and a broad range of logistics services in wartime and other operations. The Army has used LOGCAP to support both military operations and reconstruction efforts in Iraq.

oil infrastructure) was beyond the scope of the contract. Specifically, we read the LOGCAP statement of work as providing for contingency planning only when the execution of the mission involved is within the scope of the contract. In this regard, all parties—including GAO and DOD—agree that repairing Iraq's oil infrastructure would not have been within the scope of the LOGCAP contract. Consequently, we concluded that planning the oil infrastructure restoration was also not within the scope of the contract. The Army Field Support Command should have prepared a written justification to authorize the work without competition. In light of the exigent circumstances, such a justification was likely possible but needed to be made and documented to comply with the law and protect the taxpayer's interests.

DOD planners believed early on that issuance of this task order would result in Kellogg Brown & Root being uniquely qualified to initially execute the plan for restoring the Iraqi oil infrastructure, the so-called "RIO contract." Subsequently, the RIO contract was awarded in March 2003 to Kellogg Brown & Root.[7] The contracting officer's written justification for the sole-source contract outlined the rationale for the decision.[8] The justification was approved by the Army's senior procurement executive, as required. We reviewed the justification and approval documentation and determined that it generally complied with applicable legal standards.

We made several recommendations to the Secretary of the Army to review out-of-scope task orders to address outstanding issues and take appropriate actions, as necessary. DOD generally concurred with the recommendations and noted that it was in the process of taking corrective actions. DOD also agreed with our recommendation that the Secretary of Defense evaluate the lessons learned in Iraq and develop a strategy for assuring that adequate acquisition staff and other resources can be made available in a timely manner.

[7] According to the Army Corps of Engineers, more than $2.5 billion had been obligated on the contract as of May 2004.
[8] As we reported, DOD concluded that there was only one source with the capability to perform emergency repairs to the oil infrastructure given (1) the classified nature of the planning efforts, (2) the contractor's role in those efforts, and (3) the imminent commencement of hostilities.

DOD's Use of Logistics Support Contracts

I will now turn to discussing our ongoing work on DOD's use of global logistics support contracts. As I previously noted, we looked at four such contracts, which have been used by all the military services to provide a wide array of services, including operating dining facilities and providing housing, in more than half a dozen countries, including Iraq, Kuwait, and Afghanistan. In total, the estimated value of the work under the current contracts is $12 billion, including $5.6 billion for work in Iraq through May 2004. Before summarizing our preliminary findings, let me first make an overall observation about the vital services that these types of contracts provide. The contractors and the military services have, for the most part, worked together to meet military commanders' needs, sometimes in very hazardous or difficult circumstances. For example, the LOGCAP contract is providing life and logistics support to more than 165,000 soldiers and civilians under difficult security circumstances in Iraq, Afghanistan, Kuwait, and Djibouti, and customers told us they are generally pleased with the service the contractor is providing. The AFCAP contractor is providing air traffic management at air bases throughout central Asia, supplementing scarce Air Force assets and providing needed rest for Air Force service members who also perform this function. Using the CONCAP contract, the Navy has constructed detainee facilities (including a maximum security prison) at Guantanamo Bay on time and within budget. Projects at Guantanamo have increased the safety of both the detainees and the U.S. forces guarding them and resulted in real savings in reduced personnel tempo. Finally, the BSC continues to provide a myriad of high quality services to troops in Kosovo and Bosnia, and the customer works with the contractor to identify costs savings.

Within this overall context, we found mixed results in each of the four areas we reviewed—planning, oversight, efficiency and personnel—with variations occurring among the four contracts and among the various commands using them. Our report, which will be issued later this year, will make a number of recommendations to address the shortcomings we identified in these areas.

Planning

In assessing DOD's planning, we found that some customers planned quite well for the use of the contracts, following service guidance and including the contractor early in planning. For example, in planning for Operation Iraqi Freedom, U.S. Army, Europe, was tasked with supporting the anticipated movement of troops through Turkey into Iraq, and our review of that planning showed that the command followed applicable Army guidance to good effect. In October 2002, the command brought contractor personnel to its headquarters in Europe to help plan and develop the statement of work. According to a briefing provided by U.S. Army, Europe, contractor planners brought considerable knowledge of contractor capabilities, limitations, and operations, and their involvement early in the planning efforts increased understanding of the requirements and capabilities, facilitated communication regarding the statement of work, and enhanced mission completion.

Conversely, we found that the use of LOGCAP in Kuwait and Iraq was not adequately planned, nor was it planned in accordance with applicable Army guidance. Given the lack of early and adequate planning and contractor involvement, two key ingredients needed to maximize LOGCAP support and minimize cost—a comprehensive statement of work and early contractor involvement—were missing. Specifically:

- A plan to support the troops in Iraq was developed in May 2003, but was not comprehensive because the contractor was not involved in the early planning and it did not include all of the dining facilities, troop housing, and other services that the Army has since added to the task order. According to an official from the 101st Airborne Division, there was a lack of detailed planning for the use of LOGCAP at the theater and division levels for the sustainment phase of the operation. He added that Army planners should develop a closer working relationship with the divisions and the contractor.

- Task orders were frequently revised. These revisions generated a significant amount of rework for the contractor and the contracting officers. Additionally, time spent reviewing revisions to the task orders is time that is not available for other oversight activities. While operational considerations may have driven some of these changes,

we believe others were more likely to have resulted from ineffective planning. For example, the task order supporting the troops in Iraq was revised 7 times in less than 1 year. Frequent revisions have not been limited to this task order. Task order 27, which provides support to U.S troops in Kuwait (estimated value of $426 million as of May 2004), was changed 18 times between September 2002 and December 2003, including 5 changes in one month, some on consecutive days. As of May 11, 2004, the contracting office, DCMA, and the contractor had processed more than 176 modifications to LOGCAP task orders.

Contract Oversight

In some cases, we found that contract oversight processes were in place and functioning well. For example, the Defense Contract Management Agency (DCMA) had principal oversight responsibility for the LOGCAP and AFCAP contracts and the BSC,[9] and DCMA generally provided good overall contract oversight, although we found some examples where it could have improved its performance. For example:

- Effective oversight of the diverse functions performed under the contracts requires government personnel with knowledge and expertise in these specific areas. DCMA contract administrators are contracting professionals, but many have limited knowledge of field operations. In these situations, DCMA normally uses contracting officer's technical representatives. Contracting officer's technical representatives are customers who have been designated by their units and appointed and trained by the administrative contracting officer. They provide technical oversight of the contractor's performance. We found that DCMA had not appointed these representatives at all major sites in Iraq. Officials at the 101st Airborne Division, for example, told us that they had no contracting officer's technical representatives during their year in Iraq, even though the division used LOGCAP services extensively.

- For task orders executed in southwest Asia, the AFCAP procuring contracting officer delegated the property administration responsibility to DCMA administrative contracting officers. However, contract administrators in southwest Asia did not

[9] While oversight of a contract is the responsibility of the contracting officer, the contracting officer may delegate some oversight responsibilities to DCMA.

ensure that the contractor had established and maintained a property control system to track items acquired under the contract. In addition, DCMA contracting officers in southwest Asia did not have a system in place to document what the contractor was procuring in support of AFCAP task orders and what was being turned over to the Air Force. As a result, as of April 2004, neither DCMA nor the Air Force could account for approximately $2 million worth of tools and construction equipment purchased through the AFCAP contract.

An important element of contract administration is the definitizing of task orders, that is, reaching agreement with the contractor on the terms, specifications, or price of services to be delivered. All of the contracts included in our review were cost-plus award fee contracts. These contracts allow the contractor to be reimbursed for reasonable, allowable, and allocable costs incurred to the extent prescribed by the contract and provide financial incentives based on performance. Cost-plus award fee contracts allow the government to evaluate a contractor's performance according to specified criteria and to grant an award amount within designated parameters. Award fees can serve as a valuable tool to help control program risk and encourage excellence in contract performance. To reap the advantages that cost-plus award fee contracts offer, the government must implement an effective award fee process. Any delays in definitizing task orders, however, make cost-control incentives in these award fee contracts less effective as a cost control tool since there is less work remaining to be accomplished and therefore less costs to be controlled by the contractor.

While we found that AFCAP and BSC task orders were definitized quickly, and CONCAP task orders do not require definitization since the terms, specifications, and price are agreed to before work begins, we also found that many LOGCAP task orders remain undefinitized for months, and sometimes more than a year, after they were due to be completed and after billions of dollars of work had been completed. Because task orders have not been definitized, LOGCAP contracting personnel have not conducted an award fee board. I would like to note, however, that this condition is not limited to the LOGCAP contract. We stated in our report released yesterday that the Army Corps of Engineers has yet to definitize its March 2003 contract to rebuild Iraq's oil infrastructure or one of its contracts to rebuild Iraq's electrical infrastructure and recommended that the

undefinitized contracts and task orders be definitized as soon as possible. DOD agreed with this recommendation and identified a number of steps being taken to do so.

Economy and Efficiency

We again found mixed results in evaluating the attention to economy and efficiency in the use of contracts. In some cases, we saw military commands actively looking for ways to save money in the contracts. For example, U.S. Army, Europe, reported savings of approximately $200 million under the BSC by reducing labor costs, by reducing services, and by closing or downsizing camps that were no longer needed. The $200 million is almost 10 percent of the current contract ceiling price of $2.098 billion. In addition to these savings, U.S. Army, Europe, routinely sends in teams of auditors from its internal review group to review practices and to make recommendations to improve economy and efficiency. In others, however, most notably the LOGCAP contract in Iraq and Kuwait, we saw very little concern for cost considerations. It was not until December 2003, for example, that the Army instructed commands to look for ways to economize on the use of this contract. Similarly, we found that the Air Force did not always select the most economical and efficient method to obtain services. It used the AFCAP contract to supply commodities for its heavy construction squadrons, although use of the contract to procure and deliver commodity supplies required that the Air Force pay the contractor's costs plus an additional award fee. Air Force officials said that they used AFCAP because not enough contracting and finance personnel were deployed to buy materials quickly or in large quantities. AFCAP program managers have recognized that the use of a cost-plus award fee contract to buy commodities may not be the most cost-effective method and said that the next version of the contract may allow for either firm-fixed prices or cost-plus fixed fee procurements for commodity purchases.

Personnel and Training

We found that shortages of personnel have also made contract oversight difficult. For example, while DCMA has deployed contracting officers to several countries throughout southwest and central Asia and the Balkans to provide on-site contract administration, DCMA officials believe that additional resources are needed to effectively support the LOGCAP and AFCAP contracts. Administrative contracting officers in Iraq, for example,

have been overwhelmed with their duties as a result of the expanding scope of some of the task orders. Additionally, some Army and Air Force personnel with oversight responsibilities did not receive the training necessary to effectively accomplish their jobs. Finally, we found that military units receiving services from the contracts generally lacked a comprehensive understanding of their contract roles and responsibilities. For example, commanders did not understand the part they played in establishing task order requirements, nor did they fully understand the level of support required by the contractors.

Concluding Observations

In conclusion, Mr. Chairman, the United States, along with its coalition partners and various international organizations and donors, has undertaken an enormously complex, costly, and challenging effort to rebuild Iraq in an unstable security environment. At the early stages of these efforts, agency procurement officials were confronted with little advance warning on which to plan and execute competitive procurement actions, an urgent need to begin reconstruction efforts quickly, and uncertainty as to the magnitude and term of work required. Their actions, in large part, reflected proper use of the flexibilities provided under procurement laws and regulations to award new contracts using other than full and open competitive procedures.

With respect to several task orders issued under existing contracts, however, some agency officials overstepped the latitude provided by competition laws by ordering work outside the scope of the underlying contracts. This work should have been separately competed, or justified and approved at the required official level for performance by the existing contractor. Importantly, given the war in Iraq, the urgent need for reconstruction efforts, and the latitude allowed by the competition law, these task orders reasonably could have been supported by justifications for other than full and open competition.

Logistics support contracts have developed into a useful tool for the military services to quickly obtain needed support for troops deployed to trouble spots around the world. Because of the nature of these contracts, however—that is, cost-plus award fee contracts—they require significant government oversight to make sure they are meeting needs in the most economic and efficient way possible in each circumstance. While the

military services are learning how to use these contracts well, in many cases the services are still not achieving the most cost-effective performance and are not adequately learning and applying the lessons of previous deployments. Because of the military's continuing and growing reliance on these contracting vehicles, it is important that improvements be made and that oversight be strengthened.

Mr. Chairman and Members of the committee, this concludes my statement. I will be happy to answer any question you may have.

Contact and Acknowledgment

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Chairman TOM DAVIS. Thank you very much.

Mr. Waxman, I think by agreement, I am going to yield 15 minutes to you for questions, and then we will go with 15, and then we will go to the 5 minute rule.

Mr. WAXMAN. Thank you very much, Mr. Chairman.

Mr. Walker, on the Army's LOGCAP global logistics contract, your team examined several important issues, including planning, cost and efficiency, oversight, and training. And as I read your testimony and heard what you had to say, you found significant problems with each in Iraq, and I want to walk you through some of these findings.

For a logistics contract, such as LOGCAP, to be effective and efficient, it is crucial that planning be done ahead of time. And in the case of Iraq, planning should have been done regarding the number of troops, their locations, how many meals they would need, how much water they would drink, and how much housing would be required in various locations.

Mr. Walker, you believe the Pentagon's prewar planning for LOGCAP was inadequate, is that correct?

Mr. WALKER. Our report finds that there were shortcomings with regard to the adequacy of planning for post-offensive operations. At the same point in time, I think we also have to look at the timeframes involved and try to understand that there wasn't a whole lot of time. But clearly planning was not as robust as it should have been or could have been.

Mr. WAXMAN. You said that the use of LOGCAP in Iraq was not planned in accordance with applicable Army guidance, is that accurate?

Mr. WALKER. That is my understanding.

Mr. Curtin, do you have anything to add on that?

Mr. CURTIN. Yes, sir, that is exactly right. The key issue is that the contractor needs to be involved early in the planning process under the Army guidance, and in this case the contractor was not involved at all until May 2003.

Mr. WAXMAN. Mr. Curtin, isn't it true that our soldiers were eating MREs, meals ready to eat, through August and living in tents because there hadn't been adequate prewar planning for dining facilities and housing?

Mr. CURTIN. Well, they were clearly living in tents and eating MREs. That can be partially attributed to a planning problem, but remember also the environment that you had was very unsettled. It is not clear how much preplanning could have avoided that, but it certainly would have helped the situation.

Mr. WAXMAN. It seems to me that there was actually far less planning for the safety, security, and welfare of our troops than for restoring and operating Iraq's oil infrastructure. Halliburton started planning for the oil infrastructure in November 2002, 5 months before the invasion. When did the planning for our troops begin under LOGCAP?

Mr. CURTIN. Well, the Task Order 59 under LOGCAP, which supports our forces in Iraq, was finally developed in May 2003, so that was after the actual military action, fairly late in the game, probably. But the problem we have even with that May 2003 plan is that it has been having to change so frequently that it was not

a very complete or comprehensive plan. There were nine changes to that task order.

Mr. WAXMAN. Why did planning for our troops wait until 6 months after the planning for Iraq oil?

Mr. CURTIN. I can't tell you; we never got a good answer to that. I don't know why it was done like that.

Mr. WAXMAN. Well, these priorities just don't make sense.

Chairman TOM DAVIS. I think it is important to note, Mr. Waxman, though, that the failure for them to do what they should have done with regard to the task orders doesn't mean that they weren't doing some planning. But clearly they were not nearly as far along as they should have been in many critical areas.

Mr. WAXMAN. Well, they spent months preparing for plans for Iraq's oil infrastructure; they had briefings at the highest levels of the administration. Substantial resources were being devoted to planning for the oil, yet there was little or no planning under LOGCAP to provide for the basic needs of our troops during the same timeframe. And with all due respect, our priority should be protecting the troops, not Iraq's oil.

I would like to ask you about cost control. This LOGCAP is a cost-plus contract, so Halliburton has its costs reimbursed and then receives an additional profit that is a percentage of its cost. Given the size of this contract, cost control is obviously crucial. Former Halliburton employees have come forward with information indicating that Halliburton made virtually no effort to control costs under LOGCAP in Kuwait and Iraq. For instance, they cited that brand new $85,000 trucks were being torched because of a flat tire and Halliburton subcontractors charged $100 per bag of laundry. More than one whistleblower has said that Halliburton managers told them not to worry about the price because it was all a cost-plus contract.

GAO observed a lack of concern for cost considerations among LOGCAP managers in Iraq after the invasion. What did you find specifically?

Mr. WALKER. I think it is important to note that these are cost-based contracts, and to try to clarify my understanding of how they work. And I would ask, if Neal or Bill have a clarification, to jump in.

First, that under these contracts, the contractors are reimbursed for their costs, which is full absorption costing. In other words, it is not just the direct cost, it is an overhead allocation and things of that nature. Second, they can receive a separate base fee, which is supposed to be based upon the estimated cost, not the actual cost, of what it would take in order to provide the services under the contract. And, third, they can receive an award fee or a success fee of up to a certain percentage based upon actual performance.

The fact of the matter is that in order for these types of arrangements to work effectively, you have to plan up front as to what the nature and scope of the activities are going to be; you need to estimate a reasonable cost, and the fees should be based upon those numbers. To this point in time, quite frankly, they still haven't fully negotiated what the nature and scope of services would be, what the estimated cost would be, and, therefore, we have a higher level of risk than we should at this time.

Last, I would say oversight is of critical importance as well.

Mr. WAXMAN. Well, Mr. Walker, your staff gave a briefing to our staff and they said in Operation Iraqi Freedom costs were not significant concern in LOGCAP management until late in 2003; there were no periodic reviews that had been conducted, which would be, for example, the validity of the requirements and that appropriate level of services; an award fee process was not in place for LOGCAP; and that Army plans June award fee board, which requires definitization of task orders. Is this accurate?

Mr. WALKER. There were serious planning and oversight problems.

Mr. CURTIN. You have described it very accurately.

Mr. WAXMAN. When our troops are in major combat operations and in need of support, cost can't be the primary concern. But after a while it should be an important concern, and I don't understand how there can be a debate about whether costs should be considered. The whole point of having a contractor do this work, instead of the military, is to reduce costs. I want to ask you about a specific example I mentioned in my opening statement.

In early 2003 there were was a Kuwaiti company called Tamimi. They had a contract with the Army to provide four dining facilities in Kuwait. In June 2003, Halliburton was given this work under the LOGCAP agreement, but they were instructed by the Army to use Tamimi, which was already there, as its subcontractor. And more recently the work was turned back over to Tamimi.

When the dining facilities were turned back over to Tamimi, what happened to the price of the meals?

Mr. WALKER. My understanding is the total cost on that contract declined dramatically.

Mr. CURTIN. About over 40 percent by having a direct contract with the local contractor versus going through LOGCAP.

Mr. WAXMAN. That doesn't sound to me like it was providing good value to the military. Certainly that is unfair to the taxpayers, to pay an extra 40 percent for the meals that had already been served by Tamimi before Halliburton got in to take its cut.

Mr. WALKER. Mr. Waxman, one of the things I think is important to note is you are correct that when you are in a wartime environment, there are certain issues other than cost that have to be considered, such as the safety and security of our troops. And in that regard, my son fought in Iraq as a captain in the Marine Corps, so I am very sensitive to that. At the same point in time, I think you rightfully point out that a lot of the services that we are talking about here aren't directly in support of the troops, or at least aren't in combat operations directly, and, therefore, we need to be concerned with cost. Cost does matter. At the same point in time, there has to be a balancing of various interests, I think, to make sure that we can accomplish our mission.

Mr. WAXMAN. You have said that the Army did not instruct commands to look for ways to control cost under LOGCAP until December 2003. Why did they wait until 9 months after the invasion?

Mr. CURTIN. I can address that one to some extent, at least. I think the order you are talking about came down from the Department of the Army in December 2003 when they realized that fiscal year 2004 funding was tight and they were spending in Kuwait and

Iraq at almost unsustainable rates. And they looked for dollar savings at that point, and that is what got them interested in dollar savings. And what we will be showing in our report is that when you look, when the Government looks for savings potential in these types of contracts, we almost always can find it; there are savings available if the Government provides the right kind of oversight.

Mr. WALKER. And a lot of it, Mr. Waxman, has to do with the nature and scope of services that are being provided, rather than necessarily the cost, per se, of those services. It can be both; both can result in savings.

Mr. WAXMAN. But as I understand what you are saying, Mr. Curtin, there was no interest in holding down costs until December 2003, so they went practically the whole year without thinking about those costs.

Mr. CURTIN. It was not a priority. We did not see the emphasis at all.

Mr. WAXMAN. Your team also stated that an award fee process was not in place for LOGCAP. How does this affect Halliburton's incentives to control costs?

Mr. WALKER. Well, my understanding is, again, the way that these cost-based contracts work is that the contractor is reimbursed for the direct cost, as well as an overhead allocation, so it is full absorption costing, which can affect their profitability, I might add, by being able to allocate part of your overhead expenses to the contract. Second, they receive a base fee, which is supposed to be based upon the estimated cost of the contract in order to provide some control and prevent abuse. Unfortunately, those haven't been defined fully yet. And, furthermore, they can receive an award fee of anywhere from zero up to a stated percent based upon actual performance based upon the individual facts and circumstances. And, again, those are supposed to be based upon the estimated cost, not the actual cost, in order to provide some type of checks and balances against potential abuse.

And I might also add that all costs that are reimbursed are supposed to be "reasonable costs," and, therefore, there is supposed to be not only a review by the contractor, but a review by DCMA and others to try to ascertain that in fact they are reasonable costs, because we shouldn't be paying somebody for something that is not reasonable or necessary.

Mr. WAXMAN. Well, let me ask you, in conclusion on my questioning, about oversight and training. Army material command has a LOGCAP support unit to advise military commanders on how to use the contract. Is it true that reservists who had never heard of the LOGCAP contracts were given only a 2-week training course before being sent to the Middle East to provide contracting advice to commanders?

Mr. CURTIN. Yes, sir, I can comment on that. The initial team that went over at the time of the conflict was actually a well trained unit that does that type of operation. But when replacements came through a few months into the occupation period, those troops were the ones that had not had the experience and had just the 2-week orientation type training. So what you saw was a real thin layer of oversight capability there; once the first unit was gone, you lost your capability.

Mr. WAXMAN. Well, were these reservists expected to prepare independent government cost estimates so that the Army would have its own numbers to compare to Halliburton's?

Mr. CURTIN. That is one of the functions they perform, yes.

Mr. WAXMAN. Shouldn't experienced contracting specialists be preparing these estimates?

Mr. CURTIN. It is clearly better for the Government if they are experienced.

Mr. WAXMAN. You also found that the Army approved a 6-month contract renewal worth $587 million in just 10 minutes and based this decision on just six pages of documentation. Is that correct?

Mr. CURTIN. Yes, sir. That was a meeting that my staff actually attended in Kuwait. In the press of business, the time available, the documentation was very thin and the time was limited; the committee was going through very different proposals, and they literally approved it in about 10 minutes.

Mr. WAXMAN. Well, Mr. Walker, your testimony helps put a lot of what we have learned in perspective, because individual Halliburton employees have described anecdotes of egregious waste, fraud, and abuse. The Pentagon auditors are going to testify today, and they are going to tell us about systemic problems with how Halliburton kept its books and submitted its bills. But you have looked at the big picture and tried to assess whether the administration has the management and training in place to oversee Halliburton's contracts and control costs, and what you are telling us is that we have a serious problem. Essentially, Halliburton was given a blank check by this administration and has run up enormous costs at taxpayers' expense.

I thank you very much for your testimony.

Chairman TOM DAVIS. Thank you, Mr. Waxman.

DOD has been on your watch list since 1992, is that correct?

Mr. WALKER. Contract management at DOD, correct, has been on our high risk list since 1992.

Chairman TOM DAVIS. I think that is important to point out. There has been a longstanding issue.

In terms of the flat tires and dumping the trucks, do you know what the military rules are on a convoy if there is a flat tire; do you know if they stop and change a tire there in the middle of a convoy, opening it up to an attack, or if the rules are to keep moving? Do you have any idea of that or should we ask the next panel?

Mr. WALKER. I think you should ask the next panel. I would imagine it would depend upon the security and environmental circumstances.

Chairman TOM DAVIS. So there may be some satisfactory explanations why you abandon a truck when you have a large convoy of people coming, as opposed to sitting there and changing it and then opening yourself up to an attack. We will get that on the next panel.

Did you find, in your review of this, and I think it is one of the largest reviews you have done, isn't it, of a contract?

Mr. WALKER. To date. We have many others underway.

Chairman TOM DAVIS. Did you find any evidence of fraud or abuse on the part of the LOGCAP contractor in Iraq?

Mr. WALKER. We have not tried to ascertain whether or not fraud was involved, because fraud involves willful intent. Let us just say that there are serious problems, but I wouldn't go to that point in time. We don't have any evidence to say that there was willful fraud based upon the work that we have done so far.

Chairman TOM DAVIS. Now, as I understand the way the contracting works in these areas, the contractor would get reimbursed only for reasonable, allocable, and allowable costs. And what so often happens in contracts, contractors will submit costs for reimbursement, but we have a catch-all system through the Defense Contract Audit Agency that will catch a lot of those and kick them back, is that correct, and say you are not getting reimbursed; you might have charged us for this, but we don't think it is reasonable? Did you find any evidence of DCAA stepping forward in this and doing their job?

Mr. WALKER. Well, there are a number of players that are on the field, not only the COTR and the DCMA, but also you can have subsequent audits by the DCAA, the Defense Contracting Audit Agency. Let us just say a lot of people are involved, but they are very stressed. There is absolutely no question that people are being asked to do a tremendous amount; they are trying to do the best they can with the resources and training that they have. But, frankly, the ratios we are talking about here, the volume is much greater, for example, than what was happening in the Balkans, and yet the number of people actively engaged on a ratio basis is much less. So I think there is clearly a challenge there.

Neal, anything you want to add?

Mr. CURTIN. No, the same thing. It is an interesting comparison. We were trying to get a handle in this work on what would be the right number of people to have in these oversight positions for this type of situation, and there really is no criteria for it; it is a judgment by the agencies as to how much they can afford based on all their other priorities. And you mentioned the Balkans comparison. The size of the contract in Iraq is about 15 times larger than what it was in the Balkans, but DCMA has only——

Chairman TOM DAVIS. And the casualty was much higher than that. The casualty rate much higher than it was in the Balkans on a percentage basis.

Mr. CURTIN. Absolutely.

Chairman TOM DAVIS. Which obviously, under those kind of stresses, you would expect to see more mistakes, wouldn't you, and people trying to get the job done, and costs probably wouldn't be the same kind of factors if you are sitting behind a desk?

Mr. CURTIN. Yes, sir.

Mr. WALKER. It is a much more difficult environment, there is no question about that.

Chairman TOM DAVIS. So you would expect mistakes to be made in order to accomplish the mission as a practical matter, wouldn't you?

Mr. WALKER. I would expect that mistakes would be made, but I also would expect that some of the checks and balances would hopefully correct some of those.

Chairman TOM DAVIS. Well, that is right. And that is why we have you and that is why you have DCAA and you have your con-

tracting officers' technical representative and people. Before the bills are actually paid, this goes through a lot of review, and we are part of that review process. But when you are out there in the battlefield trying to feed and clothe troops and the like, I think, as we found with the gasoline, the first thing you need to do is accomplish the mission. But along the way sometimes cost is the first casualty.

Mr. CURTIN. And it is interesting, too, because we have done work in the Balkans for a number of years, and what we have seen is a progression there. In the early years in Bosnia, it was a dangerous security situation and you saw some of the same problems. And we made a lot of recommendations back at the end of 2000 that have been taken to heart, and the Balkans contract, a similar type of logistic support contract, is actually working pretty well now; with a lot of oversight they have made a lot of improvements. We are right back where we were in the early days of the Balkans now in Iraq and Kuwait.

Chairman TOM DAVIS. Considering all the circumstances here, how do you view the overall performance of DOD and the other agencies involved?

Mr. WALKER. I wouldn't want to give them a grade. I would say this, Mr. Chairman, that planning is a serious problem; that oversight is a serious problem; that as has been the case for many years, contract management is a high risk area; as has been the case for many decades, DOD is an A+ on fighting and winning armed conflicts, but they are a D on economy, efficiency, transparency, and accountability. And I think one of the problems that we have here is for any system to work, including this type of system, you have to have incentives for people to do the right thing, adequate transparency to try to hopefully assure they do, and accountability if they don't. And I think it is particularly an acute problem when you are dealing with cost-based contracts, and I think we need to learn more of the lessons from the past and apply them more rigorously, those lessons learned, and I hope that they will do that.

Chairman TOM DAVIS. Particularly regarding the challenges with the LOGCAP contract in Iraq, do you have any assessment of whether the customers of LOGCAP, how they view the performance of the contractor?

Mr. WALKER. My understanding, and I would ask for Neal to jump in, is that most of the customers are satisfied, because most of the customers are looking from the standpoint of are they getting their services in a timely and acceptable manner.

Chairman TOM DAVIS. Which is the most important factor, isn't it?

Mr. WALKER. Well, it is clearly a critical important factor, but I do think cost is important.

Chairman TOM DAVIS. Well, I didn't say. I am just saying first of all you have to accomplish the mission, and at least in that sense this was fulfilled. We can argue about costs, and that is what we are here to go over, and hopefully we have enough checks and balances in the system that we will look that over, and a contractor who ignores that, it will be to their detriment.

Mr. WALKER. In the final analysis, Mr. Chairman, as you know, we face significant deficits, and to the extent that there is any waste, there is an opportunity cost associated with that.

Chairman TOM DAVIS. You stated, in connection with the task order that was issued under the LOGCAP contract to KBR for the planning efforts for the Iraqi oil infrastructure mission, that it was beyond the scope of the contract. I notice that in commenting on your report, that DOD does not agree with your conclusion on that. Given this disagreement, would you consider is it unusual or at all alarming that lawyers within DOD wouldn't agree with you on this issue, or is this commonplace, auditors versus lawyers on these kind of issues?

Mr. WALKER. My understanding is they agree with us on one issue and that there is a disagreement within the Department on another. The issue that they agree with us on is that the type of services that ultimately would have been provided under the all infrastructure program were not covered under the LOGCAP contract. So they agree with us on that. Where there is a disagreement, and I understand there is a difference of opinion within the Department of Defense, as to whether or not you could allow for planning under this contract that wasn't otherwise coverable by the LOGCAP contract itself. And in our view, we believe that you should not, that it was only anticipated that you would be able to provide for planning for services that could and would be rendered under the normal LOGCAP contract, and there is general agreement that these types of services would not be rendered under LOGCAP contract.

Is that correct, Bill?

Mr. WOODS. Can I jump in on that?

Mr. CURTIN. Sure.

Mr. WOODS. There was a disagreement within the Department, and as we point out in our report, these are issues of contract administration, these are issues of judgment, and these are issues where reasonable people can look at the same set of facts and come to different conclusions.

Chairman TOM DAVIS. As we see up here as well.

All right. Well, thank you very much. We have a vote on. What I will do is dismiss this panel and we will move to the second panel when we return here in about a half an hour. So I will recess right now.

Mr. WAXMAN. Mr. Chairman, let me just ask if they can wait around. I know we want to get on, but other Members may have questions. I just want to protect their rights.

So if you would wait here until we come back.

Chairman TOM DAVIS. Well, we will try to move as quickly as we can though if anybody comes back, we will talk on the floor; if not, I will move the next panel.

Mr. WALKER. Thank you, Mr. Chairman.

[Recess.]

Chairman TOM DAVIS. There's been a coup, and I am going to start. We are back in session. I think Mr. Waxman had the floor.

Mr. Davis, I am going to recognize you for 5 minutes, and then I will take some time.

Mr. DAVIS OF ILLINOIS. Thank you very much, Mr. Chairman.

Mr. Walker, how are you?

Mr. WALKER. Well. Thank you, Mr. Davis.

Mr. DAVIS OF ILLINOIS. Good.

GAO examined Halliburton's task order to prepare contingency plans for Iraq's oil infrastructure and Halliburton's sole source contract to implement those plans, and that is what I would like to talk about for a moment. It is my understanding that usually the military develops a requirement, and that requirement is turned over to Career Procurement Office, who figure out how to meet the need. Career civil servants than award a contract or issue a task order, preferably after competition. A key responsibility of the career procurement officials is to determine who should get the contract.

Mr. Walker, is that your understanding, that it is generally career civil servants, and not political appointees, that decide who gets a contract?

Mr. WALKER. That is my understanding. That is correct. The responsibility for awarding contracts and running the procurement process is typically done by career civil servants.

Mr. DAVIS OF ILLINOIS. Then if that is the case, it appears to me that very different procedures were used to award Halliburton's contingency plan and task order. Michael Mobbs, a special advisor to Under Secretary of Defense Douglas Fife, recently revealed that he made the decision to choose Halliburton. He selected Halliburton based on informal contacts with Government officials and retired corporate executives.

Do you think it is unusual for political appointees to select a contractor purely on the basis of informal conversations with Government officials and formal corporate executives, if that was the case?

Mr. WALKER. If that was the case, it would be unusual, if that was the case.

Mr. DAVIS OF ILLINOIS. Isn't the normal practice to have career procurement officials decide which company receives a task order or contract?

Mr. WALKER. My understanding is that is the normal course. As we said, typically, contracts are awarded by career civil servants.

Mr. DAVIS OF ILLINOIS. It is also my understanding that the White House usually stays out of procurement decisions and is not given the opportunity to influence those decisions. Is that the understanding?

Mr. WALKER. That is also correct, sir.

Mr. DAVIS OF ILLINOIS. The administration certainly has claimed that there were absolutely no contacts between the Vice President's office and the officials who awarded the contracts to Halliburton; however, this appears to be inaccurate. According to Mr. Mobbs, in October 2003, he presented his conclusion that Halliburton should be awarded the task order to the Deputy's Committee, a group of senior level Government officials that included Scooter Libby, the Vice President's chief of staff, in order to give them an opportunity to veto his plan on political grounds.

Do you think it is unusual for Defense Department officials to give political appointees an opportunity to veto procurement decisions on the basis of political sensitivity?

Mr. WOODS. Can I? Do you mind?

We have not spoken with Mr. Mobbs in connection with the description of events that you just outlined. We did come across, in the course of our review, a classified memorandum for the record that was authored by Mr. Mobbs that outlined the rationale that went into the selection, the course of events that they decided to take in regard to the contingency task order. That memorandum, for the record, recognized, and we reported in our recently released report, that once they made the decision to go with a particular contractor for the contingency planning task order, that would pretty much decide who would eventually get the larger contract to actually execute the contingency plan.

Mr. DAVIS OF ILLINOIS. I guess the bottom line question then becomes are there instances where political sensitivities are deemed appropriate when making a selection or a decision, even though this might be outside the normal range or the normal process that is used?

Mr. WALKER. I think the bottom line is that when you are making contacting decisions, they should not be made for political reasons. And we don't have any reason to believe that was the case here. I think it is important to understand that it depends upon the timing and the nature of the communications. There could be communications, but were those communications FYI in anticipation of the fact that there could be significant press interest and activity as a result of the decisions, or was it more than FYI? And that is the key; what were the nature and extent of the communications. Merely that there were communications doesn't necessarily mean there is a problem, per se.

Chairman TOM DAVIS. Thank you. The gentleman's time has expired.

I would just note that sometimes congressional offices are notified of contracts before they are announced. We have no say in who gets this contract, but we are given a heads up if it is a contractor in our district. And that has been fairly routine since before I came here.

Let me just ask a question before I give Mr. Souder his 5 minutes.

Is there any evidence that the White House played any role in this decision?

Mr. WALKER. We have not tried to conduct an investigation as to whether or to what extent.

Chairman TOM DAVIS. You didn't find any evidence that they did, did you?

Mr. WALKER. No. And that was beyond the scope of what we tried to do.

Chairman TOM DAVIS. But you didn't undercover anything, in the course of talking to anyone, that would have indicated that?

Mr. WALKER. We have come across the document that Bill mentioned. We have come across one email, but, again, the nature of the documents that we have come across are more from the standpoint of FYI, this is going to happen.

Mr. WOODS. That is correct.

Chairman TOM DAVIS. You didn't see anything in the documents, and I think it is the same documents that Mr. Davis had, that indi-

cated do you approve of this or anything like that, it was more this is what is happening?

Mr. WOODS. That is correct, sir.

Chairman TOM DAVIS. Thank you very much.

Mr. Souder, you are recognized for 5 minutes.

Mr. SOUDER. Thank you. And I wanted to basically make some opening comments that we weren't able to do at the beginning, through the chairman's agreement, and also respond to a couple of things that have occurred, as somebody who has been a member of this committee for some time.

One, I wanted to reiterate what Chairman Davis said about mission first. And certainly at the beginning of a mission and when the danger is greatest, the mission is especially first, and cost second. I thought that the statement from Mr. Curtin about the Balkans was very informative. In other words, they saw the same problems in the earliest stages when there was the greatest danger to the troops, and then you come in and you try to clean it up as best as possible. But when you are pushing for security and speed, that you have a slightly different goal at the beginning of a battle than you do at the end.

I also want to share my frustration with the administration's lack of general responsiveness to documents to this committee. I think every subcommittee chairman has been frustrated with this administration and the lack of responsiveness, and you can see that today. On the other hand, we are not doing fishing expeditions; we are not doing political control. We are actually an oversight committee that is trying to get that information. And I agree with the statement of Mr. Walker that the Defense Department has had this problem—I was elected in 1994—certainly since 1994. When I was vice chair of the subcommittee that had defense and narcotics together with it, when now Speaker Hastert was chairman of that, we had tremendous problems in Defense Logistics Agency trying to get any kind of accounting out of the Defense Department because of the national security reasons. They seem to think more that they are exempt to some of the oversight.

On the other hand, we have to allow, particularly when they are in a shooting war and when the contractors have now gotten involved in a shooting war themselves. I think it is fairly safe to say that when we hear a hotel example, you know, the troops, with all due respect, and I have had several killed from my district and I have hundreds and thousands there now from Indiana and from my area of Indiana. They at least have some armored Hummers; they have some defense weapons. We are sending contractors who now are in effect, there is no front line to this war. They are getting beheaded, for crying out loud. You know, they may not be able to stay in a secure place except in Kuwait. They may not be able to stand there by their vehicle if it brakes down, because they don't want to be beheaded. Their families don't want them to go in the first place. I have people who work not for Halliburton, that I know of, but for other contractors over there, and their families don't want them there.

Yet, what we hear out of the other side is speed, speed, speed. Why is it taking so long to rebuild Iraq? How come this is taking so long? Why do you have to do this? And then the second you say,

OK, we are going to do speed, they go, oh, cost, cost, cost. Now, you can't have it both ways. You can't have our contractors out there taking their lives at stake with no protection, or minimal protection, not knowing where they are going to get hit, and then expect them to behave like they are working in some kind of safe environment in Indiana; it is a different type of thing.

Now, one other frustration I have here, and I realize that these hearings are partisan in nature to some degree. No matter who the administration is, the other party has to do that. I have tremendous respect for the ranking member of this subcommittee; I think he is a man of high integrity and he works aggressively to make sure we hold the administration accountable. But I sat here under 6 years of the Clinton administration, when there were people not in danger, when we were looking at travel office budgets with hundreds of emails going out to Members of Congress and to other people talking about how contracts were given and how they weren't given. And what we saw mostly out of the other side was a tremendous defense of that. Here, we are not talking about any known cases other than what it looks like is tremendous sloppiness, lack of preplanning. And, by the way, on preplanning, in reading Bob Woodward's near—the closest thing we have to tapes in the Oval Office anymore are Bob Woodward's books. When you go through his books and listen to that, maybe, just maybe the administration, while the war plan was there, didn't have enough preplanning for some of the followup because they didn't expect that they were necessarily going to have to put the boots on the ground; they were hoping for another solution. And, by the way, we were probably going to be called in on the oil even if we didn't send the troops in, because had they been U.N. troops, had they been NATO troops, had they even been the Iraqis themselves overthrowing Saddam Hussein, the oil, as an amendment was offered in this Congress by a Democratic Member of this Congress, supported by the entire other side said, we have to have that oil revenue to support that country. So regardless, whether we had preplanning for boots on the ground and how we were going to do MREs and what kind of tents we were going to have, we had to protect the oil because probably these firms were going to be called in no matter who the government of Iraq was, no matter who the troops were going to be.

Yes, there should have been more preplanning. Yes, it is terrible how they over-billed for MREs, and that is why you all are there to try to do it. And we need to get the documents and we need to hold them accountable. But I find it appalling to have this turned into some kind of a political show, where the administration is fingered for things, without talking about what is actually happening to the contractors on the ground, the pressures they are under that we have not seen anywhere. I have never heard of contractors being beheaded on television, of the dangers that they are exposed to right now. And then to kind of be "two penny ante" about this when they are under that kind of pressure is a disgrace.

Chairman TOM DAVIS. The gentleman's time has expired. Thank you very much.

Mr. WALKER. Mr. Chairman, could I mention something quickly?

Chairman TOM DAVIS. Yes, Mr. Walker.

Mr. WALKER. First, I agree with you, Mr. Souder, that mission first. Costs do matter, however, especially as time moves on. But I think, like most things in life, we need to look at value and risk, and we have to recognize that many of the services being provided here, the nature of the services vary, the timing of the services vary, and the location of the services vary. I have been in Iraq; I have been in Kuwait. The situation is very different in Kuwait than it is Iraq. And so I think we have to apply the facts and circumstances, because you get different conclusions based upon applying those facts and circumstances based on these factors.

Thank you.

Chairman TOM DAVIS. Mr. Shays.

Mr. SHAYS. Thank you very—I think you need to go——

Chairman TOM DAVIS. No, we had 15 minutes on my side, and I broke for the recess. I was going to let you finish and then we will move over here.

Mr. SHAYS. Thank you.

Mr. Walker, when you first came in there was a lot of controversy as you tried to straighten out your office and get it aligned in a way that you thought would be more effective, and I noticed you stopped getting criticism when you started wearing that pin with the flag and the Marine on it on your lapel, which reminds me of what Newt Gingrich told me. He said periodically he would take issue with what the Marines were doing, and he always lost in the battles on the floor of the House. So he just tried to figure out what they wanted and then he championed them.

So in that spirit I would like to know, first, would you summarize the biggest criticism or two you have with the procurement process, and would you please summarize your biggest commendation or two with the procurement process?

Mr. WALKER. Well, I guess I would say that in the context of the subject that we are dealing with today, inadequate planning and inadequate oversight. I would also say that you have to recognize that there are examples included in our testimony where various parties have done their job well and where they have defined the appropriate scope of the services, where they have nailed down an estimated cost, and where everybody has done their job well, and where they periodically reviewed the contract to determine whether or not the nature and scope of the services should be revised and whether or not the costs are reasonable. One example I would give you is the Balkans to give you one example of where the system worked well, where there was a review that resulted in significant savings to the taxpayers and yet the needed services were provided to the troops.

So I would say planning and oversight are the biggest areas of challenge, but I think we also have to recognize that while we have certain broad-based problems, there are examples of people doing their job well, and those should not go unnoticed.

Mr. SHAYS. So is that your only response, is your biggest saying, job well done? What is the thing that we did best when it came to procurement? You've told me what we have done worst.

Mr. WALKER. In this particular context or overall?

Mr. SHAYS. Yes. In the context of Iraq.

Mr. WALKER. Bill.

Mr. WOODS. I would say that we demonstrated that we collectively, as a Government, demonstrated that the procedures that we have in place, the laws that the Congress has put in place are flexible enough to be able to accommodate contracting under very, very difficult circumstances. In 14 of the new contracts that we looked at, they were all awarded either on a non-competitive or limited competition basis, but by and large they were all done in accordance with the way the laws require them to be made.

Mr. WALKER. And I would say the ability to act expeditiously when the circumstances required.

Mr. SHAYS. No matter what administration is in power, no matter what Congress is in power, this system has to act quickly, and what I am hearing you say is, for the most part, the job was done well. There is really a question of was it bid in the case where it could have been and was there overcharging, and I am struck by the fact that the system worked well in catching the overcharging. Do you have fear that there is a lot of overpayment that we are not being made aware of; that we have just scratched the surface?

Mr. WALKER. There are a lot of players on the field, Mr. Shays, a lot of inspector generals, DCMA obviously is involved, DCA is involved, as well as ourself. I think we are in the early stages of understanding the nature and extent of the challenge here. And as I mentioned before, contract management has been on the high risk for many years. I think the risks are particularly acute when you are dealing with a situation of urgency and when you are dealing with a cost-based contracting arrangement.

Mr. SHAYS. So you are basically testifying that you are concerned there could be a number of instances where we paid more than we should have had to have paid. That is kind of what you are suggesting.

Mr. WALKER. That is correct. And I think there are two dimensions of that. One dimension is were the services needed, because in the absence of nailing down the requirements and the specifications as to the services, in the absence of coming up with what a reasonable estimate of cost would be for that, you don't have an effective control mechanism. And there is a shared responsibility for that, and the Government has a responsibility for not having done that.

Mr. SHAYS. My time is running out and I just want to say, particularly to the point of Mr. Souder, I have been to Iraq five times, and usually we come in from Kuwait or Amman, Jordan, and I am in interaction with these consultants, these contractors, and they are very brave people. They are outside the umbrella of the military, in the communities in many cases, and they may have some security, but they are not in the green zone, they are out in the red zone doing their jobs, and I think we all know that.

Chairman TOM DAVIS. The gentleman's time has expired.

Mr. Clay.

Mr. CLAY. Thank you, Mr. Chairman.

Mr. Walker, five former Halliburton employees recently came forward with firsthand knowledge of waste, fraud, and abuse under Halliburton's LOGCAP global logistics contract with the Army. For instance, a former Halliburton convoy commander and a former truck driver explained that brand new $85,000 Halliburton trucks

were abandoned or torched if they got a flat tire or experienced minor mechanical problems because Halliburton removed spare tires from trucks and performed no maintenance.

If these accounts are accurate, don't they indicate a serious lack of cost control under the LOGCAP contract in Iraq?

Mr. WALKER. I think it is appropriate that somebody review and investigate the actual facts and circumstances here, and I understand that this committee is going to hold an oversight hearing as well to look further into some of these specific assertions.

Mr. CLAY. Let me ask you about a former Halliburton labor foreman, who said that Halliburton exercised virtually no supervision over a Jordanian subcontractor that was building a dining facility in Fallujah. He said that he would go to the site and take a few pictures each day, but that no one else was doing any supervision at all.

Doesn't this lack of subcontract oversight leave the taxpayer vulnerable to overpricing and doesn't it increase the chances that our troops will be left with inadequate facilities?

Mr. WALKER. Obviously, that is a matter of concern as well that should be reviewed.

Bill, did you want to add something?

Mr. WOODS. I don't think we are in a position to speak to the specific allegations, but I think the subsequent hearing that the panel plans to hold will provide an opportunity to get into that.

Mr. CLAY. OK, well, another example. Former employee of the subcontracts department in Kuwait revealed that employees were instructed to pay subcontractor invoices and to extend subcontracts without evaluating whether prices were reasonable and without verifying that services and equipment were actually being delivered. She also said that Halliburtonsite managers were denied access to the subcontract documents they needed to provide proper oversight of the subcontractor.

If this account is true, Halliburton isn't considering appropriate subcontractor management in Kuwait, is it? Are they considering proper management of subcontractors in Kuwait?

Mr. WALKER. You are getting to a level of detail, Mr. Clay, that was beyond the scope of the work that we did, and I think it is important to note that we tried to deal at the high level, as Mr. Waxman talked about, looking at overall contract award for new contracts, for task orders, also for the global logistical contracts. There are other players that are looking at a much greater level of detail and the type of issues that you are dealing with, some of the other inspector generals, than we are.

Mr. CLAY. Well, Mr. Walker, these are serious allegations that we have discussed and just some of the revelations the former employees were willing to share with the committee today. Despite the fact that these individuals were stationed in different locations in Iraq and Kuwait, and worked in different departments, their independent accounts all portray Halliburton as a company with a near total disregard for costs and poor or nonexistent subcontract management and oversight, and I think these claims should be fully investigated. You had something to do with awarding the contract. Did you have something to do with awarding?

Mr. WALKER. With awarding these contracts? No. That would be a separation of powers problem. No.

Mr. CLAY. Well, but you have a responsibility to oversee them, don't you?

Mr. WALKER. Well, there are a lot of people that have a responsibility. I mean, obviously there is a contracting——

Mr. CLAY. You are not shirking your responsibility, are you?

Mr. WALKER. Oh, no.

Mr. CLAY. OK.

Mr. WALKER. Keep in mind, Mr. Clay, we work for the Congress, and we are part of the oversight mechanism to try to help get facts for the Congress to be able to do its job. So we have no management responsibilities here. We don't have any responsibility for awarding the contracts; we don't have any responsibility for managing the contracts; we don't have any responsibility for reporting on the contracts.

Mr. CLAY. Well, wait a minute. When you hear these allegations, does a red flag come up?

Mr. WALKER. Absolutely. And one of the things that I have asked my colleagues with regard to some of these issues is who is following up on these types of issues. I think that is a relevant question. Because as I mentioned before, there are a lot of players on the field. You know, we have the CPAIG, we have the DOD and Army IG, we have the State IG, we have the AIDIG. There are a lot of players on the field, and so I want to make sure we are not bumping into each other.

Mr. CLAY. What has been DOD's response?

Mr. WALKER. Mr. Clay, I would respectfully suggest you ought to ask DOD what their response is.

Mr. CLAY. Well, they will be next.

Mr. WALKER. They are going to be next; they are up next.

Mr. CLAY. What has been their response to you?

Chairman TOM DAVIS. The gentleman's time has expired. You will get a chance to ask DOD in the next panel.

Mr. Van Hollen.

Mr. VAN HOLLEN. Thank you, Mr. Chairman.

I would like to followup on some of the questions that Mr. Davis of Illinois raised, because we heard statements from the administration early on that with respect to the Halliburton contracts, that contract was chosen by civil servant, as opposed to political appointees, and my understanding is some recent information has come to light that suggests that is not the case.

What is your understanding with respect to Michael Mobbs' involvement in selecting Halliburton for the purpose of the task order?

Mr. WOODS. If I could take that one. We did come across a memorandum for the record authored by Mr. Mobbs, and it was a memorandum that brought together some of the discussions that were held by a group called the Energy Infrastructure Planning Group. I do not know all of the members of that group, but I do believe that some of them were contracting professionals of the type that would award contracts. But there were other people in that group who represented customers, if you will, program officials and people that were familiar with the requirements process. And

it was the job of that group to define what the requirements were and to devise a strategy for addressing those requirements.

Mr. VAN HOLLEN. Do you know was it a group decision with respect to awarding the task order contract, or was that an individual decision? Do you know? Do you have any information that would cast light on that question?

Mr. WOODS. I do not know, sir.

Mr. VAN HOLLEN. You do not know.

Based on your experience in Government contracting, is the normal practice to allow the civilians, the nonpolitical individuals with the department to make the final decisions with respect to contract awards?

Mr. WOODS. Well, the selection decisions are certainly made by the career professionals, and they run the procurement system. But that is not done without close coordination with the people that draft the requirements, and those can be people at any level of the organization.

Mr. WALKER. But the final decision is typically made by career officials.

Mr. VAN HOLLEN. And do you know for certain, in this case, whether the final decision was made by career officials or whether it was made by somebody else?

Mr. WOODS. No, I do not know, sir.

Mr. VAN HOLLEN. The document that you mentioned, does the committee have that document, do we know?

Mr. WOODS. I do not know if the committee has that. At the time that we were doing our work, that document was classified, and it is my understanding that document is still classified.

Mr. VAN HOLLEN. All right. My understanding is there are a number of documents that the committee has requested that GAO has, is that right? Not that we have requested of GAO; that the committee has requested of the administration.

Mr. WALKER. I don't know that to be the case. As you know, generally the information that we have is restricted until we end up issuing the related report. I would be happy to have a conversation with the appropriate players on the committee as to whether or not that is the case.

Mr. VAN HOLLEN. OK. Because I have been told by our staff that is the case.

Mr. WAXMAN. Would the gentleman yield? This is a document that we have requested and we want to get, and we hope that we can work with the chairman to obtain that document.

Mr. VAN HOLLEN. My point, I guess, is it has been requested from the administration by at least some members of the committee, and I guess GAO has a copy; we don't. But that is one of the documents.

Chairman TOM DAVIS. Is it your understanding, Mr. Waxman, if I may, that we have a document that the committee is seeking? Is that your understanding?

Mr. WAXMAN. I think that is the case, yes.

Chairman TOM DAVIS. Well, I think we should have a discussion with our staff. Part of the issue is whether or not we have already completed our work and issued our report in accordance with our protocol. So I think we should have a separate conversation.

Mr. VAN HOLLEN. If I could ask, Mr. Chairman, just with respect to the issue of the oversight of some of these contracts and what the practice is with respect to contracting out the oversight process. Ranking Member Mr. Waxman raised some examples in his opening statement where Parsons was hired, I believe, to oversee some of the business that was being done in Kazakhstan and other places by one of its business partners.

My question to you is do you believe that is appropriate, to contract out the oversight process to someone who has a business relationship with an entity that they are providing the oversight of? And are you aware of these examples that were raised?

Mr. WALKER. I am not aware of this example. I would say I think looking at independence issues and business relationships is a factor that should be considered in determining whether and to what extent you should award a contract. Now, obviously it depends upon what the nature of that business relationship is, the materiality of that business relationship, etc.

And I guess I would ask Bill if you have anything to add.

Mr. WOODS. Well, fundamentally it is the Government's responsibility to administer and oversee contracts, and the Government cannot and should not walk away from that responsibility. That is not to say that they, from time to time, should not seek the assistance of contractors. They may have particular expertise in certain areas that may be of assistance to the Government in carrying out that responsibility, but when they do that, they need to make sure that the proper controls are in place and that they are particularly vigilant in guiding against potential conflicts.

Chairman TOM DAVIS. The gentleman's time has expired.

Mr. VAN HOLLEN. All right. Thank you, Mr. Chairman.

Chairman TOM DAVIS. Ms. McCollum can yield to you if you have a followup.

Gentlelady from Minnesota, welcome to the committee. You are recognized for 5 minutes.

Ms. MCCOLLUM. Thank you, Mr. Chairman. Thank you for the time.

Chairman TOM DAVIS. She can yield to you if you would like.

Ms. MCCOLLUM. I find it rather curious that in the press it reports, in several news articles, that there was an Army lawyer who was very concerned about the way that these contracts were being let; made a statement, in fact, that the contracts should be held differently, that they should not be awarded the way that they were to Halliburton. Did you come across any of this? I find it in CBS News and other places on the Internet. Did you come across that at all?

Mr. WALKER. My understanding—and I would ask for Bill to followup—is that we did ascertain as a result of our review that there were certain differences of opinion within the Department of Defense and, in fact, within the Army General Counsel's Office as to whether or not it was appropriate to issue a contract dealing with the planning for the oil services and the oil reconstruction, and that there were differences of opinion that exist within the Office of General Counsel of the Army as well as within the Department as a whole, but that ultimately the General Counsel of the Depart-

ment of the Defense made the decision that he did feel that it was legal.

Ms. MCCOLLUM. Is the general counsel for the Department of Defense—I am new to the committee—are they civilian or are they career military? That individual who made the decision to override, are they a political appointee or are they career military?

Mr. WOODS. I believe that the Department of Defense seniormost counsel is a political appointee, but these were made——

Ms. MCCOLLUM. So a political appointee.

Mr. WOODS. No, no. These were made—the memo that we saw was made by a career person in the Department of Defense General Counsel's Office. This was a career individual who ultimately decided that, yes, this contingency planning task order was within the scope of the LOGCAP contract, and that——

Ms. MCCOLLUM. After discussions with the political appointee, it sounds like.

Chairman TOM DAVIS. I just want to clarify this for the record, since we're all under oath. So, Bill, just to confirm, there was a difference of opinion between the counsel for the Army and for the Office of the General Counsel for Secretary of Defense, but you are saying the documentation we have does not deal with the general counsel, it deals at a career level where the decision was made?

Mr. WOODS. That is correct. It was not the general counsel for the Department of Defense.

Chairman TOM DAVIS. All right. That is important. I think it is important for you to understand that.

Ms. MCCOLLUM. That is helpful to know.

Mr. WAXMAN. Would the gentlelady yield to me?

Ms. MCCOLLUM. Yes, I will yield.

Mr. WAXMAN. But as I understand it, GAO thinks that the original career lawyer that thought the planning was outside the scope of the LOGCAP contract, and that was his position, and that is the one you believe is the correct decision.

Mr. WALKER. Our view is that the action that was taken was not in accordance with the law, and our view is consistent with the original Army general counsel person. At the same point in time I think it is also important to note that while we believe that it was not in accordance with the law, we also believe it is likely that it could have qualified for one of the exceptions, given the urgency and the conditions that existed. They didn't attempt to do that, but it is likely that they could have qualified for that.

Mr. WOODS. That is correct.

Ms. MCCOLLUM. Thank you. Reclaiming my time.

I find this urgency and state of emergency rather interesting, when this was a war that we chose to go into, where there was no urgency or emergency, imminent threat by Iraq to our country.

Could you please tell me, sir, I have been kind of concerned about the inventory, the manifest shipping things that I have read not only in news articles, but in the letters that were provided. When you were doing your investigation, I know that you said you weren't charged with finding fraud and abuse, and once again I would want to know who is responsible for finding fraud and abuse. We can't have the fox watching the hen house and expect everything to be caught. But inventories, shipment, over-billings, it

appears when people who worked either as military personnel or civilian personnel made questions, people who were familiar with how inventories and shipping receipts should be handled, they were told, oh, don't worry about it.

What did you find in your investigation?

Mr. WALKER. I think the way to respond to that, Congressman, is the whole concept that we saw in the early stages of the operation there in Iraq was to get the mission done, and there wasn't the cost consciousness which would have resulted in the kinds of questions you are raising until at least December 2003.

Ms. MCCOLLUM. Well, sir, I would beg to differ that this has something to do with cost, but it also doesn't. If I am at the 101st Airborne in Mosul and I have ordered protective gear or I have ordered food or I have ordered ammunition, I would certainly hope that when it comes to me, I get the amount, the quantity, the size of what I have ordered. And without any shipping manifests going along with these convoys, I find that pretty hard to say that our soldiers were in fact being served very well. In private business they are used constantly.

Chairman TOM DAVIS. Thank you. The gentlelady's time has expired.

Mr. WALKER. I think one has to keep in mind that there is a difference between whether or not they got what they wanted and whether or not what they wanted was appropriate and acquired at a reasonable cost; and there are differences there.

Chairman TOM DAVIS. I think the testimony was already that they seemed to have gotten what they wanted, that the needs of the client were met. The question you deal with is cost.

Mr. WALKER. With regard to things like kevlar vests and things of that nature, those aren't the kinds of things that we are talking about under this contract; those aren't the types of products or services that are being provided here, it is more like housing, it is more like food, which are obviously important.

Chairman TOM DAVIS. Mr. Waxman and I each get a minute to sum up.

Mr. Waxman.

Mr. WAXMAN. Mr. Chairman, I think GAO has done a good job in helping us understand the issues and also in identifying issues I think we need to pursue. GAO has said that decisions about who gets contracts should be made by career people, but Mr. Mobb, who is a political appointee, said he made the decision to use Halliburton, so this is clearly an issue that we need to investigate. GAO said there is a difference between an FYI communication to the White House and a communication that seeks White House assent, but Mr. Mobb told us that the White House was briefed so that White House officials could object, and that is more than an FYI communication. So this is an other issue we need to investigate.

I want to return to the question of whether there were contract irregularities in the issuance of the Halliburton contract. I think these are questions that we need to pursue not just with GAO, but with others. There is a question of this career lawyer who's view was overturned, that this bootstrapping, of giving authority under the LOGCAP contract in October 2002 to do the planning in fact meant that they would get the sole source contract the next March.

So in that first contract, that seems to me a question of whether a career person's decision was made or whether that was elevated. And so I think we need to learn more about it, maybe have Mr. Mobb and others here to pursue these matters before we draw any conclusions about it.

Chairman TOM DAVIS. Thank you.

I gleaned something different. First of all, we need to remember Halliburton had LOGCAP under previous administrations that had been awarded. We have heard testimony that in their analysis they found no fraud or abuse. That wasn't what they were primarily looking for, but they didn't uncover that.

We have another panel coming up that I think will be able to talk at length about some of the questions that maybe this panel wasn't charged to look at.

And the fact that you sometimes have, not just career people, but that you had Schedule C or others make decisions on contracts is not a rarity in Government contracting, particularly at the higher levels as some of this goes up. This wasn't awarded in secret in the sense that this was secret, it was classified. And when you are doing classified things, anything that you put out in the public, the enemy knows about and everybody else, and you can understand why this was done in a classified way.

We appreciate the insights that this has brought Mr. Walker, we appreciate the work that you and your group have done on this and look forward to working with you on others.

I am going to dismiss the panel at this point. We will take a 2-minute recess as we assemble our next panel. Thank you.

[Recess.]

Chairman TOM DAVIS. We have Mr. Lawrence Lanzilotta, the Principle Deputy and Acting Under Secretary of Defense, Comptroller; Mr. William Reed, the Director of the Defense Contract Audit Agency, U.S. Department of Defense; we have Mrs. Deirdre Lee, who is the Director of the Defense Procurement and Acquisition Policy and worked at OFPP in the previous administration, here with the Department of Defense.

I understand, Mr. Lanzilotta and Ms. Lee, you do not have prepared testimony, you are here for questions, is that correct? You are welcome to say anything.

Tina Ballard, who has been here before, the Deputy Assistant Secretary of the Army; General Paul Kern, Commanding General, U.S. Army Materiel Command; and Brigadier General Robert Crear, Commander, Southwestern Division, U.S. Army Corps of Engineers.

It is our policy all witnesses be sworn before your testimony, so if you would rise with me and raise your right hands.

[Witnesses sworn.]

Chairman TOM DAVIS. Thank you very much. I think everyone is aware of the rules. Mr. Reed, I guess we will start with you. Any comments?

Mr. LANZILOTTA. Mr. Chairman, if I could, I just have a very short opening comment.

Chairman TOM DAVIS. That would be fine.

STATEMENTS OF LAWRENCE LANZILOTTA, PRINCIPLE DEPUTY AND ACTING UNDER SECRETARY OF DEFENSE (COMPTROLLER), U.S. DEPARTMENT OF DEFENSE; DEIDRE LEE, DIRECTOR, DEFENSE PROCUREMENT AND ACQUISITION POLICY, U.S. DEPARTMENT OF DEFENSE; TINA BALLARD, DEPUTY ASSISTANT SECRETARY OF THE ARMY (POLICY AND PROCUREMENT), U.S. DEPARTMENT OF DEFENSE; GENERAL PAUL KERN, COMMANDING GENERAL, U.S. ARMY MATERIEL COMMAND; BRIGADIER GENERAL ROBERT CREAR, COMMANDER, SOUTHWESTERN DIVISION, U.S. ARMY CORPS OF ENGINEERS; AND WILLIAM H. REED, DIRECTOR, DEFENSE CONTRACT AUDIT AGENCY, U.S. DEPARTMENT OF DEFENSE

Mr. LANZILOTTA. Mr. Chairman, I am here to discuss the Department of Defense oversight of contracts related to military operations and reconstruction of Iraq. The Department of Defense gives the utmost seriousness to its oversight of contracts. In an environment as fast-moving and as difficult as Iraq has been, contracting can be extremely complex, and that makes oversight especially important. The Department has a number of strong organizations, policies, regulations to fulfill its contract oversight responsibility. Our task is not only to identify contract issues, but also to prevent future occurrences of problems we identify, recover any excess charges, and take appropriate action to protect the Government's interest.

The role of the Under Secretary of Defense Comptroller in contracting oversight comes primarily through the Defense Contract Audit Agency [DCAA]. DCAA's mission is to provide all contract audit and financial advisory services related to DOD acquisition of goods and services.

Other DOD organizations, notably the Defense Contract Management Agency and the DOD Inspector General, also play important contract oversight roles and work closely with DCAA. Additionally, the Under Secretary of Defense for Acquisition, Technology, and Logistics is responsible for contract policies that help ensure the Department obtains the best value when acquiring equipment and services, and is also responsible for DCMA.

In Iraq, the Army and DCAA are strategic partners in the oversight of contractor performance. The Army, as executive agent for all the Department's reconstruction requirements in Iraq, is responsible for contract and program management activities there. DCAA, which is co-located with Army personnel in Baghdad, evaluates contractor proposals and performs audit procedures on contractor-incurred costs. In addition, DCAA personnel are available upon request to assist contracting officers on all phases of the contracting process.

In the first 8 months of fiscal year 2004, DCAA issued 285 audit reports related to Iraqi reconstruction contracts. Of these 285 reports, most have not had significant findings; however, the large number of these DCAA reports underscores the seriousness of the Department's contract oversight. The findings that DCAA has made has led to actions including changes in processes, rejection of unsupported proposal costs, reductions in billed costs for potential unreasonable expenditures, and referral of suspected irregularities to the DOD Inspector General for investigation.

Contractor performance in Iraq has not been perfect, nor as bad as some characterize. Many contractors that have not had problems in performing their domestic DOD contracts have had difficulties in adjusting to the unique environment in Iraq. We are working with these contractors to help them resolve their problems in Iraq, but we are also taking whatever actions are necessary to protect the Government's financial interest.

In regarding the Army contracting, I understand that this committee has expressed concern about an email from Mr. Steven Browning of the Army Corps of Engineers. Mr. Browning prepared a memo in response to your concerns, and with your permission, Mr. Chairman, I would like to submit it for the record.

Chairman TOM DAVIS. Without objection.

[The information referred to follows:]

DEPARTMENT OF THE ARMY
U.S. ARMY CORPS OF ENGINEERS
WASHINGTON, D.C. 20314-1000

REPLY TO
ATTENTION OF:

South Pacific Division

7 June 2004

MEMORANDUM FOR RECORD:

1. I am a Registered Professional Engineer and a member of the Senior Executive Service, currently assigned to the U.S. Army Corps of Engineers (USACE) as the Director of Regional Programs, South Pacific Division, San Francisco, CA.

2. In mid-February 2003, I was assigned from USACE to work with the Office of Reconstruction and Humanitarian Assistance (ORHA), within OSD, under LTG (Ret) Jay Garner in the Pentagon. I deployed to Kuwait as part of the ORHA Advance Party on 7 March 03, after having spent about three weeks in the Pentagon. While in the Pentagon, I was primarily focused on support to pre-conflict planning for humanitarian assistance and reconstruction.

3. Part of ORHA's pre-conflict planning included actions necessary in response to potential oil fires, oil spills, and damage to oil facilities. The Secretary of the Army had previously designated, on 13 Feb 03, USACE as the Executive Agent for this effort. Project management for this effort was assigned to the Southwestern Division (SWD) of the Corps, with SWD providing support through Field Force Engineering efforts and executing contracts with the private sector (including KBR).

4. In early Mar 03, SWD had a compelling reason to have declassified certain facts regarding DoD plans to fight fires and assess damage to oil infrastructure in the event of hostilities in Iraq. As I recall, the issue involved the ability of the contractor to hire experts, purchase and deploy equipment, and more effectively discuss planning within the firm for firefighting, damage assessment, design engineering and environmental remediation. Mr. Garner was aware of this issue and strongly supported declassification of these facts in order to expedite this work.

5. I worked with SWD and the OSD planning staff to prepare an action memo for approval of the declassification action. My understanding was that Mr. Feith had the authority to declassify this portion of the project.

7. On 5 Mar 03, Mr. Garner and I met with Mr. Feith and members of his staff to explain the importance and urgency of the declassification action in order to prepare for restoration work as soon as possible. Mr. Feith concurred with the requirement subject to informing the Congress and the White House prior to the decision being announced. My understanding was that the Office of the Vice President had been previously informed. My understanding and sense of the meeting was that this "coordination" was simply to inform those offices in anticipation of a press release that was planned for 6 Mar 03.

8. At no time did I ever perceive or note any attempt by the Office of the Vice President or anyone else in the Administration to influence the course or direction of this contract. I want to be clear on this point; to my knowledge, there was absolutely no influence or pressure exerted by anyone in the Administration regarding this contract action.

9. Since I was preparing to deploy to Kuwait as part of the ORHA Advance Party on 7 Mar 03 and would not have an opportunity to communicate with the USACE team working this issue, I sent my e-mail message to SWD and others to let them know the status of the declassification action.

Stephen E. Browning, P.E.
Director, Regional Programs
South Pacific Division
U.S. Army Corps of Engineers
333 Market Street
San Francisco, CA 94105-2195
415.977.8019

Mr. LANZILOTTA. In closing, I want to underscore that we in the Department of Defense are absolutely committed to an integrated, well managed contracting process in Iraq. We will not tolerate the billing of costs that are not properly documented or supported. If internal control systems are deficient, we will continue to use protections, such as contract withholdings, to safeguard our interest, and we will provide whatever personnel and budget resources are needed to enforce the integrity of this process.

Thank you, Mr. Chairman.

[The prepared statement of Mr. Lanzilotta follows:]

Oral Statement Larry Lanzillotta
Acting Under Secretary of Defense (Comptroller)
House Committee on Government Reform
15 June 2004

Mr. Chairman, members of the committee, I am here to discuss Department of Defense (DoD) oversight of contracts related to military operations and reconstruction in Iraq.

DoD Contract Performance Oversight Responsibilities

The Department of Defense gives the utmost seriousness to its oversight of contracts. In an environment as fast-moving and difficult as Iraq has been, contracting can become exceedingly complex, and that makes oversight especially important.

The Department has a number of strong organizations, policies, and regulations to fulfill its contract oversight responsibility. Our task is not only to identify contract issues, but also to prevent future occurrences of problems we identify, recover any excess charges, and take appropriate action to protect government interests.

The role of the Under Secretary of Defense (Comptroller) in contract oversight comes primarily through the Defense Contract Audit Agency (DCAA). DCAA's mission is to provide all contract audit and financial advisory services related to DoD acquisition of goods and services.

Other DoD organizations -- notably the Defense Contract Management Agency (DCMA) and DoD Inspector General (DoDIG) -- also play important contract oversight roles and work closely with DCAA. Additionally, the Under Secretary of Defense (Acquisition, Technology and Logistics) is responsible for the contract

policies that help ensure the Department obtains the best value when acquiring equipment and services and is also responsible for DCMA.

In sum, successful contracting in the Department of Defense is very much a team effort.

Reconstruction Contracts in Iraq

In Iraq, the Army and DCAA are strategic partners in the oversight of contractor performance. The Army, as the executive agent for all Department reconstruction requirements in Iraq, is responsible for contract and program management activities there. DCAA, which is co-located with Army personnel in Baghdad, evaluates contractor proposals and performs audit procedures on contractor incurred costs. In addition, DCAA personnel are available upon request to assist contacting officers on all phases of the contracting process.

In the first eight months of FY 2004, DCAA issued 285 audit reports related to Iraq reconstruction contracts. Of the 285 reports, most have not had significant findings. However, the large number of these DCAA reports underscores the seriousness of the Department's contract oversight.

The findings that DCAA has made have led to action including changes in processes, rejection of unsupported proposal costs, reductions in billed costs for potentially unreasonable expenditures, and referral of suspected irregularities to the DoD Inspector General for investigation.

Contractor performance in Iraq has not been perfect, nor as bad as sometimes characterized. Many contractors that have not had problems in performing their domestic DoD contracts have had difficulties in adjusting to the unique environment in Iraq. We are working with contractors to help them resolve their

problems in Iraq. But we also are taking whatever actions are necessary to protect the Government's financial interests.

Regarding Army contracting in Iraq, I understand that this committee has expressed concern about an email from Mr. Stephen Browning of the Army Corps of Engineers. Mr. Browning prepared a memo in response to your concern, and I would like to submit that memo for the record.

Closing

In closing, I want to underscore that we in the Department of Defense are absolutely committed to an integrated, well-managed contracting process in Iraq. We will not tolerate the billing of costs that are not properly documented and supported. If internal control systems are deficient, we will continue to use protections, such as contact withholdings, to safeguard our interests. And we will provide whatever personnel and budget resources are needed to enforce integrity in DoD contracts.

Now let me introduce our DoD witnesses and invite them to present their statements:

- General Paul Kern, Commanding General of the Army Material Command.
- Ms. Deirdre Lee, Director of Defense Procurement and Acquisition Policy.
- Mr. William Reed, Director of the Defense Contract Audit Agency.
- Ms. Tina Ballard, Deputy Assistant Secretary of the Army for Policy and Procurement.
- Brigadier General Robert Crear, Commander, Southwestern Division of the Army Corps of Engineers.

Chairman TOM DAVIS. Thank you very much.

Mr. Reed, welcome back.

Mr. REED. Thank you, Mr. Chairman. Mr. Chairman, members of the committee, my statement for this hearing will center on the Defense Contract Audit Agency's oversight of contracts related to military operations and reconstruction in Iraq.

DCAA has been an integral part of the oversight and management controls instituted by DOD to ensure integrity and regulatory compliance in Iraq-related contracting. DCAA's services include professional advice to acquisition officials on accounting and financial matters to assist them in the negotiation, award, administration, and settlement of contracts. It is important to note that decisionmaking authority on DCAA recommendations resides with contracting officers within the procurement organizations who work closely with DCAA throughout the contracting process.

Since April 2003, DCAA has worked with all U.S. procurement organizations supporting Iraq reconstruction to establish the resources and planning information needed to carry out required audits of contract costs as they are incurred and billed. These organizations include the Coalition Provisional Authority [CPA], the Army Materiel Command, the Army Corps of Engineers, USAID, and the State Department. This coordination has enabled DCAA to build a universe of all Iraq-related auditable contracts, which is a significant step toward ensuring that needed audit procedures are timely and comprehensive.

DCAA currently is responsible for providing Iraq-related contract audit services to both DOD and other Government organizations at 56 contractors holding more than 80 prime contracts with contract ceiling amounts of $34.6 billion and funding to date under these contracts of about $12.4 billion.

To carry out the extensive and time-sensitive audit requirements, DCAA has implemented new planning and coordination procedures to effectively integrate audit work between the new Iraq Branch Office, opened in May 2003, and more than 50 DCAA CONUS Audit Offices with cognizance of companies performing contracts in Iraq. The Iraq Branch Office itself now has 22 auditors, and will increase to 28 auditors by the end of June.

As has been noted, during the first 8 months of fiscal year 2004, DCAA has issued 285 audit reports related to Iraq reconstruction contracts. These reports address forward pricing proposals, adequacy of contractor internal controls and business systems, as well as compliance with acquisition regulations and contract terms. Especially important has been DCAA's in-country testing of contractor timekeeping, subcontract management, and cash disbursement procedures which represent immediate risk in the provisional approval of interim contract payments. In the balance of my statement, I will present some of the more significant examples of what we have found in these audits, beginning with the largest contractor, Halliburton, Kellogg Brown & Root.

KBR has been awarded Iraq reconstruction contracts with ceilings totaling more than $18 billion under two major programs: Logistics Civil Augmentation Program [LOGCAP] for $10 billion, and Restore Iraqi Oil for $8.2 billion. DCAA has been providing continuous contract audit oversight on both programs.

The first area I want to address is estimating practices. DCAA has identified significant deficiencies in KBR's estimating practices related to the award of subcontract costs. Earlier this year, after consultation with the contracting officer, DCAA returned two major task order proposals worth more than $3 billion to KBR because they were inadequate for the purpose of negotiating a fair and reasonable price. On January 13, 2004, DCAA notified the appropriate Government contracting officials that KBR's subcontracting estimating process and procedures were considered inadequate. Currently, DCAA is in the process of performing a comprehensive review of the entire estimating system to address this matter as well as other possible deficiencies.

KBR's deficiencies in estimating subcontracts are contributory factors in potential dining facility overpricing and delays in definitization of task order prices under the LOGCAP contract, both of which I would like to comment on next. They were also a contributory factor in potential gasoline overpricing under the Restore Iraqi Oil contract as explained in Dr. Zakheim's testimony before this committee on March 11, 2004.

Turning to the dining facility subcontract costs, DCAA has identified issues related to the reasonableness of negotiated subcontract costs for dining facilities, which I will refer to hereafter as DFACs. KBR has been unable to support the reasonableness of subcontract prices or the appropriate billing methodology intended in its subcontracts. The DFAC subcontractor costs exceed $800 million and are continuing to increase. KBR awarded contracts to several subcontractors to provide dining facility services at more than 60 locations throughout Iraq and Kuwait. The DFAC subcontractors generally charge for meals at a negotiated fixed meal cost—per person—using various headcount schemes including estimated camp population, estimated numbers from the subcontract statement of work, and billeting records to set the number of billed meals. These billed headcount numbers exceed the actual meals served by at least 19 percent according to KBR's own studies and could be as high as 36 percent based on ongoing DCAA analysis. KBR has been unable to support the intended billing methodology or how it may relate to the fixed cost per meal negotiated with its various subcontractors.

Initially, DCAA and KBR agreed on a withholding of $176.5 million until additional supporting data could be provided by KBR, $140.7 million that KBR voluntarily withheld from future billings and $35.8 million that DCAA suspended on current billings. KBR performed an internal analysis and estimated that billed meals exceeded actual meals served based on headcount—boots through the door—by approximately 19 percent. However, KBR asserts that the excess meals are allowable, primarily because the various task orders under the LOGCAP contract do not specify a specific billing methodology. While KBR has since renegotiated the terms of most of the DFAC subcontracts to establish a "boots through the door billing methodology," they have begun now to resubmit their voluntary withhold under the original subcontracts.

DCAA found substantial deficiencies in the data provided by KBR and believes cost should continue to be suspended related to the original subcontracts until additional support and analysis can

be completed. Therefore, DCAA has currently increased its suspended DFAC costs to $186 million.

We are continuing to evaluate additional supporting information provided by KBR and will be issuing final recommendations to the contracting officer on the first of several of these DFACs in the near future. Depending on our conclusions, DCAA may either reinstate the suspended cost or convert the suspension to a disallowance. If a disallowance is recommended, this will provide the basis for the contracting officer to evaluate and decide the merits of the dispute.

KBR has voluntarily disclosed a possible violation of the Anti-Kickback Act by two of its employees. KBR has already reimbursed the Government for the estimated impact of $6.3 million, but has failed to provide data necessary for DCAA to verify the accuracy of that amount. We have brought this to the attention of the DOD IG, which is in the process of reviewing the matter as part of its normal Voluntary Disclosure Program process.

Due to urgent requirements, most of the LOGCAP task orders were issued as undefinitized contract actions. The FAR limits contract reimbursement to a maximum of 85 percent until a contract price is definitized to adequately protect the Government's interest in effective cost management. DCAA found that KBR had never applied reimbursement limitations to undefinitized LOGCAP task orders and brought the matter to the Army contracting officer's attention. She agreed to apply the clause on a prospective basis to LOGCAP task orders depending on KBR agreeing to a firm schedule for submitting the required proposals. Currently, a mutually agreeable schedule has been established and KBR proposals are being submitted for audit. AS of this date, the LOGCAP contract has 36 task orders with an estimated value of $8.2 billion that require proposal audits and final price determination. Of that amount, DCAA has received and is in the process of auditing 28 proposals with an estimated value of $7.6 billion.

DCAA recently completed a comprehensive billing system review at KBR. The audit report was issued May 13, 2004, with an overall opinion that the billing system is inadequate in part. As a result, KBR is not authorized for direct billing and is required to continue to provide all billings to DCAA for provisional approval prior to submission for payment. Key issues disclosed during our audit included: not effectively monitoring subcontract billings, for example, DFAC costs; inadequate written policies and procedures for the billing system; and failure to adjust billings for changes in indirect rates. DCAA will continue to monitor all aspects of the billing system until these matters are resolved.

Turning to another contractor, Titan Corp. Titan was awarded a contract valued at $402 million to provide linguist and translator services to the U.S. Government, mostly in Iraq. Titan presently has over 4,400 linguists working in Iraq. Recently DCAA audits disclosed deficiencies in Titan's labor distribution system which records costs for Titan employees. DCAA also found that Titan lacked procedures for adequate tracking of hours worked by foreign national consultants. Based on these findings, the DCMA contracting officer implemented a 10 percent withhold on all of Titan's labor and consultant costs until all identified deficiencies are cor-

rected and bills to the Government are based on adequate internal controls. The resulting withhold amount could be as much as $4.9 million on future billings depending on the timeliness of the needed improvements. In addition, DCAA recently discovered that Titan was not adjusting their provisional billing rates to actual rates at the end of each fiscal year. Titan agreed to make the necessary billing adjustments of $937,000. Last, Titan recently informed us they will adjust previously billed costs for the Titan employee and subcontractor employee named in connection with potential abuses at Abu Ghraib Prison. These reductions are scheduled to be made by June 18, 2004, and include Titan and subcontractor costs totaling over $178,000.

DCAA is expanding its audit coverage at another contractor, CACI, based on recent disclosure of additional contracts awarded to the company. Since August 2003, the Department of Interior, at the request of the Army, has awarded 11 task orders under a GSA Supply Contract for Information Technology services for interrogation and intelligence gathering effort in Iraq. At least three of these tasks related to the interrogation of Iraqi prisoners. Billed costs as of March 2004 under these task orders is $12.7 million, with a total funded contract value in excess of $60 million. DCAA is reviewing the potential misuse by CACI of the GSA schedule contract on this Department of Interior contract that is funded by the Army since "interrogator" type effort is not a function provided by CACI in their GSA schedule. We understand the GSA and Department of Interior inspector generals have initiated reviews of this matter as well.

Turning to another company, Washington Group International. In support of the Restore Iraqi Electricity Program, WGI received a contract totaling $309 million. As a result of a WGI proposal to definitize this contract, on February 13, 2004, DCAA reported to the Corps of Engineers' contracting officer that WGI had substantial subcontract estimating problems. On February 26th, the DCAA also reported to the contracting officer that WGI's estimating system deficiencies were significant and required immediate contractor attention. Since that period, DCAA and the Corps have worked closely with WGI to correct estimating system deficiencies and obtain improved subcontract cost support. While WGI has made excellent progress in providing additional documentation for the majority of the unsupported costs, DCAA has suspended over $11.5 million of billed costs because WGI has been unable to support the reasonableness of certain security-related subcontract costs. In addition, DCAA has suspended $4.9 million on a separate contract related to costs billed for undefinitized task orders. As discussed earlier, the FAR limits contract reimbursement until a contract price is definitized to adequately protect the Government's interest. DCAA is working closely with the Corps of Engineers and WGI to address these issues.

In closing, I want to underscore that I am committed to working with other DOD organizations to ensure an integrated, well-managed contracting process in Iraq. The Department will not tolerate the billing of costs that are not properly documented and supported. If internal control systems are deficient, we will continue to use protections such as contract withholdings and cost suspen-

sion to safeguard the Department's interest. Rest assured that I will provide whatever resources are needed for DCAA to continue to provide contract audit oversight in Iraq.

In sum, I believe that DCAA has been vigilant about contract oversight and protecting the taxpayers' interest. I am committed to making sure this continues. I look forward to addressing whatever questions or comments you may have on this oversight. Thank you.

[The prepared statement of Mr. Reed follows:]

Statement of Mr. William H. Reed
Director, Defense Contract Audit Agency
House Committee on Government Reform
15 June 2004

Mr. Chairman, members of the committee, my statement for this hearing will center on the Defense Contract Audit Agency's (DCAA) oversight of contracts related to military operations and reconstruction in Iraq.

DoD Contract Performance Oversight Responsibility

DCAA has been an integral part of the oversight and management controls instituted by DoD to ensure integrity and regulatory compliance in Iraq-related contracting. DCAA's services include professional advice to acquisition officials on accounting and financial matters to assist them in the negotiation, award, administration, and settlement of contracts. Decision-making authority on DCAA recommendations resides with contracting officers within the procurement organizations who work closely with DCAA throughout the contracting process.

DCAA Staffing and Actions

Since April 2003, DCAA has worked with all U.S. procurement organizations supporting Iraq Reconstruction to establish the resources and planning information needed to carry out required audits of contract costs as they are incurred and billed. These organizations include the CPA, the Army Materiel Command, Army Corps of Engineers, USAID, and State Department. This coordination has enabled DCAA to build a universe of all Iraq-related auditable contracts, which is a significant step towards ensuring that needed audit procedures are timely and comprehensive.

DCAA currently is responsible for providing Iraq-related contract audit services to both DoD and other Government organizations at 56 contractors holding more than 80 prime contracts with contract ceiling amounts of $34.6 billion and funding to date under those contracts of about $12.4 billion.

To carry out the extensive and time-sensitive audit requirements, DCAA has implemented new planning and coordination procedures to effectively integrate audit work between the new Iraq Branch Office, opened in May 2003, and more than 50 DCAA CONUS Audit Offices with cognizance of companies performing contracts in Iraq. The Iraq Branch Office itself now has 22 auditors, and will increase to 28 auditors by the end of June.

During the first 8 months of FY 2004, DCAA has issued 285 audit reports related to Iraq reconstruction contracts. These reports address forward pricing proposals, adequacy of contractor internal controls and business systems, as well as compliance with acquisition regulations and contract terms. Especially important has been DCAA's in-country testing of contractor timekeeping, subcontract management, and cash disbursement procedures which represent immediate risk in the provisional approval of interim contract payments. In the balance of my statement, I will present some of the more significant examples of what we have

found in these audits, beginning with the largest contractor, Halliburton, Kellogg Brown & Root (KBR).

Contract Issues related to Halliburton - KBR

KBR has been awarded Iraq Reconstruction contracts with ceilings totaling more than $18 billion under two major programs: Logistics Civil Augmentation Program (LOGCAP III) for $10 billion; and Restore Iraqi Oil (RIO) for $8.2 billion. DCAA has been providing continuous contract audit oversight on both programs.

Estimating Practices. DCAA has identified significant deficiencies in KBR's estimating practices related to the award of subcontract costs. Earlier this year, after consultation with the Contracting Officer, DCAA returned two major task order proposals (worth more than $3 billion) to KBR because they were inadequate for the purpose of negotiating a fair and reasonable price. On January 13, 2004, DCAA notified the appropriate Government contracting officials that KBR's subcontracting estimating process and procedures were considered inadequate. Currently DCAA is in the process of performing a comprehensive review of the entire estimating system to address this matter as well as other possible deficiencies.

KBR's deficiencies in estimating subcontracts are contributory factors in potential dining facility overpricing and delays in definitization of task order prices under the LOGCAP contract, both of which I would like to comment on next. They were also a contributory factor in potential gasoline overpricing under the Restore Iraqi Oil contract as explained in Dr. Dov S. Zakheim's testimony before this committee on 11 March 2004.

Dining Facility (DFAC) Subcontract Costs. DCAA has identified issues related to the reasonableness of negotiated subcontract costs for DFACs. KBR has been unable to support the reasonableness of subcontract prices or the appropriate billing methodology intended in its subcontracts. The DFAC subcontractor costs exceed $800 million and are continuing to increase. KBR awarded contracts to several subcontractors to provide dining facility services at more than 60 locations throughout Iraq and Kuwait. The DFAC subcontractors generally charge for meals at a negotiated fixed meal cost (per person) using various headcount schemes including estimated camp population, estimated numbers from the subcontract statement of work and billeting records to set the number of billed meals. These billed headcount numbers exceed the actual meals served by at least 19 percent according to KBR's own studies and could be as high as 36 percent based on on-going DCAA analysis. KBR has been unable to support the intended billing methodology or how it may relate to the fixed cost per meal negotiated with its various subcontractors.

Initially, DCAA and KBR agreed on a withholding of $176.5 million until additional supporting data could be provided by KBR ($140.7 million that KBR voluntarily withheld from future billings and $35.8 million that DCAA suspended on current billings). KBR performed an internal analysis and estimated that billed meals exceeded actual meals served based on headcount (boots through the door) by approximately 19 percent. However, KBR asserts that the excess meals are allowable, primarily because the various task orders under the LOGCAP contract do not specify a specific billing methodology. While KBR has since re-negotiated the terms of most of the DFAC subcontracts to establish a "boots through the door billing

methodology", they have begun to resubmit their voluntary withhold under the original subcontracts.

DCAA found substantial deficiencies in the data provided by KBR and believes cost should continue to be suspended related to the original subcontracts until additional support and analysis can be completed. Therefore DCAA has currently increased its suspended DFAC costs to $186 million.

We are continuing to evaluate additional supporting information provided by KBR and will be issuing final recommendations to the Contracting Officer on the first of several of the DFACs in the near future. Depending on our conclusions, DCAA may either reinstate the suspended cost or convert the suspension to a disallowance. If a disallowance is recommended, this will provide the basis for the Contracting Officer to evaluate and decide the merits of the dispute.

Violation of the Anti-Kickback Act. KBR has voluntarily disclosed a possible violation of the Anti-Kickback Act by two of its employees. KBR has already reimbursed the Government for the estimated impact of $6.3 million, but has failed to provide data necessary for DCAA to verify the accuracy of that amount. We have brought this to the attention of the DoDIG, which is in the process of reviewing the matter as part of its normal Voluntary Disclosure Program process.

Application of Federal Acquisition Regulations (FAR) on Contract Definitization. Due to urgent requirements, most of the LOGCAP contract task orders were issued as undefinitized contract actions. The FAR limits contract reimbursement to a maximum of 85 percent until a contract price is definitized to adequately protect the Government's interest in effective cost management. DCAA found that KBR had never applied reimbursement limitations to undefinitized LOGCAP task orders and brought the matter to the Army contracting officer's attention. She agreed to apply the clause on a prospective basis to LOGCAP task orders depending on KBR agreeing to a firm schedule for submitting the required proposals. Currently a mutually agreeable schedule has been established, and KBR proposals are being submitted for audit. As of this date, the LOGCAP contract has 36 task orders with an estimated value of $8.2 billion that require proposal audits and final price determination. Of that amount, DCAA has received and is in the process of auditing 28 proposals with an estimated value of $7.6 billion.

Billing System Review. DCAA recently completed a comprehensive billing system review at KBR. The audit report was issued May 13, 2004, with an overall opinion that the billing system is inadequate in part. As a result, KBR is not authorized for direct billing and is required to continue to provide all billing to DCAA for provisional approval prior to submission for payment. Key issues disclosed during our audit include:

- Not effectively monitoring subcontract billings (e.g. DFAC costs)
- Inadequate written policies and procedures for the billing system
- Failure to adjust billings for changes in indirect rates

DCAA will continue to monitor all aspects of the billing system.

Other Contract Issues

Titan Corporation. Titan was awarded a contract valued at $402 million to provide linguist and translator services to the U.S. Government – mostly in Iraq. Titan presently has over 4,400 linguists working in Iraq. Recent DCAA audits disclosed deficiencies in Titan's labor distribution system, which records costs for Titan employees. DCAA also found that Titan lacked procedures for adequate tracking of hours worked by foreign national consultants. Based on these findings, the DCMA Contracting Officer implemented a 10 percent withhold on all of Titan's labor and consultant costs until all identified deficiencies are corrected and bills to the Government are based on adequate internal controls. The resulting withhold amount could be as much as $4.9 million on future billings depending on the timeliness of the needed improvements. In addition, DCAA recently discovered that Titan was not adjusting their provisional billing rates to actual rates at the end of each fiscal year. Titan agreed to make the necessary billing adjustments of $937,000. Lastly, Titan recently informed us that they will adjust previously billed costs for the Titan employee and the subcontractor employee named in connection with potential abuses at Abu Ghraib Prison. These reductions are scheduled to be made by June 18, 2004 and include Titan and subcontractor costs totaling over $178,000.

CACI. DCAA is expanding its audit coverage at CACI based on recent disclosure of additional contracts awarded to the Company. Since August of 2003, the Army has awarded 11 task orders under a GSA Supply Contract for Information Technology services for interrogation and intelligence gathering effort in Iraq. At least three of those tasks related to interrogation of Iraqi prisoners. Billed costs as of March 2004 under these task orders is $12.7 million, with a total funded contract value in excess of $60 million. DCAA is reviewing the potential misuse by CACI of the GSA schedule contract on this Department of Interior contract that is funded by the Army, since "interrogator" type effort is not a function provided by CACI in their GSA schedule. We understand the GSA and DOI Inspectors General have initiated reviews of this matter as well.

Washington Group International (WGI). In support of the Restore Iraqi Electricity Program, WGI received a contract totaling $309 million. As a result of a WGI proposal to definitize this contract, on February 13, 2004, DCAA reported to the Corps of Engineers' Contracting Officer that WGI had substantial subcontract estimating problems. On February 26, 2004, DCAA also reported to the Contracting Officer that WGI's estimating system deficiencies were significant and required immediate contractor attention. Since that period, DCAA and the Corps have worked closely with WGI to correct estimating system deficiencies and obtain improved subcontract cost support. While WGI has made excellent progress in providing additional documentation for the majority of the unsupported cost, DCAA has suspended over $11.5 million of billed costs because WGI has been unable to support the reasonableness of certain security related subcontract costs. In addition, DCAA has suspended $4.9 million on a separate contract related to costs billed for undefinitzed task orders. As discussed earlier, the FAR limits contract reimbursement until a contract price is definitized to adequately protect the Governments interest. DCAA is working closely with the Corps of Engineers and WGI to address these issues.

Closing

In closing, I want to underscore that I am committed to working with other DoD organizations to insure an integrated, well-managed contracting process in Iraq. The Department will not tolerate the billing of costs that are not properly documented and supported. If internal control systems are deficient, we will continue to use protections, such as contract withholdings and cost suspension to safeguard the Department's interests. Rest assured that I will provide whatever resources are needed for DCAA to continue to provide contract audit oversight in Iraq.

In sum, I believe that DCAA has been vigilant about contract oversight and protecting the taxpayers' interests. I am committed to making sure this continues. I look forward to addressing whatever questions or comments you have on this oversight. Thank you.

Chairman TOM DAVIS. Thank you very much.

Dee, do you want to say anything? Ms. Lee.

Ms. LEE. I have a brief statement.

Chairman TOM DAVIS. That would be fine. Welcome.

Ms. LEE. Good afternoon, Mr. Chairman, members of the committee. I am Deidre Lee, Director of Defense Procurement for the Department of Defense. I am appearing before this committee today to provide information on Iraq contracting actions taken prior to the designation of the Army as executive agent.

As you know, many of you from your personal visits to Iraq, much has been accomplished and progress continues to be made. A vast array of projects improving water, electricity, health care, and education are ongoing. The Iraqis will assume governance on June 30th, and many ministries have already made the transition. On June 8th, Iraq assumed full authority for the national oil sector.

Much of this work is accomplished through contracts, contracts with Iraqi citizens and Iraqi companies, as well as with United States and coalition companies. As we all see on the news every day, operations in Iraq are dangerous and complex. Conditions remain harsh for our soldiers and civilians, including our contractors, and security remains a constant challenge.

As our in-country knowledge and operations have matured, so have our contracting strategies. The contracting strategies employed were those proper for the urgent mission support and protection of our troops. In the last 18 months, we have moved across the spectrum from prewar classified planning through urgent and compelling orders to full and open competition emphasizing inclusion of small business and Iraqi employment.

Procurement actions involving Iraq's oilfields are an example of this compendium. In December 2001, Kellogg, Brown & Root won a competition for the Army's Logistics Civil Augmentation Program. We all call that the LOGCAP contract. This contract was the third contract in a series of competitive contracts, and they provide capability to support global contingencies. We have been doing this since 1992.

In the fall of 2002, a classified requirement to develop a contingency support plan for repair and continuity of operations of the Iraq oil infrastructure was identified by CENTCOM. A task order under the KBR LOGCAP contract was issued on November 11, 2002 by a contracting officer. The order, for planning only, was determined to be within the scope of the global contingency support contract.

In February 2003, based upon urgent operational need, a sole source letter contract consistent with FAR requirements was issued to KBR for pre-positioning of resources such as firefighting equipment to enable rapid response in the event of oil well fires or other critical damage.

In early March 2003, still in the mission preparation stage but moving across this continuum, although for imminent urgency, a sole source indefinite delivery, indefinite quantity contract was awarded to KBR. Task orders were issued against the contract for additional pre-positioning and after the war started for work required to support the mission of repair and continuity of oper-

ations. As noted by GAO, negotiation of this contract on a sole source basis was approved and documented as required by the Federal Acquisition Regulation.

In June 2003, the strategy for competitive procurement to support oil infrastructure in Iraq was approved, resulting in competitive awards in January 2004 to Parsons Iraq Joint Venture for the north and KBR for the south. Work under these contracts is ongoing today.

Iraq contracting is not without issues, as we have discussed this morning and continued to the afternoon. The witnesses here today will talk about ongoing audits and performance monitoring, and what steps we are taking to make sure that money is spent wisely and results are delivered. Government contracting is not a simple process, even in the best of conditions. The Congress has given us numerous laws which govern the contracting process, and has recognized and authorized specific flexibilities to be applied in certain circumstances. Operation Iraqi Freedom is an example of these circumstances and of how our people successfully responded to meet urgent mission needs.

Thank you. I would be pleased to answer any questions.

[The prepared statement of Ms. Lee follows:]

6/15/05 10:00 a.m

Good Morning Mr. Chairman, members of the committee.

I am Deidre Lee, Director of Defense Procurement for the Department of Defense. I am appearing before this committee to provide information on Iraq contracting actions taken prior to the designation of the Army as executive agent. (February 2003).

This hearing has been scheduled as a follow-up to the March 11, 2004 hearing – to provide current status of mission support and contracting in Iraq.

As you know -- many of you based upon personal visits to Iraq – much as been accomplished and progress continues to be made. A vast array of projects improving water, electricity, health care and education are on-going. The Iraqis will assume governance on June 30, and many ministries have already made the transition. On June 8, Iraq assumed full authority for the national oil sector.

Much of this work is accomplished through contracts – with Iraqi citizens and companies as well as with US and Coalition companies.

As we all see on the news everyday, operations in Iraq are dangerous and complex. Conditions remain harsh for our soldiers and civilians, including contractors. Security remains a constant challenge.

As our in-country knowledge and operations have matured, so have our contracting strategies. The Contracting strategies employed were those proper for the urgent mission support and protection of our troops. In the last 18 months we have moved across the spectrum from pre-war classified planning through urgent and compelling orders to full and open competition emphasizing inclusion of Small Businesses and Iraqi employment.

Procurement actions involving Iraq's oil fields are an example of this compendium.

In December of 2001, Kellogg Brown and Root won a competition for the Army's Logistics Civil Augmentation Program (LOGCAP) contract. This contract was the third contract in a series of LOGCAP contracts that have provided capability to support global contingencies since 1992.

In In the Fall of 2002, a classified requirement to develop a contingency support plan for repair and continuity of operations of the Iraqi oil Infrastructure was identified by CENTCOM.
A task order under the KBR LOGCAP contract was issued on November 11, 2002. The order -- for planning only -- was determined to be within the scope of this global contingency support contract.

On February 14, 2003, based upon urgent operational need, a sole source, letter contract consistent with FAR requirements was issued to KBR for pre-positioning of resources, such as fire fighting equipment, to enable rapid response in the event of oil well fires or other critical damage.

In early March 2003, still in the mission preparation stage – although with imminent urgency, a sole source indefinite delivery/indefinite quantity contract was awarded to KBR. Task orders were issued against this contract for additional pre-positioning and positioning and, after the war started, for work required to support the mission of repair and continuity of operations. As noted by GAO, negotiation of this contract on a sole source basis was approved and documented as required by the Federal Acquisition Regulation

In June of 2003 the strategy for a competitive procurement to support oil infrastructure in Iraq was approved resulting in competitive awards in January 2004 to Parsons Iraqi Joint Venture for the North and KBR for the South. Work under these contracts is on-going today.

Iraq Contracting is not without issues. The witnesses here today will talk about on-going audits and performance monitoring and what steps we are taking to make sure that money is spent wisely and results are delivered. Government contracting is not a simple process – even in the best of conditions. The Congress has given us numerous laws which govern the contracting process and has recognized and authorized specific flexibilities to be applied in certain circumstances. Operation Iraqi Freedom is an example those circumstances and of how our people successfully responded to meet urgent mission needs.

Thank you.
I would be pleased to answer your questions.

Chairman TOM DAVIS. Thank you very much.

Ms. Ballard, welcome back.

Ms. BALLARD. Thank you, sir.

Good afternoon, Chairman Davis, Representative Waxman, and distinguished members of the Committee on Government Reform. Thank you again for this opportunity to report to you on the U.S. Army's role in contracting and the rebuilding of Iraq. I respectfully request that my written statement be made a part of the record for today's hearing.

Mr. Chairman, I will be brief. The Army, as executive agent, continues to make progress in an extremely difficult situation by providing contracting and program management support both in Iraq and in the United States. We continue to procure all non-construction items and services to meet the humanitarian needs of the people of Iraq, as well as the economic reconstruction and repair of Iraq's infrastructure.

Have we accomplished this tremendous task without missteps? No, we have not. But I would like to take a moment to make a few comments on the recently released GAO report on Iraq contracts.

We have been in Baghdad for only 10 months, under desperate and dangerous conditions. To date, we have awarded over 2,800 contract actions valued at more than $11 billion, and the GAO reported concluded with only four recommendations. I am very proud of the fact that the Army Field Support Command took positive steps in advance of the report to initiate a process for definitizing outstanding task orders under the LOGCAP contract in a timely manner. Additionally, we are taking proactive measures to address the other three recommendations.

Our contracting personnel on the ground in Iraq now total 65 individuals, more than double what was there when we previously visited the committee. There are multi-service and civilian personnel in Iraq. They are brave, dedicated volunteers who are doing an outstanding job under very dangerous conditions.

I would like to highlight some of the reconstruction accomplishments that we have made since last March. Ms. Lee has highlighted several, so I will be very brief.

Mr. David Nash reported on June 11 that more than 14,000 Iraqis are employed thus far in the rebuilding of Iraq. As Ms. Lee indicated, we are making significant progress in buildings in health, oil, electricity, security, and water. Our accomplishments help to continue the citizens' improvement and movement toward governing themselves and sustaining, operating, and maintaining their own infrastructure. This in turn will help our soldiers, sailors, airmen, and Marines to return home sooner.

This concludes my opening remarks, Mr. Chairman. I would be pleased to answer any questions.

[The prepared statement of Ms. Ballard follows:]

RECORD VERSION

STATEMENT BY

MS. TINA BALLARD
DEPUTY ASSISTANT SECRETARY OF THE ARMY
(POLICY AND PROCUREMENT)

BEFORE THE

COMMITTEE ON GOVERNMENT REFORM
UNITED STATES HOUSE OF REPRESENTATIVES

SECOND SESSION, 108TH CONGRESS

ON CONTRACTING AND THE REBUILDING OF IRAQ

JUNE 9, 2004

NOT FOR PUBLICATION
UNTIL RELEASED
BY THE COMMITTEE
ON GOVERNMENT REFORM

STATEMENT BY
MS. TINA BALLARD
DEPUTY ASSISTANT SECRETARY OF THE ARMY
(POLICY AND PROCUREMENT)

ON CONTRACTING AND THE REBUILDING OF IRAQ

INTRODUCTION

Mr. Chairman and distinguished members of the Committee, thank you for this opportunity to report to you again on the United States Army's role in Contracting and the Rebuilding of Iraq. It is my privilege to represent the Army leadership and the military and civilian members of the Army's contracting workforce who are at the forefront in the rebuilding of Iraq. We are very proud of these dedicated men and women.

THE ARMY AS EXECUTIVE AGENT

On May 21, 2003, the Deputy Secretary of Defense designated the Secretary of the Army as the Executive Agent for the Office of Reconstruction and Humanitarian Assistance, later to become the Coalition Provisional Authority (CPA) in Iraq. On January 14, 2004, the Deputy Secretary of Defense further assigned responsibility for Acquisition and Program Management Support for CPA to the Secretary of the Army.

The Army, as Executive Agent, continues to provide contracting and program management support both in Iraq and in the United States. We are continuing to procure all non-construction items and services to meet the humanitarian needs of the Iraqi people as well as the economic reconstruction and repair of Iraq's infrastructure.

PROGRAM MANGEMENT OFFICE

Led by David Nash, the Program Management Office (PMO) for rebuilding Iraq is located in Baghdad with a support office located in the Pentagon. As the requirement focal point for all Iraqi reconstruction contracting, the PMO is responsible for oversight and implementation of the $18.4 billion appropriated by the U.S. Congress to support the reconstruction of Iraq's infrastructure. The construction sectors are oil, electricity, public works and water, security and justice, transportation and communications, and buildings, education and health.

Overall, $12.6 billion will be spent towards actual construction over the next few years, and $5.8 billion will be spent on providing equipment, supplies and material to help support the construction. Computers are needed to monitor and control electrical transmission and water systems; vehicles are needed to transport materials or to support system maintenance; uniforms and equipment are needed to support the police and civil defense corps; and facilities are needed to educate Iraqi children.

Of the $18.4 billion appropriated in the fiscal year 2004 Supplemental, $11 billion was apportioned to various agencies. Of this amount, agencies have obligated $3.7 billion through June 2, 2004.

PERSONNEL

Our contracting personnel have been on the ground in Iraq since June 2003. We now have a total of 65 individuals there. They are multi-Service and civilian: four Army; five Navy; one Marine; 14 Air Force; and 41 civilians. They are courageous, dedicated volunteers who are doing a phenomenal job under very tough, dangerous conditions.

PROPER PROCEDURES

Currently, the General Accounting Office (GAO), the Army Audit Agency, the Defense Contracting Audit Agency, the U.S. Department of Defense Inspector General, and the CPA Inspector General, in response to a request from

Congress, are reviewing Iraq essential services contracts to confirm that the Army has been following proper procedures. We continue to work closely with them to ensure that they have all the information necessary to complete their work.

CONCLUSION

I continue to have a deep appreciation for the courage, competence, dedication, and efforts of our contracting personnel. The work has been – and continues to be – performed in accordance with proper procedures, by military and civilian volunteers who are concerned and committed to accomplishing their work under the toughest, most dangerous conditions.

We are proud of our role in helping to create and rebuild a stable and successful Iraq. Our work continues to help the citizens of Iraq rebuild, operate, maintain and sustain their own infrastructure. This, in turn, will help our Armed Forces return home sooner.

Chairman TOM DAVIS. Thank you very much.

General Kern, thanks for being with us.

General KERN. Chairman Davis, Congressman Waxman, distinguished members of the committee, thank you for the opportunity to update you on the LOGCAP, Logistics Civilian Augmentation Program. I request that my written comments be submitted for the record.

The LOGCAP contract is executed by the Army Field Support Command, one of my subordinate commands. As noted, this is the third award of the LOGCAP contract. The first, which was awarded in 1992, was to Brown & Root, administered by the Corps of Engineers, covered the Southwest Asia Pipeline, Somalia, and the Balkans. The second contract, which was awarded in 1997, was awarded to Dyncorp and was administered by the Army Materiel Command, my command. It covered East Timor, Philippines, and Colombia.

LOGCAP III was awarded in 2002, as noted, and is significantly different both in magnitude, where the others were in the order of a few hundred millions and this is in the order of a billion dollars; the others were direct contracting and this one includes the management of significant number of subcontractors, many of them for third-country nationals. It includes operations in Afghanistan, Kuwait, Iraq, Djibouti, Uzbekistan, Turkey, and the Republic of Georgia.

I recently did meet with the GAO and reviewed the report which they had previously reported to you in the earlier panel. They were very helpful in pointing out some areas that we needed to improve, as they have been since the earlier LOGCAP contracts, and which we are continuously working for lessons learned and to make an improvement in the way we do business.

I would like to put in context, however, a few of the comments, but note that I do agree with their assessment that we need better planning and better training of our personnel.

First, if we remember March of last year, when we began the operation, there were two contingency parts of the plan: one with the 4th Infantry Division to come in from the north through Turkey, and the second on who went first, the Air Force or the ground operations. In a play at the scrimmage line, the ground operations went first. Critical lesson learned from 1991 was to protect the infrastructure and, hence, the importance of making sure that we had a plan in place for ground operations to ensure that the oil infrastructure was protected in the early phases of the battle. This in part answers the question of why that planning document was critical in those early phases.

The second point that we note there, that the contingency contracting is different than procurement in the continental United States, and, hence, we have adapted to the lessons learned to make sure that the many subcontracts in our cooperation with DCAA, DCMA, and Defense Finance and Accounting System are all working toward prompt payment and correct oversight. This is an area which I think needs continual review as we look at how we do contingency contracting in the future.

I would also note that we were concerned about process, procedures, and costs early on. In June 2003, just 3 months after we ini-

tiated hostilities, I asked my inspector general to oversee the operation of the LOGCAP contract both from the process standpoint and from our ability to meet the needs of the users. They reported back to me in December and I instituted corrective action that they had found through the Army Field Support Command, General McManus. General McManus and I also visited the commanders in Kuwait and Iraq in September 2003, with an expressed purpose of looking at the lessons learned from the Balkan operations on how costs and scope of work could be controlled, and we worked that with the commanders on the ground.

There is no issue that we disagree in substance, but there is in the context of which those operations did occur. We also are looking today that the contracting officers have been asked to support the war fighters requirements, and when there is a disagreement in opinion provided by the legal community, as described earlier, the contracting officer is going to look for the best method of executing the contract, which is the case when we have a difference of opinion, he chose the opinion which would allow him to execute the contract in favor of the war fighters.

Finally, we do have strong partnerships with the Defense Contract Management Agency, which has increased the number of personnel supervising the contract, and we have met with both their civilian and military leaders to continually review whether we have them in the right places and the adequate numbers.

DCAA, as described by Mr. Reed, continues to play a critical role in the oversight and audit of the rough orders of magnitude estimates and the actual execution against the billing processes which is submitted by KBR. We agree and have been working with KBR, Kellogg, Brown & Root, for some time now to improve their billing processes both so we can finish the proposals and get to definitization quickly.

Finally, we are continually learning on the part of Kellogg, Brown & Root on managing significant subcontractors, and on the part of the Government in executing contingency contracts over a broad distance throughout Southwest Asia on how to do our job more effectively for our war fighters.

And I would add one last note, that this past month, earlier in this month, we conducted a memorial exercise in Kuwait for the lost members of Kellogg, Brown & Root. This is not contracting under peacetime conditions, these are tough conditions which they operate.

Thank you.

[The prepared statement of General Kern follows:]

RECORD VERSION

STATEMENT BY

GEN PAUL J. KERN
COMMANDING GENERAL
U.S. ARMY MATERIEL COMMAND

BEFORE THE

HOUSE GOVERNMENT REFORM COMMITTEE

SECOND SESSION, 108TH CONGRESS

ON CONTRACTING IN IRAQ

JUNE 15, 2004

NOT FOR PUBLICATION
UNTIL RELEASED
BY THE COMMITTEE
ON GOVERNMENT REFORM

Mr. Chairman and distinguished members of the Committee, thank you for this opportunity to report to you on the Logistics Civil Augmentation Program.

The LOGCAP III contract, which was competitively awarded to Kellogg, Brown and Root (KBR) Services, Inc., continues to support contingency operations in Iraq, Kuwait, Afghanistan, Djibouti, Republic of Georgia and Uzbekistan.

This support covers the full spectrum of logistics operations. Critical support functions include laundry and bath; facilities and billeting; clothing exchange and repair; waste management and sanitation; food service; mortuary affairs; supply support; maintenance; transportation and distribution; and power generation, to list a few. The austere and dangerous environment our forces operate in today presents significant challenges to the Army to provide this essential support to our troops. The environments in Iraq and Afghanistan are among the most complex our forces have operated in on a sustained basis.

Currently seventy-nine (79) task orders are awarded against the LOGCAP III contract. Of these, sixteen (16) support Operation Enduring Freedom (OEF) and forty-two (42) support Operation Iraqi Freedom (OIF). Total dollars obligated to date is $6.047 billion.

Over 33,000 employees and subcontractor employees are deployed to augment U.S. forces. Of these, approximately 9,500 are United States citizens.

The LOGCAP contractor is constantly responding to changes in requirements due to current troop rotation in support of OIF, the increase in hostile activity and attacks on convoy operations, and planned troop level increases. Planning support is ongoing for the transition of the CPA mission to the Department of State in July.

We continue to make progress to enhance administration of this contract. The Defense Contract Management Agency (DCMA) has over seventy-five (75) contract administration personnel deployed to the area of operations. The LOGCAP Support Unit, U.S. Army Reserve, provides dedicated support and the Defense Contract Audit Agency (DCAA) has a robust presence in theater.

Progress continues in negotiations of the Unpriced Contractual Actions, which we used to initiate rapid response of contract support to the troops. We received qualifying proposals from KBR on thirty-one (31) of thirty-nine (39) currently undefinitized Task Orders. DCAA audited fifteen (15) of these proposals and five (5) have been negotiated.

While we are making progress, we are still learning lessons as we continue to support our operations in theater. These are valuable lessons that will help us improve support in the future. First, we need to improve training, especially of our operational forces on how to use contracting more effectively and very importantly, how to forecast ahead so contracting is considered in the planning phase as early as feasible.

We also need to make some improvements in our contracting process. We continue to use templates from the past that do not meet the needs of today's international environment that demands agility and modularity – strengths our Joint Team is striving for at the same time. We must strive for the same agility and modularity in contracting. We need to consider the impact of contracting in a wartime situation as compared to peacetime and assess what changes we need to make – perhaps in authority and policy. We know we must work in that direction.

We also need to look at the organizational structures we have in place today, and it is apparent that they do not meet the ever increasing overseas requirements, especially in the execution, management and accountability arenas.

LOGCAP provides a flexible, viable alternative for supporting logistics requirements and providing augmentation to our support units for early entry of our forces and long-term sustainment needs that would otherwise place great strains on our warfighters. We have seen an unprecedented level of contractors on the battlefield, comparable to two Army divisions worth of contractors, working side-by-side with our Soldiers. They too, are our troops and we need to ensure that the policies and systems are in place to support and take care of our total force, including our contractors.

We are committed to supporting current operations as we simultaneously transform the military. Supporting our Soldiers remains our number one priority and ensuring they get the very best quality of life as well as other logistic support is a mission essential task of Army Materiel Command. As I described earlier, LOGCAP contracting is a process we need to constantly review and improve. We will continue to improve our program management to ensure world-class support.

LOGCAP relieves a burden on our Soldiers and frees them up to execute war-fighting missions – as well as peacetime missions – so it plays a key role in peace and during war. We have learned lessons and are looking at ways to improve what we do and how we do it. It is vital that we recognize the role of LOGCAP and how it enables us to execute missions key to our national security.

Thank you for what you do for America's Armed Forces and our efforts to support them.

Chairman TOM DAVIS. Thank you very much.

General Crear.

General CREAR. Mr. Chairman, Congressman Waxman, members of the committee, I am Brigadier General Robert Crear, Commander of the Southwest Division, U.S. Army Corps of Engineers. I am honored to appear before you today to testify on the work of the U.S. Army Corps of Engineers in concern with our coalition partners and the Iraqi people. Our mission was to extinguish fires, repair, restore, and rebuild the oil infrastructure in Iraq, and provide vital supplies of diesel, gasoline, kerosene, and propane in order to meet the demands for humanitarian assistance, and to maintain stability and ultimately to save lives. We also had the mission to work closely with the Iraqis to enable them to be able to take over this vital mission.

I returned last November, after serving 9 months as Commander of Task Force Restore Iraqi Oil [RIO]. The task force consisted of approximately 120 U.S. Army Corps of Engineers personnel, active duty military, U.S. Army reserves, coalition forces, Department of the Army civilians, over 500 contractor personnel from Kellogg, Brown & Root, and about 60,000 Iraqi oil workers. U.S. Army Corps of Engineers was assigned the mission in late January and we immediately started to plan to implement the contingency support plan. Our advance party deployed in mid-February, followed by the main body in early March. We had the distinct pleasure of working with Central Command, the Office of Humanitarian and Reconstruction Assistance, the Coalition Provisional Authority, the Combined Forces Land Component Command, Combined Joint Task Force 7, USAID, many NGO's, and other coalition partners.

Early on, we met with Central Command and the Combined Forces Land Component Command staff before deployment. They were able to give us then the combatant commanders' intent and heighten our sense of awareness and urgency for the mission. They wanted to ensure that before hostilities took place, in the event of hostilities, there would be enough equipment on the ground to be able to start putting out fires, to be able to assess the conditions as soon as the facilities could be secured by the forces, and also provide a capability to train coalition forces on actions to take in that type of environment.

The environment I will describe. In the first Gulf war we saw how Saddam Hussein set ablaze over 700 oil wells and caused a spill of over a million barrels of crude oil in Kuwait and in the Gulf. Given the size of Iraq, planners knew that should Saddam employ the same tactic, it would be nightmare for coalition forces in order to execute the tactical mission; it would cause unnecessary delay, could bog down the particular forces, and ultimately cost the death of coalition soldiers. That is why it was imperative to have a plan to execute the oil restoration and be able to put out the fire mission.

The good news is that the coalition forces were able to seize and secure the infrastructure before Saddam could go and do significant damage. However, what we found were not oil well fires, but significant damage due to looting. It was estimated to be about $1.4 billion in overall damage, and about 85 percent of that due to looting. We also found out that the infrastructure was suffering

from years of neglect, misuse, and mismanagement. Added to that was the lack of consistent electricity that directly affected oil production. Additionally, there was no phone system for communications, water, trains. These were conditions that made even the work that would seem to be easy hard in Iraq.

The looting was total. Entire buildings were emptied of their contents, meaning they were looted with only the steel frames remaining. They took everything in total, anything to value, to include wires out of the walls. And this was true of most public facilities, to include the 13 operating companies and their facilities in the oil infrastructure. Needless to say, Task Force RIO faced considerable challenges dealing with this catastrophic situation, as did other coalition forces.

The entire country, about the size of California, was our area of operation, and as we made repairs to this fragile oil infrastructure between the southern fields in Rumaila and the northern fields in Kirkuk, each task force personnel rose to the occasion. They were subject to personal hazards with movements throughout the country. I visited our wounded personnel, both military and contractor personnel, in field hospitals and I mourned the death of others.

Some of the accomplishments that I will highlight to you and am very proud to talk about is that we had civilians and contractors on the ground in Iraq Day 2 of the war, and they continue to remain there and continue to operate to restore the infrastructure. By April 13, all oil well fires were extinguished. By mid-April we had re-established the leadership, re-employment of the north oil companies in Kirkuk and the south oil companies in Basra, producing the first oil for export by June 22nd. We are now at the prewar level of production, since March, producing over 2 million barrels of crude per day. Revenues being produced are about $1 billion per month since June. This goes to the Development Fund of Iraq for use by the Iraqi people.

A mission that we had not planned for, but were faced with, was the shortage of refined products. We have imported refined products by the billions. We have prevented a humanitarian disaster, a forced security issue for our coalition forces, and loss of life.

I was happy to see recently that as of June 8 the Oil Ministry is the first Iraqi ministry to become fully functional and responsible for its future direction. That would not have happened without the efforts of the task force. And by the end of May we had executed over $2.5 billion to restore the oil infrastructure. I note that most people don't realize $1.7 billion of that came from the Development Fund of Iraq, and not taxpayers' dollars, and most of that money went to import the fuel into the country.

I am enormously proud to lead men and women of the U.S. Army Corps of Engineers, and I am continually inspired by their technical and diplomatic skills and their selfless service. On the ground there is only one team, consisting of coalition forces and civilians, contractors to include KBR, and Federal employees united with one purpose: to make Iraq a better place for the Iraqi people. Those that have deployed always say two things: that they volunteered because they knew they could make a difference and, two, I can't wait to get back. I have also witnessed what happens when they return: they bring a renewed energy and enthusiasm that is clearly

evident as they accomplish their work back home. I am proud to have been part of such a team with such a vital mission. Progress is staggering.

Thank you very much.

[The prepared statement of Brigadier General Crear follows:]

DEPARTMENT OF THE ARMY

COMPLETE STATEMENT
OF

BRIGADIER GENERAL ROBERT CREAR
COMMANDER, SOUTHWESTERN DIVISION, U.S. ARMY CORPS OF ENGINEERS

FOR THE HEARING BEFORE THE

HOUSE COMMITTEE ON GOVERNMENT REFORM
UNITED STATES HOUSE OF REPRESENTATIVES

1100 HOURS, 15 JUNE 2004

INTRODUCTION:

Mr. Chairman and members of the Committee, I am Brigadier General Robert Crear, Commander of the Southwestern Division of the U.S. Army Corps of Engineers. I am honored to appear before you today to testify on the work of the United States, in concert with our Coalition and Iraqi partners, to repair and rebuild the oil infrastructure in Iraq.

Last October, I returned after an eight months' tour in Kuwait and Iraq where I served with Task Force RIO (Restore Iraqi Oil). As Commander of the Southwestern Division, I have been involved with restoration of the Iraqi Oil system since the Corps was assigned the mission to begin planning to implement the contingency support plan back in January 2003. I deployed to Kuwait just prior to commencement of hostilities and commanded Task Force Rio during the early stages of getting the oil system back into production. I had the distinct

privilege of working with the Office of Reconstruction and Humanitarian Assistance, the Coalition Provisional Authority's Oil Minister, the excellent staff of the Iraqi Oil Ministry, the Oil Ministry's 13 operating companies, and the Combined Forces Land Component Command. I truly enjoyed the fine teamwork of these organizations as they shared tasks to get the oil infrastructure back into production.

PLANNING PRIOR TO THE WAR

As is usual in military operations, planning for post war reconstruction was conducted simultaneously with planning for war. These plans involved restoration of the oil system and included extensive use of contractors to supplement military and governmental capacity. Prior to the war, we originally expected we would have to repair the damage caused by military action, deal with the resulting humanitarian crisis, and set the stage for the new Iraqi government to oversee further exploration, production, refining and distribution facilities. Of greatest concern, however, was that Saddam Hussein's regime would repeat their actions of the Gulf War, where they set ablaze and crippled a large portion of the Kuwaiti oil infrastructure. Understanding that the flow of oil was the essential lifeblood of the future, free Iraqi economy, the Acting Secretary of the Army designated the US Army Corps of Engineers as the executive agent for Iraq Oil Infrastructure Reconstruction, and we formed Task Force Restore Iraqi Oil (RIO) to fight the expected fires and to repair any damage. Task Force

RIO also trained the forward troop units in shutdown techniques and then followed on the heels of the initial assault to make the oil system safe.

WHAT WE ENCOUNTERED

As it turned out, when we entered Iraq, we encountered relatively little war damage, but instead found an infrastructure crippled by a combination of long-term neglect, devastating looting, and damaging sabotage. The country's infrastructure was sagging under the weight of 30 years of neglect, misrule, and mismanagement. There was precious little dependable electricity to support the oil infrastructure, very limited public water supply, no sewage treatment, no communication system except what we brought with us, no railroads in operation, only limited other modes of transportation, and basically very little means for the new Iraqi government to do its work. This meant the oil system could not rely on any support from these basic infrastructure systems. Virtually all public buildings, as well as the thirteen companies which made up the Iraqi Oil Ministry and their contents – records, equipment, supplies – were destroyed by looters and saboteurs. This made it almost impossible to reestablish production data and very difficult to determine which areas of the infrastructure to concentrate on for the most gain. Furthermore, many of the experts on the country's infrastructure were Ba'ath Party members who had fled or had been removed. Under the Sadam Hussein regime, public servants did only what they were told by their supervisors, so there was no tradition of individual initiative to fill the void. Our

relatively small cadre of advisors faced considerable challenges dealing with this catastrophic situation.

During the early reconstruction period, the effects of widespread sabotage and looting constantly undermined our efforts. Because we had anticipated and planned for operations in just such a difficult and dangerous environment, one of our immediate major efforts in the early days was to secure critical facilities. The damage resulting from the actions of saboteurs and looters, however, still turned out to be significant. For example, the communication system for the Iraqi Oil Ministry was looted and destroyed, office records and equipment were looted or destroyed, fuel pipelines were sabotaged, and large pumps and major pieces of equipment were removed. No oil system plant had dependable electricity because many high voltage electricity transmission towers were toppled or significantly damaged as result of the war, sabotage and looting, as criminal elements scavenged copper and aluminum from the high voltage wires.

The greatest problem we faced, however, was dealing with an oil infrastructure that had been neglected and mismanaged for many years by the Saddam Hussein regime. The country suffered from a lack of capital investment as Saddam chose to purchase weapons and build palaces instead of repairing and improving refineries, gas plants and the means to deliver refined products to the citizens of Iraq. It is a tribute to the Iraqi engineers and staff of the Iraqi Oil Ministry that the country's oil system was able to function at all, and that we were able to assist in restoring them as quickly as we did.

All members of Task Force RIO were subjected to personal hazards as well. Movement throughout the country was extremely dangerous and required extreme security measures. It should also be noted that those of us who were part of Task Force RIO initially suffered many of the same hardships as the Iraqi people. Like them, we did not have basic services such as power, and sewage, nor did we have an adequate work area. Also like them, we were greatly hampered by the lack of reliable communications in the area. In fact, we often had no communications at all.

WHAT WE DID

Again, in Central Command's planning for Operation Iraqi Freedom, safety and security of the oil fields were considered paramount to the overall success of the operation. By setting the oil fields of Kuwait afire during the Gulf War, Saddam Hussein had already demonstrated a callous disregard for human health and the environment. Task Force RIO's immediate mission was to secure the oil fields, put out the fires, and get the oil flowing to provide refined fuel products for domestic use and ultimately oil for export. With more than 1500 wells in the Iraq Oil Fields, the potential for disaster was enormous. We knew that this effort would require extensive contractor involvement and we knew that the short notice, requirements for secrecy, and essential nature of the mission would hamper our contracting flexibility.

Task Force RIO was initially headquartered in Camp Doha, Kuwait, but later moved to Bagdhad. RIO operated with two remote field offices, each located in

the two major oil fields – Rumaila and Kirkuk. Task Force Restore Iraqi Oil (RIO) was very successful. Even before the ground war was over, we worked with our military forces to ensure the safe shutdown of the oil facilities. Rather than the hundreds of fires that were predicted, there were only 9 oil fires as a result of the war and we extinguished, in a cooperative effort with the Kuwaitis, those fires by 13 April, less than a month after entering the oil fields. Also, in spite of unprecedented looting of oil, power and other infrastructure, we were able to immediately begin an assessment of infrastructure repair needs and initiate repairs. Some of our early accomplishments included the reemployment and reestablishment of the Northern Oil Company in Kirkuk and the Southern Oil company in Basrah by mid-April, producing "1st Oil" from the wells to the refineries on the 22nd of April, and producing our first exported oil by the 22nd of June. Recently, the Iraqi Ministry of Oil has produced over 2.5 million barrels per day, with exports of 1.8 million barrels per day resulting in the receipt of over $10.0 billion to the Iraqi government. These daily production amounts are comparable with pre-war levels. In addition, while repairing the oil production and refining infrastructure, we helped to prevent civil unrest by importing over 1.7 billion liters of gasoline since May 2003 for humanitarian assistance, and large amounts of other needed types of fuel including liquid petroleum gas (over 500,000 metric tons), kerosene (over 700,000,000 liters), and diesel fuel (over 579,000,000 liters). In essence, we went from a small advance party in mid-March to a substantial operating division within just a few months, executing more than $2 billion in repair and humanitarian assistance in less than a year.

It should also be noted that, as of last Tuesday, 8 June 2004, the Iraqi Ministry of Oil has assumed all command and control of oil in Iraq. This transfer of sovereignty was accomplished ahead of schedule and is due in large part to the efforts of the Corps and its contractors, and the incredible skills and abilities of the Iraqi people who managed to keep a decrepit system going all these many years.

OTHER MISSIONS IN IRAQ

In addition to our work on Task Force RIO, the Corps has been assisting in the restoration of the power system in Iraq. In partnership with the Iraq Ministry of Electricity and the United States Agency for International Development (USAID), we have added more than 1300 MW of new power generation to the power grid in Iraq since Fall 2003. That number is expected to grow to 2000 MW once USAID/Army Corps current projects are completed this summer. In total, nearly one-third of new electric generation capacity in Iraq will be the result of the Corps civilians and soldiers working side-by-side with Iraqi engineers, USAID and contractors. In conjunction with supporting projects under the supervision of the USAID in support of the Ministry of Electricity, the Corps is continuing its efforts towards meeting its share of the 6000 MW goal for capacity by June 2004.

Upgrades have included the replacement of 600 km of transmission lines. Moreover, since September 2003, 5,355 miles of conductor has been restored or improved to date. That is enough to stretch from Savannah, GA to San

Francisco, CA and back to Cape Cod, MA and into Buffalo, NY – crossing our nation twice! To put all this in context, prior to the war, Saddam used electricity as reward and punishment with Baghdad receiving 24 hours of electricity per day while other areas were receiving less than 9 hours per day. Once current projects are completed over the next few months, and as local programs improve local distribution, all Iraqi citizens should receive reliable power 16-18 hours per day. The Corps is also continuing to support USAID as they work on long-term restoration of power in Iraq.

The Corps has also been responsible for the CEA (Captured Enemy Ammunition) program for Iraq. As you are all aware, under Saddam Hussein, Iraq was literally stockpiled in ammunition of various types, origin, and condition. This ammunition poses not only a threat to coalition forces and efforts to establish democracy, but they are also a threat to the citizens of Iraq as insurgents use them for indiscriminate IEDs and other terrorist activities. To date, the Corps has secured 264,000 tons and destroyed another 117,000 tons. It is expected that by September of this year, the Corps will have secured all the hundreds of thousands of tons of ammunition and have either demobilized it or secured it for future use by the Iraqi Defense Forces.

The primary reason we have been able to mobilize so quickly and contribute so significantly to winning the peace in Iraq is due to our ability to draw on an existing, highly trained and skilled Corps of Engineers workforce. In their normal jobs, my staff work as project managers, office and field engineers, contracting

officers, logistics managers and the like. We were able to draw on this expertise and move small numbers of our personnel, all of whom were volunteers, to similar positions in Iraq where they performed tasks similar to those they do in the United States. They are accustomed to accomplishing objectives through contractors. Our normal RIO staff of about 80 personnel in Iraq essentially managed the work of about 500 contractor personnel and a portion of the Iraqi Oil Ministry workforce. This in-country staff (normally serving 120-day tours) was drawn from 28 Corps Districts across the U.S. We also organized to minimize our in-country staff and draw heavily on our Southwestern Division staff in Dallas for much of our logistical, contracting, resource management, public affairs, legal, human resources, military contingency management, administrative and technical support. We were also able to coordinate many complex issues through regular videoconferences using our portable tele-engineering equipment located in our headquarters and field offices thereby minimizing the need for expert personnel to be physically in Iraq.

In addition, from the beginning of planning through today, we recognize that the enormity of the tasks facing us requires extensive contractor involvement on the Corps and Coalition teams. This need was not unique to either our prior wartime experience or our day-to-day operations at home and abroad. The contractors involved in the reconstruction effort brought extraordinary technical expertise, dedication and commitment to the team. I believe we would not have enjoyed the success we experienced without their contributions.

CONCLUSION

I am intensely proud that I had the opportunity to work alongside the extraordinary professionals in the U.S. military and coalition forces, Department of Defense civilians, our contractors and the new Iraqi government. I am also proud of the success of Task Force Rio and the long-term contribution is has made to an emerging free and democratic Iraq. Thank you for allowing me to spend time with you today. I will be happy to take your questions.

Chairman TOM DAVIS. Well, thank you very much.

Let me just ask each of you, did the fact of the Vice President was a former CEO of Halliburton influence the selection of Halliburton and KBR in any way?

Mr. Lanzilotta.

Mr. LANZILOTTA. No, I know of no instance.

Mr. REED. Not to my knowledge.

Ms. LEE. No.

Ms. BALLARD. No.

General KERN. I know of no incident.

General CREAR. No, sir.

Chairman TOM DAVIS. Were you or anybody in your office pressured by any political appointee or high official in the administration to award any contract or task order to a particular firm, or go easy on any contractor in carrying out contract oversight activities?

Mr. LANZILOTTA. No.

Mr. REED. No.

Ms. LEE. No, sir. In my 29 years of Government service, I have frequently had congressional remarks, but I have never——

Chairman TOM DAVIS. I didn't ask that, Ms. Lee.

Ms. LEE [continuing]. I have never had an executive department direct, no.

Chairman TOM DAVIS. OK. Thank you.

Ms. BALLARD. No, sir.

General KERN. No, sir.

General CREAR. No, sir.

Chairman TOM DAVIS. Mr. Lanzilotta, will you walk us through the KBR as one of the contractors selected to assist Government in planning of the Iraqi war continuances?

Do you want to yield to Ms. Lee on that?

Ms. LEE. Could you repeat the question, sir?

Chairman TOM DAVIS. I just wonder if you could walk us through the selection of KBR, how they were selected, so everybody can understand that this didn't come down with a memo from the Vice President's office to reward his former company. Could you walk us through how KBR was selected? I think it is important for everybody to understand how this happened.

Ms. LEE. Certainly, I will give an overview, and then General Kern may want——

Chairman TOM DAVIS. And let me ask you, Ms. Lee, since you are talking. You were a political appointee in the Clinton administration, is that right?

Ms. LEE. Yes, sir.

Chairman TOM DAVIS. And you are a professional career officer?

Ms. LEE. Yes, sir.

Chairman TOM DAVIS. Thank you very much.

Ms. LEE. The first LOGCAP contract, when we are talking about the competitive contract in 2001, was a standard competition, where we would run a competition, contractors would propose. To the best of my knowledge, we received three proposals that were evaluated; the contract was awarded. A year later the decision, when we were discussing how to in fact support, first identify the mission. I think one of the things we kind of get a little confused here is what are the operational requirements. And those are very

broadly discussed across the Department possibly, and probably beyond the Department, is do we really need to be prepared to do protection oil infrastructure. Those requirements are discussed. Once it is determined that, yes, that is a requirement, the contracting team gets involved and says, OK, how do we properly structure the business arrangement to support that.

In this particular case, after much discussion and a legal opinion, we determined that, for urgency and some other good and valid reasons, to issue an order against this existing LOGCAP contract.

Chairman TOM DAVIS. And who is the contracting team, are these basically career civil servants?

Ms. LEE. Yes, sir. A contracting officer would be awarded, a contracting officer civil servant. I am aware of no political appointees that have been contracting officers.

Chairman TOM DAVIS. Any active duty military involved in this?

Ms. LEE. Could be active military as well.

Chairman TOM DAVIS. OK.

General KERN. If I could add, Mr. Chairman, to that. It was the decision of that discussion of the requirement that Ms. Lee referred to which resulted in the use of the LOGCAP contract. Prior to its use, however, there were a number of opinions which were debated back and forth between the command counsel and my headquarters of the Army Materiel Command, the Department of the Army General Counsel's Office, and the DOD General Counsel's Office. And so we have three different legal discussions that were going as to whether it was in the scope of the contract or not.

In the opinion of my command counsel, he thought it was outside of the scope. In the opinion of the further discussions, it was decided that it was in the scope of the contract to proceed for the planning only. But the decision also said that we should proceed further with a requirement for a sole source award only with a justification and approval of that, which required us to go through a second process and a second contract effort; and that is the process which was followed. The contracting officer, looking at all those opinions, made the decision first to use it for the Brown & Root contract, the KBR contract for LOGCAP for planning, and then to ask for a J&A for approval to go forward from that position. That was the process.

Chairman TOM DAVIS. Now, it appears at one point, I don't know if any of you would have firsthand knowledge, that there were officials notified that the decision was made to award it to KBR, officials in the administration were notified prior to that. Is that a normal procedure in a large contract of this nature?

General KERN. Mr. Chairman, as you noted earlier, that is a normal procedure. We notify the Congress and the White House when we have contracts to be awarded.

Chairman TOM DAVIS. The Vice President's office in this case. Evidently there is some allegation that they knew about it. Do you know anything about that?

General KERN. I have seen the same information that you have. I couldn't tell you anything more about what may have taken place.

Chairman TOM DAVIS. It didn't strike you as out of the ordinary?

General KERN. The notification process has appeared to me to be very normal.

Chairman TOM DAVIS. All right.

Dee, you have been involved in this for years. Is that out of the normal, to involve Members of Congress or the administration? And would you tell them this was happening or would you say this may happen, or do you have any input, or how does that work?

Ms. LEE. Sir, you were right when you mentioned earlier we have a very kind of formal internal procedure when a contract is ready to get awarded. In fact, we award it after the old day's close of the market, late in the day; we notify Congress before, we make the phone calls. There is actually a process and it includes public affairs in many cases so that the Congressman with the winner in their district can in fact notify them. So there is a process. And it would be quite normal to follow that process.

Chairman TOM DAVIS. Yes, General Crear.

General CREAR. Sir, the other thing you could add to that is that at that time we were in a contingency planning mode, at that time the contingency plan was classified, and so we needed to have the contractor be able to let people know what mission they were going to be able to do in order to hire people. And so to get that to happen, they had to do notifications. They felt, certainly, that if the contingency plan is going to be declassified so you can hire personnel, then we wouldn't want KBR or Congress to find out about that we actually had a mission in the Department of Defense to secure the oil without letting you know that from us first, and that was really the purpose of getting the declassification and the notification.

Chairman TOM DAVIS. How did Mr. Mobbs become involved in this? Can anybody explain that?

Ms. LEE. I do know Mr. Mobbs. My first recollection of this was actually from my then-boss, Pete Aldridge, and it was the summer of 2002, very late in the summer, maybe even early fall; and he said we have a classified project I want to talk to you about, and he said basically what we are doing is planning to support, should there be fires and the time being appropriate, when we enter conflict, and said we are looking at how to do that; and, in fact, we assigned a contracting person to work with their team just to go through what the plan was, what the requirement was, and how it could be properly contracted for.

Chairman TOM DAVIS. And the fact that this was classified strikes this as probably appropriate in this case?

Ms. LEE. Yes, sir, given the timing.

Chairman TOM DAVIS. OK.

Let me yield to Mr. Ose for just a few questions.

We are doing 15 minutes on a side, so this is part of our 15.

Mr. OSE. Thank you, Mr. Chairman. I appreciate the opportunity to have some time. I, in particular, want to direct my questions to Ms. Ballard.

I know that the chairman and the ranking member have asked you about this previously, but subsequent to the September 11th hearing there were questions put forward. I can't express quite accurately the depth of my dissatisfaction with the fact that I do not have answers to questions 3 months old, even though we are now having the second of a series of hearings. I presume we are going to have another one in July. And I am curious whether or not I am

going to have answers to my questions by the time we have that third hearing.

Ms. BALLARD. Congressman, I too am very disappointed that the answers have not been provided to you. We have discussed this. The answers are in review and you will have them, sir. If I have to walk them over here personally, you will have them.

Mr. OSE. Well, I haven't moved since the last time we gathered, so you can still find me at that same spot.

Ms. BALLARD. Yes, sir.

Mr. OSE. I want to make sure that—rather than belabor the point, if you can get me answers to the questions that I have already asked, I will be able to pursue a line of questioning accordingly.

But, Mr. Chairman, I have to say I have done my fair share of contracting for my own account, and with all due respect to these witnesses, when I have control of the checkbook, I get my answers before I write checks. And I have to tell you I am just dissatisfied.

Chairman TOM DAVIS. Well, I think Ms. Ballard is going to make every effort to get you answers as expeditiously as possible. Thank you.

Let me ask you. I am still puzzled on Mr. Mobbs' role in this. I have gotten different conflicting opinions. Was he a decision-maker in this or is just a guy who is popped off in the press? What was his role in this?

Ms. LEE. Mr. Chairman, I know his role to have been in the Department, in working in our planning shop, our planning organization, we had a group of people, pre-conflict, saying what is it we need to do. Now, there has been some discussion here in this meeting today saying, well, you know, you focused on oil, but what about the operations themselves. Those operations were planning for the operation, as General Kern has talked about, that is done by the combatant commanders, and they were planning their own operation in accordance with whatever direction they were given.

This particular planning piece was kind of that infrastructure planning as to how do we get ready. And I know Mr. Mobbs, working in the planning organization, was kind of the head of that planning group to figure out how to support.

Chairman TOM DAVIS. So it is your understanding he was more of a big picture guy than the contracting officer with the warrant out there.

Ms. LEE. Yes, sir. As we do with all our contracts, we have a requirements group and we kind of hash out what is it we really want to do, what are the parameters for that, and then from a contracting standpoint, OK, if that is what you want to accomplish, what is the right business arrangement.

Chairman TOM DAVIS. A couple other questions occurred to me. One is when a truck would go down with a flat tire in a convoy, was it Army procedure at that point that we don't stop and repair the tire, we keep the convoy moving at that point, rather than stop and prepare, because that was danger, or was that a contractor decision? This has been an allegation by someone who hasn't appeared before the committee formally but has been interviewed.

General KERN. The convoys have taken different context over time. As we moved our forces centrally into the Baghdad region, we

were running numerous convoys between Kuwait and Baghdad that would be up to 300 vehicles a day moving, primarily focused on fuel and munitions, sometimes carrying food and parts. It is normal practice for convoys like that to carry spare vehicles, with the assumption that something would break down on that long a route, and those highways are not exactly like Interstate 95. So you expect that you are going to be under rough conditions.

If you remember, because the part that I cannot precisely tell for you is the timing of when that occurred, because this spring those convoys started coming under considerable attacks. Bridges were taken out; convoys had to be replanned around them. More security was provided to those convoys as those attacks intensified. So at one point in time we actually stopped running them and were flying supplies into Baghdad. So there were periods in there in which the tactical commanders were making decisions in conjunction with the convoy commanders about the security on that route and what would take place. And so in some cases they may have decided that a security arrangement said it was too dangerous to stop and try to recover a vehicle, and it was better to decommission it than let it fall into the hands of those who were attacking it. But I cannot precisely tell you because each convoy was run under a different set of security conditions during that period.

Chairman TOM DAVIS. Mr. Reed, let me ask you how many of the 285 audits referenced in your testimony were related to Halliburton KBR, any idea?

Mr. REED. I don't have a specific number, Mr. Chairman, but I would be happy to get that for you for the record.

Chairman TOM DAVIS. Can you give me a ball park? Was it 5, 30?

Mr. REED. I would say probably in the neighborhood of 20.

Chairman TOM DAVIS. OK. And a referral to the IG, is that a rare thing in your business; is it a unique thing; is this a once in a year happening or does this happen more often?

Mr. REED. To put it in some perspective, I believe in fiscal year 2003 we issued approximately 60 referrals. Some years we have issued several hundred. So that gives you some perspective on the question.

Chairman TOM DAVIS. As a general counsel to a contractor, you are on the receiving end to one of those, but then the process would be able to go to the IG, and then if they see anything, they would refer to Justice would be one possible way to handle it, correct?

Mr. REED. That is correct, because a referral is not a conviction, it is merely that the auditor has some reason to be concerned, and he is turning it over to experienced investigators who have the wherewithal, as well as the legal advice, to judge whether there has been a violation of civil or criminal law.

Chairman TOM DAVIS. And I want to make sure I am clear about the relationship between the DCAA auditors and the contracting officer. It is my understanding that the DCAA auditors act as professional advisors to the contracting officer on cost, pricing, and related matters. The contracting officer is free to take that advice or not. For example, DCAA may find there is an overcharge of, say, $1 million. The contracting officer can agree or not based on his or

her judgment. Any action against the contractor would be initiated by the contracting officer rather than DCAA?

Mr. REED. Yes, that is correct. Many, in fact, most of the contract issues that DCAA raises are judgmental issues that involve advice of not only DCAA, but also technical people, engineers and so forth. And we fully expect that the contracting officer is going to be advised by others, and in most cases attempt to negotiate an issue where there is not certainty. Where no one party is absolutely right or wrong, we negotiate it.

Chairman TOM DAVIS. And my time is up, but this can get pretty complicated, can't it, sometimes between the lawyers and the accountants in terms of judgments?

Mr. REED. Yes, sir.

Chairman TOM DAVIS. Thank you very much.

Mr. Waxman, you have 15 minutes.

Mr. WAXMAN. Thank you.

Mr. Chairman, your first question today of each of the members of this panel was whether any influence took place from the Vice President's office, and each one responded no. But this is a very different question than you asked in the March hearing. This is what you asked in the March hearing: I want to get this on the record, and everybody is under oath. Have you or anyone in your office ever discussed with the Vice President or with his office the award of a contract for Iraqi reconstruction prior to any contract being awarded? And General Schrock said, "No, I have not;" General Kern: "No, sir, I haven not;" General McManus: "No, sir, I have not;" Ms. Ballard: "No, sir, I have not;" Mr. Zakheim: "No, sir, I have not;" Mr. Reed: "No, sir, I have not;" Admiral Nash: "No, sir, I have not."

Is that the testimony of each of you today? And the question, of course, let me repeat it, is: Have you or anyone in your office ever discussed with the Vice President or with his office the award of a contract for Iraqi reconstruction prior to any contract being awarded.

Mr. REED. My answer remains the same.

Mr. LANZILOTTA. My answer remains the same as Dr. Zakheim gave at the previous hearing.

Ms. LEE. No, sir, I have never met the Vice President or talked to him. It would be an honor, but I have not.

Mr. WAXMAN. No, that is not the question of you. Would you or anyone in your office?

Ms. LEE. Not that I know of.

Mr. WAXMAN. OK.

Ms. Ballard.

Ms. BALLARD. No, sir, not that I know of.

Mr. WAXMAN. OK.

General KERN. My answer remains the same. I know of no one in my office who has talked to.

General CREAR. Sir, not me or anyone in my office.

Mr. WAXMAN. The problem is that we have now got additional information from Mr. Mobbs, and Mr. Mobbs told our staff collectively that he tried to make a decision as to who ought to have this planning contract in October 2002, and so he talked to different people on his own. He talked to oil executives, he talked to DOE,

and maybe others as well, to try to figure out who would do the best job. And he said there were three companies that could have done the job: Bechtel, Fluor, and Halliburton. And he thought Halliburton would be the best one to choose, and he went to this deputies committee made up of representatives from the political side of each office, including Scooter Libby, who is the political chief of staff of the Vice President of the United States, and other deputies and secretaries in charge of State and Defense, and whoever else was at the meeting. And he went to them to get their assent, their agreement that this would be OK to ask Halliburton to do this planning, and they didn't object. And then he went to the career people and said this is the decision, we want to award this to Halliburton. In fact, he even wrote what is called the justification and approval document and gave it to the career people.

Do any of you know facts to contradict what I have just said?

Mr. LANZILOTTA. Sir, on the deputies committee meeting, I wasn't at the deputies committee meeting, but I was told two things were made clear.

Mr. WAXMAN. Wait a second, you were told by somebody else, but you weren't at the meeting.

Mr. LANZILOTTA. That is correct.

Mr. WAXMAN. Now, you have said that you know about a deputies meeting. Was somebody there at the deputies meeting from the Vice President's office that you know of?

Mr. LANZILOTTA. I was told there was a representative from the deputy's office.

Mr. WAXMAN. Well, I just asked you the question, which Mr. Davis asked last time, have you or anyone in your office ever discussed with the Vice President or his office the award of a contract. So you know somebody in your office had discussed with somebody in the Vice President's office?

Mr. LANZILOTTA. No, that isn't what I said.

Mr. WAXMAN. OK.

Mr. LANZILOTTA. I didn't say that anybody in my office was at the deputy's committee meeting or anybody in my office has ever talked to the Vice President or his office concerning this contract, or, for that matter, concerning any matter.

Mr. WAXMAN. Do you know what was discussed at the deputies meeting?

Mr. LANZILOTTA. But I was told from the deputies meeting that two items were discussed when this came up. I was told one, that it was perfectly made understood that this conversation of the deputies meeting would not be shared with the Vice President and two, that the Vice President wouldn't have any involvement in the contract. And that was made known to all the members at the deputies meeting.

Mr. WAXMAN. And when were you told that?

Mr. LANZILOTTA. I was told that today.

Mr. WAXMAN. So it is not contemporaneous with October 2002, it is contemporaneous with a hearing that points out that perhaps there was more involvement with the Vice President's office and people in this administration than they ever let on. Let me just read to you what——

Mr. LANZILOTTA. Well, may I clarify that? It wasn't until yesterday that I was even told I was coming to the hearing, and so I have done some research in preparation for the hearing.

Mr. WAXMAN. Well, let me ask you this. Who told you this?

Mr. LANZILOTTA. Pardon me?

Mr. WAXMAN. Who told you this information about the deputies meeting?

Mr. LANZILOTTA. I got this from Mr. DiRita.

Mr. WAXMAN. And who is he?

Mr. LANZILOTTA. He is the Acting Public Affairs Officer.

Mr. WAXMAN. Of?

Mr. LANZILOTTA. Department of Defense.

Ms. LEE. Mr. Waxman, if I may.

Mr. WAXMAN. Was this fellow that told you about it at the meeting, to your knowledge?

Mr. LANZILOTTA. I don't believe he was.

Mr. WAXMAN. So you are telling us that somebody who wasn't at the meeting told you a story about what happened at the meeting.

Mr. LANZILOTTA. Well, I think I made it clear that I got it from somebody else. I never meant to represent that I was there or knew anybody there.

Mr. WAXMAN. No, no, no. Did the fellow who told you about this, Mr. DiRita?

Mr. LANZILOTTA. DiRita.

Mr. WAXMAN. Do you know whether Mr. DiRita was at that deputies meeting?

Mr. LANZILOTTA. I don't know.

Ms. LEE. Sir, if I may. Again, one of the things in contracting that is not at all unusual for a requirements organization or a program manager or a mission needs person, in fact, it is encouraged under the Federal Acquisition Regulation and the new FASA, is to go around and do what we call market research and say who could do this kind of work, who is in this kind of business; and then the technical community discusses that requirement and learns more about the marketplace before we make a buy.

In this particular case, my understanding is that is the kind of discussion that was ongoing, which is—What is it we really need to do? How do we fight fires? What would happen if? What would that requirement look like.

Mr. WAXMAN. No, I think it is absolutely reasonable, and I am not charging, because I don't know enough information, that there was any wrongdoing. What I am pointing out is that Mr. Mobbs' report to us is inconsistent with the statements we have heard from the Vice President and people in this administration who told us they didn't know anything about it, they were never involved, their office wasn't involved, and it was done by only career people. So that is the point I am making.

We have made a document request for additional information that has been submitted to the Vice President and the President and others, and that will help us; we will know more after that.

Mr. Reed, I want to go to you, because you were here last March and you talked about, at that time, that there were major problems with Halliburton. You issued a report on December 31 and then a memo on January 13th highlighting deficiencies in the way Halli-

burton and its subcontractors estimated their costs. Halliburton argued that these were only isolated problems; you disagreed, calling them systemic and significant. You said they were so serious that you warned other Pentagon agencies not to negotiate further contracts with Halliburton until they talked to you.

Mr. Reed, I would like to know whether the problems you identified in December and January have now been remedied, 6 months later. Let me ask you have you received information from Halliburton that has caused you to change the conclusions in your December or January reports?

Mr. REED. We continue to work the issue with Halliburton. It is not resolved yet. And I wanted to point out in regards to our comment about "not awarding until you talk to us." It is important to put that in the context of what we really were seeking, that is for contracting officers to ask us to assist them in evaluating estimates, particularly, in those areas indicated potential deficiencies in those estimates. And so if someone had contacted us, we would have said, "would you like us to assist you in evaluating the pricing information or the cost data." It was not DCAA's intent that the contracting officer not award a contract unless DCAA said yes, OK.

Mr. WAXMAN. That wasn't really the point I was asking about. I was asking about an opinion you issued the last time you were here and in those two memos, and you said the problems were systemic and significant. What I want to know is do you think there are still systemic and significant problems with Halliburton estimating systems as far as you are concerned?

Mr. REED. Yes, sir, those problems continue; they are not resolved.

Ms. LEE. Sir, if I may.

Mr. WAXMAN. I would like to pursue some questions with Mr. Reed first, and then we will let you jump in on this.

Your May 13th report, which is the most recent report on Halliburton, instead of the company's estimating system, you focused on its billing system, how they bill the Government for their work, and again you found significant problems, and I want to read from your report. "Our examination disclosed several deficiencies in KBR's billing system resulting in billings to the Government that are not prepared in accordance with applicable laws and regulations and contract terms. We also found material invoicing misstatements that are not prevented, detected, and/or corrected in a timely manner. As a result, KBR is not authorized for direct billing and will be required to continue to provide all billings to DEAA for provisional approval."

What does it mean that Halliburton has major problems with both its estimating system and its billing system? Are the problems compounded?

Mr. REED. Well, they do overlap somewhat, in the sense that costs that are proposed ultimately will be billed. If there are issues in terms of the reasonableness of the cost when you are evaluating the proposal, those same issues, if they are still not unresolved, would then become a billing issue when they actually started to bill the costs.

However, the cause of the issues that we are talking about, with in Halliburton in terms of its cause I would say, as I testified in

the earlier hearing, I believe, that Halliburton is a company whose business base expanded extremely rapidly. Their own management recognizes that their prior business systems were not adequate to keep pace with the rapid award of contracts that they received because of the contingency. Therefore, there is no dispute by KBR that their business systems need to be improved in several areas.

Mr. WAXMAN. In your May 13th report you discuss Halliburton's inability to exercise control over subcontractors, and I want to read again from the report: "KBR does not have adequate control over subcontract billings our audit activity has identified inadequate or nonexistent policies and procedures for notifying the Government of potential significant subcontract problems that impact delivery, quality, and price. KBR also does not monitor the ongoing physical progress of subcontracts or the related costs and billings."

One of the whistleblowers that we hope to hear from who came forward, Mike West, was a labor foreman for Halliburton, and he reported that Halliburton hired a Jordanian company to build a dining facility, but nobody from Halliburton supervised the work. He said he was sent over once a day to take a few photos. If Mr. West's account is accurate, it seems to track closely with your broader finding about Halliburton's failing to monitor the ongoing physical progress of subcontracts, doesn't it?

Mr. REED. Yes, sir, it is certainly related. There are contracting officials who should be on the ground. At the prime level we refer to them as contracting officer technical representatives who do oversee the progress of the work on the ground.

Mr. WAXMAN. We have another whistleblower who wants to remain anonymous who claims that a subcontractor charged Halliburton millions and millions of dollars in completely made-up costs. He reports that there was nobody there to check on the subcontractor's billings and the whole line items were simply made up out of thin air. This case too seems to be consistent with DCAA's broader conclusions.

Mr. Reed, if we make these individuals available to you, would you be willing to examine their cases further to determine whether specific remedial action is necessary?

Mr. REED. We certainly would. We will explore every single allegation and do the necessary fact-finding.

I would point out that if these deficiencies exist, every one of these costs, when they are billed to us, are going to be audited by DCAA. If there is no support for these subcontract costs, as this individual apparently is stating, I guarantee you we are not going to allow that to be billed.

Mr. WAXMAN. Ms. Ballard, you wanted to say something?

Ms. BALLARD. Yes, sir. On the question of contractors responding to the estimating system, points made by DCAA, it is our practice in contracting per the regulations, sir, that DCAA provide us a formal report on those estimating system issues, and then the contracting officer has an obligation to allow the contractor to respond to those allegations and to take corrective action relative to them.

Mr. WAXMAN. Thank you.

Mr. REED. May I add one other thing? I think I should state, to be totally fair to both parties here, that when I said that the estimating issues were not resolved, it does not mean that KBR has

not done anything. We are making progress, but we are not satisfied yet, and there is further to go.

General KERN. Could I add a comment too, Mr. Waxman?

Mr. WAXMAN. Sure.

General KERN. Remember we set out and General McManus laid out for you the last time a definitization schedule. Part of that we would like to have done sooner, but the issue has been getting adequate cost data from KBR that DCAA will support. And while we have seen improvements, neither the contracting officer working to definitize those task orders nor the data that they have provided to DCAA has been adequate, and I think what you see in process is good government. We have an auditing process overlooking it, we have a contracting officer who is doing their job making sure that we are not going to pay for things that we should not pay for.

Mr. WAXMAN. Thank you.

Thank you, Mr. Chairman.

Chairman TOM DAVIS. Thank you, Mr. Waxman.

Let me ask Mr. Reed two things. First of all, Mike West, we may have an opportunity to examine him in July, his allegations. It is not uncommon in these situations, is it, when materials maybe don't match up, the personnel gets there first and they are waiting for the materials, or vice versa? We saw this on our plane over there, where we had plenty of air conditioners, but we didn't have the air condition repair man. These can be logistical nightmares, particularly in the early parts of a conflict, is that——

Mr. REED. Mr. Chairman, it sounds like you have been in the Army. I have been in the Army too.

Chairman TOM DAVIS. I was in the Army.

Mr. REED. And we know that is the case; that the logistics stream is very effective, but it is not perfect. Personnel deployment has the same difficulties, especially where you are sending volunteers. It is important to note that we are asking civilian professionals to get up off their couch, watching their football games, and risk their lives and go to Iraq on a voluntary basis right now. So that is a process that does take a little bit of time to get people——

Chairman TOM DAVIS. I am just trying to give a perspective of how things, when you are sitting there as an armchair quarterback, it looks so easy, but when you are out there in the arena, sometimes things get a little complicated; and that is really where you come in. You come in and examine these things, and you take a look at what is reasonable, what is not reasonable. You don't know how many meals you are doing when you are pricing you are going to serve, correct? You don't know what the logistics are going to be; people are going to be there week to week. You come back and examine this and you say, well, you gave us a bill that was too high, or sometimes they are amended upwards. Is that fair?

Mr. REED. I think that is fair. It is also fair to note that the main point was that the troops needed to be fed.

Chairman TOM DAVIS. You have to feed them, No. 1, right?

Mr. REED. You have to feed them. We will worry about the accounting, the billing and the auditors later. But the main thing is the commanders were right to say our troops need hot meals; and that was what KBR was tasked to do. We will ultimately get to the fair price for those meals. That is our process.

Chairman TOM DAVIS. Now, as I understand it, most of the matters that we are discussing are still under discussion with the contractor and a lot of these issues are still open, is that right?

Mr. REED. Yes, sir.

Chairman TOM DAVIS. Many of these reports raising these issues have not been made public, or they have been made public because of just the scrutiny we have gotten? Making them public in a preliminary stage is not the usual practice, is it?

Mr. REED. No, sir. All of DCAAs reports, its formal reports, are issued for official use only, and they are protected under the U.S. Code to protect contractor proprietary data. There is a very specific process that must be gone through before these types of reports should be made public.

Chairman TOM DAVIS. But some of these preliminary reports still have been leaked, it appears; not to me, I might add, to the minority in this case.

Mr. REED. I believe the only instance I am aware of involved a DCAA draft report on the reconstruct Iraqi oil gasoline issue. I have never seen anyone show me they had that draft report.

Chairman TOM DAVIS. It has been referred to a lot, though.

Mr. REED. It has been referred to a lot, but to my knowledge that report has not—I have not seen anyone possess it who should not have it.

Chairman TOM DAVIS. Now that you have the resources in place and your organization is able to work with contractors and contracting officers to get a better picture on the ground, would you say, as far as you are concerned, the process is beginning to gel and beginning to work?

Mr. REED. Absolutely. We are making progress every day.

Chairman TOM DAVIS. There are some allegations, I think, that Halliburton and KBR are somehow trying to enrich themselves through these Iraqi contracts. Are you satisfied that at the end of the day the taxpayers will be protected from any unwarranted overcharges?

Mr. REED. With reasonable assurance, yes. And by that I mean, of course, nobody audits 100 percent of everything, but we do audit a substantial amount, and the techniques we use will assure that ultimately the taxpayers' interest, with reasonable assurance, will be protected.

Chairman TOM DAVIS. And, Ms. Ballard, let me ask you a similar question. Are you satisfied with the oversight mechanisms that have been established to oversee work performed by contractors in Iraq?

Ms. BALLARD. Yes, sir, I am satisfied with the oversight that has been provided, and I am also satisfied that we have taken significant positive measures to increase the oversight that is provided in Iraq.

Chairman TOM DAVIS. Because ultimately that is what we look to. There are always going to be disputes that we have, as you know, Federal Acquisition Regulations, pages and pages of rules and regulations to resolve these disputes, and I think at the end of the day you can point fingers and you can make a lot of allegations. We just want to make sure that the taxpayers aren't paying more than they ought to be paying and that the services are being

provided, particularly for our troops, but to accomplish our mission. The rest of it, it is an election year, and we also have a responsibility to oversee this and call you up here and make sure you understand that we are looking at these things. That is part of the ongoing responsibilities of this committee, whatever the administration.

OK, I am ready to recognize the gentleman from Massachusetts, Mr. Tierney, for 5 minutes.

Mr. TIERNEY. Thank you, Mr. Chairman. I thank the individuals for testifying.

In November 2002, Halliburton received a task order to develop a secret contingency plan to restore and operate Iraq's oil infrastructure. The task order was issued under the Army's LOGCAP global logistics contract, which is used to provide services like laundry and meals to the troops. GAO has determined that the administration violated Federal procurement law when it issued this task order because LOGCAP's contract isn't broad enough to include contingency planning for oil infrastructure.

General Kern, you are in charge of that Army Materiel Command which administers the LOGCAP contract, so let me ask you isn't it true that a career lawyer from the Army Materiel Command wrote a memorandum concluding that the LOGCAP contract should not be read to encompass contingency planning for the operation of Iraq's oil infrastructure?

General KERN. It is true that one of my legal officers within the Command Counsel Office offered an opinion that he did not think——

Mr. TIERNEY. Did you see that memorandum when it was issued?

General KERN. I did not see it until after it had been worked through the contracting channels, which would be normal.

Mr. TIERNEY. Would you provide a copy of that document to the committee?

General KERN. If it is fair that I can, I will, yes.

Mr. TIERNEY. Well, will you?

General KERN. Unless there is some legal reason I cannot, I will provide it, yes.

Mr. TIERNEY. OK, that is a better answer. Thank you.

Isn't it also true that when the memo was forwarded to the Army's Deputy of General Counsel for Procurement, he was inclined to agree that the contingency planning was outside the scope of LOGCAP?

General KERN. His initial opinion said yes, he agreed with him, and there was ensuing discussion that said in both his opinion and in discussing it further with the OSD General Counsel, three lawyers now involved, that it was right on the margin of being allowable.

Mr. TIERNEY. So he, at first, was inclined to agree that it was outside the scope, but then the Defense Department's general counsel weighed in and the career lawyer backed off and had his recommendations objected to, is that right?

General KERN. I am not going to try to put words in any lawyer's mouth, which I know I would fair anyway. They were all in a set of negotiations with one another determining if this was allowable.

Mr. TIERNEY. But the sequence was the first——

General KERN. But the senior attorney in the group from the DOD General Counsel's Office ruled that it was.

Mr. TIERNEY. So he overruled the other fellow, right?

Mr. LANZILOTTA. Sir, could I maybe add something to this? These are all career lawyers that come together. This is a judgment call that these lawyers get together. When we sit down there and say overrule, it seems like we put more definition to it than what there is. This was a gray area.

Mr. TIERNEY. Well, let me interrupt you for a second. The sequence as we understand it is that first the Army's Deputy General Counsel for procurement agreed that the contingency planning was outside the scope of LOGCAP. Then he met with the Defense Department's general counsel and they weighed in and the original lawyer's objections were rejected. So he had an opinion, and then they met and then the opinion was changed.

Mr. LANZILOTTA. But I happen to know the general counsel lawyer that we are talking about here and I have the highest regard. He is a career civil servant and he understands these issues. I work in these issues in fiscal law all the time.

Mr. TIERNEY. Are you saying that wasn't the sequence, then?

Mr. LANZILOTTA. Well, that is the sequence.

Mr. TIERNEY. OK.

Mr. LANZILOTTA. But the thing is this is an ongoing discussion that goes on among these lawyers.

Mr. TIERNEY. I understand that. And I just wanted to establish what the sequence was on that. And I guess my next question, General Kern, that general counsel's attorney was somebody who worked with Michael Mobbs, isn't that right?

General KERN. I cannot tell you that they do or not. They worked in the Office of the Secretary of Defense.

Mr. TIERNEY. As did Mr. Mobbs.

General KERN. Yes. But that is a very large office. And I have no idea whether he was included in that discussion. I would be surprised if he were.

Mr. TIERNEY. General Kern and General Crear, I wanted to ask you a particular question. Both have oversight of LOGCAP and RIO, respectively. Can you explain to us or share with us the pay differential and the benefit differential between private contractors that provide services under those programs and enlisted servicemen and women in Iraq performing similar duties? We have been told that the salaries for the private contractors range as high as $80,000 for truck drivers and $120,000 for convoy commanders. Are those accurate figures? Would you provide us information on such payment and benefit differentials to this committee when you get an opportunity? And explain to us a little bit about whether or not that is the situation.

General KERN. I cannot precisely tell you whether those are correct differentials. I can tell you under general circumstances, particularly in an international operation, regardless of whether you are at war or not, that a contractor will make more money than a uniform person. The second set of issues which we know are significantly impacting the ability to hire people today are the liabilities which they must assume under war zone conditions, and in some cases it has been very difficult for them to even one, get peo-

ple to sign up for the job and two, to get the coverage for them for their insurance.

Mr. TIERNEY. And I understand all of those risks. Obviously, our men and women are taking those risks everyday. What I guess I wonder is what can be done about those relative pay scales and what effect does it have on the morale of our troops, our men and women who are working at one pay scale and may be protecting the lives of others making substantial amounts of benefits and moneys more than they are.

Chairman TOM DAVIS. The gentleman's time has expired.

Mr. TIERNEY. If I could just have an answer to my question, Mr. Chairman.

Chairman TOM DAVIS. Sure.

General KERN. I don't have a precise answer for you. Our soldiers work side-by-side with the contractors and with other DOD civilians on a day-by-day basis, and I can tell you what they don't do is usually compare paychecks. What they are usually comparing is the conditions in which they are operating and trying to get the mission done.

Chairman TOM DAVIS. And let me just say this committee discussed that when we were working on the NSPS, the National Security Personnel System. The fact is everybody gets paid more than our uniform soldiers over there. Civilian employees doing the same thing are generally paid at a much higher level for the kind of work than you would get doing a private or a Spec 4, somebody doing that, unfortunately.

Mr. TIERNEY. Well, I look forward to having that information so we can see just how substantial the differentials are.

Chairman TOM DAVIS. That is beyond the scope of this committee in terms of looking at these contracts, but that, unfortunately, is a fact. But the goal was to make soldiers soldiers, not to have them doing other things. We have many who have criticized the administration for not having enough manpower. We are having to have the soldiers be soldiers here.

Mr. Ose, you are recognized for 5 minutes.

Mr. OSE. Thank you, Mr. Chairman.

I am intrigued by a line of questioning that the ranking member pursued earlier. If I got it verbatim, he asked each of you whether or not, relative to Mr. Mobbs, you have any knowledge to disprove Mr. Mobbs' allegations. Let me rephrase that. Mr. Mobbs has made some allegations about conduct between certain offices at the Pentagon and certain offices at the White House. Do you have any knowledge to prove those allegations? Mr. Lanzilotta. Rather than prove the negative, do you have anything to prove the positive?

Mr. LANZILOTTA. I am sorry, I really don't understand the question.

Mr. OSE. OK. Mr. Mobbs has made some allegations regarding contacts that were made between certain parties. Are you aware of that?

Mr. LANZILOTTA. When talking with Mr. Mobbs, I only know from a brief conversation, I don't have a lot of firsthand knowledge. I know that he did talk to career and non-career people versus Halliburton——

Mr. OSE. Are you aware of Mr. Mobbs' allegations regarding the Vice President's office?

Mr. LANZILOTTA. He told me——

Mr. OSE. Mr. Mobbs?

Mr. LANZILOTTA. Mr. Mobbs that it was the same as given in his previous testimony, it was more in the terms of notification of a contract award.

Mr. OSE. OK, well, I want to just run through this. So you don't have any knowledge to prove Mr. Mobbs' allegations?

Mr. LANZILOTTA. I have no firsthand knowledge.

Mr. OSE. Mr. Reed, do you have any knowledge that would prove Mr. Mobbs' allegations? You were asked whether you have anything to disprove it. Do you have anything that would prove his allegations?

Mr. REED. No.

Mr. OSE. Ms. Lee.

Ms. LEE. No, sir. I can't speak for Mr. Mobbs.

Mr. OSE. Ms. Ballard.

Ms. BALLARD. No, sir.

Mr. OSE. General Kern.

General KERN. Sir, I never heard of Mr. Mobbs until yesterday.

Mr. OSE. General Crear.

General CREAR. No, sir, no firsthand knowledge.

Mr. OSE. So we not only have no knowledge to disprove his allegations, we have no knowledge to prove it.

Mr. Lanzilotta.

Mr. LANZILOTTA. In talking with Mr. Mobbs, though, he tells me that there was no inappropriate contact made.

Mr. OSE. I know that. It is a political year, and I just want to make sure we get this flushed out properly in the course of the record.

There have been many elected officials who have been involved in elective office during the time in question of the Vice President's tenure at Halliburton. For instance, Senator Boxer has held significant amounts of stock in Halliburton, almost consistent with Mr. Cheney's tenure at Halliburton. Do you have any knowledge of Senator Boxer weighing in to influence the award of any of these contracts to Halliburton, Mr. Lanzilotta?

Mr. LANZILOTTA. No, I do not.

Mr. OSE. Mr. Reed.

Mr. REED. No, I do not.

Mr. OSE. Ms. Lee.

Ms. LEE. No, sir.

Mr. OSE. Ms. Ballard.

Ms. BALLARD. No, sir.

Mr. OSE. General Kern.

General KERN. No, sir.

Mr. OSE. General Crear.

General CREAR. No, sir.

Mr. OSE. OK. Senator Feinstein's husband, Mr. Richard Bloom, is a significant shareholder in Parini and UBS. Do you have any knowledge of Senator Feinstein weighing in regarding the award of contracts to Parini or UBS, Mr. Lanzilotta?

Mr. LANZILOTTA. I do not.

Mr. OSE. Mr. Reed.
Mr. REED. No, I do not.
Mr. OSE. Ms. Lee.
Ms. LEE. No, sir.
Mr. OSE. Ms. Ballard.
Ms. BALLARD. No, sir.
Mr. OSE. General Kern.
General KERN. No, sir.
Mr. OSE. General Crear.
General CREAR. No, sir.
Mr. OSE. Thank you, Mr. Chairman.
Mr. Lynch.
Mr. LYNCH. Thank you, Mr. Chairman. Let me just do a followup on that, because I am a little bit confused.
Mr. Lanzilotta, earlier on questions from Mr. Waxman, you stated that you got your information from Mr. DiRita and that you didn't speak to Mr. Mobbs.
Mr. LANZILOTTA. Pardon me?
Mr. LYNCH. Is that true or false?
Mr. LANZILOTTA. I spoke to Mr. DiRita concerning the deputies committee meeting and what was said at the deputies committee meeting. I spoke to Mr. Mobbs as to what his contact was with the Vice President's office.
Mr. LYNCH. OK. All right. Just so I am clear. All right, thank you.
First of all, I want to thank the panel for helping the committee with its work.
General Kern, at the committee's last meeting, on March 11th, we had an opportunity to have a brief conversation on the record, and I asked you about two Halliburton employees who took kickbacks from a Kuwaiti subcontractor in the amount of about $6.3 million in exchange for steering contracts to that Kuwaiti company, and I asked you for their identity, and I also asked you for the information on the Kuwaiti company to find out if they are doing similar things in other areas. Here is what I asked you. I said, we put a lot of sunlight on this process to find out who these people were, and we need to do more of that. We need to find out how many contracts they oversaw, we need to find out who the Kuwaiti contractors were that were offering these bribes or kickbacks, and we need to find out are those subcontractors who are providing these bribes doing other work in the country as well, and obviously we need to find out who these employees are.
And in response to my question you stated, "I promise you I will get back to you." Unfortunately, sir, with all due respect, I have not heard from you. It has been a couple of months now and I just want to ask you why that is.
General KERN. Mr. Lynch, one, I was under the assumption that our offices had gotten back to you and given you the information which I was given, which was an advisory from the Department of Justice, because they have this under investigation, that I could not provide you the information at this time because it is an active investigation.
Mr. LYNCH. An active criminal investigation?

General KERN. An active criminal investigation by the Department of Justice.

Mr. LYNCH. It is a little bit inconsistent. I just want to explain. We have had situations like this before with Mary Robinson. We were investigating the situation where the Kuwaitis were charging us 100 percent over what we should have been paying for gasoline from certain Kuwaiti contractors. This committee, both the majority and the minority leaders had Ms. Robinson, who was also under a criminal investigation, she came in, testified. I will point out that her testimony was expected to be favorable to the administration, but she was offered to the committee even though it was in the midst of a criminal investigation.

So I am just curious why these two individuals who—Halliburton has already paid the money back, the $6.3 million that they received in kickbacks. I don't know what the Kuwaitis got on the deal, how much they got, but the kickbacks have been paid back to the Government. And I am just curious why we can't get the identity of these folks. This is not a criminal investigation, this is a congressional investigation. I just want to know the identity of these folks and how widespread this practice of bribing our people, Halliburton's people through these Kuwaiti contractors.

General KERN. Mr. Lynch, one, I have to believe that the lawyers in the Department of Justice are giving me good advice so that I do not prejudice the ongoing investigation so that we all see that this comes out the way we think it should equitably. Second, I do know that there is a threshold associated with these investigations where the fraud issues of $10 million changes, and we have not proved yet what the amount that has been alleged as being involved is the right amount, and I think that is one of the critical factors in this particular investigation. And if I could, I will bring one of my counsels over to your office and we can talk about this in more detail.

Mr. LYNCH. That would be terrific. OK, general, let me ask you, then. We have other Federal departments that are investigating this misconduct.

General KERN. That is correct.

Mr. LYNCH. Have you shared that information with them?

General KERN. We have shared all the information with them, yes.

Mr. LYNCH. OK.

Let me ask Mr. Reed, then. Mr. Reed, have you gotten information regarding the identity of these two employees that took the $6 million, or some such amount, from these Kuwaiti contractors? You are doing the audit here for the Department of Defense. Have you got the information?

Mr. REED. No, we haven't, but that is not unusual. When a matter of this nature is being investigated, the identities of the parties, both the ones who may have taken the kickbacks as well as the ones who may have given the kickbacks, is not publicly disclosed or provided to people outside of the investigation, because to do so might compromise an investigative approach of the criminal investigators or whoever else is investigating. So I would not expect to be told that kind of detailed information.

Mr. LYNCH. Let me be clear here.

Chairman TOM DAVIS. The gentleman's time has expired.

Gentleman from Maryland, he can yield to you.

Mr. VAN HOLLEN. Mr. Chairman, I would be happy to yield a moment to my colleague.

Chairman TOM DAVIS. OK.

Mr. LYNCH. OK, so, Mr. Reed, you haven't been given the information.

General, can you tell me what department are you sharing this information with if it is not with the contract auditing wing of the Department of Defense?

General KERN. It is the Department of Justice.

Mr. LYNCH. OK.

All right, in deference to my colleague, my kind colleague, I want to end my questioning. Thank you.

Chairman TOM DAVIS. The gentleman from Maryland is still recognized.

Mr. VAN HOLLEN. Thank you, Mr. Chairman.

Mr. Lanzilotta, I just want to followup on some of the statements you made this morning. I understand you were not working at the Defense Department, or were you, at the time of the 2002 meeting, the deputies meeting?

Mr. LANZILOTTA. I was not at the deputies meeting. I was working at the Department of Defense.

Mr. VAN HOLLEN. OK. And can you tell me what individuals you have spoken to about what took place at the deputies meeting? You mentioned earlier today that you had gotten some information from the public affairs officer, Mr. DiRita, I believe, is that right?

Mr. LANZILOTTA. He is the only one.

Mr. VAN HOLLEN. OK. Did you ever have any conversation with Mr. Michael Mobbs about the meeting?

Mr. LANZILOTTA. About the deputies meeting?

Mr. VAN HOLLEN. Yes.

Mr. LANZILOTTA. No.

Mr. VAN HOLLEN. About anything that took place at that meeting.

Mr. LANZILOTTA. Not concerning that meeting.

Mr. VAN HOLLEN. OK. I am trying to get a sense, and anyone on the panel who has information about this, if you could jump in, but my understanding is that Michael Mobbs was the presenter at the deputies meeting that took place in 2002, where they discussed this. Does anyone have any information to contradict that assessment?

Ms. LEE. I was not at the meeting, sir.

Mr. VAN HOLLEN. I am sorry?

Ms. LEE. I was not at the meeting.

Mr. VAN HOLLEN. Have you had any conversations with anybody about what took place at that meeting?

Ms. LEE. Just a discussion. In fact, when we were prepping yesterday, there was a discussion yesterday that said what happened here, and we got into discussing it, that was the notification. I still characterize that as here is an operational question: is this what we want to do operationally. In fact, do we want to be prepared to fight fires in Iraq. And that is my understanding that was the discussion. Any subsequent discussion would have been a notification

of we are getting ready to declassify and do some things that have been discussed here.

Mr. VAN HOLLEN. OK. I think the reason this is important is, as Mr. Waxman said, no one has made any allegations about influence from the Vice President's office taking place at that meeting, but the earlier statements suggested that there was almost a firewall between the political appointees and the professional civil servants with respect to the Halliburton contracts. And the information that has come out more recently suggests that there was not a firewall. Now, that may be standard practice for the contract officers to be talking to other people in the decisionmaking capacity, but getting this story right, it seems to me, is important because there have been statements that were made that were interpreted that Mr. Mobbs essentially made the decision, took it to the deputies meeting, and then went on and told the contracting officers essentially this is what we want, do it, give it to Halliburton.

And so as I understand, none of you are in a position to really tell us whether that is the way events unfolded or whether they didn't. I guess we need other witnesses to followup on that.

Ms. LEE. No, sir, but I can tell you we have been working for years to try to get the requirements organization and the contracting organization to work together to make sure we support the mission properly, something we have been working on.

Mr. VAN HOLLEN. No, I understand that is important, but it is also important, I think you would agree, to make sure that these decisions are insulated as much as possible from the political process in terms of who gets a contract award. And people have bent over backward within the administration to make statements representing that is in fact how it happened, without any political influence, and so that is why some of these recent facts coming to light I think have raised a lot of serious questions about exactly how things unfolded there.

If I could, Mr. Chairman, I would like to yield to my colleague, Mr. Lynch.

Chairman TOM DAVIS. Mr. Lynch, you have another minute.

Mr. LYNCH. Just to go back, General Kern and Mr. Reed. We know that there was mishandling here, that there was over $6 million in kickbacks that were paid to Halliburton employees. You won't tell me the names of the individuals. I can't find out the names of the Kuwaiti companies involved. I can't find out if they are doing other work other places. I can't understand why someone won't tell me what other contracts these two individuals were overseeing.

Can you at least tell me, either of you, have we severed all contracts with this company, this Kuwaiti company that has been paying kickbacks to Halliburton employees? Can you at least tell me that?

General KERN. Sir, I cannot tell you that. Part of what you are asking me is to presume that we have already judged that they are guilty, and I can't do that until the investigation takes place to make any judgments against them. And I can't prejudice the investigation while it is ongoing by divulging information which is not under my purview, but under the investigator's purview right now.

Chairman TOM DAVIS. Thank you. The gentleman's time——

Mr. LYNCH. So have we suspended the contracts or anything like that?

General KERN. What I can assure you, Mr. Lynch, is that this is being pursued by our Government to do the right thing legally, and at the right time I think it all will be shared with you. We are watching this very closely to do the right thing.

Chairman TOM DAVIS. Thank you. The gentleman's time has expired.

There are hundreds of contracts under dispute right now. If you were to suspend all of these, the Government would never get anything done. That is the nature of contracting; that is why we have the DCAA and these other groups to come in afterwards and look at the forward pricing and compare it to the reality on the ground. I think normal procedures are working.

Ms. McCollum, you are recognized for 5 minutes.

Ms. MCCOLLUM. Thank you, Mr. Chairman.

In looking at part of the testimony from the Brigadier General, you talk about the planning prior to war. On page 2 you talk about "Prior to war, we originally expected that we would have to repair the damage caused by military action, deal with the resulting humanitarian crisis, set a stage for a new Iraqi government to oversee further exploration production, refining, distribution facilities for the oil."

Did you have any contact with the State Department? I understand the State Department had made contingency plans. Did you look at any of them, were they consulted?

General CREAR. We did not look at any State Department plans that I know of.

Ms. MCCOLLUM. OK, thank you. Then I have a concern and a question. I too had the opportunity to go to Iraq, and our servicemen and women are heroes trying to do a difficult job under very difficult circumstances. Our civilian contractors, our civilian employees in the Department of Defense and State Department all face grave danger in trying to do their jobs, as well as it is day-to-day life or death for many Iraqi citizens. But when I was in the dining hall, I have to wonder because it crossed my mind so often when I saw the civilian employees there. That was the day that Al Rashid had first been shelled inside the green zone; it was a very, very tense situation. And I looked at these civilian employees and I looked at all these soldiers I had been with and I thought, geez, what happens? What happens if there is civilian contract employees when a situation goes to gunfire? Who is responsible for the safety of the civilian contractors? How does our soldiers' role become challenged? Because many of the soldiers that I spoke with said, ma'am, I don't know whether I am a humanitarian worker, a police officer or soldier today. How does that get sorted out and who is responsible for their security in situations like that, and who is paying for the contractors' security in the convoy situations?

General KERN. Let me try to answer that question for you. First, the combatant commander in the theater is responsible for the security of the people——

Ms. MCCOLLUM. I am sorry, there is something wrong with the acoustics, sir, and I am not understanding you.

General KERN. The combatant commander is responsible for the security of the people in his area of operation, and that includes the civilians, DOD, and contractors. In some cases within the green zone, you are in Ambassador Bremer's area, and he has hired other people to provide security within his immediate vicinity. So you have a two-tiered kind of operation that is going on there, one in the immediate CPA facilities, and then in the area of operations, and depending upon when you were there would depend upon who the commander was in charge of that particular area.

We have, in the case of security for the convoy operations, placed a uniformed soldier in the cab with the contractors riding those since last April, when security became much more of a problem for those convoys. So we have changed and we have worked that out with KBR, and they have placed one of their personnel in theater to look at very particularly the security of those operations on a daily basis.

Ms. MCCOLLUM. Sir, thank you. And I am not trying to be flippant about this, but it sounds very complicated at a time when you might not know what is happening around you or what your orders might be to respond to fill in to a line or to do something that you have a group of American civilians that I would think, from meeting the, as I said, terrific soldiers that I met, would feel conflicted about what they may or may not need to do. And they follow orders and they would do the best job that they could under the circumstances, but we have really changed contracting. First the Department of Defense was contracting out what civilians would typically do. This is the first situation, to my knowledge, where we have so many civilian contractors working side-by-side, described in some of the testimony here as part of our troops, in other words, as part of the military, when the military used to perform many of these functions with people who had been through boot camp, who did know what to do, and we have civilians who don't. And I find that rather a concern.

And that brings me to my other question. Do you have a summary on what happened with the contractors that is available to either this committee or Members of Congress on the prison situation?

General KERN. I am not sure that I fully understand what you mean do I have a document that describes. We have many thousands of contractors there working on very different kinds of operations. And I share your concerns about how we run that whole security operation. Some of them are field service reps that do technical contracting in support of operations; some of them are the civilians working for the CPA and the reconstruction effort, as well as State Department and other; and then we have the third level of the support kind of contractors that are running services that we have. So there are lots of different categories, and I don't have a single report that covers that.

Chairman TOM DAVIS. Thank you very much.

Thank you, Ms. McCollum.

Mr. Waxman, you want to give a summary?

Mr. WAXMAN. Well, Mr. Chairman, I think this panel has been very helpful, and I want to thank them for their participation in the hearing today. A lot of people ask why is there so much pas-

sion, why do we care so much about this issue. At a time of massive budget deficits and stories about our troops not getting everything they need to support them in Iraq, when I hear about these egregious situations where there are overcharges by Halliburton and anyone else, it really gets me angry. And when I hear from the DCAA, telling us there are no internal controls to stop the overcharging, the DOD hasn't done enough to prevent this sort of thing from happening, from stopping waste, fraud, and abuse, I think the whole situation is ripe; it is a perfect situation for those contractors that want to take advantage and overcharge for them to do it, somewhat like what we had in California with the energy crisis. We had a situation where the energy suppliers could overcharge us. People said it wasn't happening, it couldn't be, and now we know from the internal tapes of the discussions at places like Enron and some of these other companies that they knew what they were doing.

Well, I think what is missing is accountability, and that, to me, means that we in the Congress have to be more aggressive, hold hearings, get the documents, and pursue the truth. And, Mr. Chairman, I want to thank you for your commitment to doing that and your willingness to continue pursuing the matter, because I think that is a very serious part of our job as Members of Congress.

Chairman TOM DAVIS. Mr. Waxman, thank you.

Let me thank our panel for this.

Let me just note this committee originally started as five different committees, all overseeing the expenditure of Government funds, and in the 1950's was consolidated in the old Government Operations Committee. In 1995 they consolidated Civil Service Committee and the D.C. Committees and molded us into one, but one of our primary objectives is to oversee waste, fraud, abuse in Government expenditures, and that is what we are doing.

From what I have heard, I don't see any real strong evidence of fraud or political favoritism, but there is always waste when you are dealing with contracts of this magnitude in a war zone; there are things that may be in the calm of the day might have been done differently. Our job is to now come back and examine these. We hope that it is a learning experience for you.

The one thing Enron didn't have to face was DCAA. We can see from Mr. Reed and his troops that are over there we are not going to pay a penny more than they can substantiate, and that there are literally hundreds of millions of dollars in dispute in the one contract that has been highlighted today, and there are hundreds of other contracts where there is money in dispute, where people make decisions in a war zone that, on reflection, maybe the taxpayer shouldn't be responsible for.

So, Mr. Reed, we are glad you and your cohorts are here. Go to it. As Mr. Waxman said, these are Federal tax dollars that are taken from hardworking people, and we don't want them wasted.

We will be doing more oversight on this, as we discussed at the beginning of this.

Mr. Waxman, thank you for your cooperation. I thank the members for their perseverence, as well.

This meeting is adjourned.

[Whereupon, at 3:40, the committee was adjourned, to reconvene at the call of the Chair.]

[The prepared statements of Hon. Katherine Harris and Hon. Dutch C.A. Ruppersberger follow:]

June 14, 2004

Hearing: "Unprecedented Challenges: The Rebuilding of Iraq"

Rep. Katherine Harris' Statement:

Thank you, Mr. Chairman. I wish to express my appreciation for your leadership in conducting this hearing on a challenge that ranks alongside the tasks America confronted at the close of the Second World War – both in its degree of difficulty and in its potential to shape the next half-century.

At the heart of the Middle East, a proud and productive nation lies in ruins. Unlike Germany and Japan in 1945, however, coalition bombs were not the primary source of this destruction. The most egregiously underreported fact about the War in Iraq is the extent to which our men and women in uniform placed **their own lives at risk** in an effort to avoid injury to civilians or the infrastructure they depended upon for their basic needs.

Saddam Hussein left precious little infrastructure for our military to preserve, however. As he raped, murdered, and pillaged over the course of three decades, he cast a modern, prosperous nation into an abyss of misery and privation. Freed from the clutches of this malignant tyrant, the Iraqi people continue to face the long, arduous task of recovering from the devastation he left behind. Bolstered by

the courage and determination of our armed forces, the Iraqi people have gained strength for the journey.

Like a cancer survivor, Iraq is regaining its health and strength one day at a time. Setbacks have occurred, just as we anticipated. Nevertheless, we must not permit temporary obstacles to diminish our determination to help Iraq regain its rightful place in the community of nations. Moreover, we must not allow bad news to outweigh the enormous progress that we have made in partnership with the Iraqi people.

- For example, last week the Ministry of Transportation and the Ministry of Environment became the 14th and 15th cabinet-level ministries to be transferred to full Iraqi control since beginning of the occupation.

- Moreover, by the end of August Baghdad International Airport will become a fully functional transportation hub for the first time in years. This critical international gateway will eventually enable commerce to flourish, bringing Iraq's capital city at last into the 21st century.

- Further, as part of our efforts to build the foundation for Iraq's future as a self-sustaining democracy with an informed population, more than 32,000 high school teachers and 3,000

school supervisors have been trained in modern teaching methods and curriculum development.

- To ensure that Iraq's educational system is populated by healthy children, more than 85% of Iraqi children have now been immunized.

- Iraq's oil industry is recovering, as it exported nearly ten times more oil in April of 2004 than it did in June of 2003. In fact, the *average* monthly Iraqi crude production is now approaches – and at times exceeds - pre-war ***peak*** production.

- Most important, the Iraqi people are just a few weeks from regaining full sovereignty – under an interim president and prime minister who have obtained the recognition and support of a unanimous U.N. Security Council.

While the road to democracy is fraught with danger, our continued resolve will empower the Iraqi people to seize control of their own destiny – proving once and for all that liberty can flourish in the Cradle of Civilization. Let us remain steadfast in seeking that goal.

Thank you, Mr. Chairman.

Opening Statement of Rep. C.A. Dutch Ruppersberger

Full Committee on Government Reform Hearing

Unprecedented Challenges: Contracting and the Rebuilding of Iraq

June 15, 2004

Thank you Mr. Chairman. I appreciate the time and attention both you and Ranking Member Waxman have put into this critical issue. I realize there is great divide within this committee right now over the issues of contractors attempting to rebuild Iraq – divide between the focus, issues, and solutions. I hope today's hearing will be a first step in exercising congressional oversight responsibilities and searching for facts to find solutions.

Throughout my professional career – as an investigator, prosecutor, police officer, and politician - I have consistently advocated for thorough investigations. Politics is like water and will always find its way into the process. Rather than fighting that reality, we should focus on finding facts, corroborating them, authenticating documents, building cases from the ground up, and then holding individuals accountable should the facts show wrong doing.

The hearing we are holding today is critical for many reasons. First, there is an economic implication. Many of the charges individuals not allowed to testify before the committee today have levied deal with waste, fraud, theft, and poor business

practices – all drains on a limited pot of money in a time of fiscal crisis in this country. That troubles me. Second, I am concerned about the resources wasted that could have been used in better support of our men and women on the ground. We've been debating flack jackets and humvee armor for almost a year now, but large contractors are dealing with cost-plus-plus contracts and disregard for spending. That troubles me. And third, I am disappointed that we have not – either in open or closed hearings in this committee – discussed these issues at greater length.

So I look forward to today's testimony and what we will learn. And I hope that the committee will be able to obtain further documents and testimony to follow the facts and get to the bottom of these problems. We owe it to our troops and we owe it to our Nation to get this right. If wrong doing has occurred, we should hold those responsible accountable. But further, we should take the lessons learned from these events and improve the way we are doing business in Iraq, Afghanistan and anywhere we have boots on the ground.

Thank you Mr. Chairman.

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UNPRECEDENTED CHALLENGES: THE COMPLEX TASK OF COORDINATING CONTRACTS AMID THE CHAOS AND THE REBUILDING OF IRAQ

THURSDAY, JULY 22, 2004

HOUSE OF REPRESENTATIVES,
COMMITTEE ON GOVERNMENT REFORM,
Washington, DC.

The committee met, pursuant to notice, at 10:05 a.m., in room 2154, Rayburn House Office Building, Hon. Tom Davis (chairman of the committee) presiding.

Present: Representatives Tom Davis of Virginia, Shays, Burton, Ros-Lehtinen, McHugh, Mica, Souder, LaTourette, Ose, Lewis of Kentucky, Jo Ann Davis of Virginia, Platts, Cannon, Schrock, Duncan, Deal, Miller of Michigan, Murphy, Turner of Ohio, Carter, Blackburn, Tiberi, Harris, Waxman, Lantos, Owens, Towns, Kanjorski, Sanders, Maloney, Cummings, Davis of Illinois, Tierney, Clay, Watson, Lynch, Van Hollen, Sanchez, Ruppersberger, Norton, Cooper, and McCollum.

Staff present: David Marin, deputy staff director/communications director; Keith Ausbrook, chief counsel; Ellen Brown, legislative director and senior policy counsel; David Young, counsel; Robert Borden, counsel/parliamentarian; Rob White, press secretary, Drew Crockett, deputy director of communications; John Cuaderes, senior professional staff member; Edward Kidd, professional staff member; John Brosnan, GAO detailee; Teresa Austin, chief clerk; Brien Beattie, deputy clerk; Allyson Blandford, office manager; Leneal Scott, computer systems manager; Andrew Stein, legal intern; Phil Barnett, minority staff director; Kristin Amerling, minority deputy chief counsel; Karen Lightfoot, minority communications director/senor policy advisor; Anna Laiti, minority communications and policy assistant; Jeff Bara, Rosalind Parker, and David Rapallo, minority counsels; Mark Stephenson and Nancy Scola, minority professional staff members; Earley Green, minority chief clerk; Jean Gosa, minority assistant clerk; and Cecilia Morton, minority office manager.

Chairman TOM DAVIS. Good morning. The committee will come to order, and I want to welcome everybody this morning to our full committee oversight hearing entitled, "Unprecedented Challenges: The Complex Task of Coordinating Contracts Amid the Chaos and the Rebuilding of Iraq." This is the fourth in the series of hearings this committee has held on the challenges involved in the execution of contracts for rebuilding Iraq amid the chaos and dangers of war.

Just a few short weeks ago, the Coalition Provisional Authority turned over the reins of government to the people of Iraq. This transition to self-government shows that our commitment to the Iraqi people is genuine and real. Yet we still have much to accomplish, and the road ahead is still difficult and perilous. American soldiers and civilians continue to lose their lives protecting freedom. Make no mistake, as long as we have the resolve to finish the job, I am certain we are going to prevail.

As a major part of our mission to bring peace to Iraq and the surrounding area, we have committed a substantial amount of taxpayer money. To that end, we rely on our military and civilians to carry out day-to-day activities which are essential to security and the rebuilding process. The military has been nothing short of superb and the unsung heroes are the many civilians in Iraq, who, like the military, work tirelessly and under very dangerous conditions.

The majority of civilians working in Iraq are private contractors. The sacrifices these people make are inspiring, and I believe history will give them the credit they deserve for changing the face of this region.

I can't emphasize how hard it is to conduct normal business in Iraq, and yet we continue to make progress. Nevertheless, whatever the danger and no matter the difficulties, we demand that contractors doing business in Iraq do so in accordance with the governing laws and regulations. I can understand how the difficulties of a war zone can lead to poor recordkeeping. I know there are those individuals who think they can turn a quick but questionable buck because they hope the fog of war will cover their actions. And, yes, there are bad apples who can turn up wherever opportunity presents itself. Such opportunism cannot be condoned.

We are having this hearing today because there are those who believe we have a company, in this case Kellogg Brown and Root, that is wasting tax dollars or abusing its contracting role, or even defrauding the U.S. taxpayer. From what I have seen to date, I happen to disagree. I have yet to see any serious evidence of this, but we do have reviews going on across the spectrum with Defense Contract Audit Agency and others, and as allegations are brought to us we need to make sure these are forwarded on to the appropriate officials who are trained in these areas to review them and to make sure the taxpayers aren't fleeced.

What I see and what we have seen to date are occasional failures to communicate, inattentiveness in adhering to strict business procedures, and a clearly less-than-perfect accounting process. Of course, in a perfect world, we would have contractors that would accomplish the mission and maintain perfect peacetime business practices with the appropriate paper trails. But even when the best business practices aren't maintained, the taxpayer is still protected because our government procurement system prohibits reimbursement to KBR or any other contractor until they have shown the military that the costs presented, as determined by the contracting officer, are reasonable, allocable to the contract, and allowable under the government's cost principles.

We have seen a display of this process through the various Defense Contract Audit Agency reports on cost issues that have been

made public. To me, these reports show that the oversight process is alive and working. They reveal issues of contract interpretation, cost reimbursements that are not at all unusual in large, complex, cost-type contracts.

The last hearing we held on Iraq contracting, a little more than a month ago, explored those issues with those responsible for contract management and oversight. Because of the overheated political atmosphere surrounding the war in Iraq, and a misplaced concern about the use of KBR as a contractor in particular, we are holding yet another hearing on Iraq contracting. But this time, instead of contracting experts, we are hearing from so-called whistleblowers who will air their complaints against KBR. We will also hear the firm's reaction to those complaints.

Today, we will hear from representatives of Kellogg Brown and Root, a subsidiary of the Halliburton Co., and the prime contractor on two of the larger contracts associated with Kuwait and Iraq, the LOGCAP and initial Restore Iraqi Oil [RIO] programs.

I want to publicly thank KBR for testifying today. They come of their own accord. I, for one, still believe that if it weren't for the fact that the Vice President was the former—and I emphasize former—CEO of the parent company, we probably would not be here today. Politics is driving this agenda, and I suspect that not even the truth will keep detractors at bay.

Despite this, KBR has decided to answer under oath allegations that continue to be shopped to the media. In fact, I want to highlight that point by submitting for the record, if there is no objection, a Washington Post article dated July 20, page A–15 under the White House Notebook, by Dana Milbank titled "The Kerry Campaign One-Word Weapon." The gist of the article is how the Democrats are using Halliburton as fodder for the Presidential campaign.

[The information referred to follows:]

WHITE HOUSE NOTEBOOK

Dana Milbank

The Kerry Campaign's One-Word Weapon

There is seemingly no charge the Bush campaign can level against John F. Kerry that will not produce a one-word retort: Halliburton.

Kerry's proposed tax increases? Halliburton.

Kerry's vote against Iraq war spending? Halliburton.

Kerry's anti-terrorism credentials? Halliburton.

Kerry's ties to Hollywood liberals? Halliburton, Halliburton, Halliburton.

"Halliburton," says Kerry spokesman Chad Clanton, "will always be the fire Dick Cheney can't put out." That is certainly the Democrats' hope, as they try to portray the oil services company once run by Vice President Cheney as a metaphor for all things anti-Bush.

When Cheney spoke about health care yesterday in Toledo, Kerry forces held a counter-rally featuring signs saying "Health Care, Not Halliburton." Explaining that apparent non sequitur, the campaign said in a news release that health care costs would be lower if Cheney spent "as much energy on lowering health care costs as getting Halliburton their no-bid contracts."

Likewise, when the Bush campaign last week demanded video footage of an event where Whoopi Goldberg delivered a crude anti-Bush message, the Kerry campaign had a ready response: The Bush campaign should release correspondence about Halliburton's contracts.

Bush campaign spokesman Steve Schmidt said the "baseless charges" by the Kerry campaign are a sign of desperation. "As they flail around, unable to explain the fact that John Kerry has multiple positions on every issue from the war on terror to what type of car he owns, you see the silly chants and slogans," he said.

There is no proof the government was wrong to award Iraq contracts to Halliburton without competitive bidding, or that Cheney helped his former employer. Democrats, though, are hoping the image of Halliburton, and President Bush, could be damaged further by news from one of the ongoing investigations into the company. The Treasury Department is examining whether a Halliburton unit violated laws against doing business in Iran. The Securities and Exchange Commission is probing a change in Halliburton accounting practices. And various entities are examining charges about Halliburton bribery in Nigeria.

Already, the company has a serious image problem stemming from overcharging and kickbacks. A Newsweek poll earlier this year found that, by 58 percent to 32 percent, Americans disapproved of the awarding of Iraq rebuilding contracts to Halliburton. The Kerry campaign is doing whatever it can to worsen that image problem, linking the company to everything from higher fuel prices to lower funding for community policing.

Democrats held a "Halliburton Week" last month with events in 20 states portraying the Bush-Halliburton relationship as cronyism. It was Vermont Sen. Patrick J. Leahy's role in Halliburton Week that prompted Cheney's obscenity last month on the Senate floor—leading the Kerry campaign to distribute bars of soap outside a Cheney appearance in Cleveland.

Oh—Canada?

During last year's enactment of the Medicare prescription drug benefit, the White House vigorously opposed legalizing the "reimportation" of drugs from Canada, where they are cheaper. So it came as a surprise yesterday to visit the Web site of Sav-Rx, one of the companies tapped by the administration to provide the new Medicare drug discounts championed by President Bush.

"Sav-Rx is giving you the opportunity to save an additional 20%-30% on your mail order prescriptions through the use of our Canadian Mail Order Pharmacy," boasts the company, which states that the consumer is appointing an "agent to bring this prescription into the United States."

It is illegal to bring prescription drugs into the United States, and Medicare chief Mark McClellan said in a White House briefing last month that there are "real safety problems" with reimported drugs. But Sav-Rx says it "guarantees the same quality product from Canada that you have come to expect from regular Sav-Rx." A Sav-Rx saleswoman cheerfully explained yesterday that Medicare cardholders are eligible.

A spokesman for the Health and Human Services Department told The Washington Post's Ceci Connolly yesterday that Sav-Rx has been warned about the matter. The company did not respond to a reporter's inquiry yesterday.

The Misquotable Bush

"I trust God speaks through me. Without that, I couldn't do my job."

— statement attributed to President Bush in the Lancaster (Pa.) New Era from a private meeting with Amish families on July 9. The White House said Bush said no such thing.

Chairman TOM DAVIS. However, before we hear from the representatives of KBR, we will first hear testimony from former employees who believe they personally witnessed waste and abuse. I think it will become clear that these individuals are not experts in government contracting, but they have, for various reasons, something against the company. Although the minority has worked with these witnesses for a long time, in the case of Ms. deYoung who is here, the minority knew of her allegations 8 months ago. They were brought to our attention only 2 months ago. At that time, the ranking member wanted an immediate hearing without allowing us to evaluate their claims and determine whether a hearing would be appropriate.

After a preliminary evaluation, we agreed to a hearing involving some of the whistleblowers, only to see that the whistleblower statements were on their Web site, which also led to the appropriate television news interviews. Again, all without any concern for the validity of the statements. In other words, the minority was more about the sensational accusations getting out to the media than in the actual fact-finding that this committee is generally equipped to look at.

We decided to hold this hearing and have the whistleblowers testify and to help put this in context to help us move beyond the rhetoric and to try to get to the truth of the matter. I have asked my staff to verify their accusations, even though I thought it should have been incumbent on the minority to do this.

For those who came hoping to hear witnesses' firsthand evidence of waste, fraud and abuse by KBR, in my opinion you are going to have to brace yourself for some disappointment. The accusations leveled by the whistleblowers against KBR, both in their written testimony and through personal interviews, are either in some cases flat-out wrong, or are minor or a naive or myopic view of contracting in a wartime environment.

Ms. deYoung's experiences in Kuwait led her to accuse KBR of waste and abuse. Her claims focus on what she calls poor oversight of the subcontractors, who she believes were fleecing the taxpayer. She also claims that KBR wastefully leased a five-star hotel for its employees, when the employees should have been staying in air-conditioned tents on U.S. military bases.

Ms. deYoung is quick to jump to conclusions without understanding the whole story. As for leasing the five-star hotel, KBR is guilty of this, but let me put that in context. I've been to Kuwait, a couple of times. In Kuwait, most hotels start at the five-star level. Kuwait is not like any country you've ever been to. It's rich. That's why Saddam wanted it so badly. It seems that KBR had little choice. The only real choice was to pick the particular five-star hotel. And what Ms. deYoung did not know was that KBR wanted to be stationed on the base, and had even requested to house employees on that base. A military base is more secure than a hotel and the base was where the work is.

As I understand it, the military, for good reasons, didn't want KBR on the base. By the way, I understand these hotel rooms had many occupants. So it wasn't like a suite for an individual; sometimes up to five or six people were in a room at a time.

The majority of her allegations concern subcontract administration. In her interview with committee staff, she painted herself as a contract specialist who uncovered subcontractors overcharging for goods and services. I think you will look at the math skills, and maybe there is a little to be desired there. She attacks the kind of contracts the minority has been touting. The accusations surrounding soda and laundry are tied to fixed-price contracts. Again, this all seems to be explainable, or, at worst, relatively minor when the entire story is told.

Mr. Mike West's problems started early with KBR. He claims that prior to starting with the company, he negotiated a starting salary of $130,000, only to learn his salary would be $82,000 per year, based on a 12-hour day, 7-day-per-week schedule. Although Mr. West felt he was cheated, he decided to accept the salary and join KBR as a labor foreman. In his interview with the committee staff, Mr. West often complained that he had to wait; wait to get from point A to point B, wait to be assigned work, wait to get a ride back to the States.

Well, as a former member of the military myself, I'm familiar with this feeling. We used to call it, when I was in the Army, "hurry up and wait." Hurry up and wait isn't waste and abuse; it's, unfortunately, part of the logistical challenges that are presented when working with the Army that changes its mind more often than not.

Mr. West did eventually work, but he didn't like the work and he left after 2 months. The experience left a bad taste in his mouth, so he quit. Obviously, this type of environment didn't suit him. Unlike working in the States, the atmosphere in Iraq was not conducive to his plans being carried out like clockwork. It's just the opposite.

In the early days after the war, adapting to the situation was more the rule than the exception. I know my colleagues who traveled with me to Iraq can verify this is true.

James Warren and David Wilson are truck drivers who drove convoys in Iraq. They both have similar stories, and I see their similarity extends to the lawyers that they brought with them today. The gist of these gentlemen's allegations has to do with what they see as waste and abuse of taxpayer assets. They claim that poor maintenance and the lack of proper spare parts led to trucks breaking down, and a lack of interest in conserving assets resulted in disabled vehicles being destroyed onsite rather than fixed or towed. After all, these were not KBR's trucks, so why should they care.

Again, what we have here are accusations made with very myopic tunnel vision. I think we will see when we have the opportunity to hear the whole story, that most of the actions of the contractor were likely out of its control, and make sense given the security concerns in running convoys through Iraq in hostile fire.

Yes, it makes sense to retrieve a truck, and I understand how a professional truck driver loathes seeing a piece of equipment like that being destroyed. However, an $85,000 truck is simply not worth a life, whether it's one of our soldiers or a civilian who might be in harm's way without the protection of an entire convoy. Mr.

Warren and Mr. Wilson ought to be grateful that they returned from Iraq unharmed.

These truck drivers, like the rest of these whistleblowers, believe that what they saw while working in Kuwait and Iraq were not simply examples of paperwork problems or the hurry-up-and-wait environment, but were, instead, the result of wanton and careless disregard of KBR toward American taxpayer funds.

Our acquisition system is a complex web of regulations and safeguards put in place to protect the taxpayer. A person with a view of only a small part of an entire process cannot see that there are many players and considerations involved in decisions that, in wartime especially, might sometimes overlook some formalities to ensure the mission is accomplished and that no one gets hurt.

Unfortunately, even with these goals in mind, this conflict has cost 47 KBR employees their lives. I believe that tunnel vision, inexperience, and naivete are behind many of the allegations we will hear today. But to be honest, I fear some are here because they have ulterior motives, whether it's a book or a try at the litigation lottery jackpot. Today, the truth will come out. I tried to convince the minority that there was not much here. But, again, there are some who have a different view of this and think that oversight advances their political agenda.

As we saw clearly in past hearings, the contract oversight process is hard at work here. All the charges under the LOGCAP contract will come under the scrutiny of government auditors, career employees trained to ferret out waste, fraud, and abuse, and they are not going to be paid unless the contracting officer is confident that they are reasonable, allocable to the particular contract, and allowable under the government's cost principles.

Our second panel today is made up of representatives of Kellogg Brown and Root, a subsidiary of the Halliburton Co. KBR is the major prime contractor on executing the Army's LOGCAP program.

LOGCAP was established in 1985 to manage the use of various civilian contractors who perform services in support of DOD missions during times of war and other military mobilizations. LOGCAP has been used to support DOD missions from Somalia to Afghanistan to Iraq. It was used effectively during military operations at Bosnia and Kosovo. The effort in Iraq is the largest in the history of the LOGCAP program. As of last May, the estimated value of the contract services in Iraq is $5.6 billion. The LOGCAP contractor in Iraq provides such logistics and engineering services as food preparation, laundry, housing, and construction in support of military operations.

This particular contract, held by KBR, is the third iteration of the Army's LOGCAP contract. The first was awarded to KBR in 1982, the second was awarded to DynCorp in 1994, and the current contract awarded to KBR in 2001 competitively. I think it is important to keep in mind that all three of these contracts were awarded under competitive acquisitions.

The LOGCAP contract was awarded on a cost-plus award fee basis. Such contracts provide that the contractor is only to be reimbursed for reasonable, allowable, and allocable costs incurred as prescribed in the contract.

A cost-plus award fee contract provides financial incentives based on performance. The logistical needs of our military in Iraq and Kuwait are massive, time sensitive and ever changing. In order to meet these needs, KBR must be able to react swiftly. These requirements dictate the use of such cost-type contracts. Cost-type contracts are commonly used where, as in Iraq, urgency and uncertainties do not permit costs to be estimated with sufficient accuracy to permit the use of fixed-price contracts.

Indeed, defense auditors have criticized KBR for inadequate cost estimating and problems with its accounting and documentation practices. There are a number of outstanding issues concerning KBR, particularly concerning food service. These types of issues often arise in the context of cost-type contracts and are part of the normal contract oversight process. The issues tend to be exacerbated here because of the large amounts of money involved and the extremely difficult conditions in Iraq.

KBR has told committee staff that they were prepared to answer all the questions relating to the whistleblowers and other allegations that have been leveled against them through the press or by congressional critics. These include answering dining facilities charges, kickback schemes, gasoline subcontracts, and other allegations of overcharging. We look forward to hearing their side of the story today and taking appropriate questions from Members.

In closing, I want to ask that everyone here, especially my colleagues and the members of the media, stick around and listen to our third panel witness, Dr. Steven Kelman of Harvard University. Dr. Kelman is the Weatherhead professor of public management at the Harvard Kennedy School of Government, and the former director of the Office of Federal Procurement Policy in the Clinton administration. He is above the political fray. Dr. Kelman is here to offer some general observations about our acquisition system and its operations in a wartime atmosphere in Iraq.

The minority has questioned the contracting activities in Iraq, and I can think of no better person to testify as to whether or not our acquisition system and its contract vehicles can do the job in Iraq. In many ways, Dr. Kelman's testimony is the most important here today.

[The prepared statement of Chairman Tom Davis follows:]

Opening Statement of Chairman Tom Davis
Committee on Government Reform
"Contracting and the Rebuilding of Iraq: Part IV"
July 22, 2004

I would like to welcome everyone this morning to our Full Committee oversight hearing entitled "Contracting and the Rebuilding of Iraq: Part IV." This is the fourth in a series of hearings the Committee has held on challenges involved in the execution of contracts for rebuilding Iraq amid the chaos and dangers of war.

Just a few short weeks ago, the Coalition Provisional Authority turned over the reins of government to the people of Iraq. This transition to self-government shows that our commitment to the Iraqi people is genuine and real. Yet we still have much to accomplish, and the road ahead is still difficult and perilous. American soldiers and civilians continue to lose their lives protecting freedom. Make no mistake -- as long as we have the resolve to finish the job, I am certain we will prevail.

As a major part of our mission to bring peace to Iraq and the surrounding area we have committed a substantial amount of taxpayer money. To that end, we rely on our military and civilians to carry out day-to-day activities, which are essential to security and the rebuilding process. The military has been nothing short of superb, and the unsung heroes are the many civilians in Iraq who, like the military, work tirelessly and under very dangerous conditions. The majority of civilians working in Iraq are contractors. The sacrifices these people make are inspiring. I believe history will give them the credit they deserve for changing the face of this region.

I cannot emphasize how hard it is to conduct normal business in Iraq, yet we continue to make progress. Nevertheless, whatever the danger and no matter the difficulties, we demand that contractors doing business in Iraq do so in accordance with the governing laws and regulations. I can understand how the difficulties of a war zone can lead to poor record keeping. I know there are those individuals who think they can turn a quick, but questionable, buck because they hope the "fog of war" will cover their actions. And yes, there are bad apples who can turn up wherever opportunity presents itself. Such opportunism cannot be condoned. We are having this hearing today because there are those who believe we have a company, Kellogg, Brown and Root, that is wasting tax dollars or abusing its contracting role, or even defrauding the U.S. taxpayer.

I happen to disagree. I have yet to see any serious evidence of this. What I see are occasional failures to communicate, inattentiveness in adhering to strict business procedures, and a less than perfect accounting process.

Of course, in a perfect world, we would have contractors that would accomplish the mission and maintain perfect peacetime business practices with the appropriate paper trails. But even when the best business practices are not maintained, the taxpayer is still protected because our government procurement system prohibits reimbursement to KBR and other contractors until

they have shown the military that the costs presented, as determined by the contracting officer, are reasonable, allocable to the contract, and allowable under the government's cost principles. We have seen a display of this process through the various Defense Contract Audit Agency reports on cost issues that have been made public. To me, these reports show that the oversight process is alive and working. They reveal issues of contract interpretation and cost reimbursement that are not at all unusual in large, complex cost-type contracts.

The last hearing we held on Iraq contracting, little more than a month ago, explored those issues with those responsible for contract management and oversight. Because of the overheated political atmosphere surrounding the war in Iraq and a misplaced concern about use of KBR as a contractor in particular, we are holding yet another hearing on Iraq contracting. But this time, instead of contracting experts, we are hearing from so-called whistleblowers who will air their complaints against KBR. We will also hear the firm's reaction to those complaints.

Today, we will hear from representatives of Kellogg, Brown and Root, a subsidiary of the Halliburton Company and the prime contractor on two of the larger contracts associated with Kuwait and Iraq -- the LOGCAP and initial Restore Iraqi Oil (RIO) programs. I want to publicly thank KBR for testifying today. They came on their own accord. I, for one, still believe that if it weren't for the fact that the Vice President was the former – and I emphasize former -- CEO of the parent company we wouldn't even be here today. Politics is driving this agenda, and I suspect that not even the truth will keep the detractors at bay. Despite this, KBR has decided to answer, under oath, allegations that continue to be shopped to the media. In fact I would like to highlight that point by submitting for the record – without objection – a Washington Post article dated July 20, page A-15 under the White House Notebook, by Dana Milbank titled " The Kerry Campaign One-Word Weapon." The gist of the article is how the Democrats are using Halliburton as fodder for the presidential campaign.

However, before we hear from the representatives of KBR we will first hear testimony from former employees who believe they personally witnessed waste and abuse. I'm afraid that it will become clear that these individuals are far from experts in government contracting and have, for various reasons, some personal bias against their former employer.

Although the minority has worked with these witnesses for a long time, in the case of Ms. Marie deYoung, the minority knew of her allegations eight months ago – they were brought to our attention only two months ago. At that time, the Ranking Member demanded an immediate hearing without allowing me and my staff to evaluate their claims to determine whether a hearing would be appropriate. After a preliminary evaluation, I agreed to a hearing involving some of the whistleblowers only to see the minority post whistleblower statements on their website, which also led to television news interviews: Again, all without any concern for the validity of their statements. In other words, the minority appears to care more about sensational accusations than the facts. Indeed, I decided to hold this hearing and have the whistleblowers testify to help put them in context, to help us move beyond rhetoric to the truth.

I directed my staff to verify their accusations even though I thought it should have been incumbent on the minority to do this. For those of you who came hoping to hear these witnesses' firsthand evidence of waste, fraud, and abuse by KBR, I am afraid you should brace

yourselves for disappointment. The accusations leveled by the whistleblowers against KBR, both in their written testimony and through personal interviews, are either flat out wrong or at worst minor or represent a naïve or myopic view of contracting in a wartime environment.

Ms. Marie DeYoung's experiences in Kuwait led her to accuse KBR of waste and abuse. Her claims focus on what she calls poor oversight of the subcontractors who, she believes, were fleecing the taxpayer. Ms. deYoung also claims that KBR wastefully leased a five-star hotel for its employees when the employees should have been staying in air-conditioned tents on the US military base. Ms. deYoung, is quick to jump to conclusions without knowing the whole story. As for leasing the five-star hotel, KBR is guilty of this. But, let me put that in context. I have been to Kuwait. In Kuwait most hotels start at 5-star. Kuwait isn't like any country you have ever been to. It is rich. That is why Saddam wanted it so badly. It seems that KBR had little choice. The only real choice was to pick the particular five-star hotel. And, what Ms. deYoung did not know was that KBR wanted to be stationed on the base and had even requested to house employees on the base. A military base is more secure than a hotel, and the base is where the work is. As I understand it, the military, for good reasons, didn't want KBR on the base. By the way, I understand, these hotel rooms had many occupants, sometimes up to 5-6 people in the room at once.

The majority of Ms. deYoung's allegations concern subcontract administration. In her interview with Committee staff, she painted herself as a contract specialist who uncovered subcontractors overcharging for goods and services. I think you will see her math skills leave a little to be desired. She attacks the kind of contracts the minority has been touting. The accusations surrounding soda and laundry are tied to fixed-price contracts. Again, this is all seems to be explainable, or at worst relatively minor, when the entire story is told.

Mr. Mike West's problems started early with KBR. He claims that prior to starting with the company he negotiated a starting salary of $130,000 only to learn his salary would be $82,000 per year, based on a 12-hour-day, 7-days-per-week schedule. Although Mr. West felt he was cheated, he decided to accept the salary and join KBR as a labor foreman. In his interview with Committee staff, Mr. West often complained that he had to wait. Wait to get from point A to point B. Wait to be assigned work. Wait to get a ride back to the States. As a former military member myself, I am familiar with this feeling. We call that "hurry up and wait." Hurry up and wait isn't waste and abuse, it is unfortunately part of the logistical challenges that are presented when working with the Army that changes its mind more often than not. Mr. West did eventually work, but he didn't like the work and left after two months. The experience left a bad taste in his mouth, so he quit. Obviously, this type of environment didn't suit Mr. West. Unlike working in the States, the atmosphere in Iraq wasn't conducive to plans being carried out like clockwork. It's just the opposite. In the early days after the war, adapting to the situation was more the rule than the exception. I know my colleagues who traveled with me to Iraq can verify that this is true.

James Warren and David Wilson are truck drivers who drove convoys in Iraq. They both have similar stories, and I see that their similarity extends to the lawyers they brought here with them today. The gist of these gentlemen's allegations has to do with what they see as waste and abuse of taxpayer assets. They claim that poor maintenance and the lack of proper spare parts

led to trucks breaking down, and a lack of interest in conserving assets resulted in disabled vehicles being destroyed on site rather than fixed or towed. After all, these weren't KBR's trucks so why should they care? Again, what we have here are accusations made with tunnel vision. I think we will all see when we have the opportunity to hear the whole story that most of the actions of the contractor were likely out of its control here and make sense given the security concerns in running convoys in Iraq. Yes, it makes sense to retrieve the truck, and I understand how a professional truck driver loathes seeing a piece of equipment like that being destroyed. However, an $85,000 truck is simply not worth a life, whether it is one of our soldiers or a civilian who might be in harm's way without the protection of the convoy. Mr. Warren and Mr. Wilson ought to be grateful that they returned from Iraq unharmed.

These truck drivers, like the rest of these whistleblowers, believe that what they saw while working in Kuwait and Iraq were not simply examples of paperwork problems or the "hurry up and wait" environment, but were instead the result of wanton and careless disregard of KBR towards American taxpayer funds. Our acquisition system is a complex web of regulations and safeguards put in place to protect the taxpayer. A person with a view of only a small part of an entire process cannot see that there are many players and considerations involved with decisions that, in wartime especially, might sometimes overlook some formalities to ensure that the mission is accomplished and that no one gets hurt. Unfortunately, even with these goals in mind, this conflict has cost 47 KBR employees their lives.

I believe that tunnel vision, inexperience, and naiveté are behind most of these witnesses' allegations. But to be honest, I fear some are here because they have ulterior motives, whether it is a book idea or a try at the litigation lottery jackpot. Today the truth will come out. I tried to convince the minority that there was nothing here, but again, there are some who aren't interested in constructive oversight, but only oversight that advances their narrow political agenda.

As we saw clearly in past hearings the contract oversight process is hard at work here. All the charges under the LOGCAP contract will come under the scrutiny of government auditors and will not be paid unless the contracting officer is confident they are reasonable, allocable to the particular contract and allowable under the government's cost principles.

Our second panel today is made up of representatives of Kellogg Brown and Root (KBR), a subsidiary of the Halliburton Company. KBR is the major prime contractor executing the Army's Logistical Civil Augmentation Program (LOGCAP). LOGCAP was established in 1985 to manage the use of various civilian contractors who perform services in support of DOD missions during times of war and other military mobilizations. LOGCAP has been used to support DOD missions from Somalia to Afghanistan to Iraq. It was used effectively during military operations in Bosnia and Kosovo. The effort in Iraq is the largest in the history of the LOGCAP program. As of last May the estimated value of the contract services in Iraq is $ 5.6 billion. The LOGCAP contractor in Iraq provides such logistics and engineering services as food preparation, laundry, housing, and construction in support of military operations.

This particular contract held by KBR is the third iteration of the Army LOGCAP contract. The first was awarded to KBR in 1992, the second was awarded to DynCorp in 1994

and the current contract awarded to KBR in 2001. I think it is important to keep in mind that all three of these contracts were awarded under competitive acquisitions.

The LOGCAP contract was awarded on a cost-plus award fee basis. Such contracts provide that the contractor is only to be reimbursed for reasonable, allowable, and allocable costs incurred as prescribed in the contract. A cost-plus award fee contract provides financial incentives based on performance. The logistical needs of our military in Iraq and Kuwait are massive, time sensitive and ever changing. In order to meet these needs KBR must be able to react swiftly. These requirements dictate the use of such a cost-type contract. Cost-type contracts are commonly used where, as in Iraq, urgency and uncertainties do not permit costs to be estimated with sufficient accuracy to permit the use of fixed-price contracts.

Indeed, Defense auditors have criticized KBR for inadequate cost estimating and problems with its accounting and documentation practices. There are a number of outstanding issues concerning KBR, particularly concerning food services. These types of issues often arise in the context of cost-type contracts and are a part of the normal contract oversight process. The issues tend to be exacerbated here because of the large amounts of money involved and the extremely difficult conditions in Iraq.

KBR has told Committee staff that they are prepared to answer all the questions relating to the whistleblowers and other allegations that have been leveled against them through the press or by congressional critics. This includes answering dining facility charges, kickback schemes, gasoline subcontracts and other allegations of overcharging. We look forward to hearing their side of the story.

In closing I want to ask that everyone here, especially my colleagues and the members of the media, to stick around and listen to our third panel witness, Dr. Steve Kelman. Dr. Kelman is the Weatherhead Professor of Public Management at the Harvard Kennedy School of Government and the former Director of the Office Federal Procurement Policy under the Clinton Administration, and he is above the political fray.

Dr. Kelman is here to offer some general observations about our acquisition system and its operations in a wartime atmosphere in Iraq. The minority has questioned the contracting activities in Iraq, and I can think of no better person to testify as to whether or not our acquisition system and its contract vehicles can do the job in Iraq. In many ways, Dr. Kelman's testimony is the most important today.

Chairman TOM DAVIS. Mr. Waxman, I recognize you for an opening statement.

Mr. WAXMAN. Thank you, Mr. Chairman. Today is the committee's third hearing this year on Halliburton's contracts in Iraq, and I want to begin by commending Chairman Davis for holding this hearing. The Bush administration is notoriously opposed to oversight, so it has taken independence and a commitment to oversight for our chairman to agree to hold this hearing.

Halliburton holds the two largest contracts in Iraq: a $5.6 billion contract called LOGCAP, to provide support services to the troops; and a $2.5 billion contract, called RIO, to restore Iraq's oil fields. Yet from the very beginning, these two contracts have been plagued by mismanagement and inflated billings.

There is an old saying, "Don't miss the forest for the trees." But sometimes the reverse is true. You have to study the individual trees to really understand the forest. That is why this hearing is so important. The administration's approach to the reconstruction of Iraq is fundamentally flawed. It is a boondoggle that is enriching a lot of contractors but not accomplishing enough on the ground, and there is no better window on what is going wrong than Halliburton.

Halliburton is an $8 billion microcosm that symbolizes the administration's misplaced priorities. Our troops are clamoring for body armor. But when it comes to Halliburton, GAO has found that there were no spending limits. Two years ago, the administration started the drum beat for war by providing Congress and the American people with misleading information about the threat posed by Saddam Hussein and his alleged links to al-Qaeda. We know now that what we were told was unreliable and often wrong, but we didn't know enough to correct the mistakes until after the fact. We can't let that happen again.

The administration says it has a highly sophisticated plan for rebuilding Iraq, but in fact it is doling out monopoly contracts worth millions to private contractors, squashing competition that could discipline prices, and paying millions of dollars to so-called oversight contractors who are the business partners of the very companies they are supposed to be monitoring. We know this is occurring, but where is the outrage? This committee is investigating, but no one else is, and no legislation is moving to fix these problems.

Yesterday, Mr. Dingell and I released two reports about Halliburton's contracts. This is what they reveal. Halliburton is gouging the taxpayers. And aside from the independent auditors at the Defense Contract Audit Agency, the Bush administration doesn't seem to care. The whole justification for hiring private contractors and private companies like Halliburton is that the companies can save the taxpayers money. But Halliburton has turned this principle on its head.

In April, a government agency took over the responsibility of importing gasoline into Iraq. My staff's investigation revealed the agency is now doing this job at a fraction of what Halliburton charged. Here is one example, which is illustrated by a chart over to the left.

Both Halliburton and the Defense Energy Support Center used the same company, Altanmia, to import gasoline from Kuwait into

Iraq, but Halliburton billed $1.30 in transportation charges for every gallon trucked across the border while the Defense Energy Support Center is paying just 42 cents per gallon, less than one-third of the price.

The GAO report released yesterday is a top-to-bottom indictment of how the administration has mismanaged Halliburton's LOGCAP contract. The GAO found that the administration's planning was "ineffective and piecemeal;" that there were no spending limits for LOGCAP until spring 2004; that "It is difficult to know how much the contractor has actually spent;" and that the military officials responsible for oversight had "little or no training."

Here is a telling fact. We know from last month's hearing that the administration started to plan for taking control of Iraq's oil fields in the summer of 2002, months before the war began, yet GAO's report reveals that there was no contingency planning for feeding and housing our troops until May 2003, after the fall of Saddam. Those are not the priorities of most Americans.

Today, we are going to hear from a panel of former Halliburton employees. They will describe their firsthand experiences working for Halliburton in Iraq and the instances of waste, theft, and mismanagement they personally witnessed. It is not easy to come before a congressional committee and blow the whistle on these kinds of abuses, and I want to commend them for their candor and their patriotism for appearing here today.

What they will say to us in their testimony in a few minutes is not the first indication that waste is going on. They are telling us from the inside perspective what we have seen from an outside perspective from three different audit agencies, the DCAA, the CPA IG and the GAO. Now, those are letters, but the Defense Contract Audit Agency works in the Pentagon, the Coalition Provisional Authority is the organization that was running the government in Iraq, now more behind the scenes, and their Inspector General has told us the same thing, as has the General Accounting Office. All three audit agencies have told us Halliburton is wasting our money. They have told us from their outside review. The witnesses, who are whistleblowers, are going to tell us from their insider perspective. They are not telling us something new, they are just telling us something from a different perspective.

And for the first time Halliburton officials will testify before Congress, and I especially welcome their participation. There can be two sides to every story, and I look forward to learning Halliburton's side of this one.

But let me contrast the fact that the witnesses who are whistleblowers were not allowed to testify before, because the majority wanted to talk to them at length to review what they had to say and also to try to find any evidence they could to try to discredit them. Well, I suppose that is not politics. But Halliburton witnesses were not open to any substantive review by our staff in advance and we are not complaining about that. Witnesses who have something to say ought to come forward, we ought to hear their testimony, and we ought to be able to ask them questions. And sometimes the questions—to get out the truth—are going to be hostile or adversarial. But I wanted to just compare the two panels of witnesses that we have today.

I want to conclude by addressing the role of the Vice President and the allegations that the attention and criticism Halliburton has received is politically motivated. My focus and my concern has been for the U.S. taxpayer. We are spending tens of billions of dollars in Iraq, and the company with the two largest contracts is Halliburton. If you want to know whether the taxpayers' interests are being protected, you have to follow the money, and in this case the money leads to Halliburton.

Last September, Vice President Cheney appeared on national television and said "I have absolutely no knowledge of, in any way, shape, or form, of contracts let by the Corps of Engineers or anybody else in government." Senior government officials assured the public that Halliburton's no-bid contract was done by career civil servants.

Well, I accepted those assurances at face value, and many Americans did also. But we now know those assurances were false. The decision to give Halliburton the sole-source Iraq oil work was made by a political appointee, not career procurement officials, and the Vice President's chief of staff received an extensive briefing. These revelations fundamentally change our oversight responsibilities.

A shrewd politician once said, "Fool me once, shame on you. Fool me twice, shame on me." We've been fooled once by the White House about the role of the Vice President and political appointees in the Halliburton contract. Now we need to investigate to learn the full story.

Today, we will take another step forward, and a big one, in our oversight of contracting in Iraq. And I commend the chairman for holding this hearing and look forward to working with him as our investigative efforts continue.

I also want to ask, Mr. Chairman, that the reports that Mr. Dingell and I released yesterday be made a part of the hearing record.

Chairman TOM DAVIS. We will be happy to make it part of the record, but just make it clear that these are minority views. Be happy to include it as part of your statement.

Mr. WAXMAN. Yes, as part of our statements, we will include the report.

[The information referred to follows:]

UNITED STATES HOUSE OF REPRESENTATIVES
COMMITTEE ON GOVERNMENT REFORM — MINORITY STAFF
SPECIAL INVESTIGATIONS DIVISION
JULY 21, 2004

HALLIBURTON'S GASOLINE OVERCHARGES

PREPARED FOR

REPS. HENRY A. WAXMAN AND JOHN D. DINGELL

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EXECUTIVE SUMMARY

For the past nine months, Reps. Henry A. Waxman and John D. Dingell have been investigating the high prices charged by Halliburton to import gasoline into Iraq under a no-bid contract awarded by the U.S. Army Corps of Engineers. As part of this investigation, the staff consulted with energy experts inside and outside of the government, received detailed cost information from the Army Corps and the Defense Energy Support Center (DESC), and interviewed numerous individuals in Iraq and Kuwait. The staff also met on multiple occasions with Halliburton officials to understand the company's perspective on the allegations of overcharging.

This report presents the results of the investigation. It finds that the decision to give Halliburton the contract to import millions of gallons of gasoline from Kuwait into Iraq significantly increased the costs to the government. Compared to the Defense Energy Support Center, which has taken over the responsibility to import gasoline into Iraq from Halliburton, Halliburton charged much more to purchase fuel in Kuwait, to transport the fuel into Iraq, and to cover its fees and markups. In total, these unnecessary charges increased the costs to the government by $167 million, an increase of over 90%.

Halliburton was awarded the task order to import gasoline into Iraq on May 4, 2003. Halliburton promptly entered into a contract with a Kuwaiti company, Altanmia Commercial Marketing Company, to purchase gasoline from the Kuwait Petroleum Company (KPC) and transport it into Iraq. Between May 5, 2003, and March 31, 2004, Halliburton imported 131 million gallons of gasoline from Kuwait into Iraq under the contract with Altanmia.

On April 1, 2004, DESC took over the responsibility of importing gasoline into Iraq. Like Halliburton, DESC also entered into contracts with other companies to supply and transport the fuel to Iraq. In fact, DESC hired the same company that Halliburton used, Altanmia, to transport the fuel from Kuwait into Iraq. Unlike Halliburton, however, DESC purchases the gasoline itself directly from KPC, not through a middleman like Altanmia.

Halliburton's and DESC's costs can be broken into three basic components: (1) fuel costs; (2) transportation costs; and (3) fees and markups. This report finds that Halliburton charged the government substantially more than DESC in each category.

Gasoline is a commodity, and its prices fluctuate daily on a "spot" market. Halliburton paid Altanmia approximately $0.32 per gallon above the spot price to purchase gasoline from KPC. In contrast, DESC pays KPC approximately $0.16 per gallon above the spot price. Compared to DESC, Halliburton paid twice as much above the spot price for gasoline.

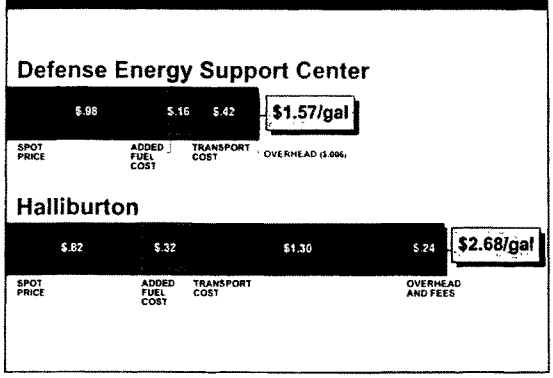
Halliburton's transportation costs also exceeded DESC's. Halliburton paid Altanmia an average cost of $1.30 per gallon to transport the gasoline into Iraq. In contrast, DESC

pays Altanmia only $0.42 per gallon to transport the gasoline into Iraq. Compared to DESC, Halliburton paid Altanmia over three times more for transportation services.

Halliburton's fees and markups added $0.24 per gallon to the cost of importing gasoline from Kuwait into Iraq. In contrast, DESC charges no fee and has a "markup" of less than $0.006 per gallon to cover its management and oversight costs. Compared to DESC, Halliburton charged the U.S. government 40 times more per gallon in fees and markups.

The difference between Halliburton's prices and DESC's prices is large. During the period from May 5, 2003, to March 31, 2004, Halliburton charged an average price of $2.68 per gallon to import gasoline from Kuwait into Iraq, consisting of a spot price of $0.82 per gallon, a fuel surcharge of $0.32 per gallon, a transportation cost of $1.30 per gallon, and fees and markups of $0.24 per gallon. In contrast, DESC has charged an average price of only $1.57 per gallon since taking over the fuel importation responsibilities, consisting of a spot price of $0.98 per gallon, a fuel surcharge of $0.16 per gallon, a transportation cost of $0.42 per gallon, and markups of $0.006 per gallon. See Figure 1.

Figure 1:
Price of Gasoline Imported Into Iraq from Kuwait



In total, Halliburton charged the government the spot price plus $1.86 per gallon to import gasoline from Kuwait to Iraq, while DESC charges the government the spot price plus $0.59 per gallon. Compared to the costs DESC incurs, the decision to give the contract to import gasoline from Kuwait into Iraq to Halliburton increased costs to the U.S. government by $1.27 per gallon. This is an increase of over 90%, assuming constant spot prices. When this overpayment is multiplied by the 131 million gallons imported from Kuwait into Iraq by Halliburton, the total increased cost is $167 million.

I. BACKGROUND

A. Halliburton's Fuel Importation Contract

On March 8, 2003, the Army Corps of Engineers awarded Halliburton a secret no-bid monopoly contract to restore and operate Iraq's oil infrastructure, currently valued at $2.53 billion but worth up to $7 billion.[1] Under this cost-plus contract, Halliburton's costs are reimbursed and the company receives an additional fee of 2% to 7% of its costs.

On May 4, 2003, the Army Corps issued Task Order 5 under the contract, instructing Halliburton to begin purchasing and importing fuel into Iraq for civilian use.[2] Nearly $1.5 billion has been obligated for fuel importation into Iraq under this and subsequent task orders.[3]

Rather than perform the work itself, Halliburton selected an obscure Kuwaiti subcontractor, Altanmia Commercial Marketing Company, to import gasoline from Kuwait. Altanmia had no previous fuel procurement or transportation experience.[4] According to Halliburton, Halliburton knew about Altanmia because Halliburton had previously leased real estate from an affiliated company within the same family-owned conglomerate.[5]

Halliburton awarded the subcontract to Altanmia in a single day after obtaining quotes from just two other bidders.[6] On May 4, the same day Task Order 5 was issued, the Army Corps requested that Kuwait's Oil Minister approve Halliburton's choice of Altanmia.[7] The next day, Halliburton told Altanmia to begin purchasing and delivering gasoline.[8]

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1 U.S. Army Corps of Engineers, *Frequently Asked Questions: Engineer Support to Operation Iraqi Freedom* (May 11, 2004) (online at www.hq.usace.army.mil/CEPA/Iraq/March03-table.htm).

2 U.S. Army Corps of Engineers, *Information Paper: Business Case by USACE for the Use of Altanmia as a Supplier of Fuel under the RIO Contract* (Jan. 6, 2004).

3 U.S. Army Corps of Engineers, *supra* note 1.

4 *Fuel for the Fire: At Center of Halliburton Uproar, Little-Known Kuwaiti Company*, Wall Street Journal (Apr. 14, 2004)

5 Meeting between Halliburton representatives and Minority Staff, Committee on Government Reform (June 2, 2004).

6 U.S. Army Corps of Engineers, *supra* note 2.

7 Letter from John M. Weatherly, Jr., Administrative Contracting Officer, U.S. Army Corps of Engineers, to Sheikh Ahmad Al-Fahad Al-Sabah, Oil Minister of Kuwait (May 4, 2003).

Halliburton officials described their subcontractor selection process as "open and competitive."[8] However, the process was not open to all competitive bidders. Rather than seeking out experienced companies, Halliburton contacted companies that some industry experts had never heard of. The two other bidders contacted by Halliburton were Elafco General Trading and Ma'mar Specialties.[10] Neither of these companies was a leader in the purchase or transportation of fuel. Halliburton failed to obtain bids from companies that are recognized as leaders in the fuel industry in Kuwait. For example, the Independent Petroleum Group, which imports fuel for Iraq's State Oil Marketing Organization (SOMO), was not offered an opportunity to bid on the subcontract.

In October, Halliburton decided to re-bid the Kuwait subcontracts. Altanmia submitted a bid of $1.14 per gallon to procure the gasoline. Its bid for transportation was $23,810 month for each fuel tanker used to transport the gasoline. Halliburton received two lower bids: one from Kuwait Establishment Company (KEC) at $0.91 per gallon to procure the gasoline and $13,527 per tanker; and one from Burgan Express at $0.97 per gallon to procure the gasoline and $9,950 per fuel tanker for transport.[11]

Despite receiving two substantially lower bids, Halliburton continued the subcontract with Altanmia. According to Halliburton, the company rejected KEC because KEC was unable to demonstrate that it had KPC approval to purchase the gasoline.[12] Halliburton also says it rejected Burgan Express's bid because the company needed ten days before it could begin operations.[13] The Army Corps approved of Halliburton's decision to continue the subcontract with Altanmia.[14]

In November 2003, the Army Corps reported to Rep. Waxman that Halliburton had charged an average price of $2.64 per gallon to import gasoline from Kuwait into Iraq.[15] In July 2004, the Army Corps provided updated cost figures to the

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8 U.S. Army Corps of Engineers, *supra* note 2.

9 Halliburton, *Halliburton Provides Update on Fuel Delivery Mission in Iraq* (Oct. 21, 2003).

10 U.S. Army Corps of Engineers, *supra* note 2.

11 Meeting between Halliburton representatives and Minority Staff, *supra* note 5.

12 *Id.*

13 *Id.*

14 *Id.*

15 Briefing by U.S. Army Corps of Engineers to Minority Staff, Committee on Government Reform (Nov. 17, 2003).

Government Reform Committee. According to these more recent figures, Halliburton's average price for the entire period of Halliburton's performance under the contract — from May 2003 though March 2004 — was $2.68 per gallon. Halliburton paid Altanmia $1.14 per gallon to purchase the gasoline from KPC and $1.30 per gallon to transport the gasoline from Kuwait to Iraq by truck. Halliburton then charged $0.24 per gallon in overhead and administrative markups and fees.[16]

Overall, Halliburton imported 131,181,054 gallons of gasoline from Kuwait into Iraq, charging the Army Corps $351,691,346 for these imports.[17]

B. Pricing Concerns

On October 15, 2003, Reps. Waxman and John D. Dingell wrote to Joshua Bolten, Director of the Office of Management and Budget, to raise concerns about Halliburton's fuel charges.[18] In the following months, Reps. Waxman and Dingell wrote eight more letters raising additional concerns about Halliburton's fuel choices and its relationship with Altanmia.[19]

As the letters from Reps. Waxman and Dingell pointed out, independent experts consulted by the staff expressed grave doubts about the reasonableness of

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16 E-mail from U.S. Army Corps of Engineers, transmitted to Minority Staff of the Committee on Government Reform by the Department of Defense (June 20, 2004). According to Halliburton, the company charged for the full 5% award fee, but has not actually received the fee as no award fee board has met. Halliburton charged for and received its 2% base fee. Meeting between Halliburton representatives and Minority Staff, *supra* note 5.

17 E-mail from U.S. Army Corps of Engineers, transmitted to Committee on Government Reform Minority Staff by the Department of Defense (June 20, 2004).

18 Letter from Reps. Henry A. Waxman and John D. Dingell to Joshua Bolten, Director, Office of Management and Budget (Oct. 15, 2003).

19 Letter from Reps. Henry A. Waxman and John D. Dingell to Lt. Gen. Robert B. Flowers, U.S. Army Corps of Engineers (Oct. 21, 2003); Letter from Reps. Henry A. Waxman and John D. Dingell to Condoleezza Rice, Assistant to the President for National Security Affairs (Oct. 29, 2003); Letter from Reps. Henry A. Waxman and John D. Dingell to Lt. Gen. Robert B. Flowers, U.S. Army Corps of Engineers (Nov. 5, 2003); Letter from Reps. Henry A. Waxman and John D. Dingell to Joseph E. Schmitz, Inspector General, U.S. Department of Defense (Nov. 25, 2003); Letter from Reps. Henry A. Waxman and John D. Dingell to Condoleezza Rice, Assistant to the President for National Security Affairs (Dec. 10, 2003); Letter from Reps. Henry A. Waxman and John D. Dingell to Lt. Gen. Robert B. Flowers, U.S. Army Corps of Engineers (Jan. 6, 2004); Letter from Rep. Henry A. Waxman to Condoleezza Rice, Assistant to the President for National Security Affairs (Jan. 15, 2004); Letter from Reps. Henry A. Waxman and John D. Dingell to Joseph E. Schmitz, Inspector General, U.S. Department of Defense (Feb. 24, 2004).

Halliburton's prices. Phil Verleger, a California oil economist and the president of a consulting firm, said of the prices: "It's as if they put the gasoline on the Queen Mary and take[] it around the globe before they deliver it."[20] Jeffrey Jones, until recently the Director of the Defense Energy Support Center, stated: "I can't construct a price that high."[21] Another expert, who asked that his identity not be disclosed, characterized Halliburton's prices as "highway robbery."

The letters also compared Halliburton's prices to other benchmarks. One letter revealed that Iraq's state owned oil company, the State Oil Marketing Organization (SOMO), hired contractors to purchase gasoline and deliver it to Baghdad for about $1.00 per gallon.[22] Another letter disclosed that Halliburton's prices to purchase gasoline and deliver it from Turkey were far lower than those for purchasing and delivering from Kuwait.[23] According to data that the Army Corps provided to Rep. Waxman, Halliburton's per-gallon price from Turkey was $1.24 — less than half the price from Kuwait. Halliburton's $0.22 per-gallon transport cost from Turkey was less than one-fifth of the transport cost from Kuwait.[24]

In December, the Defense Contract Audit Agency (DCAA) announced that its draft audit found that Halliburton had overcharged the U.S. government by as much as $61 million for gasoline imported from Kuwait into Iraq as of September 30, with significant additional overcharges likely in the months thereafter.[25] DCAA concluded that Halliburton "has not demonstrated . . . that they did an adequate subcontract pricing evaluation prior to award" of the Altanmia subcontract.[26] Pentagon auditors also noted the large unexplained disparity between Halliburton's gasoline prices from Turkey and Kuwait.[27] The DCAA auditors sought certified cost and pricing data from Halliburton and Altanmia in

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20 *The High Price of Gasoline for Iraq*, NBC News (Nov. 5, 2003).

21 *Army Eyes Halliburton Import Role in Iraq*, Associated Press (Nov. 5, 2003).

22 Letter from Reps. Henry A. Waxman and John D. Dingell to Lt. Gen. Robert B. Flowers, U.S. Army Corps of Engineers (Oct. 21, 2003). *See also*, Letter from Mohammed M. Al-Jibouri, General Manager, State Oil Marketing Organization, to Minority Staff, Committee on Government Reform (Oct. 16, 2003). Recent conversations with experts in the region confirm this pricing.

23 Letter from Reps. Henry A. Waxman and John D. Dingell to Condoleezza Rice, Assistant to the President for National Security Affairs (Dec. 10, 2003).

24 Briefing by U.S. Army Corps of Engineers, *supra* note 15.

25 U.S. Department of Defense, News Briefing (Dec. 11, 2003).

26 *Id.*

27 *Id.*

order to assess whether the costs being billed to the government were fair and reasonable.

While these concerns mounted, Halliburton consistently claimed that it imported gasoline into Iraq at the best possible price. Several Halliburton press releases insisted that the company "delivered fuel to Iraq at the best value, the best price and the best terms."[28] In a *Washington Post* op-ed, Halliburton's chairman and CEO, David Lesar, wrote, "We are confident that it will be proven that Halliburton delivered the fuel at the best price on the best terms, even under emergency wartime conditions."[29]

The Army Corps of Engineers also defended Halliburton's prices. On December 19, 2003, the Corps unilaterally declared Halliburton's gasoline prices to be "fair and reasonable."[30] As part of this action, the Corps gave Halliburton a waiver from the requirement to provide "any cost and pricing data" from Altanmia relating to the importation of gasoline.[31]

On February 1, 2004, Army Corps spokesman Scott Saunders addressed the fuel prices, stating: "We have our own internal audit process [and we] haven't turned up any serious wrongdoing or major problems."[32]

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28 Halliburton, *Halliburton Successes: Improving the Lives of Soldiers and Iraqis* (Mar. 18, 2004); Halliburton, *Halliburton Sets the Record Straight on KBR's Government Contracts* (Mar. 11, 2004); Halliburton, *Halliburton: KBR Delivered Fuel at Best Value, Price, Terms* (Feb. 24, 2004); Halliburton, *Halliburton Addresses Defense Draft Audit* (Dec. 18, 2003).

29 *Piling on Halliburton*, Washington Post (Mar. 3, 2004).

30 U.S. Army Corps of Engineers, *Waiver for Submission of Cost and Pricing Data* (Dec. 19, 2003).

31 *Id.* The primary rationale for the waiver was that Kuwaiti law prohibited Altanmia from submitting certified cost and pricing data to Halliburton and the Corps. The Corps expressly stated in the waiver document, "[the Department of State] as well as other defense agencies . . . have verified that it is a violation of Kuwaiti law for contractors to submit cost and pricing data for fuel products." This underlying premise appears to be false. Several independent sources, including a Library of Congress legal specialist and a former managing director of the Kuwait Petroleum Corporation in Europe, have indicated that there is no such prohibition in Kuwaiti law. *See* Library of Congress, *Kuwaiti Fuel Laws* (Jan. 15, 2004); Telephone conversation between Samad Al-Blouki and Minority Staff, Committee on Government Reform (Jan. 20, 2004); Telephone conversation between Samad Al-Blouki and Minority Staff, Committee on Government Reform (Jan. 14, 2004).

32 *Halliburton Contract Questions Dog White House*, Chicago Tribune (Feb. 1, 2004).

C. The Move to DESC

Amid the controversy about Halliburton's gasoline prices, the Pentagon decided to relieve Halliburton of its fuel importation responsibilities and assign this duty to an office within the Pentagon, the Defense Energy Support Center (DESC). On December 30, DESC announced that it would replace Halliburton and begin importing fuel into Iraq for civilian use.[33] DESC delivers fuel around the world, usually for military customers, and often on short notice. DESC has had a permanent Persian Gulf office in Bahrain for 50 years.

After its announcement, DESC began preparations to award new fuel and transportation contracts through a full and open competition. DESC issued solicitations for fuel importation from Turkey, Jordan, and Kuwait.

On March 15 and 16, after receiving and evaluating 34 timely proposals in response to two solicitations, DESC awarded new contracts for the importation of gasoline into southern Iraq from Kuwait.[34] One contract was awarded to Kuwait Petroleum Company for the gasoline itself, and another was awarded to Altanmia for transportation of gasoline from Kuwait to Iraq. Performance of the contracts began on April 1.[35]

II. EVALUATION OF HALLIBURTON'S GASOLINE PRICES

The transfer of the gasoline importation responsibilities from Halliburton to DESC provides a unique opportunity to assess the reasonableness of Halliburton's prices. DESC is now performing the same function that Halliburton performed for 11 months. Both Halliburton and DESC located and hired contractors to acquire gasoline in Kuwait and transport it into Iraq for civilian use. In fact, both Halliburton and DESC hired the same firm, Altanmia, to transport the fuel. Because of these similarities, a direct "apples-to-apples" price comparison can be made between Halliburton's prices and DESC's costs.

In making this comparison, Halliburton's prices and DESC's costs can be broken into three components: (1) payments above the spot price to procure the fuel; (2) payments to transport the gasoline from Kuwait into Iraq; and (3) fees and

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33 Defense Logistics Agency, *Defense Energy Support Center to Help Restore Iraqi Oil* (Dec. 30, 2003).

34 U.S. Department of Defense, *Contracts: Defense Logistics Agency* (Mar. 16, 2004).

35 E-mail from Legislative Affairs, Defense Logistics Agency, to Minority Staff, Committee on Government Reform (Apr. 9, 2004).

markups to cover the cost of their services. Halliburton's costs are substantially higher than DESC's costs in each category.

A. Gasoline Procurement Costs

After controlling for market fluctuations, Halliburton charged more than DESC for the purchase of the gasoline. Gasoline is a commodity, and its prices fluctuate daily on a "spot" market. According to the Army Corps, Halliburton paid Altanmia an average price of $1.14 per gallon for gasoline.[36] While Halliburton was paying Altanmia to buy gasoline from KPC for $1.14 per gallon, the average spot price for Arab Gulf gasoline was just $0.82.[37] Thus, Halliburton paid approximately $0.32 per gallon above the spot price to purchase gasoline.

In contrast to Halliburton, DESC contracts directly with KPC for the purchase of gasoline. Unlike Halliburton, DESC is not paying a middleman to buy the gasoline from KPC. DESC has a three-month "fixed price with economic price adjustment" contract. Under this contract, there is an established differential between the price charged by KPC and the published Platt's Arab Gulf spot price. Every two weeks, the gasoline price is adjusted to take changes in the market price into account. Under this arrangement, DESC pays KPC approximately $0.16 per gallon above the prevailing spot price.[38]

As Figure 2 shows, Halliburton paid twice the amount that DESC paid beyond the spot price for gasoline.

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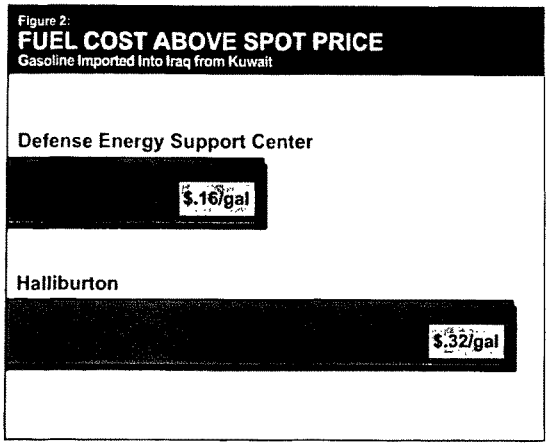
[36] E-mail from U.S. Army Corps of Engineers, *supra* note 16.

[37] Congressional Research Service, *Average of Recent Gasoline Prices in the Persian Gulf* (Apr. 19, 2004) (surveying *Platt's Oilgram* spot prices for Arab Gulf gasoline from May 5, 2003, to April 2, 2004).

[38] *Id.*; E-mail from Legislative Affairs, Defense Logistics Agency, to Minority Staff, Committee on Government Reform (June 24, 2004). The DESC price was $1.14 for the initial two-week period beginning April 1, 2004. On April 2, the Arab Gulf spot price was $0.98 per gallon.



According to Halliburton, Altanmia purchased gasoline from KPC at market prices but sold it to Halliburton at a fixed price. The company contends that Altanmia was actually losing money on the gasoline purchases in January 2004, when spot prices were particularly high. However, an eleven-month survey of Persian Gulf spot prices demonstrates that the spot price never reached the $1.14 per gallon price Altanmia was charging.[39] According to Halliburton, Altanmia billed Halliburton $0.16 per gallon for labor and other miscellaneous costs.[40] Assuming Altanmia actually incurred fuel procurement costs of $0.16 per gallon, Altanmia would have lost money on its gasoline procurements in only two weeks in January when the spot prices were as high as $1.07 and $1.00.[41] At other times during the contract, Altanmia purchased gasoline for Halliburton with spot prices as low as $0.59 per gallon.[42]

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39 Congressional Research Service, *supra* note 37.

40 Meeting between Halliburton representatives and Minority Staff, *supra* note 5. Halliburton reported the following nongasoline costs borne by Altanmia for the procurement of each gallon of gasoline: $0.05 for labor, $0.03 for "cost of funds," $0.02 for insurance, $0.02 for the refinery fee, $0.02 for the "bank cost," $0.01 for "overtime cost," and $0.01 for currency fluctuation.

41 Congressional Research Service, *supra* note 37.

42 *Id.*

B. Transportation Costs

Halliburton also failed to arrange a reasonable transport cost. Instead, Halliburton charged over three times as much as the Defense Energy Support Center for transportation from Kuwait.

Both Halliburton and DESC selected Altanmia to transport gasoline from Kuwait. However, Halliburton paid Altanmia far more for this service than DESC currently does. According to the data from the Army Corps, Halliburton paid Altanmia an average of $1.30 per gallon to transport gasoline from Kuwait into Iraq.[43]

By comparison, DESC pays Altanmia just $0.42 per gallon, regardless of the destination and any unanticipated costs incurred by Altanmia.[44] Under this firm fixed-price contract, Altanmia, not the U.S. government, bears the risk of price fluctuations and costs from any delays or damage to fuel trucks. Altanmia delivers gasoline for DESC to multiple locations, including the Baghdad area.

Halliburton and the Army Corps have said that a $1.30 per gallon transport charge is reasonable because a round-trip to Baghdad for a fuel truck can take as long as ten to twelve days.[45] Halliburton informed the staff that Altanmia's fuel trucks made as few as two round-trips per month, but that the price would have been $0.82 per gallon if four round-trips per month had been possible.[46] DESC's transport cost of $0.42 per gallon is based on just three round-trips per month, or one trip every ten days. If four or five round-trips can be made, the price drops to $0.41 or $0.40, respectively.[47] Thus, DESC's highest price is about half of Halliburton's lowest price projection.

As shown in Figure 3, Halliburton's actual transportation costs were over three times larger than DESC's.

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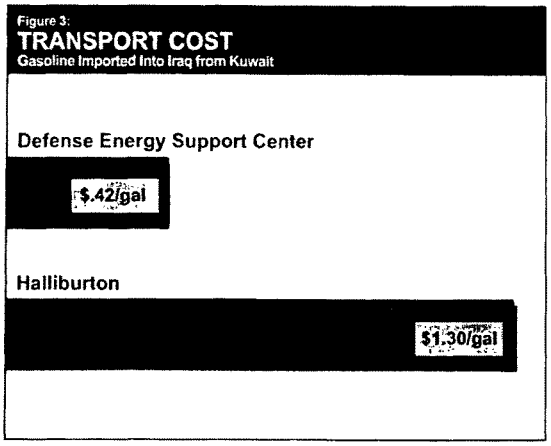
43 E-mail from U.S. Army Corps of Engineers, *supra* note 16.

44 E-mail from Legislative Affairs, Defense Logistics Agency, to Minority Staff, Committee on Government Reform (Mar. 18, 2004).

45 Halliburton, *Halliburton Sets the Record Straight on KBR's Government Contracts* (Mar. 11, 2004); U.S. Army Corps of Engineers, *supra* note 2.

46 Meeting between Halliburton representatives and Minority Staff, *suprai* note 5.

47 E-mail from Legislative Affairs, Defense Logistics Agency, *supra* note 44.



C. Fees and Markups

In relative terms, the largest difference between Halliburton's prices and DESC's costs involved fees and overhead costs. According to data from the Army Corps, Halliburton charged $0.24 per gallon in markups and fees. This $0.24 per gallon results from a 0.61% overhead markup, a 1.99% "General & Administrative" markup, a 2% base fee, and a 5% award fee.[45]

By contrast, DESC's management and overhead costs for a gallon of gasoline amount to just $0.006, or about half a cent, per gallon.[46] As a government agency, DESC charges no fee.

As summarized in Figure 4, Halliburton charged the U.S. government 40 times more per gallon in fees and markups than DESC did. Its total charges for fees and markups amounted to $31,375,045.

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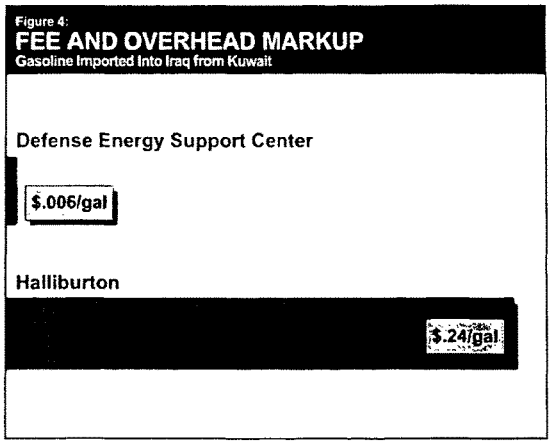
[45] E-mail from U.S. Army Corps of Engineers, *supra* note 16.

[46] E-mail from Legislative Affairs, Defense Logistics Agency, *supra* note 44.



D. Total Per-Gallon Price Difference

The difference between Halliburton's price and DESC's price is substantial on a per-gallon basis. Halliburton's total cost of $2.68 per gallon to import gasoline from Kuwait was equal to the spot price plus $1.86 per gallon. DESC's total cost of $1.57 per gallon to import gasoline from Kuwait is equal to the spot price plus $0.59 per gallon. Halliburton's costs beyond the applicable spot price were thus $1.27 more per gallon than DESC's. In percentage terms, and assuming constant spot prices, Halliburton charged over 90% more per gallon than DESC to import fuel from Kuwait into Iraq.[50]

E. Total Overpayment to Halliburton

Between May 4, 2003, and March 31, 2004, Halliburton imported 131 million gallons of gasoline from Kuwait through its subcontractor, Altanmia.[51] Halliburton charged more than DESC on all cost components of this imported fuel: fuel procurement, transportation, and fees and markups. On a per-gallon

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50 From May 2003 through March 2004, average spot prices were $0.82 per gallon and Halliburton's total charge was $2.68 per gallon. If the spot price had remained at $0.82 per gallon after April 1, 2004, when DESC assumed fuel importation responsibilities, DESC's price would have been $1.41 per gallon. Halliburton's price of $2.68 per gallon is 90% higher than this price.

51 E-mail from U.S. Army Corps of Engineers, *supra* note 16.

basis, Halliburton's total charges beyond the relevant spot price were $1.27 more than DESC's. When this per-gallon overpayment is multiplied by 131 million gallons, the total amount of the overpayment to Halliburton is $166,550,000.

III. FUEL IMPORTS FROM OTHER COUNTRIES

Kuwait is not the only country from which Halliburton and DESC have imported gasoline. Both have also imported gasoline from Turkey at lower costs than from Kuwait. Between May 5, 2003, and March 31, 2004, Halliburton imported 335 million gallons of gasoline from Turkey into Iraq at an average per-gallon cost of $1.24.[52] Both in absolute terms and relative to DESC prices, Halliburton's Turkey prices are more reasonable than its Kuwait prices. DESC pays approximately $1.19 per gallon to import gasoline from Turkey.[53]

According to Halliburton, the company was instructed to continue importing gasoline from Kuwait into Iraq despite the higher prices because the Army Corps did not want to be dependent on one country for gasoline imports.[54] Halliburton could not explain, however, why it continued to use Kuwait as the second source of gasoline instead of another less expensive source of gasoline, such as Jordan. Although Halliburton imported relatively small amounts of kerosene and diesel from Jordan, Halliburton did not import any gasoline from Jordan.[55]

In contrast, DESC has sought proposals for gasoline imported from Jordan and has awarded a contract to Shaheen Business & Investment Group for the purchase and delivery of nearly 24 million gallons of gasoline from Jordan. DESC paid Shaheen $1.19 per gallon to buy and import the gasoline.[56] This new route provides significant amounts of additional fuel at more reasonable prices than those from Kuwait.

IV. CONCLUSION

Halliburton has maintained that it delivered gasoline from Kuwait to Iraq "at the best value, the best price and the best terms." A comparison of its prices to those

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52 E-mail from U.S. Army Corps of Engineers to Minority Staff, Committee on Government Reform (Apr. 13, 2004); Briefing by U.S. Army Corps of Engineers, *supra* note 15.

53 Defense Energy Support Center, *Fact Sheet* (Mar. 9, 2004).

54 Meeting between Halliburton representatives and Minority Staff, *supra* note 5.

55 E-mail from U.S. Army Corps of Engineers, *supra* note 52.

56 Defense Energy Support Center, *Fact Sheets* (Mar. 15, 2004).

being charged by DESC for the same services does not support Halliburton's claim. Halliburton's charges over the applicable spot price were $1.27 more per gallon of gasoline imported from Kuwait to Iraq than those of DESC. In total, the U.S. government has paid Halliburton $167 million in unnecessary costs.

Chairman TOM DAVIS. Without objection, so ordered.

Mr. WAXMAN. Mr. Chairman, I have completed my opening statement, but I want to bring to the attention of the members of the committee a motion that I am going to make for a subpoena.

Since March 2003, administration officials have repeatedly said there are absolutely no contacts between the Vice President's Office and the Pentagon regarding Halliburton's November 2002 task order to develop a contingency plan for Iraq's oil infrastructure and its March 2003 no-bid contract to implement that plan. Administration officials also have consistently said that career civil servants were responsible for choosing Halliburton to conduct the planning and oil infrastructure work.

My motion that is before us—and maybe you want to report it so it is before the body, and I can then continue with my opening statement—is a request for a subpoena.

Chairman TOM DAVIS. The motion offered by the gentleman from California is in order under House Rule XI clause 2(k)(6). Mr. Waxman and I have talked about this prior. We talked about it yesterday and today. That rule states that the chairman shall receive and the committee shall dispense with requests to subpoena additional witnesses. Pursuant to that rule, the chairman may determine the timing of the consideration of such request.

At this time, the motion shall be considered as entered, and the committee will consider the motion offered by the gentleman from California today.

[The prepared statement of Hon. Henry A. Waxman follows:]

Statement by Rep. Henry A. Waxman
July 22, 2004

Today is the Committee's third hearing on Halliburton's contracts in Iraq. I want to begin by commending Chairman Davis for holding this hearing. The Bush Administration is notoriously opposed to oversight, so it has taken independence and a commitment to oversight for our Chairman to agree to hold this hearing.

Halliburton holds the two largest contracts in Iraq: a $5.6 billion dollar contract called LOGCAP to provide support services to the troops and a $2.5 billion dollar contract called RIO to restore Iraq's oil fields. Yet from the very beginning, these two contracts have been plagued by mismanagement and inflated billings.

There is an old saying: Don't miss the forest for the trees. But sometimes the reverse is true. You have to study individual trees to really understand the forest.

That is why this hearing is so important. The Administration's approach to the reconstruction of Iraq is fundamentally flawed. It's a boondoggle that is enriching a lot of contractors, but not accomplishing enough on the ground. And there is no better window on what is going wrong than Halliburton.

Halliburton is an $8 billion microcosm that symbolizes the Administration's misplaced priorities. Our troops are clamoring for body armor, but when it comes to Halliburton, GAO has found that there were "no spending limits."

Two years ago, the Administration started the drumbeat for war by providing Congress and the American people with misleading information about the threat posed by Saddam Hussein and his alleged links to al Qaeda. We know now that what we were told was unreliable and often wrong. But we didn't know enough to correct the mistakes until after the fact.

We can't let that happen again. The Administration says it has a highly sophisticated plan for rebuilding Iraq. But in fact, it is doling out monopoly contracts worth billions to private contractors, squashing competition that could discipline prices, and paying millions of dollars to so-called "oversight contractors" who are the business partners of the very companies they are supposed to be monitoring.

We know this is occurring, but where is the outrage? This Committee is investigating, but no one else is. And no legislation is moving to fix these problems.

Yesterday, John Dingell and I released two reports about Halliburton's contracts. This is what they reveal: Halliburton is gouging the taxpayer, and aside from the independent auditors at the Defense Contract Audit Agency, the Bush Administration doesn't seem to care.

The whole justification for hiring private companies like Halliburton is that the contractors can save the taxpayer money. But Halliburton has turned this principle on its head. In April, a government agency took over the responsibility of importing gasoline into Iraq. My staff's investigation revealed that the agency is now doing this job at a fraction of what Halliburton charged.

Here's one example, which is illustrated in a chart: Both Halliburton and the Defense Energy Support Center use the same company, Altanmia, to import gasoline from Kuwait into Iraq. But Halliburton billed $1.30 in transportation charges for every gallon trucked across the border, while DESC is paying just $0.42 per gallon – less than one-third of the price.

The GAO report we released yesterday is a top-to-bottom indictment of how the Administration has mismanaged Halliburton's LOGCAP contract. GAO found that Administration planning was "ineffective" and "piecemeal" … that there were "no spending limits for

LOGCAP until spring 2004" … that "it is difficult to know how much the contractor has actually spent" … and that the military officials responsible for oversight had "little or no training."

Here's a telling fact: We know from last month's hearing that the Administration started to plan for taking control of Iraq's oil fields in the summer of 2002, months before the war began. Yet GAO's report reveals that there was no contingency planning for feeding and housing our troops until May 2003, after the fall of Saddam.

Those aren't the priorities of most Americans.

Today we are going to hear from a panel of former Halliburton employees. They will describe their first-hand experiences working for Halliburton in Iraq and the instances of waste, theft, and mismanagement they personally witnessed. It is not easy to come before a congressional committee and blow the whistle on these kinds of

abuses. I commend them for their candor and their patriotism for appearing here today.

And for the first time, Halliburton officials will testify before Congress. I especially welcome their participation. There can be two sides to every story, and I look forward to learning Halliburton's side of this one.

I want to conclude by addressing the role of the Vice President and the allegation that the attention and criticism Halliburton has received is politically motivated.

My focus and my concern has been the U.S. taxpayer. We are spending tens of billions of dollars in Iraq and the company with the two largest contracts is Halliburton. If you want to know whether the taxpayer's interests are being protected, you have to follow the money. And in this case, the money leads to Halliburton.

Last September, Vice President Cheney appeared on national television and said: "I have absolutely no … knowledge of in any way, shape or form of contracts led by the Corps of Engineers or anybody else in government." Senior government officials assured the public that Halliburton's no-bid contract was "done by career civil servants."

I accepted those assurances at face value, and many Americans did also.

But we now know that those assurances were false. The decision to give Halliburton the sole-source Iraq oil work was made by a political appointee, not career procurement officials. And the Vice President's chief of staff received an extensive briefing.

These revelations fundamentally change our oversight responsibilities.

A shrewd politician once said, "fool me once, shame on you; fool me twice, shame on me." We've been fooled once by the White House about the role of the Vice President and political appointees in Halliburton's contracts. Now we need to investigate to learn the full story.

Today, we will take another step forward – and a big one – in our oversight of contracting in Iraq. I commend the Chairman for holding this hearing and look forward to working with him as our investigative efforts continue. I also ask that the reports Mr. Dingell and I released yesterday be made part of the hearing record.

SUBPOENA

BY AUTHORITY OF THE HOUSE OF REPRESENTATIVES OF THE CONGRESS OF THE UNITED STATES OF AMERICA

To The Honorable Donald H. Rumsfeld, Secretary of Defense

You are hereby commanded to be and appear before the Committee on Government Reform

of the House of Representatives of the United States at the place, date and time specified below.

☐ **to testify** touching matters of inquiry committed to said committee or subcommittee; and you are not to depart without leave of said committee or subcommittee.

Place of testimony: _____

Date: _____ Time: _____

☑ **to produce the things identified on the attached schedule** touching matters of inquiry committed to said committee or subcommittee; and you are not to depart without leave of said committee or subcommittee.

Place of production: 2154 Rayburn House Office Building, Washington, DC

Date: September 8, 2004 Time: 10:00 a.m.

To U.S. Marshals Service

_____ to serve and make return.

Witness my hand and the seal of the House of Representatives of the United States, at the city of Washington, this _____ day of _____, 20___.

_____
Chairman or Authorized Member

Attest:

_____
Clerk

PROOF OF SERVICE

Subpoena for The Honorable Donald H. Rumsfeld, Secretary of Defense

Address U.S. Department of Defense, 1000 Defense Pentagon, Washington, DC 20301

before the Committee on Government Reform

U.S. House of Representatives
108th Congress

Served by (print name) _____

Title _____

Manner of service _____

Date _____

Signature of Server _____

Address _____

SCHEDULE

Subpoena Duces Tecum
Committee on Government Reform and Oversight
United States House of Representatives
2157 Rayburn House Office Building
Washington, DC 20515

Serve: The Honorable Donald H. Rumsfeld
Secretary of Defense
U.S. Department of Defense
1000 Defense Pentagon
Washington, DC 20301

The Committee hereby subpoenas Secretary of Defense Donald H. Rumsfeld to produce certain records relating to contracting and the rebuilding of Iraq. If you have any questions, please contact chief counsel J. Keith Ausbrook at (202) 225-5074 or chief minority counsel Philip S. Barnett at (202) 225-5051.

Instructions

1. In complying with this subpoena, you are required to produce all responsive documents that are in your possession, custody, or control, whether held by you or your past or present agents, employees, and representatives acting on your behalf. You are also required to produce documents that you have a legal right to obtain, that you have a right to copy or to which you have access, as well as documents that you have placed in the temporary possession, custody, or control of any third party. No records, documents, data or information called for by this request shall be destroyed, modified, removed, transferred or otherwise made inaccessible to the Committee.

2. In the event that any entity, organization or individual denoted in this subpoena has been, or is also known by any other name than that herein denoted, the subpoena shall be read also to include them under that alternative identification.

3. Each document produced shall be produced in a form that renders the document capable of being copied.

4. Documents produced in response to this subpoena shall be produced together with copies of file labels, dividers or identifying markers with which they were associated when this subpoena was served. Also identify to which paragraph from the subpoena such documents are responsive.

5. It shall not be a basis for refusal to produce documents that any other person or entity also possesses non-identical or identical copies of the same document.

6. If any of the subpoenaed information is available in machine-readable form (such as punch cards, paper or magnetic tapes, drums, disks, or core storage), state the form in which it is available and provide sufficient detail to allow the information to be copied to a readable format. If the information requested is stored in a computer, indicate whether you have an existing program that will print the records in a readable form.

7. If compliance with the subpoena cannot be made in full, compliance shall be made to the extent possible and shall include an explanation of why full compliance is not possible.

8. In the event that a document is withheld on the basis of privilege, provide the following information concerning any such document: (a) the privilege asserted; (b) the type of document; (c) the general subject matter; (d) the date, author and addressee; and (e) the relationship of the author and addressee to each other.

9. If any document responsive to this subpoena was, but no longer is, in your possession, custody, or control, identify the document (stating its date, author, subject and recipients) and explain the circumstances by which the document ceased to be in your possession, custody, or control.

10. If a date or other descriptive detail set forth in this subpoena referring to a document is inaccurate, but the actual date or other descriptive detail is known to you or is otherwise apparent from the context of the request, you should produce all documents which would be responsive as if the date or other descriptive detail were correct.

11. This request is continuing in nature and applies to any newly-discovered information. Any record, document, compilation of data or information, not produced because it has not been located or discovered by the return date, shall be produced immediately upon location or discovery subsequent thereto.

12. All documents shall be bates-stamped sequentially and produced sequentially.

13. Two sets of documents shall be delivered, one set to the majority staff and one set to the minority staff. When documents are produced to the Committee, production sets shall be delivered to the majority staff in Room 2157, Rayburn House Office Building and the minority staff in Room B350A, Rayburn House Office Building.

Definitions

1. The term "document" means any written, recorded, or graphic matter of any nature whatsoever, regardless of how recorded, and whether original or copy, including, but not limited to, the following: memoranda, reports, expense reports, books, manuals, instructions, financial reports, working papers, records notes,

letters, notices, confirmations, telegrams, receipts, appraisals, pamphlets, magazines, newspapers, prospectuses, interoffice and intra office communications, electronic mail (e-mail), contracts, cables, notations of any type of conversation, telephone call, meeting or other communication, bulletins, printed matter, computer printouts, teletypes, invoices, transcripts, diaries, analyses, returns, summaries, minutes, bills, accounts, estimates, projections, comparisons, messages, correspondence, press releases, circulars, financial statements, reviews, opinions, offers, studies and investigations, questionnaires and surveys, and work sheets (and all drafts, preliminary versions, alterations, modifications, revisions, changes, and amendments of any of the foregoing, as well as any attachments or appendices thereto), and graphic or oral records or representations of any kind (including without limitation, photographs, charts, graphs, microfiche, microfilm, videotape, recordings and motion pictures), and electronic, mechanical, and electric records or representations of any kind (including, without limitation, tapes, cassettes, disks, and recordings) and other written, printed, typed, or other graphic or recorded matter of any kind or nature, however produced or reproduced, and whether preserved in writing, film, tape, disk, videotape or otherwise. A document bearing any notation not a part of the original text is to be considered a separate document. A draft or non-identical copy is a separate document within the meaning of this term.

2. The term "communication" means each manner or means of disclosure or exchange of information, regardless of means utilized, whether oral, electronic, by document or otherwise, and whether face-to-face, in a meeting, by telephone, mail, telexes, discussions, releases, personal delivery, or otherwise.

3. The terms "and" and "or" shall be construed broadly and either conjunctively or disjunctively to bring within the scope of this subpoena any information which might otherwise be construed to be outside its scope. The singular includes plural number, and vice versa. The masculine includes the feminine and neuter genders.

4. The terms "person" or "persons" means natural persons, firms, partnerships, associations, corporations, subsidiaries, divisions, departments, joint ventures, proprietorships, syndicates, or other legal, business or government entities, and all subsidiaries, affiliates, divisions, departments, branches, and other units thereof.

5. The term "identify," when used in a question about individuals, means provide the following information: (a) the individual's complete name and title; and (b) the individual's business address and phone number.

6. The terms "referring or relating," with respect to any given subject, means anything that constitutes, contains, embodies, reflects, identifies, states, refers to, deals with or is in any manner whatsoever pertinent to that subject.

Subpoenaed Items

Please provide the Committee with the following:

1. All documents relating to communications between the Department of Defense (DOD) and Vice President Cheney or persons within the Vice President's office, or between DOD and any other person within the White House, relating to the existing or potential Halliburton contracts for work in Iraq.

Chairman TOM DAVIS. If we want to try to set a time certain, Mr. Waxman, here at the conclusion of the third hearing?

Mr. WAXMAN. I will leave it to the discretion of the Chair to determine a time certain, so long as it is fairly noticed to all Members on each side of the aisle.

Chairman TOM DAVIS. Let me say 2 p.m. We should be through with the third panel, and we will have Members here for a vote at 2 p.m. on Mr. Waxman's motion.

Mr. Waxman, you may address it, and then I'll address it, and we can then move on to our witnesses.

Mr. WAXMAN. Mr. Chairman, I want to play a video excerpt from a hearing we had in March. On this tape you will hear Chairman Davis ask each witness whether there were any contacts with any person in the Vice President's Office before any Halliburton contract was issued.

Could we have that videotape?

[Videotape shown.]

Mr. WAXMAN. The facts, however, depict a very different set of circumstances. We now know that the Vice President's Office had contacts with the Defense Department in October 2002, prior to the award of the contingency planning task order, and in March 2003, prior to the award of the sole- source contract.

Vice President Cheney's chief of staff, Scooter Libby, was briefed about the proposal to issue the November 11 task order to Halliburton and was given the opportunity to object. According to a Pentagon e-mail and the author of that e-mail, the Defense Department also coordinated with the Vice President's office in March 2003 before the award of the sole-source contract to Halliburton.

So while the administration said for months that there were no contacts between the Pentagon and the Vice President's Office, we now know that there were contacts on at least two occasions. We also know that a political appointee, Michael Mobbs, not career civil servants, made the decision to award the task order to Halliburton, knowing that the company that did the planning would receive a sole-source contract to implement the plan.

Mr. MCHUGH. Would the distinguished ranking member yield?

Mr. WAXMAN. No, I won't at this point.

Chairman TOM DAVIS. Let him finish his statement first.

Mr. WAXMAN. The claims of the administration that the Vice President's Office knew nothing about Halliburton's contracts have been contradicted by the facts. That is why it is essential for the administration to disclose all contacts between the Vice President's Office and the Defense Department relating to these contracts.

Mr. Chairman, at the last Iraq contracting hearing, I moved to subpoena these documents. After you agreed to consider a joint request, I withdrew that motion. You have since notified me that you will not join me in a joint request. Given the importance of these documents, I am left with no choice but to renew my motion to subpoena them.

Mr. Chairman, I am not claiming the Vice President exerted inappropriate influence over the award of these contracts. We don't have enough information at this point to answer that question. The point is that the administration has repeatedly asserted that there were no contacts at all between DOD and the Vice President's Of-

fice regarding Halliburton contracts. The Vice President himself said this. We now have clear statements that this is not true. We have the right to know, and I think the duty to know, the extent of those contacts.

Chairman TOM DAVIS. Thank you. Mr. Waxman, let me just add that where we agreed to issue subpoenas did not include the Vice President. Those were on previous issues we had talked about. I just said I would look at this and work with you.

But, look, over the past year, I have tried to establish a reasonable strike zone on this issue. This is our fourth hearing. We have jointly requested and received thousands of pages of documents and participated in dozens of joint briefings. But the minority, led by the ranking member and his staff, keep trying to stretch the strike zone and make it wider and wider and wider, and there comes a time where we have to say we are not going to let it go any further. And this is an attempt, in my opinion, to embarrass the Vice President in an election season.

The Washington Post article by Dana Milbank said, "There is seemingly no charge the Bush campaign can level against John F. Kerry that will not produce a one-word retort: Halliburton. Kerry's proposed tax increases? Halliburton. Kerry's vote against Iraq war spending? Halliburton. Kerry's anti-terrorism credentials? Halliburton. Kerry's ties to Hollywood liberals? Halliburton, Halliburton, Halliburton. Halliburton, said Kerry's spokesman, Chad Clanton, will always be the fire Dick Cheney can't put out. That is certainly the Democrats' hope as they try to portray the oil services company once run by Vice President Cheney as a metaphor for all things anti-Bush. When Cheney spoke about health care in Toledo, Kerry forces held a counter rally saying 'health care, not Halliburton.'" And it goes on and on and on.

We have already received the most important and relevant information on this question at two hearings and a joint briefing that no influence was exerted by the Vice President's Office on a decision to award the RIO contract and task order, and that the decision was made by career acquisition personnel. The Vice President's Office may have been notified the contract was coming, as our congressional offices are when there is a contract awarded in our districts. These assurances that there was no improper communication were given under oath. If I were to agree with this motion, I am fearful the minority's witch-hunt would continue.

When Mr. Mobbs spoke to staff, not under oath by the way, the minority heard what it wanted to hear. I don't see his statement that White House staff in a pro forma fashion received notice of an imminent award as amounting to a hill of beans. The question is one of efforts to exert influence, and there is no evidence that there was any effort to exert influence.

So I understand you have the right to ask for a subpoena. We all understand the election season is upon us, and I think we will schedule a vote for 2 p.m., if that is convenient with Members here, so Members can be here and can vote appropriately on it. And we will postpone the vote until that time.

Thank you. Mr. Waxman.

Mr. WAXMAN. Mr. Chairman, if I might just respond briefly.

Chairman TOM DAVIS. Sure, please.

Mr. WAXMAN. Briefly. I just want to point out the reason I showed the tape is that the first time in any of the hearings that the question of the Vice President came up is when you asked each of the witnesses, under oath, whether they knew of or had any contact, or their office had any contact with the Vice President, each witness answered your question under oath in the negative. Now we have information to the contrary, from an interview we had with a political appointee at the Department of Defense that shows a contradiction of the facts.

I have not heard you deny any of the facts that we have put forward. You have only suggested that it is political. Well, I think asking these questions is our responsibility. It is our responsibility to get to the truth, even if it might be embarrassing. And I don't know if it will be. But it is our responsibility to get to the truth, to do the oversight that is necessary, and that is why I think the subpoena ought to be issued, since we are not jointly requesting it nor are they volunteering to give us the information to clarify the record.

Chairman TOM DAVIS. I just don't see any ambiguity here. The Vice President's Office may have been notified that a contract was forthcoming, which routinely happens to executive branch personnel and certainly to Members of Congress, but in no way is there any indication that there was any influence. And I take the people who testify here under oath, who are career Federal employees, at their word. So I am going to oppose the subpoena, but the committee will have an opportunity to vote on that today at 2 p.m.

And thank you, Mr. Waxman.

We are now ready to move to our first panel. We have four scheduled witnesses, I see three are hear, so if you would rise with me. Mr. James Warren is a former truck driver for KBR; Mr. David Wilson, who is a former truck driver for KBR; and Ms. Marie deYoung, who is a former logistics specialist at KBR.

Mr. BURTON. Mr. Chairman, may I make an inquiry please?

Chairman TOM DAVIS. Yes.

Mr. BURTON. Mr. West is not here, and I had questions for him. Is he going to be here, do you know?

Chairman TOM DAVIS. Let me ask the minority. He is a minority witness. Is Mr. West——

Mr. WAXMAN. Mr. Chairman, we don't know why he's not here. Maybe he'll still——

Chairman TOM DAVIS. We don't know. If he comes in, we will swear him at the appropriate point.

I would say for Mr. Waxman, that to come before a committee and face questioning under oath, we appreciate your willingness to do that.

[Witnesses sworn.]

Chairman TOM DAVIS. We have a light down here in front of you that will be green. Generally, we allow 5 minutes for witnesses. If you have a written statement, the entire statement will go in the record and the questions will be based on that. But when the light turns orange, that means 4 minutes are up. When it turns red, 5 minutes.

We would appreciate your summarizing, but this is important testimony, and if you feel you need to go over it I won't gavel you, but it just moves things along.

Mr. Waxman and I have also agreed we would have a half-hour of questioning on each side to be controlled by myself and the ranking member that we will be able to yield out, so that we can get a continuity of questions instead of going back and forth. Is that correct, Mr. Waxman?

Mr. WAXMAN. Yes.

Chairman TOM DAVIS. Mr. Warren, we'll start with you. Thank you for being with us.

STATEMENTS OF JAMES WARREN, FORMER TRUCK DRIVER, KBR; DAVID WILSON, FORMER TRUCK DRIVER, KBR; AND MARIE DEYOUNG, FORMER LOGISTICS SPECIALIST, KBR

Mr. WARREN. You're welcome. My name is James Warren. Thank you for the opportunity to speak with you about my work as a truck driver in support of our troops in Iraq. I have given a signed statement to the committee staff. I would like to read a summary of that statement, and will then answer any questions you may have.

I worked as a truck driver for Kellogg Brown and Root in Iraq from October 2003 to the end of March 2004. Before coming to Iraq, I worked as a truck driver for 13 years. For 11 years I worked for private trucking companies, including Builders Transport, Cal-Ark International, and Truck Service Inc.

Mr. WAXMAN. Mr. Warren, would you pull the mic a little closer to you? Some of the Members are having a hard time hearing. Thanks.

Mr. WARREN. For 2 years I worked as an independent truck driver. During my time in Iraq, KBR didn't seem to care about what happened to its trucks. KBR bought its trucks new, usually Mercedes or Volvos, with virtually no mileage on the odometers.

KBR removed the spare tires from the trucks on my convoys. I don't know why they did this, but one convoy, one of the trucks got a flat tire. Since we didn't have any spares, we had to leave the truck on the side of the road. As someone who has been in trucking for 13 years, I do not understand how a company could ditch a brand-new truck because they didn't have a spare tire. No trucker I know would have been that careless with his own truck.

For the first 4 months I was in Iraq, it was common to torch trucks that we abandoned. The Army torched the trucks, even though we all carried chains and could have towed them to be repaired.

Basic maintenance was nonexistent. The only maintenance I saw done was changing tires and some electrical work. The biggest problem was that KBR provided no air filters, fuel filters, or oil changes for these trucks. Especially in Iraq, these trucks should have been getting replacement filters and oil changes on a regular basis.

By the time I left Iraq, about 6 months later, the truck assigned to me had 59,000 miles on it and never got a single oil change. The joke from one of the two or three mechanics we saw working out

of the Conex container, was "We may not have any filters, but Iraq has plenty of oil."

On a lot of the convoys there were empty trucks. Normally, convoys had 28 flatbed trucks. There were plenty of times we would run with seven, eight, or even a dozen empty trucks. Sometimes we had to carry equipment and supplies out of Camp Anaconda. We called this retro. We would also have empty trucks both coming and going, which didn't make any sense. One time there were 27 empty trucks in one convoy. It just didn't seem like there was good planning about where things were going and when. This was a major waste of time and money, and it put us and our military escorts in danger for absolutely no reason. Thank you.

Chairman TOM DAVIS. Thank you very much.

[The prepared statement of Mr. Warren follows:]

Statement of James Warren
Former KBR Convoy Truck Driver in Iraq

I worked as a truck driver for Kellogg Brown & Root ("KBR") in Iraq from October 2003 to the end of March, 2004. I started at orientation in Houston from September 2-28, 2003, where KBR put everybody up at various hotel. I stayed at the Hyatt Regency. We were served catered food from waiters wearing tuxedos. I then flew to Kuwait, where I was assigned to Camp Cedar II in southern Iraq. I drove supply trucks between Camp Cedar II and Camp Anaconda in Balad, north of Baghdad. I also worked at the TDC Yard near Kuwait City supervising third country nationals and helping them load and unload trucks. Before coming to Iraq, I worked as a truck driver for 13 years. For 11 years, I worked for private trucking companies, including Builders Transport, Cal-Ark International, and Truck Service Corp. For two years, I worked as an independent truck driver.

During my time in Iraq KBR didn't seem to care about what happened to its trucks. KBR bought its trucks new, usually Mercedes or Volvo, with virtually no mileage on the odometers. KBR removed the spare tires from the trucks on my convoys. I don't know why they did this. But on one convoy, one of the trucks got a flat tire. Since we didn't have any spares, we had to leave the truck on the side of the road. As someone who has been in trucking for 13 years, I do not understand how a company could ditch a brand new truck because they didn't have a spare tire. No trucker I know would have been that careless with his own truck.

For the first four months I was in Iraq, it was common to torch trucks that were abandoned. I personally saw the Army put burn grenades into the gas tanks and the transmission of a truck to basically destroy it so the Iraqis couldn't have it. Army torched the trucks even though we all carried chains and could have towed them to be repaired.

Basic maintenance was non-existent. The only maintenance that I saw done was changing tires and some electrical work. The biggest problem was that KBR provided no air filters, fuel filters, or oil changes for these trucks. Especially in Iraq, these trucks should have been getting replacement filters and oil changes on a regular basis. By the time I left Iraq about six months later, the truck assigned to me had 59,000 miles on it and never got a single oil change. The joke from one of the two or three mechanics we saw working out of a Conex container was, "We may not have any filters, but Iraq has plenty of oil."

While I was driving for these KBR convoys, people would steal things off the trucks on a daily basis. It was quite obvious. I heard the phrase, "let's go shopping." I personally witnessed thefts. Sometimes I would wake up inside the truck as it was rocking back and forth from people on top of the truck loosening boxes and taking things.

Security was part of it. The theft was rampant. Most of the stealing was done between 9 pm and midnight, when the trucks were at Camp Anaconda. I reported this to my convoy commander, Don Martin, who told me, "Don't worry about it, it's the Army stealing from the Army."

In March, I called Randy Harl personally, who I believe was the president of Halliburton. I had his home phone, his cell phone, and his work phone. I called him up and told him about the theft going on at night at Camp Anaconda. He promised he would get to the bottom of it, and thanked me.

I never saw any evidence that KBR tried to stop the theft after my call to Mr. Harl. No KBR officials ever asked me about the theft after the call.

A problem was that KBR wasn't using enough containers on the trucks. Instead, they would just strap down the supplies on flatbeds. They couldn't secure all the supplies that way. People could just loosen the straps and take things away. Also, supplies would just fall off the trucks. An Army escort traveling with our convoy told me he recovered some valuable helicopter radios that fell off some of our trucks. Containers are also easier to load and unload. I know from when I worked at the TDC Yard that there were a lot of containers just sitting empty in Kuwait. Even if KBR used up all of those containers, they should have gotten more – it would have saved money in the long run since they are more efficient and they prevent loss and theft.

Another problem was that we didn't have manifests for our cargo. I was never required to certify that the supplies I started with were the supplies I ended with. I have no idea how KBR accounted for all the equipment that was stolen and lost.

On a lot of the convoys, there were empty trucks. Normally, convoys had 28 flatbed trucks. There were plenty of times we would run with seven, eight, even a dozen empty trucks. Sometimes we had to carry equipment and supplies out of Camp Anaconda – we called this "retro." We would also have empty trucks both coming and going, which didn't make any sense. One time, there were 27 empty trucks in one convoy. It just didn't seem like there was good planning about where things were going and when. This was a major waste of time and money, and it put us and our military escorts in danger for absolutely no reason.

About three weeks after I spoke with Mr. Harl, I was called in to the headquarters at Camp Cedar II. They also called in my foreman, who sat next to me during an interview. They said that I knew who was ordering truck drivers to force Iraqi cars off the road. In fact, it was the convoy commanders, their superiors, and the military who told us to maintain the integrity of the convoys <u>at all costs</u>. My foreman, his superiors, and the military escorts had all told us, "If they don't move out of the way, just get them off the road." During this interview, I would not provide the names of the people who gave us these orders, especially when one of them was sitting right next to me. About five days later, as a result of this interview, KBR transferred me to Kuwait. After about another two weeks, KBR terminated my employment, and I was sent back to the United States.

James Warren
James Warren

6/13/04
Date

Chairman TOM DAVIS. Mr. Wilson.

Mr. WILSON. My name is David Wilson. I appreciate the invitation to this committee to speak about my experience working as a truck driver in support of our Armed Forces in Iraq. Last month, I gave a signed statement about this experience to the committee's staff. Today, I will give a summary of that statement and answer any questions that you may have.

I was an alternate convoy commander and a convoy commander for Kellogg Brown and Root [KBR], in Iraq from November 2003 until March 2004. I arrived in Kuwait at the end of October and went to work in Iraq the first week of November as part of KBR's sustainer mission, delivering supplies within Iraq under its LOGCAP contract with the military.

I ran over 100 missions during my employment with KBR. While I was in Iraq, I saw problems with KBR's mission. In my opinion, the company did not adequately plan how they were going to do this job. I arrived in Iraq 6 months after the war and they still did not have the right personnel and equipment in place.

KBR ran two convoys each day, each in a different direction. The convoys usually had 28 trucks with trailers and two bobtails. These trucks were used for recovery, and they went from Camp Cedar II in southern Iraq to Camp Anaconda, 300 miles to the north above Baghdad. We also stopped at Camp Scania, which is a mid-point station between Cedar II and Anaconda. The problem with having only two crews was that if one had problems, there would be nobody there to pick up the sustainer the next day.

When I arrived at Camp Arafjan—we called it Truckville—in Kuwait last November, I noticed there were about 50 to 100 brand-new trucks sitting there unused. I was told that KBR brought these trucks into Kuwait to use in the convoys. Five months later, when I came home, a large number of trucks were still there, not being used. These are $85,000 or more Mercedes and Volvo trucks that are marked KBR-owned assets. I have been told that KBR could not get the right tags to license the vehicles to do business in Kuwait. I don't know if KBR billed the U.S. Government for these trucks, but they were not used for a third or fourth crew on the Cedar to Anaconda sustainer convoys.

As every other trucker working on these convoys will tell you, KBR had virtually no facilities in place to do maintenance on the trucks. It was like their whole preparation was to buy the trucks, hire the drivers, and let the rest take care of itself. There were absolutely no oil filters or fuel filters for months on end. I begged for filters but never got any. I was told that oil changes were out of the question. The lack of maintenance was a major problem for trucks doing daily runs on Iraqi highways.

In addition to being the convoy commander, I also drove a truck. During one convoy, my truck shut down because my fuel filter was completely clogged. Luckily, we were at the mid-point station at Camp Scania, and I got an Army bobtail to pull me inside the barriers. At that point, I borrowed a fuel filter wrench from a local Iraqi and I removed the fuel filter myself. I ran gasoline through it to clear it out, and then I found some ether to clear it out further. I learned this from my years in trucking. At any rate, I was able to replace the filter and at least get the truck going again. But

when I got back to Camp Cedar and requested a new fuel filter, they refused. They said "Your truck's running now, isn't it?"

I am 100 percent certain that if we had been out on the open Iraq highway instead of near Camp Scania, we would have lost that truck, and all because of an $8 fuel filter. I have no idea how KBR or the military were planning these convoys, or how they dealt with all the lost equipment and supplies. Basically, all they were looking for was the number of trucks with freight on them.

A related problem was that KBR would run trucks empty quite often. Sometimes they would have five empty trucks, sometimes a dozen. One time we ran 28 trucks and only one had anything on it. Nobody knew why we were hauling empty trucks around, but it definitely caused extra wear and tear, which just made maintenance a bigger problem.

Personally, I came under fire myself, including mortar fire, IEDs, and shrapnel bouncing off my truck, so I know from firsthand experience the dangers. Our convoys had rocks thrown through the windshields, we had Iraqis attack us on the roads, and in some cases our drivers were seriously injured. Mike Stroud, one of my drivers, got hit with IEDs a couple of times and managed to drive through it. That wasn't always the case, however. I lost a good friend of mine, Al Kaden, who got killed driving an SUV for KBR.

In March, my job was terminated. The documents terminating me stated that this was because of a breach of the business code of conduct, when supposedly I failed to report vehicles in my convoy that ran Iraqis off the road.

The problem with that was that both KBR and the military made clear to everyone that was in the convoys that this was what we were supposed to do. They would say, we can't tell you to do this, but just remember that if you get captured, you will be raped, beaten, raped again, and beaten again. So if you need to put vehicles off the road, that's what you need to do. Although I never witnessed it, I know trucks ran Iraqis off the road.

Finally, although I was a convoy commander, KBR did not pay me a convoy commander's salary, but a regular truck driver's salary. I don't have any way of knowing whether KBR billed my time to the U.S. Government as a truck driver or a convoy commander.

This information basically repeats the information I provided to the Government Reform Committee on June 2, 2004, when I was willing to testify, if required. Thank you.

Chairman TOM DAVIS. Thank you very much.

[The prepared statement of Mr. Wilson follows:]

Statement of David Wilson
Former KBR Convoy Commander in Iraq

I was an alternate convoy commander and a convoy commander for Kellogg Brown & Root ("KBR") in Iraq from November 2003 until March 2004. I arrived in Kuwait at the end of October and went to work in Iraq in the first week of November as part of KBR's sustainer mission, delivering supplies within Iraq under its LOGCAP contract with the military. I ran over 100 missions during my employment with KBR.

While I was in Iraq, I saw problems with KBR's mission. In my opinion, the company did not adequately plan how they were going to do this job. I arrived in Iraq six months after the war and they still did not have the right personnel and equipment in place.

KBR ran two convoys each day, each in a different direction. The convoys usually had 28 trucks with trailers, and 2 bobtails (trucks for recovery), and they went from Camp Cedar II in southern Iraq to Camp Anaconda 300 miles to the north, above Baghdad. We also stopped at Camp Scania, which is a mid-point station between Cedar II and Anaconda. The problem with having only two crews was that if one had problems, there would be nobody there the next day to take its place.

When I arrived at Camp Arafjan ("Truckville") in Kuwait, last November, I noticed that there were about 50-100 brand new trucks sitting there, unused. I was told that KBR brought these trucks into Kuwait to use in the convoys. Five months later, when I came home, a large number of trucks were still there, not being used. These are $85,000 (or more) Mercedes and Volvo trucks that are marked "KBR-owned assets." I've been told that KBR could not get the right tags to license the vehicles to do business in Kuwait. I don't know if KBR billed the U.S. government for these trucks, but they were not used for a third or fourth crew on the Cedar-Anaconda convoys.

As every other trucker working on these convoys will tell you, KBR had virtually no facilities in place to do maintenance on the trucks. It was like their whole preparation was to buy the trucks, hire the drivers, and let the rest take care of itself. There were absolutely no oil filters or fuel filters for months on end. I begged for filters, but never got any. I was told that oil changes were "out of the question."

The lack of maintenance was a major problem for trucks doing daily runs on Iraqi highways. In addition to being the convoy commander, I also drove a truck. During one convoy, my truck shut down because my fuel filter was completely clogged. Luckily, we were at the mid-point station at Camp Scania, and I got the Army to use a bobtail truck to pull me inside the barriers. At that point, I borrowed a fuel filter wrench from a local Iraqi, I removed the fuel filter myself, I ran gasoline through it to clear it out, and I then found some ether to clear it out further. (After years in the trucking business, I had a few tricks up my sleeve.) At any rate, I was able to replace the filter and at least get the truck going again. But when I got back to Camp Cedar and requested a new fuel filter, they refused. They said, "Your truck's running now, isn't it?" I am 100% certain that if we had been out on the open Iraqi highway instead of near Camp Scania, we would have lost that truck – and all because of a fuel filter.

Sometimes we were not so lucky. For some reason that was never explained to us, KBR removed all the spare tires in Kuwait. So when one of our trucks got a flat tire on the highway, we had to leave it there for the Iraqis to loot, which is just crazy. I remember saying to myself when it happened, "You just lost yourself an $85,000 truck because of a spare tire."

We lost other trucks too. We lost a truck because we didn't have a $25 hydraulic line to assist the clutch. Some of the trucks we lost due to accidents, but even these we could have saved if we had some way to tow them. In my time on the road, I saw disabled trucks -- or what was left of them -- abandoned on the side of the road on a daily basis.

Theft from the trucks was also a major problem. KBR had us carry the majority of supplies on open pallets instead of inside containers. Although the flatbeds we drove were designed to carry Conex containers, which are actually easier to load and unload, we didn't use them enough. Just about every person working on the convoys preferred, and specifically recommended, that KBR use more containers, but they did not. So when we traveled through small Iraqi towns at 4 or 5 miles per hour, the local Iraqis would just grab things off the truck.

The Army and KBR employees took things off the trucks going south, although they did not take anything of the truck going north. While the trucks were secured in Anaconda, both KBR and Army personnel would come at all hours of the night and rock the truck while they raided the supplies. It was like rats swarming on cheese.

KBR did not have good coordination about where the cargo was going or when. Sometimes, we would bring supplies into Iraq for a military unit, but the unit was already gone. We would take all these supplies back to Cedar II, and another convoy would take them back to Kuwait, even if there was another unit near Anaconda that might need the same things. If units at Cedar II or Anaconda learned that we were bringing supplies back from Anaconda, they would take what they could get.

I have no idea how KBR or the military were planning these convoys, or how they dealt with all the lost equipment and supplies. As far as accountability, the paperwork I carried had no details about the contents of our cargo. The operation wasn't like in the United States where you have "SLC," or shipper load and count. Basically, all they were looking for was the number of trucks with freight on them.

A related problem was that KBR would run trucks empty quite often. Sometimes they would have five empty trucks, sometimes they would have a dozen. One time, we ran 28 trucks and only one had anything on it. Nobody knew why we were hauling around empty trucks, but it definitely caused extra wear and tear, which just made maintenance a bigger problem. It also didn't make sense for security. We only had three military gun trucks escorting the whole convoy of 28 trucks, which was two miles long. There were several times when we had empty trucks both on the way to Anaconda and then on the way back to Cedar II. I don't understand why KBR would have placed our lives in danger that way for no reason.

Personally, I came under fire myself, including as mortar fire, improvised explosive devices ("IEDs"), and shrapnel bouncing off my truck, so I know from first-hand experience the dangers. Our convoys had rocks thrown through the windshields, and we had Iraqis attack us on the roads. In some cases, our drivers were seriously injured. Mike Stroud, one of the drivers, got hit with IEDs a couple times and managed to drive on through it. That wasn't always the case, however. I lost a good friend of mine, Al Kaden, who got killed driving an SUV for KBR.

In March, my job was terminated. The documents terminating me stated that this was because of a "breach of the code of business conduct" when supposedly I failed to report vehicles in my convoy that ran Iraqis off the road. A problem was that both KBR and the military made clear to everyone that this was what we were supposed to do. They would say, "We can't tell you to do this, but just remember that if you get captured, you will be raped, beaten, raped again, and beaten again. So if you need to put vehicles off the road, that's what you need to do." Although I never witnessed it, I know trucks ran Iraqi's off the road because I once heard over the radio someone say, "I had to ease that one to the side of the road." I have documented my response to my termination, which you may read.

Finally, although I was a convoy commander, KBR did not pay me a convoy commander salary, but a regular truck driver salary. I don't have any way of knowing whether KBR billed my time to the U.S. government as a convoy commander.

This information basically repeats the information I provided to the Government Reform Committee on June 2, 2004, when I was willing to testify if required.

David Wilson

6/15/2004
Date

Chairman TOM DAVIS. Ms. deYoung, thanks for being with us.

Ms. DEYOUNG. My name is Marie deYoung. Mr. Chairman and distinguished members of the committee, thank you for this opportunity to testify on issues related to the Halliburton LOGCAP subcontracts department in Kuwait. And, I emphasize, Kuwait not Iraq.

Since receiving my commission through Officer Candidate School in 1984, I served more than 10 years in the military as a chief of services, a commander, a chaplain, and, last, as an operations officer. I attained the rank of captain, and, yes, I published two books about women in the military. I am currently pursuing a doctorate in education leadership and public policy analysis.

During my time with Halliburton, I came to the conclusion that very poor subcontract management practices were evident in every phase of the company's work, from the negotiation and drafting of subcontracts to the oversight of subcontract work and implementation of inventory and property controls, as well as to the management of data, costs, and the proper closure of each subcontract.

As a matter of policy, the Kuwait Document Control Department made only a few subcontract documents available to operations management. That's in the first year. And then only shells, without specific delivery or performance schedules. Lack of subcontract documentation made it impossible for site supervisors to properly manage their subcontracts.

After receiving negative publicity about subcontracts, Halliburton established a Tiger Team to address these problems. When the Tiger Team examined a subcontract, they just checked to make sure all the forms were in the file. The Tiger Team looked at subcontracts with no invoices and no confirmation that the products contracted for were being used. Instead of investigating further, they often recommended extending the subcontract and, I will add, adding funds.

At one point, KBR Tiger Team members told us to bring 400 expired subcontracts up to date. The staff was instructed to cut change orders and requisitions to extend subcontracts without verifying if site managers and subcontract administrators had already updated the file or determining if equipment or services were still needed. We were instructed to pay invoices without verifying whether services were delivered.

I personally told a KBR Tiger Team member not to pay an invoice that I knew was a double billing because I helped set up another subcontract through which the services were properly delivered. The long-term KBR employee told me I didn't know what I was doing, and she proceeded to cut a change order and an invoice payment and authorization for the wrong account, under the prodding of the vendor who had not provided the services.

Halliburton rarely collected adequate information from subcontractors to justify payment of their invoices. When I attempted to properly verify invoice terms before setting up payment authorization, I was chastised. Management's intent was to pay the old accounts as quickly as possible and to close them, because only open accounts were being audited by the government.

Given these practices, it is not surprising that I observed significant waste and overpricing. Under a subcontract with La Nouvelle,

a Kuwaiti company, Halliburton was paying a fixed price of between $1 million and $1.2 million per month for laundry for a facility in Kuwait. Because there wasn't very much laundry to be done, Halliburton was paying La Nouvelle about $100 a bag for a 15-pound bag. At the same time, Halliburton was paying $28 per bag under a separate contract with the same company, and this laundry originated in Iraq, not in Kuwait.

In August 2003, Halliburton entered into another subcontract with La Nouvelle to provide cans of soda with ice for a hospitality bar at the same facility in Kuwait. La Nouvelle charged for 37,200 cases of soda per month, at a cost of about $1.50 per case. However, La Nouvelle delivered only 37,200 cans, and the sodas were just dropped off, without ice or a hospitality bar.

Only after I insisted that there was a problem did the Tiger Team confirm this overpayment. Meanwhile, Halliburton procurement and Tiger Team staff live at the five star Kempinski Hotel while the troops in Kuwait live in tents. It costs about $110 to House one KBR employee per day at the Kempinski while it costs the Army $1.39 per day to bunk a soldier in a leased tent. The military requested that Halliburton move into tents, but Halliburton refused.

During my 5 months working on subcontracts in Kuwait, I've tried to correct some of these practices, but the Halliburton corporate culture is one of intimidation and fear, and I would add, as I experienced this morning, a little bit of ridicule. When I approached my new interim subcontracts manager with concerns about overbilling and duplicate accounts for the same service, he fearfully said, I think you are trying to make this company look bad. When I began to make progress in getting La Nouvelle to revise its invoices downward to reflect actual costs for services provided, La Nouvelle complained to the vice president who headed the Tiger Team. She had me taken off the La Nouvelle accounts.

I brought my concerns to the Government Reform Committee because it is critical that our troops, and I will add our truck drivers and other personnel in Iraq who work for KBR—that they receive the services that they need and deserve. Every dollar that is squandered because of waste, fraud or abuse is a dollar that we do not have for critical equipment and supplies for our troops.

Mr. Chairman, I've prepared additional remarks, including more detailed knowledge and analysis of the Kuwait LOGCAP project. I request that you add this statement to the official record of these proceedings so your committee can in good faith consider this information in its ongoing review of contract operations in Kuwait and Iraq.

[The prepared statement of Ms. deYoung follows:]

Written Statement of Marie E.deYoung, Former KBR Employee
House Committee on Government Reform
22 July 2004

Mr. Chairman and distinguished members of the Committee, thank you for this opportunity to testify on issues related to the Halliburton LOGCAP Subcontracts Department in Kuwait.

Since receiving my commission through Officer Candidate School in 1984, I served more than ten years in the military, as a chief of services, a commander, a chaplain and lastly, as an operations officer. I attained the rank of captain and published two books about women in the military. I'm currently pursuing a doctorate in education leadership and public policy analysis.

During my time with Halliburton, I came to the conclusion that very poor subcontract management practices were evident in every phase of the company's work, from the negotiation and drafting of subcontracts to the oversight of subcontract work and implementation of inventory and property controls, as well as to the management of data, costs, and proper closure of each subcontract.

In December 2003, I began working for Halliburton through the LOGCAP contract in Kuwait. Based on my military service and my work for Halliburton in Kosovo, I was specifically asked to join the Kuwait project as a logistician and a writer for operations and briefings. I worked for night operations at Camp Udairi in Kuwait for two weeks.

On January 2, I was reassigned to Camp Udairi logistics, specifically to tackle subcontracts for Camp Udairi. I was tasked by the manager to bring all expired subcontracts up to date and to address subcontracts issues that were making it difficult for staff to deliver timely services to the Army.

I soon discovered there was not a complete up-to-date list of all the subcontracts in the Subcontracts or Document Control departments. I also discovered that the Document Control Department had provided incorrect lists to all of the task order managers from an inaccurate data base. I later observed that the Document Control Database was never adequately updated until after government audits were over, under the assumption that a limited database would also limit the amount of auditable information that could be accessed by the government. A consequence of this approach was that operations management had bad information about the status of subcontracts most of the time, which in turn, contributed to cost overruns and poor management.

As a matter of policy, the Kuwait Document Control Department made only a few subcontract documents available to the Camp Udairi management – and then, only shells, without specific delivery or performance schedules. Lack of subcontract documentation made it impossible for site supervisors to properly manage their subcontracts. This practice continued until at least mid-February 2004.

At the request of KBR's Kuwait Project Manager, I was transferred from Camp Udairi to the Kuwait Subcontracts Department on February 29.

After receiving negative publicity about some of these issues, Halliburton established a "Tiger Team" to address subcontract issues. Not only did the "Tiger Team" fail to correct the problems, it continued questionable auditing and subcontract administration practices. When the Tiger Team examined a subcontract, they just checked to make sure all the forms were in the file. They didn't assess the reasonableness of prices or consult with site managers. The Tiger Team looked at subcontracts with no invoices and no confirmation that the products contracted for were being used. Instead of investigating further, they would recommend extending the subcontract. For three months, this Tiger Team occupied waterfront villas at the Hilton Hotel and shuffled papers, but did nothing to effectively clean up old subcontracts.

I worked in the subcontracts department until May 16, 2004. At one point, KBR Tiger Team members told us to bring 400 expired subcontracts up to date. The staff was instructed to cut change orders and requisitions to extend subcontracts, without verifying if site managers and subcontract administrators had already updated the file, or determining if equipment or services were still needed. We were instructed to pay invoices without verifying whether services were delivered. I personally told a KBR Tiger Team member not to pay an invoice that I knew was a double-billing because I helped set up another subcontract through which the services were properly delivered. The long term KBR employee told me I didn't know what I was doing, and she proceeded to cut a change order and an invoice payment authorization for the wrong account, under the prodding of the vendor who had not provided the services. Halliburton rarely collected adequate information from subcontractors to justify payment of invoices. When I attempted to properly verify invoice terms before setting up payment authorization, I was chastised. Management's intent was to pay the old accounts as quickly as possible to close them because only open accounts were being scrutinized in the government audit.

Given these practices, it's not surprising that I observed significant waste and overpricing. Under a subcontract with La Nouvelle, a Kuwaiti company, Halliburton was paying a fixed price of between $1 million and $1.2 million per month for laundry for a facility in Kuwait. Because there wasn't very much laundry to be done, Halliburton was paying La Nouvelle around $100 per 15-pound bag. This was a much higher price than under other subcontracts. For example, Halliburton was paying $28 per bag under a separate subcontract with the same company, and this laundry originated in Iraq, not Kuwait. However, Halliburton management didn't want to hear about this overpricing. There was no effort by subcontract administrators or the Tiger Team to renegotiate the subcontract or to analyze the price being paid. Logs showing how much laundry was actually being done were maintained from the beginning of this contract by site managers. The subcontract department did not request copies of the logs to determine price reasonableness until DCAA requested an analysis of costs in February or March of 2004. When I started to raise concerns about this contract, I was told that I was providing too much information to the DCAA auditors, and encouraged to discontinue my analysis and attempts to adjust invoices to a reasonable price.

In August 2003, Halliburton entered into another subcontract with La Nouvelle to provide cans of soda with ice for a hospitality bar at the same facility in Kuwait. La Nouvelle charged for 37,200 cases of soda per month at a cost of about $1.50 per case. However, La Nouvelle delivered only 37,200 cans, and the sodas were just dropped off, without ice or a hospitality bar.

Not only were we paying for cases when we received cans, we effectively paid five times the wholesale cost for cans of soda. Only after I insisted that there was a problem did the Tiger Team confirm this overpayment.

Meanwhile, Halliburton procurement and Tiger Team staff live at the 5-star Kempinski hotel while the troops in Kuwait live in tents. For a three-month period, the Kempinski hotel charged almost $1 million to house 100 Halliburton employees. By comparison, it costs less than $200,000 a year to lease tents that could house 400 soldiers. To put it differently, it costs $110 to house one KBR employee per day at the Kempinski, while it costs the Army $1.39 per day to bunk a soldier in a leased tent. The military requested that Halliburton move into tents, but Halliburton refused.

During my five months working on subcontracts in Kuwait, I tried to correct some of these practices. But the Halliburton corporate culture is one of intimidation and fear. When a new procurement manager, the thirteenth since the start of the Kuwait project, encouraged subcontract staff to speak up about the failed efforts of the Tiger Team, my co-workers cried out: 'the *last* subcontract manager tried to speak up, but *he* was fired. He was the *twelfth* subcontracts manager.' Ironically, other previous managers who tolerated bad practices were promoted to better paying jobs in Iraq or Houston or Jordan. Some had returned to preside over the Tiger Team efforts, but they were not even correcting bad files they created in the past year. When I approached my new interim subcontracts manager with concerns about over billing and duplicate accounts for the same service, he fearfully said, "I think you're trying to make this company look bad." When I began to make progress in getting La Nouvelle to revise its invoices downward, to reflect actual costs for services provided, La Nouvelle complained to the Halliburton Vice President who headed the Tiger Team. She had me taken off the La Nouvelle accounts. I had been advised by subcontract administrators who quit the company that employees get moved around when they get too close to the truth. I personally observed and experienced this as a routine company practice.

It became evident to me that Halliburton was not going to address systemic business deficiencies, such as badly negotiated subcontracts and inflated and overpriced management and consultant teams that did not provide legitimate operations management or oversight of subcontract operations. This lack of systemic oversight resulted in grossly inflated charges to the government. Consequently, I resigned my position in May. I brought my concerns to the Government Reform Committee because it is critical that our troops receive the services that they need and deserve. Every dollar that is squandered because of waste, fraud, or abuse is a dollar we do not have for critical equipment and supplies for our troops. There are structural problems with the way Halliburton does business that must be fixed so that we don't let down these soldiers, many of whom I know personally from my time in the military.

Supplementary Statement of Marie E.deYoung, Former KBR Employee
House Committee on Government Reform
22 July 2004

Mr. Chairman, and distinguished members of this committee:

Subsequent to my first meeting with committee staff members, I have analyzed data related to the Hallliburton LOGCAP III contract in Kuwait. I believe there are numerous systemic examples of waste, fraud and abuse that must be corrected in the Halliburton contract. I am submitting the following summary of my concerns because I believe the insights will help your committee to pursue systemic reforms to improve practices by contractors on the battlefield. Following are the patterns of waste, fraud and abuse that I observed in Halliburton's LOGCAP III contract in Kuwait:

Waste. The Halliburton LOGCAP III Kuwait contract is fraught with waste. Here are just a few examples that I observed while administering subcontracts at Camp Udairi and the Khalifa Resort, which was the headquarters for the Kuwait KBR project:

1) **Luxury Hotels.** While thousands of soldiers lived in tents, KBR headquarters employees lived in waterfront hotels and upscale townhouses. The Army asked us to move out of the hotels and into fest tents where soldiers lived. KBR employees refused to move out of the hotels. As of May 20, 2004, hotel leases topped $27 million. This figure represented housing expenses for a small fraction of Halliburton employees in LOGCAP, and did not include hotel expenses for the Coalition Provisional Authority, or those who lived in hotels in Iraq, Jordan, or Dubai. It did not include millions of dollars spent on man camp buildings for KBR employees in Kuwait or Iraq. Because we housed hundreds of employees at the Palms Club Hotel and the Hilton, these individuals collected $75 per day for food. If the Palms Club Hotel continues to house 400 employees, the annual per diem cost to the taxpayer will be an extra $11 million.

2) **Associated Luxuries**. As you can see in the attached figure (Table 1), KBR's decision to house employees in hotels rather than on Army camps resulted in extravagant costs associated with living on the economy, including special KBR laundries, dining facilities, cell phones, security, and non-tactical vehicles. In table 1, subcontracts that support lifestyle costs for KBR employees who lived in hotels are listed. In Table 2, totals for each category of subcontract are summarized. The combined total of costs associated with hotel living was roughly $73 million, based on contracts through 20 May 2004 (Figure 1). Procurement decisions to allocate high tech cell phones to headquarters staff, while KBR staff in the remote desert were required to use cell phones without antennae, forced desert employees to run outside to take calls, even in heavy sandstorms and rainstorms. Flat screen monitors, computers with DVD players were purchased for procurement and headquarters staff, but there was resistance to purchase of

management software such as MS Project or Visio for operations managers and logistics personnel.

3) **Luxury Vehicles**. The figures for vehicle leases and purchases do not include functional trucks, passenger vans, or buses that were purchased for mission purposes. All non-tactical vehicles should have been purchased for functional purposes, and assigned to employees based on job requirements. Instead, the SUVs and high end trucks were distributed to personnel as status symbols. When KBR management finally decided to purchase or rent passenger vans and buses for KBR commuters between waterfront chalets and our waterfront offices, SUV, Lumina and designer truck purchase orders were not cancelled. Instead, as the subcontract administrator who purchased vehicles mentioned each day that we were required to ride buses by project management, luxury vehicles that were assigned to KBR insiders were still driven to and from five star hotels every day.

4) **Excess Personnel.** Complaints of waste in personnel expenses were frequent and valid. Given upper management's decision to subcontract most construction, operations and services, the personnel structure for the Kuwait project should have been realigned. Labor foremen, vehicle maintenance, and logistics personnel whose operations were being performed by subcontractors should have been sent north to Iraq where personnel shortages were acute, or sent home if they did not have subcontract management skills. Conversely, once management made a decision to use the new subcontract paradigm, recruitment should have been targeted to skilled government subcontract administrators and managers, rather than small town cooks, mechanics, and general laborers.

Fraud. I observed the following systemic problems with Halliburton's purchasing and subcontracting systems that could explain some of the waste, fraud and abuse in this LOGCAP Contract:

1) **Inventory Management.** The Kuwait and Iraq Procurement Departments did not have a perpetual inventory system in warehouses and supply shops. KBR's inventory management in Kuwait was guided by the practice: "next ordered, if it ever comes in, next out." To order screws and ridge caps or to subcontract anything, one had to fill out a three-part requisition and drive for two hours across the desert and highways of Kuwait, deliver it to the headquarters for processing and wait for a month, two months, three months for the paper to work its way through a 1970's bureaucracy known as "the Black Hole." In January, the Army asked us to repair the roof of the Technical Control Facility at Camp Udairi, which had millions of dollars of electronic equipment. The job was delayed for more than a month because KBR did not have a perpetual inventory system with basic stock on hand for such emergency repairs. Each week, we had to report to the Army that we could not do this simple repair job because we were waiting on our requisition

for screws and a ridge cap. And so it went. Many of our subcontractors, by contrast, had automated enterprise systems, and they could provide immediate, flexible responses to the Army's needs.

2) **Manual Data Management.** Because Halliburton ran LOGCAP contracts for more than ten years, and because it was a leading multinational corporation, I expected a "cradle to grave" automated procurement system, so that we could be highly responsive to the Army's temporary construction needs in the war theater. I expected an "enterprise data management" software package to track all procurement actions from the point of requisition to payment of invoices. Because KBR was using paper requisitions and individual data systems to run this seven billion dollar contract, the document control and subcontract management departments did not have accurate records to distribute to the work sites or to auditors. One example: The Subcontracts Department gave Camp Udairi a list of 27 contracts to monitor with no monetary value included. Three on the list did not belong to Camp Udairi. Through what I called "shoe box research," I discovered we actually had 41 open subcontracts for this task order. Plus, there were dozens of paper requisitions that were "lost in the black hole." The list given to us by Document Control had a contract value of about $9 million, but the actual value of the 41 subcontracts that belonged to Camp Udairi was approximately $22 million.

3) **Subcontract Information Withheld.** Site managers throughout the project did not have the ability to properly manage subcontracts, because they could not obtain copies of the subcontracts from the Kuwait Subcontracts Office during the performance period. We leased forklifts, fuel tankers, trucks, SUVS, backhoes – for months after the contracts expired because site personnel were not allowed to have the documents to track turn-in or renewal dates. As late as April 2004, Kuwait-wide, we did not know which forklifts were on which subcontracts. Repeated suggestions to build data banks that matched equipment to subcontracts or property records went ignored. How could production schedules, inventory, equipment delivery and pickup be monitored if the people in charge don't know what they were in charge of? This was partly corrected in mid-February, 2004, when the KBR regional Vice President directed that subcontract documents be provided to site managers. I emphasize partly corrected: the document control department continued to resist giving subcontract information as late as April, 2004. In March and early April of 2004, however, I and other subcontract administration staff were still tracking down large numbers of reefers, trucks, forklifts, and other leased equipment for which we could not produce inventory management records, but for which we were receiving subcontract invoices.

4) **Data hiding.** In subcontracts, the pattern of hiding data from government auditors persisted until the day I left the company:

a) We billed the government and were paid $44 million although we had not paid subcontractors. The proposal writers broke down information requests so that you could overlook status of invoices while it was billing the government.
b) Efforts to notate problems in reports for pay proposals were criticized, even after we were informed that the government paid us $44 million for subcontracts that we had not paid.
c) Efforts to forward information to DCAA auditors about items such as $100 per bag laundry agreements were criticized as "giving too much information."
d) When DCAA realized they did not receive a complete list of laundry subcontracts from our office, I was tasked to reconcile our list with the Finance and Accounting Department list, but not to add any more laundry accounts if I found more accounts than what F&A provided on its list. My supervisor instructed: "Only give them what they ask for."
e) When completing reports about KBR's solicitation practices, I noticed that the Subcontracts Department gave me a file with 37 subcontracts listed as missing. Towards the end of my tenure in the subcontracts department, when my workload declined, I volunteered to research these accounts, because we should have been able to identify them as "terminated," "never executed," or a "valid subcontract." I was not given the chance to do this, but in the latest subcontract list, 35 of the missing 37 subcontracts were deleted altogether from the list. If these were real transactions pending resolution, the total value could have been small. But subcontract values tended to range from a half million to 129 million dollars. Thus, hiding this list of initiated subcontract transactions would have implications for current and future audits and reports if any of them turned out to be real. (I had the experience of "disappeared files" turning up in unlikely corners as real transactions, and so, I would not have abandoned attempts to definitize the status of these 37 missing subcontracts.)

5) **Unskilled Management and Supervision.** I believe that KBR defrauded the government by staffing high paid, high skilled positions with unskilled personnel, in procurement and throughout the project, based on family and personnel relationships. Managers and supervisors at a number of sites had no prior experience with government operations, construction and site supervision, or procurement. When I first raised this point, I was introduced to the historical joke about the true meaning of the acronym KBR: kinfolk, brothers and relatives. As nice as all the kinfolk, brothers and relatives were to me and my co-workers, there is no substitute for years of logistics, contingency operations and subcontract management experience that it takes to properly run a $7 billion war time contract. Very often, third country nationals from the Balkans, India and Pakistan had stronger literacy, engineering and construction, operations and bookkeeping skills than those who held the high paying KBR jobs.

6) **Inexperienced Consultants.** The first Tiger Team, consisting of high paid consultants and KBR employees who took home more than $10k per month and lived in waterfront Hilton Chalets, crippled the Subcontract Department's ability to support operations during the largest troop rotation since World War II. The Tiger Team held onto subcontracts files, without taking responsibility for on-going management of these subcontracts. At the same time, their audit of subcontracts was shallow and bureaucratic. On February 4th, I went to the Hilton Hotel to track down a copy of one contract for leased SUVs and trucks, because the subcontract had expired, and we could not turn in vehicles or renew the subcontract until we were able to match our fleet of vehicles with a specific subcontract, that would show us rental rates, dates of expiration for each vehicle lease, and the process for handling lost, damaged, and destroyed vehicles. In a few hours, I was able to match license plates to eight months of payment vouchers to determine that 53 of Camp Udairi's non-tactical vehicles were on this subcontract. I was horrified to discover, however, that after holding onto this file, the Tiger Team had only checked to determine if three or four subcontractor checklists were completed. No effort was made to match vehicles to the payment vouchers, or to determine if the prices we paid were fair and reasonable, or to bring the contract current. Every day this subcontract sat on the desk of a consultant, we owed more money for vehicles we could not turn in because the contract was expired in December, and no effort had been made by the Tiger Team to bring it current. The file was returned to subcontracts administrators in March, without resolution, but with instructions for the subcontract administrator to bring the account current. I presented similar examples to Congressman Waxman's office, of accounts that were "audited" by the Tiger Team. In each case, the Tiger Team recommended actions that were wildly divergent from the true status of the account. At one point, the Vice President of Operations and Tiger Team leaders instructed subcontract administrators to start cutting requisitions to bring 400 expired subcontracts up to date – without researching what had been done, to determine if services were still needed, if the contracts were ever executed, or the amount of funds required for each requisition.

Abuse. It is hard to imagine that a company that pays its employees so generously could be capable of psychological abuse, but the management style at KBR was too often abusive. The following are examples of management abuse within KBR's corporate culture that I witnessed, or my co-workers witnessed:

1) Pressuring employees to comply with management dictates by threatening transfer to Iraq.
2) Threatening employees in Iraq to comply with management dictates by threatening transfer to less protected job sites.
3) Threatening employees in Iraq by forcing them to take convoys into Najaf and Fallujah during the height of hostilities there.

4) Having lower safety standards for convoys driven by Third Country Nationals. The safety manager at Camp Udairi complained that several people died in two accidents that would never have happened if the employees were American KBR, because the convoys were conducted through the desert with zero visibility.
5) Continuing convoys in Iraq during the war and recent insurgency. I have spoken with many drivers who went home after their bases were attacked, and their trucks were repeatedly attacked. One man showed me the bullet holes in his truck. KBR had a zero tolerance policy for unnecessary loss of life for its own employees. Drivers work for a subsidiary off shore corporation, as subcontracted drivers do. The drivers may have volunteered for the transportation mission, but once the pictures of bullet ridden trucks were brought to management's attention, and KBR drivers publicly expressed their fear about being unarmed in convoys during the insurgency directly to Mr. Lesar in a public meeting after the April 9 massacre, I expected Mr. Lesar to return home and reassess this portion of the KBR mission in Iraq. Truck drivers are not combatants. They cannot protect themselves without violating the "Law of Land Warfare." They have been given very mixed messages since the insurgency increased, and they are being put at unnecessary risk as civilians. I believe the government is placed at unnecessary risk because many of these drivers will file lawsuits to recover damages for the unnecessary trauma they experienced. In the end, the Halliburton shareholder will not pick up that cost. Eventually, that cost will be paid by the taxpayer.

Conclusion. Halliburton is billing the government for a personnel and operations structure that is very wasteful, given that most of the logistics, construction and transportation operations are performed by subcontractors. Halliburton's data management and data reporting practices are fraudulent, preventing site managers from effectively reducing costs as projects are performed, and preventing auditors and contracting officers from grasping the true costs of the project as it progresses. I would like to make it clear that I am sure that with proper oversight, Halliburton will correct the deficiencies that I and other employees have brought to the attention of this committee. My sole reason for bringing my concerns to Congress is because I did not see appropriate management responses to the concerns that I raised in this presentation.

The money wasted by Halliburton could have been spent armoring HUMVEES, or buying vests for the Iraqi National Guard. If it was not really needed for the war effort, I believe it should have been returned to the states to pay for teachers in poor communities, or health care for working families who cannot afford health care, or for homeland security. I do not begrudge the self-indulgent lifestyle expenses that Halliburton employees incurred while in Kuwait. I do believe, however, that the corporation should charge these indulgences not to the taxpayer, but to the shareholder. Similarly, if a manpower assessment confirms what I have described as a duplicative personnel structure, I believe the cost overages should be charged not to the taxpayer, but to the shareholder.

I was recruited to Halliburton by former Army commanders, and I served the company in two theaters: Kosovo and Kuwait. I joined the company because I hoped to support Army soldiers with the best logistics, operations and support services at a time when the Army suffered critical manpower shortages in logistics and operations. I will continue to address the concerns raised in this testimony, because I believe that we must spend the taxpayer's dollars prudently and judiciously.

Table 1. Subcontracts for KBR Employee Hotel and Associated Expenses

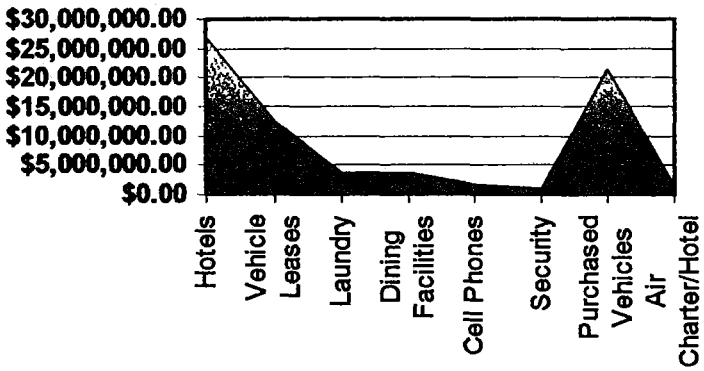
SC Number	Transactions	Subcontractor	Amount	Type
S00010	4	LorieKillingsworth	$7,375.00	1
S00162	3	JawharatAlFanar	$281,296.74	1
S00188	6	NCC Apartments	$1,663,024.85	1
S100276	2	Safir Airport	$3,456,000.00	1
S100305	3	Gulf Facilities	$1,826.00	1
S100310	13	Kempinski	$4,433,890.95	1
S100315	3	AlGhannam	$1,627,670.40	1
S100321	3	Hilton	$25,124.53	1
S100354	2	NCC watania	$1,901,059.40	1
S100358	2	Vector International	$5,057,031.11	1
SK00366	1	Natl Real El Joan	$814,828.80	1
SK00422	1	Sharja Rotana Hotel	$50,335.00	1
SK00429	2	Palms Club Hotel	$4,165,789.62	1
SK00527	1	Khalifa	$1,732,177.63	1
SK00550	1	Global Services	$65,391.67	1
SK00562	1	Movenpick	$1,757,931.96	1
MA00016	18	Gulf Union	$1,000,879.90	2
MA0002	20	Kuwait Automotive	$2,200,951.64	2
MA0013	4	Arabian Motors	$83,148.00	2
MA0023	9	Kuwait Finance	$1,690,182.43	2
ML0025	2	GM Vehicle	$5,340,600.00	2
S00034	4	AutoMak	$225,818.00	2
S0004	4	AlMulla	$247,500.00	2
S00047	4	Global Services	$283,224.00	2
S00118	4	Automak	$34,371.00	2
S00119	3	AlMulla	$66,310.74	2
S00161	0	AlMulla	$83,598.53	2
S00176	0	AlMulla	$59,684.53	2
S00178	0	Gulf Union	$196,938.84	2
S00193	1	Kuwait Finance	$49,586.57	2
S00196	3	Kuwait Finance	$801,415.20	2
S00200	0	AlMulla	$55,097.30	2
S00205	2	AlMulla	$29,753.03	2
S00207	2	AlMulla	$131,433.00	2
S00216	2	Global Services	$17,948.36	2
S100277	2	AlSamer	$18,685.82	2

S100471	0	AlMulla	$31,167.20	2
S20084	0	Gulf Facilities	$12,375.00	2
SK00365	0	AlSamer	$20,340.00	2
MA00035	7	Najlaa	$3,249,129.03	3
S00194	5	Najlaa	$622,556.12	3
SK00467	2	Najlaa DFAC	$3,858,577.00	4
MA0017	17	EAMAR	$1,153,714.30	5
ML0024	8	Dehdari	$431,677.97	5
S100325	2	Kempinski	$2,442.00	5
SK00393	2	Kempinski	$3,993.92	5
SK00528	2	Kempinski	$4,769.34	5
S00018	9	AlRaedSecurity	$866,750.16	6
S100333	0	AlMullaSecurity	$93,863.70	6
S100342	2	AlRaedSecurity	$72,683.97	6
MA0052	0	Arabian Motors	$6,107.71	7
MA0052	45	NCC Sponsor	$831,105.98	7
MA0053	0	Arabian Motors	$7,510,958.71	7
ML0027	25	GM	$12,829,565.60	7
S100337	2	Western Auto	$308,000.00	7
SK00380	1	YAAlGhanim	$51,200.00	7
SK00403	4	ChapmanFreebornFZE	$1,313,100.00	9
		Total Value	**$72,931,958.26**	

Table 2. KBR Kuwait Hotel and Associated Expenses

Hotels	$27,040,753.66
Vehicle Leases	
Laundry	$3,871,685.15
Dining Facilities	$3,858,577.00
Cell Phones	$1,596,597.53
Security	$1,033,297.83
Purchased Vehicles	$21,536,938.00
Air Charter/Hotel	$1,313,100.00
Total	**72,931,958.26**

Figure 1. KBR Kuwait Hotel and Associated Costs: $72,931,958.26



Chairman TOM DAVIS. Do we have a copy of that additional? We are happy to look at it. It would be good to have the committee members look at it so we can ask questions based on that. And without objection, it will be entered in the record.

Committee staff get that.

Thank you all very much for being here.

Mr. Waxman, we are going to start on our side, and we will take a half an hour. And I would yield 15 minutes to Mr. Schrock.

Mr. SCHROCK. Thanks to all of our witnesses for being here today. I am particularly interested in the circumstances surrounding the allegation made about operations of convoys with KBR drivers. Most of my questions will be addressed to Mr. Wilson and Mr. Warren, and I can see that the both of you have a good deal of time under your belts driving trucks in the United States; is that correct?

Mr. WARREN. Yes.

Mr. WILSON. Yes.

Mr. SCHROCK. Neither of you is still in the employ of KBR; is that correct?

Mr. WILSON. That's correct.

Mr. WARREN. That's correct.

Mr. SCHROCK. And I believe in both of your cases, Mr. Wilson and Mr. Warren, your employment was terminated by KBR for violations of their business code and improper behavior in Iraq; is that correct?

Mr. WILSON. I was terminated for breach of the code of business conduct.

Mr. WARREN. I couldn't tell you exactly why I was terminated.

Mr. SCHROCK. Your testimony does not mention it, but am I safe in saying that both of you in your experience working for KBR, this is the first time you have ever been in a war zone?

Mr. WARREN. For me, it is.

Mr. WILSON. Yes.

Mr. SCHROCK. In your statements, you both wrote that you believe the practice of Army personnel purposely using incendiary devices destroying trucks that could not keep up with the convoy was wasteful; is that correct?

Mr. WARREN. Yes, sir.

Mr. WILSON. No, sir. I never stated that.

Mr. SCHROCK. Mr. Wilson, I see from your written testimony and you so state that you personally were in convoys that came under attack from mortar fire, IEDs and such; and I believe you testified you and other drivers were injured working for KBR; is that true?

Mr. WILSON. Yes, sir.

Mr. SCHROCK. Iraq is unlike any other driving experience in the United States?

Mr. WILSON. Similar to New York on occasion.

Mr. SCHROCK. Mr. Wilson, in your testimony you stated you had a convoy of 28 trucks accompanied by armed military escort vehicles. Am I safe in assuming that all of your convoys were escorted by uniformed military personnel, heavily armed and responsible for the security of your convoy during your drives?

Mr. WILSON. Yes, sir, we had excellent escorts.

Mr. SCHROCK. Mr. Warren, I would imagine your experience with the convoys would be similar to those of Mr. Wilson; is that correct?

Mr. WARREN. That's correct.

Mr. SCHROCK. I was privileged to spend 24 years in uniform, including time in Vietnam, and I have been a close observer of this war and of every major conflict this country has been engaged in for the last 30 years.

My assessment would be that convoys such as the ones that you participated in are safer when they are moving forward as a single unit, presenting a more difficult target and able to be secured by your military escorts as a single unit. Would you gentlemen agree with that?

Mr. WILSON. I would agree with it to an extent. The size of the convoy in the situations has a lot to do with it. Our number of escorts was limited. We had, on the average, three to four vehicles with armed personnel in them at one time—a 28 truck convoy. I am sure, if you have been in that situation, it stretches quite a distance.

Mr. SCHROCK. But did you feel safer when you were moving than when you were standing still?

Mr. WILSON. Depending on the area we were in. Generally we felt safer moving.

Mr. SCHROCK. As a member of the Armed Services Committee and former military officer myself, I cannot imagine a situation in which a military commander anywhere would require a security detachment assigned to protect a convoy to place either the civilian contract drivers under his charge or his military personnel in danger if he believed that the environment was too dangerous to halt the entire convoy while maintenance was performed on a disabled vehicle, can you?

Mr. WILSON. Sir, that is not the way we did that. If we had a vehicle with a problem, say the vehicle was in 15th position in the convoy and the vehicle had a problem in that position, that vehicle would pull off to the side of the road, a military escort would immediately go to that vehicle. I would take the rest of the convoy and continue up the road until my escort, who was generally the NCOIC, would determine that we were in a safe enough location that we could go into a box formation and stop and wait for them to decide if they were going to be able to recover that vehicle or they were going to have to abandon it.

Mr. SCHROCK. Do you agree with that?

Mr. WARREN. Yes.

Mr. SCHROCK. I believe the loss of a relatively expensive truck in Iraq is certainly unfortunate and certainly wasteful. We are going to explore the maintenance practices more extensively with the second panel. However, I would not trade a single truck in Iraq for the life of either an American civilian or a soldier. And as a military commander, I would certainly not endanger an entire convoy of trucks, their drivers or other military personnel under my command, if I believed that the threat from insurgents precluded recovering that vehicle.

Do you believe that perhaps when you witnessed trucks being purposely destroyed, it was because the Army believed it was tactically necessary to do so?

Mr. WARREN. In my opinion, I don't think it was necessary to do so. Maybe the Army or KBR.

Mr. SCHROCK. Were you in on the military planning to make this decision?

Mr. WARREN. No, sir.

Mr. SCHROCK. Mr. Wilson.

Mr. WILSON. I don't know of any instance in which the Army took it upon themselves to destroy a KBR asset. Every instance that I am aware of when that happened, the NCOIC talked to the convoy commander; and we did work closely together, and we made decisions together.

Mr. SCHROCK. You think they maybe took that action because it was in the best interest of the convoy and your best interest to protect your lives and the lives of the soldiers who were assigned to you all?

Mr. WILSON. As far as destroying the trucks that were left? No, sir, that wasn't the intent on destroying the trucks. The intent in destroying those vehicles was so that there would be nothing left for the Iraqis to use against us. People would come out of the sand—we would call them the "sand people"—when we had a truck break down like that, wearing their native garb, and you would never see any tools or anything like that.

By the time we would leave, I would have NCOIC tell me they were thugs.

Mr. SCHROCK. So what I hear you saying is, destroying it might prevent the enemy from taking parts of the chassis, for instance, for their use?

Mr. WILSON. I didn't consider them the enemy. They were civilians.

Mr. SCHROCK. If you can figure out what civilian is an enemy and which one is not an enemy, we need you up here to help us with that. I don't know how anybody could control that.

Mr. WILSON. That wasn't my job. That was the Army.

Mr. SCHROCK. They were the ones who were making the decisions.

Don't you think it is a little capricious for us to sit here in this air-conditioned room questioning the tactical decisions of our military personnel charged with protecting lives in Iraq.

I believe your life is worth far more than $85,000 as well as every single life of every American in Iraq. Do you agree with that assessment.

Mr. WILSON. I agree with you.

Mr. WARREN. I agree.

Mr. SCHROCK. Perhaps there is a little more to this situation than there would be had these trucks been driving down some big interstate in California and Texas; don't you agree?

Mr. WARREN. Much different.

Mr. SCHROCK. No pun intended, but I want to shift gears here for a second. In your written testimony, you both stated that running convoys with some empty trucks was wasteful and inappropriate, or the convoys would sometimes arrive at the scheduled loca-

tion to find that the unit they expected to be there was gone. Is that true?

Mr. WILSON. We didn't necessarily discover they were gone. We were told that was the reason we were hauling retro back from Anaconda to Cedar II to later be transported back to Kuwait. A lot of times this was new material and a lot of times it was used-up material, was the way they referred to it.

We just generally questioned at one time why we were taking new equipment back to Kuwait, and we were told that it was considered retro and the reason that happened is maybe the unit that had ordered had rotated out.

Mr. SCHROCK. Let me state again, as I understand your responsibilities in Iraq, I believe you were hired to drive trucks in a military convoy, correct?

Mr. WILSON. Correct.

Mr. WARREN. That's right.

Mr. SCHROCK. So you did not participate in the decisions on what needed to be transported on a given day or where it needed to go?

Mr. WARREN. That's correct.

Mr. WILSON. That's correct.

Mr. SCHROCK. I would surmise the military commanders with greater situational awareness knew what each individual unit needed and where they needed it and they made those decisions. After all, they were plugged in to the military command structure and were responsible for deploying and equipping military units in Iraq as well as for the security of those units.

Deciding how to fight the war was the military's responsibility, not yours; is that correct?

Mr. WILSON. Absolutely right.

Mr. WARREN. Uh-huh.

Mr. SCHROCK. That is what I thought.

Is it conceivable to think that perhaps in that situation, a military commander with a job to do, a mission to complete, might have made a judgment that it was more important to have those trucks available at point A so they could move supplies, even if they had to come from point B without carrying any cargo on them? Isn't that a possibility?

Mr. WILSON. That is one possibility, yes, sir.

Mr. WARREN. I would agree. I am not in charge of the logistics and stuff like that. I don't know why they do stuff like that.

Mr. SCHROCK. Do you think it was possible that a unit may have to pick up and leave on short notice because they had received military tasking and leave without waiting for your supplies to arrive? Is that a possibility in a war zone?

Mr. WILSON. Yes.

Mr. WARREN. Possibly.

Mr. SCHROCK. Did you think that perhaps those trucks had to run empty for a reason because when you were engaged with insurgents in a fast-moving, fluid environment like the war we have in Iraq, sometimes the logistics and the judgment of the truck drivers have to take second place to the mission of the military units that you were supplying?

Mr. WILSON. As far as the number of trucks?

Mr. SCHROCK. That the military requirements for what they do with those trucks take precedence over what the truck drivers might think needs to be done.

Mr. WARREN. Sure.

Mr. WILSON. Sure.

Mr. SCHROCK. Very different than driving on our highways around here, I can assure you.

You both mentioned theft of supplies from the convoys. Is it safe to say that the majority of this occurred when the trucks were in Army camps during the evenings?

Mr. WARREN. The stealing was going on in Army camps, and while en route to Army camps. Both instances.

Mr. WILSON. It happened in staging lanes at the Army camps as well as on the road.

Mr. SCHROCK. Did either of you witness this theft either on the road or in the camps at night?

Mr. WARREN. Yes, sir.

Mr. WILSON. Yes, sir.

Mr. SCHROCK. Did either of you participate in that theft at any time?

Mr. WARREN. No, sir.

Mr. WILSON. No, sir.

Mr. SCHROCK. Of course, I certainly cannot endorse the unauthorized removal of supplies from military convoys by U.S. military personnel, but the experience I had in Vietnam, I can tell you that I believe that this is a fact of military life in a wartime environment since the dawn of time. When I was in Vietnam we called it comsho.

If troops saw parts that they needed and they were in the staging area and they needed to put the equipment back together, they took it. They didn't take it for their own benefit, but for the folks they were trying to protect and to defeat the enemy. And we must do all we can to limit this.

However, I just wanted to clarify with both of you, gentlemen, that you were hired to drive trucks and that was your responsibility and KBR's responsibility and that did not include management of the inventory you were assigned to haul nor were you or KBR, to the best of your knowledge, responsible for the purchase, delivery or receipt of this cargo. You just drove the trucks.

Mr. WARREN. That's correct.

Mr. WILSON. I made that statement in my statement.

Mr. SCHROCK. Mr. Wilson, you testified you did not have any details about what you were carrying in the truck. Could that be because, in fact, you were not responsible for the cargo manifest, that the control of the inventory was the responsibility of the Army and not yours?

Mr. WILSON. Yes, sir.

Mr. SCHROCK. I would think that the reason that you as a KBR employee or KBR as a company, for that matter, was not charged with security is the same reason that you were not charged with fighting the war, because you did not have the training or the tools to do that. And gentlemen, you both took issue with the decision to not containerize most of the shipments on the trucks that were military—that the commanders and the logistics officers——

Mr. WARREN. Yes.

Mr. WILSON. Yes.

Mr. SCHROCK. The way I understand the situation, you and your colleagues were hired to drive trucks under the command of our military personnel, under the security they provide, so our troops could carry rifles and do the jobs they were trained to do?

Mr. WARREN. That's correct.

Mr. WILSON. That's correct.

Mr. SCHROCK. I believe we will hear testimony shortly from the second panel that the Army required that open, flatbed containers be used to facilitate easy loading and unloading and there is certainly a reason for everything.

Now Mr. Wilson, Mr. Warren, as we briefly discussed earlier, both of you were terminated for cause by KBR. May I ask, do you know the exact details of why you were terminated?

Mr. WARREN. In my instance, I don't know why I was terminated. What happened was, I was—I had made a phone call with Mr. Harl one evening, I believe it was in mid-March or the first part of March, somewhere around that timeframe. I spoke to him on the phone, and I was telling him about—that I felt like I was being pushed out the door, like—and I wanted a fair hearing, you know, to present my case.

And what happened was, security wanted to talk to me about running people off the roads in convoys and I would not disclose the names of who was doing that. And I was transferred to Kuwait, and I stayed in Kuwait for a period of approximately 2 weeks; and after 2 weeks, I was terminated. And I was told to sign some paperwork by the KBR, and I refused to sign them; and they would not tell me why I was terminated because I did not cooperate with them in the termination process.

Mr. SCHROCK. I believe my time has expired.

Chairman TOM DAVIS. Mrs. Blackburn.

Mrs. BLACKBURN. Thank you, Mr. Chairman.

Ms. deYoung, I will come to you first. And I would like to ask you some questions specifically about your background and work product, since many of your allegations and conclusions seem to draw from what you claim is expertise in government contracting and procurement and subcontract administration.

Your resume, which I am going to ask the Chair to enter into the record, lists your last employment at Camp Bondsteel Kosovo.

[The information referred to follows:]

Marie E. deYoung
[redacted]

Telephone: [redacted]

Permanent Address Effective 1 September 2003:
[redacted]

Employment History

Mobilization: Administrative Assistant. Kellogg Brown and Root Services. Area Support Group Falcon Command Group, Camp Bond Steel, Kosovo. 2003.

Director. Northeast Nodaway Marching Band and Choirs. Taught general music classes (grades 5-12), band classes (grades 5-12), senior high choir classes. 2002-2003.

Director. Rock Port High School Bands and Choirs. Elementary Band. Taught instrumental classes grades 5-12 and choir classes grades 7-12. 2001 to 2002.

Special Projects Officer. U.S. Army Reserve. 12th BN (CAS3). Omaha, NE. Edited training procedures. Drafted battalion standing operating procedures. Draft commander's documents, letters, guidance. Prepared battalion monthly newsletter. 2001-present.

Director. Newman Catholic Center. Northwest Missouri State University. 2000 to 2001.

Director. Center for Women in Church and Society, Our Lady of the Lake University. September 1997 to August 2000. Wrote $250K grant proposal for after-school abstinence education program for at-risk urban youth in eleven schools. Obtained funding for this multi-year project. Designed brochures, website, bi-annual newsletter. Drafted proposals for Women's Studies Program, Strategic Plan, and Service Corps that were staffed through academic and administrative departments. MS Publisher, all MS office programs, and simple web page software.

Chaplain. U.S. Army. 2nd Armored Cavalry Regiment. 19th TAACOM (Deputy Command Chaplain). 44th Engineer Battalion. 4th Division Engineer Brigade Chaplain. 363 Corps Support Group Chaplain. Normal Chaplain duties. Wrote post newspaper articles, standing operating procedures, and instruction blocks related to military ethics and family support issues. These included domestic violence prevention, suicide prevention, and family wellness. Prepared briefings for 19th TAACOM. 1993-1998.

Minister. Unitarian Universalist Society of Martha's Vineyard. July 1992 to August 1993. Preaching and counseling responsibilities. Served as volunteer hospital chaplain and volunteer for Women's Support Services, to include domestic violence volunteer services.

Chaplain Resident. Hospital of the University of Pennsylvania. September 1991 to May 1992. Served on Medicare Patient Self-Determination Act Committee and on Organ Transplant Committee. Handled

many domestic violence and urban trauma cases. Neonatal Intensive Care, Cardio ICU, General Surgery ICU, Trauma On-Call.

Intern Minister: All Souls Unitarian Church, Manhattan, NY. Coordination of public media events, preaching, counseling, retreat facilitation, community service projects. September 1990 to May 1990. Prepared newsletter copy, public relations copy.

Assistant to the Director of Development. Starr King School for Ministry. May 1989 to August 1990. Updated donor base in computer system.

Principal Clerk. College of Engineering, University of California-Berkeley. Prepared budget projections for research grants for engineering professors. Reviewed proposals for adherence to agency guidelines. Wrote monthly "grant opportunities" newsletter. May 1988 to April 1989. All MS office programs, Word Star, and Mac programs used to draft proposals.

Dean's Assistant. Pacific School of Religion, Berkeley, California. March 1987 to April 1988. Managed Dean's office, correspondence. Prepared Dean's responses to routine correspondence. Drafted fifth chapter of the seminary's accreditation self-study. Upgraded computer systems.

Commander, Headquarters Detachment. Military Traffic Management Command-Western Area, United States Army. Coordinated garrison support for reservists during 1986 Team Spirit Exercise. Developed and drafted plans for barracks renovations and for command events such as the first Command Run. 1985-1986. Handled domestic violence, other crisis cases. Responsible for professional development of 60 soldiers.

Chief, Services Branch. Oakland Army Base, Oakland, California. United States Army. Oversight of guest house, child Child Development Center (63 children), Army Community Services and Military ID card section. Designed and obtained funding for Domestic Violence Counseling Project (60k annually). Suicide Prevention Officer. Planned and implemented $750K renovation of Jacobs Guest House. Prepared manpower survey documentation, decision briefs, strategic plans for reorganization and renovations. Coordinated Brigadier General John Stanford's Town Meetings. Briefed visiting dignitaries on model family support programs. 1984-1985.

Shopkeeper. Westport Wine and Cheese, Kansas City, Missouri. July 1979 to May 1981. Drafted sales brochures. Maintained daily sales operations.

Assistant Manager. Coffee Garden Restaurant, Crown Center Hotel, Kansas City, MO. July 1976 to July 1977.

Patient Account Representative. New England Medical Center, Boston, Massachusetts. March 1973 to December 1975. Correspondence and research of medical billing errors. Negotiated payment settlements via correspondence.

Account Representative. Boston College, Chestnut Hill, Massachusetts. July 1972 to March 1973.

Publications:

Women in Combat: Civic Duty or Military Liability. Lorry Fenner and Marie E. deYoung. Georgetown University Press, 2001. Hardback and paperback.

This Woman's Army: The Dynamics of Sex and Violence in the Military. Hellgate Press, 1999. 374 pages.

"Sexuality: History, Behaviors and Lifestyles that impact Military Readiness," in *Women in the Military.* Edited by Dr. Rita Simon. Transaction Publishers (Rutgers), 2000.

Other college newspaper articles, journal articles, media interviews, etc. can be furnished upon request.

Military Education

2001 Quartermaster Officer Advanced Course (Correspondence).
1993 Chaplain Officer Basic Course
1984 Adjutant General Officer Basic Administrative and Personnel Management Course. Army Community Services Management Course . Morale Welfare and Recreation Management Course.
1983 Basic Training, Officer's Candidate School.

Civilian Education

2001- University of Missouri-Columbia. Ed. D. Education Leadership, in progress. Courses emphasized organization development and organization leadership theory. I will complete comprehensive examinations on August 28, 2003.
1988-90 Starr King School for the Ministry. M. Divinity.
1986 Stanford University. Orchestral conducting courses, one trimester.
1977-81 University of Kansas City-Missouri-Conservatory of Music. Degree in Music Theory (With Distinction). Three years of orchestral conducting.

Other courses at local universities to obtain teachers certification and to improve management skills.

Chairman TOM DAVIS. Without objection.

Mrs. BLACKBURN. From what you have written on your resume, you were an administrative assistant there; and your two previous jobs were as musical director for elementary, junior and high school bands. And your work with our Lady of the Lake University, you designed brochures, a Web site and a newsletter. And prior to that, you describe your experience as a chaplain.

Your resume does not indicate that you are a specialist in procurement or contracting, although the closest you come to procurement expertise seems as a shopkeeper over 20 years ago. You have never been a contracting officer or a contract specialist, have you?

Ms. DEYOUNG. I do not claim to be a contracting specialist. I said I was a logistics specialist. I base my testimony on firsthand documentation and documents.

Mrs. BLACKBURN. You have never been a procurement specialist?

Ms. DEYOUNG. I was asked by the manager, who was the president of the Contract Management Association, to be his assistant in subcontracts. And he, "favored my tough investigative skills to help him get the truth about the subcontracts."

Mrs. BLACKBURN. You might have received some logistics training in a correspondence quartermaster course while you were in the Army. I don't believe you have ever received any extensive formal training in government contracts.

Ms. DEYOUNG. On-the-job training there and also—and Congresswoman, also you are leaving out part of my resume. I managed a government grant, $213,000, Federal grant that President Bush awarded to my Center for Women. It was a government contract.

I managed grants for the Army. I managed construction for the Army in 1984. I helped build the child development center, a $1 million project, and renovate——

Mrs. BLACKBURN. Even though you have had some experience with contracts as part of your other work experience, isn't it true that you don't have the expertise that a contracting officer, contracting specialist or an auditor would have? Is that correct?

Ms. DEYOUNG. Congresswoman, half of the people in the subcontracts department have not been certified. And a subcontract specialist——

Mrs. BLACKBURN. You are not answering the question that I am asking.

Ms. DEYOUNG. Am I certified auditor, no. And I never claimed to be, ma'am.

Mrs. BLACKBURN. In your statement posted on the minority's Web site, you explained that your position was a writer, logistics center writer for operations and briefings. Being a writer seems to be something supported by your resume and your work experience. And it seems logical that a writer would write reports on various subjects.

The job you were hired for was not to buy products and services for Halliburton or KBR or act as a procurement officer or subcontracts administrator, was it?

Ms. DEYOUNG. I was hired to do logistics on the operations side. They moved me to subcontracts because of the audits, to help the managers to prepare for audits, because they, "needed the help desperately."

Mrs. BLACKBURN. You make multiple allegations regarding KBR's Tiger Team. Are you aware of Tiger Team's recommendations and how they were implemented?

Ms. DEYOUNG. Which recommendations? I describe specific accounts, and I provided documentation to the committee of specific accounts where recommendations—for example, one contract, No. 23, the recommendation was to add money, extend the subcontract even though the Tiger Team member said, there are no invoices in there, that nothing has been paid. On specific accounts, recommendations were made without any research to add money, to pay bills, and there was no evidence that the services had been provided.

There was no investigation.

Mrs. BLACKBURN. Ma'am, are you aware of the recommendations the team made and how those were implemented? Yes or no? Are you aware of the Tiger Team's recommendations that were made and how those were implemented, yes or no?

Ms. DEYOUNG. I did not see implementation.

Mrs. BLACKBURN. Thank you. When companies notice a problem in a particular area and when companies notice there is a problem in a particular area of operations, they might send a team of experts to try to solve that problem. And you allege that Halliburton and KBR lacked adequate subcontract documentation.

So could that not be the reason that they sent the Tiger Team in there to try to fix that?

Ms. DEYOUNG. The experts were not looking for documentation. All they did was go down checklists to see if a form had been signed. They were not matching invoices with records of inventory. They were not matching invoices with records of services being provided. And that, to me, was inadequate supervision. And both the GAO and DCMA and DCAA were complaining about that.

I am a corroborating firsthand witness who observed that.

Mrs. BLACKBURN. We understand that in February 2004, you were—you asked to be reassigned to the procurement department.

Ms. DEYOUNG. No, ma'am. I requested to go to Iraq to be on the operations side of the house.

Mrs. BLACKBURN. Isn't it true you were turned down for the position because you had no procurement experience? And, further, isn't it true when the company asked you questions about basic subcontracts administration, such as the difference between a subcontract and a purchase order, you were unable to answer them and you ultimately agreed that you were unqualified for the position?

Instead, we are going to hear that you were given an administrative job of helping the subcontracts administrator gather documents and information. You were never given the title of subcontracts administrator, were you?

Ms. DEYOUNG. I did not ask to go to the contracts department; I was put there. I wanted to go to Iraq to be in logistics, which is my specialty. The reason I was put there was because I, "had the ability to fix problems" as I had done with subcontracts out at Camp Udairi. I did not ask to go there. I had asked to be assigned in Iraq in logistics.

Mrs. BLACKBURN. You were never given signature authority over any contracts, right?

Ms. DEYOUNG. No, I was not. But I was asked to monitor and correct problems, to create ITFs and cut change orders and to prepare reports for the manager.

Mrs. BLACKBURN. Let's go specifically to one of your major allegations, which concerns contractors staying in very nice hotels. And you have this on your supplemental statement.

Many members of this committee have been to Kuwait and I, for one, have noticed that the hotels are of nice quality with good amenities. It is my understanding that KBR requested that the military provide lodging for its employees at Camp Arafjan in the tents, but we are told there was no room.

I expect the witnesses will also testify that it was KBR's intention to have the company employees lodging in a central location for security reasons, very obvious security reasons, as well as for logistical reasons. Most employees actually worked at the camp and required transportation there from their hotels.

Were you aware that employees were sometimes housed three, four and five to a room?

Ms. DEYOUNG. The hotels that I described, they were housed one to a room unless there were social relations going on.

Mrs. BLACKBURN. Are you aware that sometimes they were housed three, four, five to a room?

Ms. DEYOUNG. When you say room, a room—they are villas. And in those hotels that I——

Mrs. BLACKBURN. I have a copy of the contract with me, and I understand that testimony from KBR will corroborate this. And I can see that without having access to the entirety of this information regarding KBR's housing options, a person might think that the employees were taking the government for a ride.

Ms. deYoung, would you agree if what I told you about KBR's option for housing is true, employees staying in centralized hotels might actually be the most fiscally responsible and secure arrangement for the circumstances in which they were working?

Ms. DEYOUNG. Army officers and managers of the project were communicating in March that the Army had asked them to move into tents, not to build a man camp, not to continue the hotels. And retired General Peterson had meetings. I was sitting adjacent to the courtyard where all of the managers came and these meetings were discussed.

Various managers continually repeated——

Mrs. BLACKBURN. That is not the information I asked for, and I am going to ask that we put a copy of the subcontract into the record.

[The information referred to follows:]

9/30/03

SUBCONTRACT TERMS

Subcontract No.: GU49-KU-S100310

1.0 **DEFINITIONS**

1.1 PROJECT shall mean LOGCAP III, Kuwait.

1.2 OWNER shall mean the United States Government.

1.3 CONTRACTOR, GENERAL CONTRACTOR or PRIME CONTRACTOR shall mean Brown & Root Services, a division of Kellogg Brown & Root Services, Inc.

1.4 SUBCONTRACTOR shall mean "Kempinski Julai'a Hotel & Resort".

1.5 CONTRACT shall mean the prime contract between CONTRACTOR and the U.S. Government, DAAA09-02-D-0007

1.6 SUBCONTRACT shall mean this subcontract between CONTRACTOR and SUBCONTRACTOR.

1.7 SUBLET WORK shall mean all work and other requirements, expressed or implied, necessary for the performance required of the Subcontractor by the Subcontract Documents.

2.0 **SUBLET WORK**

In accordance the Sublet Work the SUBCONTRACTOR shall furnish all labor, equipment, materials, supervision, insurance, freight, overhead, and all other services necessary to provide accommodation of Kellogg Brown and Root Services, Inc. in one bedroom, two bedroom, there bedroom and four bedroom chalets at the "Kempinski Julai'a Hotel & Resort", Kuwait and laundry service for the Resort guests.The work shall be as described herein and all other items specified in the sublet work and in accordance with all attachments.

2.1 SUBCONTRACTOR shall provide accommodation for Kellogg Brown and Root Services, Inc. employees, in accordance with the following:

2.1.1 Twenty (20) one bedroom chalets

2.1.2 Twenty one (21) two bedroom chalets

2.1.3 Four (4) three bedroom chalets

2.1.4 Four (4) four bedroom chalets

2.2 SUBCONTRACTOR shall ensure that no meals are provided to the Reasort guests and all the chalets under this Subcontract are cleaned on a daily basis. The linen shall be changed twice a week.

2.3 GENERAL CONTRACTOR'S employees will enjoy the services and benefits of the Hotel, health club, pools and restaurants, during the working hours.

2.4 SUBCONTRACTOR shall ensure that charges other than the chalet rate will not be considerd by this Subcontract. All the charges for phone and other amenities, as well as room or chalet damages made by the guests, are responsibilities of the guest.

EXHIBIT G

2.5 SUBCONTRACTOR shall provide Laundry Service for the Resort guests, in accordance with the following:

2.5.1 The turn over time for the service will be 24 hours.

2.5.2 GENERAL CONTRACTOR'S employees shall sign laundry inventory lists/delivery tickets for every submitted/received laundry bag.

2.5.3 The laundry inventory lists/delivery tickets shall be submitted along with every invoice for laundry service.

3.0 **PRICING**

GENERAL CONTRACTOR agrees to pay SUBCONTRACTOR based on the Firm Fixed Unit Prices contained herein for complete, satisfactory and timely performance of SUBLET WORK in strict accordance with the requirements set forth in this SUBCONTRACT, in addition to all applicable sales, use and other taxes.

Quantity	Description	Unit Rates	Total
20	One bedroom chalet, for approximately 93 days or three months period.	33.000 KWD per chalet, per night	61,380.000 KWD
21	Two bedroom chalet, for approximately 93 days or three months period.	50.000 KWD per chalet, per night	97,650.000 KWD
4	Three bedroom chalet, for approximately 93 days or three months period.	70.000 KWD per chalet, per night	26,040.000 KWD
4	Four bedroom chalet, for approximately 93 days or three months period.	95.000 KWD per chalet, per night	35,340.000 KWD
lot	15 % Service Charge as per the Kuwait Law.		33,061.500 KWD
lot	Laundry Service, for approximately 93 days or three months period and approximately 100 persons, per day	1.000 KWD per person, per day	9,300.000 KWD

NOT TO EXCEED 262,771.500 KWD

TWO HUNDRED SIXTY TWO THOUSAND, SEVEN HUNDRED SEVENTY ONE KUWAIT DINARS AND FIVE HUNDRED FILS
(Words)

3.1 Compensation to SUBCONTRACTOR for changes in the SUBLET WORK shall be in accordance with the provisions of Special Condition No. 5.0 entitled "Changes".

"Kempinski Julai'a Hotel & Resort"

4.0 **TIME OF PERFORMANCE**

4.1 SUBCONTRACTOR shall commence the SUBLET WORK as directed by the GENERAL CONTRACTOR on 30 September 2003 and continue through 31 December 2003.

4.2 GENERAL CONTRACTOR reserves the right to terminate portions or all services at any time throughout the period of this subcontract by providing thirty (30) days notice to the SUBCONTRACTOR.

4.3 If required, the time of performance of this Subcontract will be extended and GENERAL CONTRACTOR shall notify the SUBCONTRACTOR thirty (30) days in advance.

5.0 **PAYMENT**

5.1 SUBCONTRACTOR shall submit two (2) original invoices with all requested supporting documentation showing signed delivery tickets for actual services completed and accepted by the GENERAL CONTRACTOR. GENERAL CONTRACTOR shall make payment of an initial deposit of one (1) month in advance. All other payments will be made by Bank Transfer within fifteen (15) days after receiving of an acceptable invoice, acceptance of SUBLET WORK by GENERAL CONTRACTOR, and receipt of all required documentation and reports by GENERAL CONTRACTOR.

5.2 Aftert the first payment, SUBCONTRACTOR shall submit invoices every 15th and 30th of the month, during the time of performance of this Subcontract.

5.3 If the GENERAL CONTRACTOR terminates the Subcontract before the expiration date, one month rental penalty will be paid.

5.4 One (1) copy of GENERAL CONTRACTOR'S "Affidavit for Subcontractor" is attached hereto. SUBCONTRACTOR shall execute and submit it with its final invoice.

5.5 SUBCONTRACTOR will create a Subcontract billing format and delivery tickets acceptable to GENERAL CONTRACTOR, to be used for payments. This form will include, but not be limited to: The subcontractor's name, the subcontract number, the date of the invoice and the Electronic Funds Transfer information.

6.0 **TAXES**

SUBCONTRACTOR shall be responsible for all taxes imposed by Federal, State, or Local jurisdictions measured by or assessed upon SUBCONTRACTOR'S income or payroll. SUBCONTRACTOR shall be responsible for all applicable state or local sales, use, gross receipts or any other tax imposed on SUBCONTRACTOR'S purchase or rental of consumable supplies, construction equipment or tools or incidentals necessary to complete the work.

GENERAL CONTRACTOR shall include specific tax instructions as to the proper application and handling of service charge, any sales, use, gross receipts or other tax imposed on the work in each subcontract or work release.

7.0 **INSURANCE**

Prior to mobilization, SUBCONTRACTOR shall forward its certificate of insurance stating the names and addresses of its insurance carriers and certifying that its insurance coverage's meet or exceed the requirements of General Condition No. 5 (03/92). The certificate shall also reference the SUBCONTRACT number.

The certificates shall include a waiver of subrogation to the benefit of Brown & Root Services, Inc. and the U. S. Government.

8.0 **PERFORMANCE AND PAYMENT BONDS**

The following paragraph supplements General Condition Number 5:

GENERAL CONTRACTOR instructs SUBCONTRACTOR **not** to furnish Performance and Payment Bonds.

9.0 **COMMUNICATION/CORRESPONDENCE**

The following supplements General Condition No. 8.3:

All SUBCONTRACTOR communication/correspondence regarding this Subcontract shall be addressed as set forth in 10.1, 10.2, 10.3, 10.4 and 10.5 below. Subcontract correspondence shall include the CONTRACTOR'S Subcontract number, SUBLET WORK description, and subject and shall be sequentially numbered with an alpha-numeric number and dated for identification.

9.1 Insurance certificates shall be submitted as follows. (Reference General Condition No. 5.2 Insurance.)

9.2 Original Certificates of Insurance plus one copy shall be submitted to:

Eleonora Spasovska
Kellogg Brown and Root Services, Inc.
Camp Arifjan, Kuwait

The certificates shall include a waiver of subrogation to the benefit of Brown & Root, Inc. and the U. S. Government.

9.3 SUBCONTRACTOR is responsible for maintaining proper insurance coverage. SUBCONTRACTOR shall provide to the CONTRACTOR new certificates of insurance, as set forth in 16.1.1 above, no later than thirty (30) days prior to the expiration date(s) on its certificates and insure uninterrupted coverage during the life of the subcontract and any extensions thereof. Should SUBCONTRACTOR fail to provide these renewed certificates of insurance within the time set forth above, CONTRACTOR shall accept this as an indication that

SUBCONTRACTOR cannot provide the insurance coverage and is therefore in default of its subcontract and CONTRACTOR may promptly commence action to terminate the subcontract.

9.4 One copy of each invoice shall be delivered to the CONTRACTORS project office. The remaining two copies, with original signatures, shall be mailed directly to the Subcontract Administrator.

9.5 All other correspondence not otherwise shown shall be mailed to Ms Sherry Sullivan, Sr. Subcontracts Administrator, at the following address with a copy to CONTRACTOR'S PROJECT office.

Eleonora Spasovska
Kellogg Brown & Root Services, Inc.
Camp Arifjan, Kuwait

10.0 **QUALITY**

It is the policy of CONTRACTOR to execute projects and deliver services and products in conformance to the requirements agreed upon with Clients. Anticipating, clearly understanding and conforming to these agreed upon requirements is quality. Subcontractors are expected to adopt a standard of performance that demands conformance to the agreed upon requirements. This standard includes: 1) clearly understanding the requirements, 2) providing required documentation and technical submittals at the time specified, 3) delivering ordered quantities or performing services at the time specified, 4) satisfying warranty obligations, 5) responding in a timely way to questions and 6) having a system in place to assure that products or services meet the mutually agreed-upon requirements. In order to satisfy the above mentioned standard, CONTRACTOR and the SUBCONTRACTOR mutually agree to create an atmosphere to improve communications, understand needs and requirements, exchange ideas and information and cooperate in the solution of problems.

10.1 SUBCONTRACTOR shall be responsible for all Quality Control Requirements which pertain to its scope of work per the Specification.

10.2 CONTRACTOR will be responsible for Quality Assurance.

SUBCONTRACT

Payment Terms
See Paragraph 5.0 Subcontract Terms

DPAS Rated DO C9
Job Number: GU84-559710-56601
GU49-05275A10-56601
GU66-05435A10-56601

Subcontract No. GU49-KU-S100310

PRIME CONTRACT NUMBER DAAA09-02-0007
LOGCAP III

Accommodation in chalets in "Kempinski Julai'a Hotel & Resort"

30 September 2003
Effective Date

This SUBCONTRACT by and between **Brown and Root Services, a division of Kellogg Brown & Root Services, Inc., "GENERAL CONTRACTOR"**, whose address is 4100 Clinton, BLDG 01-260, Houston Texas 77020-6299 and **"Kempinski Julai'a Hotel & Resort", "SUBCONTRACTOR"**, P.O. Box 488, Sabahiya 54575, Kuwai, whose telephone number is +965 689 9006 and fax number is +965 328 3601 entered into as of the EFFECTIVE DATE stated above.

Vendor Number:	**N/A**
Product Code:	**N/A**
Requisition Number:	**KU06340**
Amount:	**Not to Exceed 262,771.500 KWD** **Approximately $877,105.00 USD** **3.3379 USD = 1 KWD**
Socioeconomic Status:	**Foreign**
Tax Identification Number:	**N/A**

WITNESSETH

In consideration of the mutual promises herein contained GENERAL CONTRACTOR and SUBCONTRACTOR agree, promise and obligate themselves as follows:

1. SUBCONTRACTOR promises to perform the SUBLET WORK for the PROJECT in accordance with the Subcontract Documents.

2. CONTRACTOR promises to pay SUBCONTRACTOR, for full, accurate and timely performance of the SUBLET WORK in accordance herewith, the Price, and promises to perform all of the other obligations of CONTRACTOR, as set forth in the Subcontract Documents.

3. The Subcontract Documents constituting this Subcontract consist of:

   a) Subcontract Signature Page, 2 pages
   b) Subcontract Terms, 6 pages
   c) Subcontract General Conditions (03/92), pages GC-1 through GC-8
   d) LOGCAP Purchase Order / Subcontract Special Requirements for Overseas Subcontracts, 8 pages
   e) Subcontract Backcharge Procedures, 2 pages
   f) Subcontract Backcharge Agreement, 2 pages
   g) Representations, Certifications and Other Statements of Offerors for overseas Subcontractors/Suppliers, 5 pages
   h) Supplementary Agreement, 3 Pages
   i) Affidavit for Subcontractor, (10-88), 1 page

   The foregoing constitutes the entire contract and supersedes all prior proposals, negotiations, agreements, awards, letter of intent and written or oral statement, representations or agreements.

4. The EFFECTIVE DATE set forth above is the date as to which all Subcontract Documents and provisions thereof have references for purposes of coordination of their meaning and effect. The price relates to the SUBLET WORK as described in drawings, specifications and other Contract Documents in their condition on that date. Changes after the effective date will be dealt with in accordance with the provisions for changes. Any work commenced and any payments made pursuant to an Award or Letter of Intent prior to the execution hereof shall be deemed to have been done and paid after the EFFECTIVE DATE under the terms of this Subcontract.

SUBCONTRACTOR:	**GENERAL CONTRACTOR:**
_____	_____
(Signature)	(Signature)
_____	**Eleonora Spasovska**
(Name)	
Title: _____	Subcontract Administrator
Date: _____	Date: _____

Memo for Record
Change Order Number Three (3)
2 December 2003

Subcontract No.: GU49-KU-S100310
Subcontract for accommodation of KBRII employees at Kempinski Julai'a Hotel and Resort
Reference: Change Order Number Three (3)

PARTICULARS

Subcontract number S100310 for accommodation on KBRII employees was awarded to "Kempinski Julai'a Hotel and Resort" on 30 September 2003, for a period of three (3) months.

Troy Miller, the Billeting Manager contacted me on 23 November 03 and informed me that requisition for additional 10 four bedroom chalets at the same resort was submitted for approval and that the chalets were needed from 1 December 03, for a period of one month.

Requisition number IG03525 was received on our office late on 1 December 03. The Manager of the Hotel was notified that we finally received approved funds for the additional chalets. Their best prices and availability for the 10 different types of chalets were requested, so a Change Order to the existing Subcontract could be issued in timely manner and the employees could be moved in the resort on 2 December 03. The Manager of the resort sent the proposal, stating that 8 chalets were available at the moment, at the following rates:
Total of five (5) Amwaj chalets - 115.000 KWD + 15% service charge per night and
Total of three (3) Jude chalets – 95.000 KWD + 15% service charge

The Amwaj chalets are more expensive than the Jude chalets and the four bedroom chalets that are already occupied by our employees, because they are with sea view. Although the 8 additional chalets are four bedroom, five residents can stay in them.

Change Order Number Three (3) was administered to add additional chalets, incorporate daily rate for lease of Amwaj chalet, add funds and increase the total NTE amount of the Subcontract and it's in best interest of Kellogg Brown & Root International, Inc. and the client to. The prices are determined to be fair and reasonable, as identified in the Price Reasonableness Memo (filed under Tab 3 of this file).

Eleonora Spasovska
Subcontract Administrator

Attachments: 1. Email correspondence with Kempinski
2. Email correspondence with Troy Miller-Billeting Manager
3. Email correspondence with Randy Webb-Deputy Project Manager

Chairman TOM DAVIS. Without objection.

Mrs. BLACKBURN. In the written and oral testimony you have provided for the committee, you state that it cost $110 to house one KBR employee per day at the Kempinski Hotel. You provided, through the minority, a copy of what seems to be the subcontract between KBR and the Kempinski Hotel, and I will enter those records so we have that.

And looking at the subcontract, it seems that the hotel rooms were priced per room and not per employee. And as I said before, the committee expects to hear testimony later in the hearing stating that as many as five people stayed in the rooms.

Would you agree that if the rooms were charged per night regardless of the number of occupants and that several employees shared many rooms, that your cost estimate would be high?

Ms. DEYOUNG. I would ask that you have line-for-line documentation of every instance where they were paying for "five persons per room." They were five per villa.

Mrs. BLACKBURN. I would like you to answer the questions as they are asked.

Ms. DEYOUNG. If that was true, I would say yes, but it is not true.

Mrs. BLACKBURN. Let's talk about soft drinks.

Your second allegation concerns wasteful spending on a contract to provide our soldiers with soda. You allege that a subcontractor charged KBR for 37,200 cases of soda per month at $1.50 per case and delivered 37,200 cans of soda instead. You believe that KBR failed to maintain adequate quality control over the goods and services it was receiving from subcontractors; isn't that correct?

Ms. DEYOUNG. That is correct.

Mrs. BLACKBURN. It is my understanding after reviewing the subcontract, and I am not an expert in contracting, that the subcontract did not specifically call for cases or even cans of soda. The subcontract seems to indicate that the subcontractor, La Nouvelle, was required to provide up to 1,000 soldiers per day with a bag that contained two cans of soda, 2 pounds of ice and nonglass cups.

Given what the subcontract provides, how did you arrive at $1.50 per case versus the $1.50 per can prices?

Ms. DEYOUNG. I arrived at that by taking the logs which you have in your records and doing the math.

Now, as I pointed out, if the contract had been done according to the terms, the payment was still inflated by two to three times what it should have been. You have the logs, and if you compare the logs to the actual statement, you can see. Anybody who has done—I have been a restaurant manager.

Mrs. BLACKBURN. "Cases" is not mentioned anywhere on this, and I understand that KBR was still unsatisfied with La Nouvelle's performance of the subcontract. And I expect we are going to hear testimony from the second panel that KBR suspended further payment and withheld over $110,000 in payments on this specific soda contract.

Now, you have already said that you did not believe that KBR was keeping its subcontractors accountable, correct?

Ms. DEYOUNG. I'm sorry?

Mrs. BLACKBURN. You said you did not think that KBR was keeping its subcontractors accountable?

Ms. DEYOUNG. That is a fact.

Mrs. BLACKBURN. Wouldn't you agree that if, in fact, KBR withheld payment from La Nouvelle as a result of La Nouvelle's incomplete performance on the contract that KBR was, in fact, ensuring that money wasn't being wasted for services that were not received?

Ms. DEYOUNG. When I brought that contract to the investigating team, I was ridiculed for an extended period of time; and after a week, when I persisted and insisted that this was just one example of how——

Mrs. BLACKBURN. Would you agree that the money was withheld?

Ms. DEYOUNG. The 4 months that I brought to them were paid. I have no knowledge—until the day that I left, until the testimony was made public, I had no knowledge that they had corrected it.

Chairman TOM DAVIS. Time has expired.

Did you share this with government auditors?

Ms. DEYOUNG. I'm sorry?

Chairman TOM DAVIS. Did you share this information with the government auditors?

Ms. DEYOUNG. I did not. This instance I shared with the Tiger Team investigative team and with management.

Chairman TOM DAVIS. The only people, outside of Halliburton and KBR, that you shared this with was with this committee?

Ms. DEYOUNG. Yes.

Chairman TOM DAVIS. Not to government auditors and so on that would be auditing these contracts?

Ms. DEYOUNG. No.

Chairman TOM DAVIS. Mr. Waxman, you are recognized for 30 minutes.

Mr. WAXMAN. I want to thank you for being here. You are doing a service, but you are feeling a discomfort from the questions that I have been hearing asked of you. You would think with the kind of questions that you have had that you have made all this up. I guess that's what the Republicans are trying to suggest.

It was interesting also from the last questions, she talked about specifics of what we are going to hear from the next panel, the Halliburton panelists. Well, this sounds like the Republicans had a private meeting with the Halliburton witnesses to go over what they're going to say. We weren't invited to that meeting, but we have tried to work together with the staffs on both sides to interview witnesses. But I want to go through some points, because obviously you didn't make all this up.

Since last December, government auditors have produced a series of reports that have found widespread, systemic problems with every aspect of Halliburton's work in Iraq, from accounting and billing practices to subcontractor management to exorbitant overcharging. And I am going to list a few of these.

In December, the Defense Contract Audit Agency prepared a draft audit that found Halliburton was overcharging for the gasoline it was importing from Kuwait. The draft report found $61 million in overcharges. DCAA concluded that Halliburton had not

demonstrated that they did an adequate subcontract pricing evaluation prior to award of the Altamira contract.

On December 31, the auditor at DCAA issued a flash report concluding that Halliburton's cost estimating system was deficient and that a $2.7 billion Halliburton proposal did not contain accurate, current and complete data regarding subcontractor costs. DCAA concluded the estimating deficiency is not a one-time occurrence; it's systemic.

In January, the DCAA review warned agencies throughout the Pentagon that they should not negotiate any further contracts with Halliburton until they check with DCAA to make sure these problems were addressed.

In May, DCAA examined Halliburton billing practices. This audit found systemic deficiencies in the way Halliburton prepares and submits its bills to the Federal Government.

In June, the Inspector General of the Coalition Provisional Authority issued an audit that found that Halliburton was overcharging for unauthorized and unnecessary expenses at a five-star hotel in Kuwait. That was the Inspector General of the Coalition Provisional Authority, reporting on the same example that you have given us, Ms. deYoung.

And just yesterday, GAO completed its audit and GAO found a pattern of recurring problems with almost every aspect of Halliburton's work on the LOGCAP contract to supply the troops with essential services. And GAO raised problems with cost control, subcontracts, and a host of other areas.

That is six audits by three different independent auditors, all of whom reached the same conclusion: Halliburton has been repeatedly overcharging and overbilling the U.S. taxpayers.

And I ask, Mr. Chairman, that these audits be made part of the hearing record.

Chairman TOM DAVIS. Absolutely. It will be put in the hearing record.

[NOTE.—The report entitled, "Military Operations, DOD's Extensive Use of Logistics Support Contracts Requires Strengthened Oversight," may be found in committee files.]

[The information referred to follows:]

CENTRAL REGION
ARLINGTON BRANCH OFFICE
DEFENSE CONTRACT AUDIT AGENCY
1201 NORTH WATSON ROAD, SUITE 174
ARLINGTON, TX 76006-6223

IN REPLY REFER TO
3311 820.5/keb

January 13, 2004

MEMORANDUM FOR CORPORATE ADMINISTRATIVE CONTRACTING OFFICER, DEFENSE CONTRACT MANAGEMENT AGENCY SAN ANTONIO (DCMAW-GEHC), 4100 CLINTON DRIVE, MAIL DROP 01-660, HOUSTON, TEXAS 77020

SUBJECT: Status of Brown & Root Services (BRS) Estimating System Internal Controls

During the summer of 2002, DCAA conducted a full review of BRS's estimating system to assure controls were adequate to provide estimated costs that are reasonable, compliant with applicable laws and regulations, and subject to applicable financial control systems, and to evaluate BRS's compliance with the system's internal control requirements. Audit Report Number 3521-2001D24010001 was issued on August 20, 2002 which concluded BRS's estimating system and related internal control policies and procedures were adequate.

DCAA generally cycles internal control reviews on the 10 major contractor systems (e.g. estimating, accounting, labor, billing, budgeting, compensation, material, purchasing, EDP, Indirect/ODC) every three to four years. Based on this cycle, we were not scheduled to evaluate BRS's estimating system until FY 2005. However, since we issued the August 2002 audit report, conditions have dramatically changed. Operation Iraqi Freedom and significant increases in contract requirements to support the reconstruction of Iraq have resulted in the significant growth in the volume and dollar value of proposals issued by BRS. Presently, we are auditing five task order proposals proposed at approximately $2.1 billion. Based on the government developed definitization schedule, the U.S. Army Field Support Command, Rock Island, Illinois is expecting BRS to submit 27 proposals between January 9, 2004 and July 2, 2004 at a rate of approximately one per week.

The purpose of this memorandum is to inform you DCAA no longer believes the opinion expressed on August 20, 2002 is accurate. Accordingly, we have initiated a full review of the BRS estimating system. The field work for this system review is scheduled to be completed by February 29, 2004. We are also in the process of conducting a subcontract management operations audit to identify process improvements that will assist BRS in implementing corrective action.

Based on proposal evaluations over the past three months, we consider BRS's estimates in the area of subcontracts to be inadequate. Our findings and recommendations with respect to our evaluation of the $2.7 billion Task Order 59 proposal for Contract Number DAAA09-02-D-0007 were reported to you in our Flash Report on Estimating System Deficiencies dated December 31, 2003 (copy attached). Specifically,

- BRS's proposal did not contain current, accurate, and complete data regarding subcontract costs resulting in an approximate $67 million overstatement of proposed costs;

- BRS did not disclose the termination of two subcontracts, proposed at $70 million, with KCPC/Morris for food services at sites C-1 and C-2. These two subcontracts were the basis for over $1 billion of projected food service costs for 26 sites. The proposal submitted to the Government on October 7, 2003 made no mention of the actual negotiated values with KCPC/Morris nor did BRS inform the government they had terminated the KCPC/Morris subcontract for default on or around July 31, 2003 and;

- BRS's proposal did not comply with the requirements of FAR 15.408, Table 15-2. Among other things, BRS did not (i) include a consolidated spreadsheet for proposed subcontract and equipment costs and (ii) provide or conduct cost analysis on sole-source subcontracts.

Our findings and recommendations with respect to our evaluation of the $347.7 million Task Order 61 proposal for Contract Number DAAA09-02-D-0007 were reported to the Procurement Contracting Officer, Headquarters, U.S. Army Field Support Command in our December 15, 2003 memorandum. Specifically,

- BRS did not include a summary of their cost analysis and a copy of cost or pricing data in their proposal for prospective subcontractors exceeding $10 million or more than 10 percent of BRS's proposed price as required by FAR 15.408, Table 15-2;

- Detailed support contained in procurement files in Kuwait did not reconcile to amounts contained in BRS's proposal;

- BRS did not clearly identify the basis of estimates for $20.7 million proposed for Container Living Spaces under a Master Agreement and;

- Procurement files in Kuwait supporting $25.1 million proposed for power generator tents were not readily available.

As a result of these deficiencies, we issued a memorandum to the Procurement Contracting Officer, U.S. Army Field Support Command, recommending proposals for Task Orders 59 and 61 be returned to BRS as inadequate. The delay associated with returning inadequate proposals increases government resources required to support the pre-award acquisition process. It also decreases the government confidence in and reliance on the contractor estimating system.

3311 820.5/keb January 13, 2004
SUBJECT: Status of Brown & Root Services (BRS) Estimating System Internal Controls

In addition to the above, we identified four other Task Orders totaling $227M where BRS did not use current, accurate and complete cost or pricing data. Collectively, the deficiencies described above bring into question BRS's ability to consistently produce well-supported proposals that are acceptable as a basis for negotiation of fair and reasonable prices.

We recommend you contact us to ascertain the status of the BRS' estimating system prior to entering into future negotiations. Any comments or questions regarding this memorandum should be directed to Darlene G. Brown, Supervisory Auditor, at (713) 753-2142, fax (713) 753-2919 or e-mail darlene.brown@dcaa.mil.

Sincerely,

/Signed/
William F. Daneke
Branch Manager

Copy furnished
Distribution

FOR OFFICIAL USE ONLY

3311 820.5/keb January 13, 2004
SUBJECT: Status of Brown & Root Services (BRS) Estimating System Internal Controls

DISTRIBUTION

	E-mail Address
Procuring Contracting Officer Logistics Civil Augmentation Program HQ, U.S. Army Operations Support Command AMSOS-CCS, 1 Rock Island Arsenal Rock Island, IL 61299-6000	watkinsm@osc.army.mil
Procuring Contracting Officer Balkans Support Contract U.S. Army Corps of Engineers, Transatlantic Programs Center Attn: CETAC-PD-CT-L, P.O. Box 2250 201 Prince Frederick Dr. Winchester, VA 22604-1450	a.brian.brobson@tac01.usace.army.mil
USACE Fort Worth District ATTN: Mr. John H. Rodgers Contracting Division 819 Taylor Street, FM 2A19 P. O. Box 17300 Fort Worth, TX 76102-0300	john.h.rogers@swj.usace.army.mil
Administrative Contracting Officer Defense Contract Management Agency International DCMA Southern Europe (Germany) CMR 410 Box 761 APO AE 09096	slantz@dcmdi.dcma.mil

DEFENSE CONTRACT AUDIT AGENCY

AUDIT REPORT NO. 3311-2004K24020001

December 31, 2003

PREPARED FOR: Corporate Administrative Contracting Officer
Defense Contract Management Agency San Antonio
ATTN: Catherina Ignacio
4100 Clinton Drive, Mail Drop 01-660
Houston, Texas 77020-6237

PREPARED BY: Arlington Branch Office
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4100 Clinton Drive Bldg. 1 Rm. B-2
Houston, Texas 77020-6237
Telephone No. (713) 753-2167
FAX No. (713) 753-2919
E-mail Address dcaa-fao3318@dcaa.mil

SUBJECT: Flash Report on Estimating System Deficiency Found in the Proposal for Contract No. DAAA09-02-D-0007, Task Order No. 59

CONTRACTOR: Brown & Root Services (BRS)
A Division of Kellogg Brown and Root, Inc.
4100 Clinton Dr.
Government Compliance Building 1 (648)
Houston, TX 77020-6237

REPORT RELEASE RESTRICTIONS: See Page 13

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Audit Report No. 3311-2004K24020001

SUBJECT OF AUDIT

Our price proposal audits include determining if Brown and Root Services (BRS) consistently complies with established estimating system internal controls for developing accurate, current and complete cost estimates. Consistent application of sound estimating procedures should reduce instances of defective pricing and facilitate audit and evaluation of the contractor's proposals submitted in connection with government procurement actions.

SCOPE OF AUDIT

Our examination was limited to certain contractor estimating practices used in preparing its proposal submitted in connection with Contract No. DAAA09-02-D-0007, Task Order No. 59. We did not perform sufficient audit procedures to constitute an examination of all applicable estimating system internal controls in accordance with generally accepted government auditing standards.

RESULTS OF AUDIT

Certain contractor estimating practices used in preparing its proposal submitted in connection with Contract No. DAAA09-02-D-0007, Task Order No. 59, require corrective action to improve the reliability of future cost estimates. During our examination of the proposal, we noted certain significant deficiencies in complying with the Federal Acquisition Regulations (FAR), Defense Federal Acquisition Regulations Supplement (DFARS) and BRS' Estimating Manual. In our judgment, these deficiencies could adversely affect the organization's ability to propose subcontract costs in a manner consistent with applicable government contract laws and regulations. This condition is detailed in the Statement of Condition and Recommendation below.

STATEMENT OF CONDITION AND RECOMMENDATION

1. Condition

Based on our preliminary audit, we noted BRS did not use the most current, accurate and complete cost or pricing data available prior to the proposal submission to estimate subcontract cost proposed for Contract No. DAAA09-02-D-0007, Task Order No. 59. The proposed costs for Task Order No. 59 (thru Change Order 4) are approximately $2.7 billion of which approximately $1.7 billion relates to proposed subcontract costs. Specifically, the proposal did not contain current, accurate, and complete data regarding subcontract costs. For instance, BRS proposed $208.8 million for food services at seven sites in their October 7, 2003 proposal without disclosing, referencing, or mentioning the fact they had already issued subcontracts for these sites in June through August 2003 totaling $141.5 million. As such, based on our computation, subcontract costs for the seven sites alone were overstated by $67.3 million as detailed in Appendix 1, page 14. In addition, BRS did not disclose the termination of two subcontracts, proposed at $70 million, with KCPC/Morris for food services at sites C-1 and C-2.

These two subcontracts were the basis for over $1 billion of projected food service costs for 26 sites. The proposal submitted to the Government on October 7, 2003 made no mention of the actual negotiated values with KCPC/Morris nor did BRS inform the government they had terminated the KCPC/Morris subcontract for default on or around July 31, 2003.

In our opinion, we believe the deficiencies described above and detailed in Appendix 1 represent indicators of potentially significant estimating deficiencies as described in DFARS 215.407-5-70 (d) (3). Specifically, BRS estimators did not utilize relevant historical experience (e.g. use actual subcontracts issued) in preparing their estimates for subcontract food service costs. Also, management reviews of the proposal failed to identify data readily available to the company was not used in the proposal submitted to the Government.

We also found the proposal for Contract No. DAAA09-02-D-0007, Task Order No. 59 does not comply with the requirements of FAR 15.408, Table 15-2. Specifically, FAR 15.408, Table 15-2 requires:

- The contractor to submit, with its proposal, cost or pricing data (that is, data that are verifiable and factual and otherwise as defined at FAR 2.101).
- the contractor to provide a consolidated priced summary of individual material quantities included in the various tasks, orders, or contract line items being proposed and the basis for pricing (vendor quotes, invoice prices, etc.).
- the contractor to provide data showing the degree of competition and the basis for establishing the source and reasonableness of price for those acquisitions (such as subcontracts, purchase orders, material order, etc.) exceeding, or expected to exceed, the appropriate threshold;
- the contractor to conduct price analyses of all subcontractor proposals and to include the analyses as part of its own cost or pricing data submissions for subcontracts expected to exceed the appropriate threshold. The contractor did not perform prior to the award, the price analysis as required by FAR 15.404-3 to determine the reasonableness of subcontractor's proposed cost on the following purchases:

Subcontract No.	Subcontractor	Date of Subcontractor Proposal	Award Date
KU-MA00009, Work Release #3	Daoud & Partners	July 1, 2003	July 12, 2003
KU-MA00007, Work Release #3	LaNouvelle/ESS	June 25, 2003	July 4, 2003

- the contractor to conduct cost analyses for all subcontracts when cost or pricing data are submitted by the subcontractor;
- The judgmental factors applied and the mathematical or other methods used in the estimate, including those used in projecting from known data;

- the contractor to include the name and address of the offeror (subcontractor) in its proposal; and

- the contractor to include the type of subcontract action in its proposal (that is, new contract, change order, price revision/redetermination, letter contract, unpriced order, or other).

In addition, we determined the contractor is in noncompliance with its Cost Estimating Manual (BRS Government Operations Cost Estimating Manual Section 17.0 - Subcontract Costs, dated July 2002) which also addresses the items described above, specifically those related to documentation of recommended subcontractor source selection and performance of subcontract cost/price analyses.

2. Recommendation

The estimating system deficiencies described above and in Appendix 1 resulted in the loss of significant audit resources both in Houston and Kuwait. Based on these preliminary findings, DCAA recommended to the PCO the proposal be returned to the contractor for revision. A commitment was obtained from BRS on November 13, 2003 stating they would formally revise their proposal using a November 7, 2003 cutoff date. The contractor's failure to provide current cost or pricing data has also resulted in delays in definitizing the Task Order No. 59 procurement.

We recommend the contractor take corrective action to ensure all proposals, which include subcontract costs comply with FAR 15.408, Table 15-2, and its Cost Estimating Manual, Section 17.0, Subcontract Costs. If the contractor does not within a reasonable time period correct the proposal inadequacies we also recommend withholding of the award until such time as the contractor complies with the requirements in FAR and provides a revised proposal permitting an adequate evaluation of the proposed subcontract prices.

3. Contractor's Reaction

In their response, dated December 4, 2003, BRS agreed it failed to use current, accurate, and complete information in estimating proposed subcontract costs for Contract No. DAAA09-02-D-0007, Task Order (TO) No. 59. However, BRS disagrees with DCAA on whether this constitutes a significant estimating system deficiency. BRS states this was a unique situation due to the large cost, amount of data, and volume of effort associated with the TO No. 59 proposal. Even though BRS does not think the condition is a significant deficiency, it reported a $37 million difference between the proposed subcontract costs and updated estimated amounts using more current data instead of the $67.3 million reported in DCAA's draft audit report. Further, in an attempt to avoid this issue on future LOGCAP III proposals, BRS agrees to establish a "cut-off date", and perform a "sweep" in an attempt to identify the most current information available which BRS will incorporate into its cost proposals for subcontracts equal to or exceeding $550,000.

BRS also responds to DCAA's findings that:

a. It agrees to provide DCAA with consolidated spreadsheets for subcontracts, equipment, other direct costs (ODC) and materials. In addition, BRS has agreed to provide clearer explanations in their proposals for the judgmental factors applied, the mathematical or other methods used, and subcontractor names, addresses, and other information to be included in the consolidated subcontract spreadsheet.

b. It disagrees with DCAA's position in respect to BRS failing to perform price analyses, prior to the award, as required by FAR 15.404-3, on master procurement agreements KU-MA00009, Work Release #3 and KU-MA00007, Work Release #3. BRS indicates in performing a price analysis FAR 15.404-1(b) (2) requires a comparison of competitive offers or the comparison of previously proposed prices and current prices for same or similar items. BRS stated it met these tests.

c. No cost analysis was required in the evaluation of the proposed subcontractors on Task Order No. 59, since BRS strives to obtain competition or obtain commercial items to the maximum extent possible.

d. Estimators have the latitude to depart from the requirements identified in BRS' Cost Estimating Manual since the manual states the guidelines do not cover every possible type of cost or fixed-price arrangement available to the Government and allows BRS to tailor and implement their procedures to the individual project contract requirements as established by the various Government Clients.

See Appendix 2 for a copy of BRS's complete response.

4. Auditor's Comments

BRS has agreed to correct most of the deficiencies identified in our condition. However, we do not believe these deficiencies are insignificant as opined by BRS.

The contractor has agreed in its response it failed to use current, accurate, and complete information in estimating proposed subcontract costs for Contract No. DAAA09-02-D-0007, Task Order No. 59. This failure is significant because Task Order No. 59 has an estimated total price of $2.7 billion, and the subcontract costs constitute approximately $1.7 billion of the proposed costs. Specifically, in our analysis shown in Appendix 1, we determined the difference in proposed amounts for food services as compared to negotiated subcontract amounts for seven purchases portrayed a material difference of $67.3 million. These seven purchases were based on the negotiated number of troops estimated to be fed per day. In contrast, BRS's analysis was based on comparing proposed versus negotiated amounts for all 26 sites where food service would be provided. However, BRS did not use the negotiated troop strength with its vendors as the basis for its updated proposed amounts. Instead, it proposed the number of troops from its original proposal. For example at site B-1, BRS negotiated with the vendor 3,800 troops were to be fed but bid 4,800. Also, the 3,800 troops negotiated with the vendor and used by DCAA

agree with the original statement of work. The impact of BRS's approach for site B-1 compared to the DCAA approach shows a difference of $6.4 million as shown below:

Analysis By	No. of Days	No. of Troops	Daily Cost	Total Cost
BRS	183	4,800	$35.00	$30,744,000
DCAA	183	3,800	$35.00	$24,339,000
Cost Difference				$ 6,405,000

As the foregoing example shows, BRS did not use the negotiated number of troops which agrees with the original statement of work to compute its revised proposal amount. Also, BRS did not provide supporting data to show its proposed number of troops was based on current information. The result is BRS has proposed more subcontract costs than the data supports, thus its overall analysis shows a $37 million difference between the original proposed and updated proposed amounts for subcontracts. However, a review of BRS's revised proposal for Task Order No. 59 indicates proposed subcontract costs were reduced by approximately $195 million for food services which is in accord with the DCAA position the condition cited above represents a significant estimating system deficiency.

Another important aspect making this a significant estimating system deficiency is the recurring nature of the deficiency. The DCAA Iraq Branch Office has determined BRS failed to utilize the most current, accurate and complete information in estimating proposed subcontract costs on other task order proposals under the LOGCAP III contract. The following schedule identifies other task orders and associated proposed costs for which the contractor did not use the most current, accurate, and complete cost or pricing data available prior to the proposal submission for estimating subcontract costs:

DAAA09-02-D-0007 Task Order Nos.	Proposed Subcontractor Costs
Proposal for Task Order 56	$ 28,114,216
Proposal for Task Order 61	$ 178,478,936
Proposal for Task Order 63	$ 3,257,240
Proposal for Task Order 64	$ 17,463,315
Total	$227,313,707

The result is the estimating deficiency is not a one time occurrence; it is systemic. Therefore, due to the materiality of the issue and its systemic nature, we believe by not using current, accurate, and complete information in estimating proposed subcontract cost, the cited condition is a significant estimating system deficiency.

In reference to items 1 and 2 above, we concur with BRS' response.

In reference to item 3 above, we determined the contractor was required to perform cost analysis. Several subcontracts were awarded based on sole source justification for food services. For instance, LaNouvelle/ESS was awarded a subcontract at site C-1 based upon sole source justification. The bid was for $44.6 million for food services for 180 days. Support provided

included a bid tabulation table, a justification memo, and a quote. The bid tabulation shows one bidder, LaNouvelle/ESS, who was awarded the contract based on sole-source justification. Even though the bid tabulation shows a comparison was performed to a prior purchase, no cost analysis was provided and no reference was made in the justification memo that a cost analysis was performed. This does not comply with the provisions of FAR 15.404-3 (b) (1) and FAR 15.408, Table 15-2, II Cost Elements, Paragraph A, which states contractors are to conduct appropriate cost analyses for all subcontracts when cost or pricing data are submitted by the subcontractor.

In reference to item 4 above, BRS' response implies the estimating manual does not apply to the condition cited above because the manual does not cover every possible contractual arrangement available to the government and the procedures can be tailored to individual project requirements. However, in this case BRS' estimating manual specifically addresses subcontract costs. Our review of the estimating procedures regarding subcontract requirements states BRS should "obtain all required cost/pricing data, including required certifications from the proposed vendor/subcontractor(s) as required by the RFP and certainly prior to agreement on price." This procedure is in accord with FAR and to tailor it for Task Order No. 59 is unnecessary. In addition, BRS provides no basis for not following company estimating procedures. BRS does not identify any extenuating circumstances warranting a major departure from its estimating procedures and the FAR. Neither does BRS provide justification that exempts it from following its own estimating procedures. BRS also does not identify any project-specific estimating procedures which it is relying on to compile estimated subcontract and other proposed costs. Therefore, since BRS' estimating manual addresses subcontract costs and no valid reason for deviating from the manual was provided, we believe BRS should comply with its own Cost Estimating Manual.

In summary, we believe our recommendations above should be fully implemented by BRS. The company is expected to comply with all provisions of FAR, including FAR 15.408, Table 15.2, and the provisions of its estimating manual.

This report is limited to the cited deficiency. Accordingly, we express no opinion on the adequacy of the contractor's estimating system internal controls taken as a whole.

Within approximately three months we will perform a follow-up audit on the contractor's estimating system internal controls to determine the status of the cited deficiencies, the status of the contractor's corrective action, and the impact of the deficiencies on the overall adequacy of the contractor's estimating system internal controls taken as a whole.

We discussed our findings with Mr. William Walter, Director, Government Compliance, BRS, Government Operations, in a teleconference on November 13, 2003. We provided the contractor a draft copy of this report on November 17, 2003. The contractor's written response is included in its entirety in Appendix 2.

CONTRACTOR ORGANIZATION AND SYSTEMS

1. Organization

Kellogg Brown & Root, Inc. (KBR), also known as the Engineering and Construction Group (E&C), is one of the two operating subsidiaries of Halliburton. The other subsidiary is Halliburton's Energy Services Group (ESG). KBR consists of several segments which include Brown & Root Services (BRS) and other KBR Commercial units. The legal structure of Halliburton is different from its operational structure. Halliburton owns all the stock of DII Industries, LLC (DII). DII in turn owns all the stock of numerous Halliburton legal entities including KBR.

Halliburton's segments are organized around the products and services provided to the customers they serve. The ESG provides a broad array of products and services to upstream oil and gas customers worldwide, ranging from the manufacturing of drill bits and other down hole and completion tools and pressure pumping services to subsea engineering. The E&C under KBR deals with large-scale construction projects including construction and designing of oil and gas processing and refining plants, production facilities, and onshore and offshore pipelines. KBR's non-energy business meets the engineering and construction needs of governments and civil infrastructure customers.

KBR revenues were approximately $5.736 billion (B) in contractor fiscal year (CFY) 2002 and $5.235B in CFY 2001, or about 46 percent of Halliburton Company's total revenue of $12.572B for CFY 2002 and about 40 percent of $13.046B for CFY 2001. KBR's operating loss for CFY 2002 was $685 million (M) and income for CFY 2001 was $111M. Halliburton's total operating loss for CFY 2002 was $112M and operating income for CFY 2001 was $1.084B.

BRS consists of two operating segments that perform government contracts, Brown & Root Service Operations (BRSO) and KBR Civil Infrastructure (KBRCI). BRSO is the primary government segment that provides engineering, construction, operation, and maintenance services for the Air Force, Army, Navy, and NASA. It also provides logistical support services for the U.S. troops in foreign countries through contracts with the Army Corps of Engineers and Army Material Command. BRSO also operates as Management Logistics, Inc. (MLI) to perform projects with a union-represented work force.

KBRCI provides consulting and civil engineering services primarily for commercial projects. Projects include highways, bridges, stadiums, aviation and water and wastewater infrastructure, facilities modification, and on-call construction.

BRSO's CFY 2002 estimated costs incurred were approximately $566M and for CFY 2001 costs incurred were approximately $579M. For CFY 2003, costs are projected to increase to over $1 billion. In CFY 2001, BRSO had 95 percent federal-government participation, of which 63 percent was cost reimbursable, 30 percent fixed-price work, and 2 percent time and material. KBRCI reported CFY 2001 revenues of $95M with about 18 percent federal-government participation. Government participation was 10, 5, and 3 percent for cost

reimbursable, time and material, and fixed-price contracts, respectively. The remaining 82 percent of KBRCI's costs was incurred on commercial contracts.

Effective in CFY 2003 a new subsidiary, KBR Services, Inc. (KBRSI), has been formed to include most government contracts. Under KBRSI, BRSO and KBRCI will remain the operating segments for the performance of government contracts.

In CFY 2002, corporate home office expenses such as executive management, accounting, communications, human resources, information technology, legal, risk management, and taxes were allocated to operating segments using the three-factor formula. Effective January 2003, a majority of corporate expenses were specifically identified either to KBR or ESG. The only expenses currently allocated using the three-factor formula from the Corporate home office are HALCO 21 costs relating to SAP software implementation and state taxes. Specific Corporate costs now identified to KBR are charged into the Intermediate Management III (IM-III) Home Office. IM-III provides management support, accounting, and business acquisition functions for all KBR's business units. The residual expenses for these services are allocated to the following business units using the three-factor formula: BRSO, KBRCI, Government Operations United Kingdom (UK) and Asia Pacific (AP), Commercial Infrastructure Americas, Commercial Infrastructure United Kingdom and Asia Pacific, and KBR Other Commercial.

Government OPS Intermediate Management II (IM-II) Home Office provides global business unit management and accounting and sales and marketing functions. Residual expenses are allocated to BRSO and Government Operations UK and AP using the three-factor formula.

Americas BRS Intermediate Management I (BRS IM-I) Home Office provides various functions including accounting, human resources, information technology, sales and marketing, government compliance, quality, and contract administration. The costs associated with these functions are allocated to only BRSO except for government compliance which is also allocated to KBRCI using the three-factor formula.

Infrastructure Intermediate Management II Home Office provides business unit management and accounting and finance to the Infrastructure business unit. Residual expenses are allocated to KBRCI and Commercial Infrastructure United Kingdom and Asia Pacific.

The Americas Infrastructure Intermediate Management I Home Office provides business unit management, accounting and finance, and chief engineer functions to the America Infrastructure activities. Residual expenses are allocated only to KBRCI.

2. Systems

a. Accounting System

We are currently performing a comprehensive review of the accounting system and expect to issue the report in the near future. KBR's accounting period is from January 1 to December 31. KBR's accounting system was developed in-house in 1983 and was specifically

designed for commercial use. The accounting system accumulates direct cost under individual project numbers but does not allocate indirect costs to its final cost objective. Therefore, KBR's Government Compliance department develops its indirect cost pools and bases from data runs generated by the accounting system and as required they adjust the financial data to comply with FAR and CAS requirements.

BRSO has one overhead pool and a G&A pool that allocates to final cost objectives. Overhead pool costs consist of indirect labor and associated burdens and benefits, consultants, relocation, travel, facility costs, supplies, data processing, engineering services, professional services, and other indirect type expenses. The Overhead pool costs are allocated over a prime cost base consisting of direct labor, fringe benefits, materials, equipment, subcontractor, and other direct cost. The G&A pool consist of costs from home office allocations and bid and proposal costs. Home office costs consist of allocations from Intermediate Management III, Intermediate Management II, and Intermediate Management I. The G&A pool costs are allocated over a total cost input (TCI) base.

KBRCI has two overhead pools, a use and occupancy pool, and a G&A pool. The two overhead pools, the Professional Services and Construction, are organized by function. Both overhead pools consist of indirect labor and associated burdens and benefits, consultants, relocation, travel, supplies, data processing, engineering services, professional services, and other indirect type expenses. The use and occupancy pool consists of communications and facility costs. The overhead pools and use and occupancy pool costs are allocated using a direct labor base. The G&A pool consist of costs from home office allocations and bid and proposal costs. Home office costs consist of allocations from Intermediate Management III, Intermediate Management I, Infrastructure Intermediate Management II, and Infrastructure Intermediate Management I. The G&A pool costs are allocated over a direct labor base.

b. Estimating System

BRS' estimating system was reported as generally adequate in Audit Report No. 3521-2001D24010001, dated August 20, 2002. However, due to the condition cited in this report, we assess the risk associated with proposed subcontract costs to be high. For all other elements of costs, we assess risk as low in relation to contract pricing actions.

BRS currently has about 18 employees who work in the Estimating Department. The Estimating Department begins preparing a proposal after the KBR Interest Review Committee, usually consisting of Business Development, Legal and Contract functions, has evaluated and decided to bid on a request for a proposal. Estimating is responsible for preparing the proposal, including the development of direct cost estimates and applying the latest indirect rates and factors. BRS' detailed estimating policies and procedures are described in its "BRS Cost Estimating Manual – Revision 12/1/2000."

c. Procurement Policies, Procedures, and Practices

The ACO extended approval of KBR's Government Purchasing System effective April 30, 2001. The approval will continue in effect until the ACO withdraws the approval.

d. Compensation System

DCAA considers BRS' compensation system adequate to provide reasonable employee compensation costs to government contracts in accordance with FAR 31.205-6(a) and FAR 31.205-6(b). BRS' compensation system is based on a flow of authority and incorporated periodic compliance reviews, including written policies and procedures, and training for compensation administration employees.

Audit Report No. 3311-2004K24020001

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AUDIT REPORT AUTHORIZED BY:

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Audit Report No. 3311-2004K24020001

RESTRICTIONS

1. Information contained in this audit report may be proprietary. It is not practical to identify during the conduct of the audit those elements of the data which are proprietary. Make proprietary determinations in the event of an external request for access. Consider the restrictions of 18 U.S.C. 1905 before releasing this information to the public.

2. Under the provisions of Title 32, Code of Federal Regulations, Part 290.7(b), DCAA will refer any Freedom of Information Act requests for audit reports received to the cognizant contracting agency for determination as to releasability and a direct response to the requestor.

3. Do not use the information contained in this audit report for purposes other than action on the subject of this audit without first discussing its applicability with the auditor.

APPENDIX 1

Listing of Subcontracts Awarded Prior to Issuance of Task Order No. 59 Proposal on October 7, 2003

Subcontract No.	Scope of Work/Site	Proposed Amount	Awarded Subcontract Amount	Difference	Award Date
KU-MA00009 Work Release 3	Food Service Camp Site C-5 (Gunner)	$ 24,906,081	$ 18,576,000	$ 6,330,081	July 12, 2003
KU-MA00007 Work Release 3	Food Service Camp Site D-6	26,064,504	17,581,046	8,483,458	July 4, 2003
KU-MA00003 Work Release 2	Food Service Camp Site E	46,336,896	12,806,852	33,530,044	June 19, 2003
KU-MA00007 Work Release 2	Food Service Camp Site C-3	27,802,137	24,793,193	3,008,944	June 19, 2003
KU-MA00009 Work Release 1	Food Service Camp Site B-1	27,802,137	23,940,000	3,862,137	July 1, 2003
KU-MA00007 Work Release 4	Food Service Camp Site D-7	19,693,181	16,348,870	3,344,311	July 4, 2003
KU-MA00004 Work Release 5	Food Service Camp Site H-2	36,212,284	27,470,707	8,741,577	August 6, 2003
	Total	$208,817,220	$141,516,668	$67,300,552	

APPENDIX 2

CONTRACTOR'S RESPONSE

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KBR

Government Operations, 1550 Wilson Boulevard, Suite 700, Arlington, Virginia 22209
(703) 526-7500 Fax (703) 526-7585

December 4, 2003

William F. Daneke
Branch Manager
Defense Contract Audit Agency
Arlington Branch Office
Arlington, TX 76006-6223

Dear Mr. Daneke:

The purpose of this letter is to respond to your draft audit report regarding the Task Order 59 cost proposal under Audit Report No. 3311–2004D24010001. Based on the comments contained in the report, we provide the following responses:

DCAA Comment #1: Based on our preliminary audit, we noted BRS did not use the most current, accurate and complete cost or pricing data available prior to the proposal submission to estimate subcontract cost proposed for Contract No. DAAA09-02-D-0007, Task Order No. 0059. The proposed costs for Task Order 59 (thru Change Order 4) are approximately $2.7 billion of which approximately $1.7 billion relates to proposed subcontract costs. Specifically, the proposal did not contain current, accurate, and complete data regarding subcontract costs. For instance, KBR proposed $208.8 million for food services at seven sites in their October 7, 2003 proposal without disclosing, referencing, or mentioning the fact they had already issued subcontracts for these sites in June – August 2003 totaling $141.5 million. As such, subcontract costs for the seven sites alone were overstated by $67.3 million. In addition, BRS did not disclose the termination of two subcontracts, proposed at $70 million, with KCPC/Morris for food services at sites C-1 and C-2. These two subcontracts were the basis for over $1 billion of projected food service costs for 26 sites. The proposal submitted to the Government on October 7, 2003 made no mention of the actual negotiated values with KCPC/Morris nor did BRS inform the government they had terminated the KCPC/Morris subcontract for default on or around July 31, 2003.

In our opinion, we believe the deficiencies described above and detailed on Attachment 1 represent indicators of potentially significant estimating deficiencies as described in DFARS 215.407-5-70 (d) (3). Specifically, BRS estimators did not utilize relevant historical experience (e.g. use actual subcontracts issued) in preparing their estimates for subcontract food service costs. Also, management reviews of the proposal failed to identify that data readily available to the company was not used in the proposal submitted to the Government.

KBR Response: KBR agrees with the DCAA position that in the initial preparation of the proposal for TO 59, we did not use current, accurate and complete information that was available for pricing of subcontracts.

There are many excuses and reasons available – but – in the end, KBR did not include the most current data in our proposal. During the audit of this proposal, DCAA raised this issue and requested that KBR provide current cost or pricing data on selected subcontracts by November 7, 2003. KBR prepared and provided the DCAA with a comprehensive package of current cost or pricing data regarding the issues raised regarding the proposed subcontract costs – by the due date. In the response, we disclosed the fact that the vendor used by the estimators as the basis of estimate was terminated for default by KBR.

Note: Based on the information provided to the DCAA, the difference between the proposed cost of total dining facility costs and the amount using the current, accurate and complete data provided was a total of $37M over a total food service cost proposed of $1,179M – a difference of 3% as opposed to the DCAA's calculation of $67.3M over 7 sites estimated at $208.8M – a difference of 32%.

Although the additional information demonstrates that the use of the single vendor price for the project produced an estimated value that was within 3% of the total, we concur with the DCAA that the estimators should have taken the steps to obtain the more current data obtained during our "sweep" required by the DCAA prior to November 7, 2003.

We would also like to take this time to identify that this issue is not a "significant estimating system deficiency" as stated in the DCAA draft report. Rather, this was a unique situation due to the significant cost, amount of data and volume of effort that was associated with the TO 59 proposal. With earlier proposals prepared on the LOGCAP program, this was not an issue identified by the DCAA. For non-contingency proposals such as Ft. Leonard Wood and Bluegrass issued earlier this year, these issues did not arise either.

To avoid this issue on future LOGCAP proposals, KBR will establish a "cut-off date", perform a "sweep" with procurement and other significant functions before the cost proposals are submitted in an attempt to identify, for those subcontracts that exceed $550,000, the most current information available which we will incorporate into the cost proposal.

DCAA Comment #2: We also found the proposal for Contract No. DAAA09-02-D-0007, Task Order No. 0059 does not comply with the requirements of FAR 15.408, Table 15-2. Specifically, FAR 15.408 Table 15-2 requires:

- the contractor to submit, with its proposal, cost or pricing data (that is, data that are verifiable and factual and otherwise as defined at FAR 2.101).
- the contractor to provide a consolidated priced summary of individual material quantities included in the various tasks, orders, or contract line items being proposed and the basis for pricing (vendor quotes, invoice prices, etc.).
- the contractor to provide data showing the degree of competition and the basis for establishing the source and reasonableness of price for those acquisitions (such as subcontracts, purchase orders, material order, etc.) exceeding, or expected to exceed, the appropriate threshold;

KBR Response: Based on discussions with the DCAA, these issues were raised by the auditor at the entrance conference for the TO59 proposal. At that time, KBR prepared a consolidated summary of the subcontractors proposed identifying if the subcontracts were competitively awarded or not. In future LOGCAP proposals, KBR agrees to provide the DCAA with consolidated spreadsheets for subcontracts, equipment, ODC's and materials which can be sorted by the auditor on a number of fields to facilitate their review.

DCAA Comment #3: [FAR 15.408 Table 15-2 requires:] the contractor to conduct price analyses of all subcontractor proposals and to include the analyses as part of its own cost or pricing data submissions for subcontracts expected to exceed the appropriate threshold. The contractor did not perform prior to the award, the price analysis as required by FAR 15.404-3 to determine the reasonableness of subcontractor's proposed cost on the following purchases:

Subcontract No.	Subcontractor	Date of Subcontractor Proposal	Award Date
KU-MA00009, Work Release #3	Daoud & Partners	July 1, 2003	July 12, 2003
KU-MA00007, Work Release #3	LaNouvelle/ESS	June 25, 2003	July 4, 2003

KBR Comment: KBR does not agree with the DCAA position. As discussed in our response on November 7, 2003, the KBR procurement staff used a multiple award ID\IQ proposal process which resulted in several bidders for the food service subcontracts. Based on the process of a multiple award process, there are generally multiple bidders for each site, however there may be times where only one bid is received. The procurement staff uses comparable bids on other site work releases to perform a price

reasonableness analysis. Per FAR 15.404-1(b)(2) the primary price analysis techniques include the comparison of competitive offers in response to the instant solicitation or the comparison of previously proposed prices and current proposed prices for the same or similar items. These tests were met by KBR procurement. Price is not the only factor involved in making an award decision as schedule and availability are also critical to the successful bidder.

DCAA Comment #4: [FAR 15.408 Table 15-2 requires:] the contractor to conduct cost analyses for all subcontracts when cost or pricing data are submitted by the subcontractor;

KBR Comment: No cost analysis was required in evaluation of the proposed subcontractors on this proposal. KBR strives to obtain competition or obtain commercial items to the maximum extent practical. If cost analysis is required per FAR 15.403, KBR procurement policies require cost analysis be performed and those results and analysis will be included in the procurement file which is available to the DCAA for review at the site of the procurement office performing the work.

DCAA Comment #5: [FAR 15.408 Table 15-2 requires:] The judgmental factors applied and the mathematical or other methods used in the estimate, including those used in projecting from known data;

KBR Comment: In the past, KBR provided brief explanations of factors and methods used in computing cost estimates and estimators assumed that the inclusion of a formula in an Excel® worksheet was satisfactory. As included in our November 7th submission. KBR will attempt to provide a clearer explanation in future cost proposals.

DCAA Comment #6: [FAR 15.408 Table 15-2 requires:] the contractor to include the name and address of the offeror (subcontractor) in its proposal; and the contractor to include the type of subcontract action in its proposal (that is, new contract, change order, price revision/redetermination, letter contract, unpriced order, or other).

KBR Comment: As discussed in response to DCAA Comment #2 above, this information, if available, will be included in the consolidated table of subcontracts.

DCAA Comment #7: In addition, we determined the contractor is in noncompliance with its Cost Estimating Manual (KBR Government Operations Cost Estimating Manual Section 17.0 - Subcontract Costs, dated July 2002) which also addresses the items described above, specifically those related to documentation of recommended subcontractor source selection and performance of subcontract cost/price analyses.

KBR Comment: The Managing Statement to the Cost Estimating manual states that the manual "guidelines are intended to provide general estimating procedures

normally found in Government contracts. However these guidelines are not intended to cover every possible type of cost or fixed-price arrangement available to the Government. These procedures should be tailored and implemented to the individual project contract requirements as established by the various Government Clients."

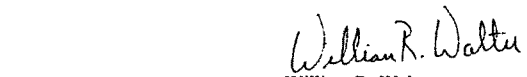
Further, FAR 15.403-5(b)(1) provides that a proposal can be submitted in the "format specified in FAR table 15-2 of FAR 15.408, specify an alternative format, or permit submission in the contractor's format." Since the beginning of the contract, and as a carryover from prior contingency contracts, the cost proposal format presented has been used for preparing cost proposals for contingency operations. Proposals submitted under this format have been audited and evaluated over the past 12 months. Accordingly, KBR has not had any reason to change the proposal format until the significant issues that TO59 generated.

KBR does not concur that with the DCAA position that this issue is a "significant estimating system deficiency" This situation was a unique situation due to the significant cost and volume of effort that was associated with the TO 59 proposal.

However, in meeting with DCAA auditors this morning, KBR proposed that we work together on the update to the TO59 to obtain an acceptable format and process for developing and evaluating this and future cost proposals under contingency programs. We look forward to achieving a mutually acceptable plan to move forward on this most important program.

Should you have any questions regarding this matter, please feel free to contact me at *bill.walter@halliburton.com*, at (713) 753-4931 or my cell phone (703) 627-1007.

Sincerely,



William R. Walter
Director, Government Compliance

cc: Mr. Gary Catt, Supervisory Auditor, DCAA
Ms. Catharina Ignacio, CACO, DCMA
Mr. Al Neffgen, Chief Operating Officer, KBRSI
Mr. Bob Herndon, Vice-President, KBRSI

APPENDIX 3

OTHER MATTERS TO BE REPORTED

Halliburton reported in its Securities and Exchange Commission (SEC) filing dated June 30, 2003 and on its corporate web site that in December 2002 it reached an agreement in principle to settle asbestos and silica litigation of claimants against its subsidiaries DII Industries and Kellogg Brown & Root and their current and former subsidiaries with United States operations. Subsequently, in 2003, DII Industries and Kellogg Brown & Root entered into a definitive written agreements finalizing the terms of the agreements in principle with attorneys representing more than 95% of the current asbestos and silica claimants. The settlement consists of up to $2.775 billion in cash (limited to this amount as of November 6, 2003), 59.5 million shares of Halliburton stock, and notes with a net present value for less than $100 million, or approximately $4 billion in total. The plan intends to resolve fully and permanently all personal injury asbestos and silica liabilities against the company for all present claims and future claims.

In addition, the company has entered into Chapter 11 Bankruptcy filings for Dresser Industries, Inc. and Kellogg Brown & Root. Halliburton Company, Halliburton Energy Services, Inc., Landmark Graphics Corporation, BRS's U.S. Government operations business and most other Halliburton subsidiaries will not be included in the filing. The Chapter 11 Bankruptcy filing has been "prepackaged" in that the company has already obtained agreement from all the affected creditor groups on the Plan. The company asserts that such Pre-packaged filings differ significantly from other Chapter 11 filings since the outcome is much more certain, because all affected parties have agreed in advance to the Plan of Reorganization. Contractor representatives indicate the company will remain financially strong, and all BRS contracts, which include government contracts, will be fully honored and all obligations performed. According to contractor representatives, there will be no impact to employees, all creditors will be paid in full, and there will be no effect on present or future projects. Also, a new subsidiary, BRS Services, Inc., would be formed to include all government contracts.

According to Halliburton June 30, 2003 SEC filing there were 425,000 open claims pending against Halliburton. Total open claims have increase by 78,000 since December 31, 2002. But Halliburton states it has factored all claims into the calculation of its asbestos liability. Halliburton asserts it manages asbestos claims to achieve settlement of valid claims for reasonable amounts. On November 18, 2003, DII Industries, Kellogg Brown & Root, and other affected subsidiaries have completed amendments to documents implementing the companies' planned asbestos and silica settlement and are mailing supplemental solicitation materials to asbestos and silica creditors in connection with voting on the amended plan of reorganization. The Company also announced that the proposed filing entities have set December 11, 2003 as the deadline for voting, or changing votes, on the proposed plan. Of the votes validly cast, over 98 percent of asbestos claimants and over 99 percent of silica claimants have voted to accept the proposed plan of reorganization. However, at this time, since all the requirements surrounding the bankruptcy have not been finalized, we do not know what effect, if any, this will have on the cost of government contracts.

DEFENSE CONTRACT AUDIT AGENCY

AUDIT REPORT NO. 3311-2002K11010001

May 13, 2004

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SUBJECT: Audit Report of Kellogg Brown and Root, Inc.
Billing System Internal Controls

CONTRACTOR: Kellogg Brown and Root, Inc.
ATTN: Government Compliance
4100 Clinton Drive, Mail Drop 01-660
Houston, TX 77020-6237

REPORT RELEASE RESTRICTIONS: See Page 24

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Audit Report No. 3311-2002K11010001

SUBJECT OF AUDIT

By submitting payment requests under government flexibly-priced and fixed-priced contracts, Kellogg Brown and Root Services, Inc. (KBR) asserts that its internal controls are adequate to provide reasonable assurance that:

- Applicable laws and regulations are complied with;
- The accounting system and cost data are reliable;
- Risk of misallocations and mischarges are minimized; and
- Contract allocations and charges are consistent with invoice procedures.

We have examined KBR Houston's billing system as of April 1, 2004, to assure that KBR's system of billing controls is adequate to provide billed costs that are reasonable, compliant with applicable laws and regulations, and subject to applicable financial control systems, and to evaluate KBR's' compliance with the system's internal control requirements. Our results of audit only cover the billing system processes in Houston, TX. We have not completed our testing of the accounting system which includes KBR's in-theatre accounting and accounts payables systems. The accounting system information coming from in-country addresses the adequacy of KBR's requisitioning, purchasing, and payment policies and procedures, which directly affect the billing of costs incurred in Kuwait and Iraq.

KBR is responsible for establishing and maintaining an adequate billing system. Our responsibility is to express an opinion on the adequacy of the billing system based on our examination.

EXECUTIVE SUMMARY

In our opinion, the contractor's billing system is inadequate in part. Our examination disclosed several deficiencies in KBR's billing system resulting in billings to the governments that are not prepared in accordance with applicable laws and regulations and contract terms. We also found system deficiencies resulting in material invoicing misstatements that are not prevented, detected and/or corrected in a timely manner. As a result, KBR is not authorized for direct billing and will be required to continue to provide all billings to DCAA for provisional approval prior to submission for payment. We recommend that KBR submit a detailed milestone plan for correcting the deficiencies cited in the report.

SIGNIFICANT ISSUES

1. Our audit has found KBR does not properly brief its contracts and the associated task orders. KBR's Contract Policy & Process, CA-S-03, dated August 29, 2002 states the contractor "shall develop a contract post award summary and the DCAA contract brief" as soon as possible but no later than three business days after contract award. Our audit found that KBR is not following its established procedure.

2. Policies and procedures currently outlined in KBR's November 2002 Handbook, *Guidelines and General Billing Procedures for U.S. Government Contracts* are

inadequate or do not exist to ensure billings on government contracts are in compliance with the Federal Acquisition Regulation. Policies and procedures are inadequate for the processing of offsets and vouchers on inactive and physically completed contracts. We also found policies do not exist for the processing of Time and Material (T&M) billings, and for monitoring the adequacy of the subcontractor's accounting and billing system.

3. KBR is not following its current written billing procedures when processing vouchers. KBR personnel do not complete or only partially complete the Management and Project checklists; do not adjust billing rates to actual rates in a timely fashion; fail to notify the Administrative Contracting Officer (ACO) or paying office of refunds and overpayments; do not properly brief task orders associated with all contracts; and by bill the government unallowable costs.

4. KBR does not have adequate controls over subcontract billings. Our audit activity has identified inadequate or nonexistent policies and procedures for notifying the government of potential significant subcontract problems that impact delivery, quality, and price. KBR also does not monitor the ongoing physical progress of subcontracts or the related costs and billings. This lack of controls resulted in significant issues with the billings processed for KBR's Dining Facility Subcontract (DFAC) costs in Kuwait and Iraq.

SCOPE OF AUDIT

We conducted our examination in accordance with generally accepted government auditing standards. Those standards require that we obtain a sufficient understanding of internal controls to plan financial audits and determine the nature, timing, and extent of tests to be performed. An examination of internal controls includes:

- identifying relevant system control objectives and associated control activities;
- obtaining an understanding of all applicable components of internal control for the identified control objectives and activities;
- determining if the internal controls are adequate and in operation; and
- assessing control risk to use as a basis for planning the nature, timing, and extent of substantive testing in other financial related audits.

We evaluated the billing system using the applicable requirements contained in:

- Federal Acquisition Regulation (FAR);
- Defense FAR Supplement (DFARS); and
- Cost Accounting Standards (CAS).

Our examination specifically tested the billing system's internal control procedures used in Houston, TX associated with the following control objectives:

- Billing System Policies and Procedures;
- Implementation of Policies and Procedures;

- Training of Employees;
- Contract Briefings;
- Management Reviews and Approvals;
- Reconciliation of Recorded and Billed Costs;
- Management of Contract Overpayments, Refunds and Offsets;
- Subcontractor Billing Oversight;
- Exclusion of Non-billable Costs; and
- Adjustment of Cost and Rates.

Test procedures were applied from August 30, 2002 to April 1, 2004. We believe that our examination provides a reasonable basis for our opinion.

RESULTS OF AUDIT

In our opinion, the billing system and related internal control policies and procedures of KBR are inadequate in part. As a result, KBR is not authorized for direct billing and will be required to continue to provide all billings to DCAA for provisional approval prior to submission for payment.

Our examination noted 10 significant deficiencies in the design or operation of the internal control structure. In our judgment, these deficiencies could adversely affect the organization's ability to record, process, summarize, and report billings in a manner that is consistent with applicable government contract laws and regulations. The conditions are detailed in the "Statement of Conditions and Recommendations" below. The cost impact to the government is indeterminable; however, we consider the potential impact to be significant based on the size of KBR's operations. KBR's estimated annual and Department of Defense (DoD) sales for CFY 2003 are $4.1 billion and $3.9 billion respectively. The significant increase in sales is principally due to two Department of Defense (DoD) contracts for work in Kuwait and Iraq. As a result, we expect the contractor's billings to the government, especially for DoD to increase significantly in CFY 2004.

As a result of control risk assessments, our audit effort in the following areas will be increased:

- Incurred Indirect/Direct Costs;
- Contract Status Reporting;
- Billings; and
- Contract Close-outs.

We examined only the billing system. Accordingly, we express no opinion on the contractor's internal controls taken as a whole.

On February 12, 2004 we provided a draft copy of the Statement of Conditions and Recommendations and discussed the results of our examination with Todd Bishop, KBR

manager of Government Compliance. KBR provided their written response on March 5, 2004. The contractor partially concurred with condition statements and has completed or outlined corrective action to resolve the conditions. The contractor's complete response is included in the Appendix. The contractor's responses for each condition statement have been incorporated in their entirety in each respective condition statement.

We will conduct a follow-up audit in approximately six months to determine if the contractor's corrective actions have been implemented and the conditions have been corrected.

We wish to express our appreciation to KBR for the cooperation extended to the audit team throughout our review.

STATEMENT OF CONDITIONS AND RECOMMENDATIONS

Our condition statements 1, 2, and 8 identified below were originally reported in our billing system Audit Report No., 3521-2001D11010001, dated August 9, 2002. The remaining conditions were identified as a part of this audit as well as our Audit of Contract Overpayments, 3311-2003K173100001 which has been provided as a draft to KBR for comments and our Subcontract Management Operations Audit, 3311-2004Q10503003 which has also been provided to KBR for comments. We expect to issue these reports in the next 45 days.

1. Lack of Written Billing Policies and Procedures

a. Prior Condition:

KBR does not have formal written policies and procedures in place to assure instructions for both automated and manual tasks are clearly defined, delegated duties and responsibilities are formally documented and communicated to employees, and processes are performed consistently. Without formal written policies and procedures and instruction on their use, the risk of submitting inaccurate billings to the government increases.

b. Status of Corrective Action Taken on Prior Recommendations

As a result of our prior condition KBR issued *Guidelines and General Billing Procedures for U.S. Government Contracts* dated November 1, 2002. We reviewed the procedures issued by KBR to determine if they had corrected the prior condition cited. We found the procedures general in nature with few specifics. KBR representatives explained that more detailed procedures were issued by project.

We reviewed the general procedures in conjunction with KBR's project specific procedures and found the following specific deficiencies:

(1) The project specific procedures do not address many of the criteria necessary to ensure proper and accurate completion of billings. KBR sated due to the unique

nature of the various contracts, generic billing procedures could not possibly cover the myriad of situations that would need to be addressed and that KBR has project specific billing procedures for the various contracts it performs. We found the project specific billing procedures contained little more than the directions to prepare the paperwork.

(2) KBR does not have written policies and procedures for processing offsets. KBR stated that it does not process offsets. However, during our review, we noted instances where KBR processed offsets by reducing current requests for payment on contract billings. Examples of offsets processed by KBR include:

- The Balkan Support Contract, contract number DACA78-99-D-0003, scrap sales proceeds are processed as offsets against current requests for payment.
- An Army contracting officer advised KBR in July 2003 to offset a $17,000 overpayment against current request for payment, contract number DABT-63-98-C-0060.
- The Navy CONCAP contracting officer advised KBR in July 2003 that the preferred method of processing overpayments or over-billed amounts was offsets on subsequent public vouchers or requests for payment, contract number N62470-00-D-0005.

(3) KBR has not developed formal, written procedures for processing contract cost data after extraction from the KBR Financial application system. Documented formal procedures will ensure compliance with management's intentions and allow for a consistent application on all contract billings. The contractor's general policy identifies steps for preparing the monthly booked costs to billed costs reconciliation; however, the explanation begins with the costs on a spreadsheet with no indication of where or how these costs are accumulated.

Clearly documented policies, procedures, and processes are essential because failure to comply with the FAR and contract requirements can result in harm to both the contractor and the government due to over or under billings on government contracts.

c. Recommendations:

We recommend KBR implement the following corrective actions:

(1) Review the individual program guidance to ensure it incorporates the elements of the overall company policies to ensure compliance with the FAR and contract provisions.

(2) Develop adequate policies and procedures for processing offsets on government contracts to ensure contract offsets are processed only after providing notification to the ACO and receiving instruction from the ACO and/or the paying office.

(3) Expand the General Guidance to include procedures for obtaining and analyzing contract cost data.

d. Contractor's Reaction:

Response dated March 5, 2004

(1) As noted by DCAA, KBR developed and implemented KBR Government Operations Guidelines and General Billing Procedures for U.S. Government Contracts (Billing procedures) dated November 1, 2002.

(2) Billing Procedures will be revised to incorporate the statement, "It is not company practice for Government Operations projects to create offset invoices unless directed specifically by the customer, procurement office, etc." Under the Balkan's support contract KBR was directed to record scrap sales as an offset.

(3) KBR is currently developing additional procedures and information for processing contract cost data after extraction from the KBR Financial Application System through invoice preparation.

e. Auditor's Comments:

We reviewed the Balkans Desktop Manual and Restore Iraqi Oil (RIO) Procedures to determine if the programs' guidance expanded on the KBR guidance. In both cases the guidance was for preparing the actual invoice with no reference to FAR or contract requirements.

Additionally, the contractor's revised general policies address the prior identified conditions; however, we also found the revised general policies do not address the monitoring of subcontractor's accounting and billing systems for adequacy and the preparation of Time and Material billings. Therefore we recommend the following changes to KBR's general policies:

(1) Develop policies to ensure compliance with FAR 52.216-7, Allowable Costs and Payments. The contractor's policies and procedures should provide for monitoring the subcontractor's accounting and billing systems; obtaining, on a periodic basis, the subcontractor's reconciliation of billed and paid amounts on major subcontracts, require timely notification to the prime contractor of any overpayments and that refunds or offsets be processed within 30 days. Additionally the policies should address the contractor's requirement to immediately notify the subcontractors of any contract administration adjustment impacting the subcontractor's billings and to timely adjust its billings or submit refunds to the government for identified subcontractor overpayments that have been included in billings to the government. The policies and procedures should also address how KBR buyers determine the adequacy of subcontractor billing systems. The end result of not monitoring the subcontractor's accounting and

billing systems are increased costs billed to the government because of duplicate or incorrect subcontractor invoices and noncompliance with FAR 52.216-7.

(2) Develop written policies for generating T&M invoices in accordance with contract and FAR requirements. KBR's policies do not address the procedures for preparing invoices on T&M contracts. Billings on T&M contracts are unique in that labor and material rates establish what the contractor can bill; additionally FAR 52.232-7, Payments Under Time and Material and Labor Hour contracts require a five percent withhold on labor costs, not to exceed $50,000 and establishes other billing limitations. The potential exists that over payments could occur if billings are not prepared correctly.

We will conduct a follow-up audit in approximately six months to determine if our recommended additional corrective actions have been implemented and the conditions have been corrected.

2. Failure to Adjust Billings Promptly for Changes in Indirect Rates

a. Prior Condition:

KBR does not adjust its indirect billing rates to year –end actual rates in a timely fashion. Adjusting indirect billing rates in a timely manner ensures at year end, the amount of indirect costs reimbursed is as close to the certified amount as possible. Incurred cost billings are cumulative, and therefore, should reflect the impact of any adjustments as soon as they are known. The contractor should have procedures and controls in place to ensure the prompt adjustment of billings to reflect adjustments in indirect rates.

b. Status of Corrective Action Taken on Prior Recommendations

The contractor's corrective action taken since the initial audit has not adequately addressed the condition reported in the prior audit. In our current audit, we found that KBR is not adjusting billings on all contracts and is not completing the adjustments timely. We reviewed adjustment vouchers on a test basis and documented the following conditions:

- The contractor has not made the required indirect rate billing adjustments on contract number FA2550-96-C-0003 for FY 2000 and 2001 and on contract number DAKF11-99-D-0006, task order LM05 for FY 2001.
- We also found instances where the contractor did not make billing adjustments within the required 45 days after final indirect rates were established as prescribed by its billing procedures.

c. Recommendations:

We recommend KBR implement corrective action to assure proper and timely billing adjustments on all cost-reimbursable contracts. KBR must ensure timely year-end adjustments

are performed on all contracts within 45 days of determining its year-end indirect rates. KBR should notify its billing personnel of any changes to the billing procedures to ensure compliance.

d. Contractor's Reaction:

Response dated March 5, 2004

The two contracts referenced (FA2550-96-C-0003 for FY 2000 and 2001; and DAKF11-99-D-0006, task order LM05 for FY 2001) were adjusted in August of 2002. This adjustment supporting data was provided to DCAA.

KBR has submitted adjusting invoices for the actual final un-audited years (FY2000, FY 2001, and FY 2002) indirect cost rates. FY 1999 is the most current audited and negotiated final indirect cost rate.

In the past KBR Government Compliance has notified the projects of rate updates via e-mail. KBR will formalize this practice, in conjunction with the FY 2003 incurred cost submission preparation, as part of its billing procedure manual.

e. Auditor's Comments:

The revised contractor's General Guidance directs Government Compliance to update and distribute to the program offices, a rate matrix within 15 days of (i) submission of final indirect cost rate proposal for the calendar year; (ii) any update to the FPRA; negotiation/settlement of final rate agreement or (iii) when other adjustments are determined. However, the guidance should direct timely submission of vouchers, within 30 days, to adjust for over or under billings of indirect rates.

To test KBR's assertions made in its response, we tested the timeliness and accuracy of the rate adjustments for five task orders on contract DACA78-99-D-0003. Provisional billing rates were issued on December 5, 2003 and the contractor submitted adjustment vouchers on December 29, 2003.

3. <u>Incorrectly Prepared Adjustment Vouchers</u>

a. Condition:

Our audit determined prior to 2003, KBR incorrectly prepared its year-end billing adjustment vouchers. We examined adjustment vouchers on a test basis to determine if the vouchers were properly prepared, mathematically correct, and reconcilable to KBR's accounting records. While performing our evaluation, we found KBR uses its project year-to-date billed amount to calculate its adjustment voucher amount instead of booked or claimed costs. KBR now has a process to reconcile these differences on every voucher submitted.

However, KBR's system currently does not segregate cost by year so that rate adjustments and reconciliations can be easily made and the rates used can be identified.

b. Recommendation:

We recommend KBR ensure its procedures and controls to prepare year-end adjustment vouchers and booked-to-billed reconciliations are always followed. The process should provide for segregation of cost by year so rate adjustment can be easily made and the rates used can be identified and reconciled.

c. Contractor's Reaction:

Response dated March 5, 2004:

KBR will formalize the DCAA's recommendation, in conjunction with the FY 2003 incurred cost submission preparation, as part of its billing procedure manual.

Rates for the year 1999 are the most current audited and negotiated final indirect cost rates. KBR has submitted adjusting invoices for the actual final un-audited years (FY 2000, FY 2001 and 2002) indirect cost rates.

d. Auditor's Comments:

KBR's comments are responsive to our recommendations. After receiving KBR's comments, we reviewed the rate adjustments made for revised provisional billing rates on 5 task orders for contract DACA78-99-D-0003 and determined that costs and rate applications were segregated by year.

4. Lack of Appropriate Reviews and Approvals of Vouchers

a. Condition:

Our audit found KBR failed to follow its billing procedures requiring appropriate management review and approval of vouchers prior to submission to the government for payment. *KBR Government Operations Guidelines and General Billing Procedures for U. S. Government Contracts* (billing procedures) states "The project business manager (sometimes called project accountant), or designee, must complete and sign the checklist entitled *"Project Checklist for Reviewing Invoices before Submittal."* The billing procedures also states "The project manager, or designee, must complete and sign the *"Checklist for Management Review of Invoice"* before the invoice can be submitted for payment."

We examined 14 interim vouchers prepared between April and August 2003 and found KBR had not completed the management checklist on 9 of the 14 interim vouchers. We also found KBR had had not completed either the project checklist or the management checklist for 2 of 14 interim vouchers. These deficiencies impact 3 major contracts, DACA78-99-D-0003, DABT23-01-C-0008 and DAKF11-99-D-0006.

We believe cost-reimbursement contracts represent an increased risk to the government when the contractor's billing system does not protect against or detect billing errors. It is vital that the contractor has controls in place to minimize the risk of over billing the government.

b. Recommendation:

We recommend KBR follow its current billing procedures and prepare the appropriate checklists to ensure properly documented billings. KBR procedures specifically state that the project business manager should complete both the project checklist and management checklist when processing vouchers.

c. Contractor's Reaction:

Response dated March 5, 2004

KBR has implemented corrective action and is monitoring the completion of the checklists in accordance with KBR procedures.

d. Auditor's Comments:

The contractor has proposed adequate corrective action. As a follow-up, we reviewed recently submitted vouchers for the Balkans program and vouchers being submitted for the RIO program and in both instances the project checklist and management checklist were completed.

5. Failure to Notify ACO of Contract Over Payments

a. Condition:

Our current audit found KBR is not notifying the ACO or the paying offices prior to submission vouchers to correct contract overpayments. KBR's government billing procedures require contacting clients and/or the paying office to resolve issues regarding past-due invoices and any overpayments or underpayments within 30 days of identification of the issue and/or follow up as necessary until final resolution. Recently the FAR was amended to require the contractor to notify the contracting officer if the contractor becomes aware of an overpayment on a contract invoice (see FAC 2001-02).

KBR must comply with its polices and procedures and FAR for notifying contracting officers and paying offices for instruction to resolve issues regarding past-due invoices and overpayments or underpayments within 30 days of identification of the issue and follow up as necessary until final resolution. All significant overpayments/duplicate payments or over-billed amounts returned to the paying offices as refunds must be accompanied with checks for the amount of the credit voucher.

We found the following overpayments were not resolved in a timely manner or in accordance with FAR and KBR policies:

- A $382,000 credit public voucher for contract number N62470-00-D-0005, delivery order 003, invoice number 0208-304-UR651, dated August 27, 2002, was sent to the Navy CONCAP payment office without prior notification to the ACO or paying office. KBR refunded the Navy contract overpayment for $382,000 on June 10, 2003, which was 490 days after the overpayment was made.
- A $17,000 credit public voucher for contract number DABT-63-98-C-0060, voucher number 03034, was sent to the Army contract paying office without prior notification to the ACO or paying office; and KBR did not include the check due the government with the voucher.
- During 2001, KBR identified and reported to the General Accounting Office three overpayments totaling $53,000 relating to contract numbers DAKF11-99-D0066 and FA2550-96-C-0003, but it did not refund the overpayments in a timely manner. The $53,000 overpayment was not resolved until September 2003 or about 845 days after KBR received the overpayment.
- In September 2002, KBR identified a duplicate payment of $107,000 for Army Corps of Engineers contract number DACA31-97-D-7000. KBR has yet to provide adequate documentation to show this overpayment has been resolved.

b. Recommendation:

We recommend KBR comply with its current polices and procedures for resolving overpayments. Notification to the ACO must be made immediately and the refund of the overpayments must be made in a timely manner. KBR procedures require notification and resolution within 30 days of identifying an overpayment.

c. Contractor's Reaction:

Response dated March 5, 2004

The duplicate payment of $107,000 for contract number DACA31-97-D-700 was resolved with the client's directive in September 22, 2003 and the information was provided to the DCAA October 29, 2003.

KBR has implemented corrective action to comply with its procedures and is currently contacting the client and the paying office by correspondence within the 30 days after identifying an overpayment. After notification the resolution may extend beyond the 30 days; however, KBR will continue to work towards final resolution.

d. Auditor's Comments:

The contractor has proposed corrective action to comply with its own procedures. The documentation provided by KBR for $107,000 dollar overpayment was not considered adequate; therefore, until KBR provides adequate support, the overpayment is still considered outstanding. We are working to resolve this issue. We will address this issue in our follow-up audit scheduled to be completed in approximately six months.

6. Lack of Reconciliation of Recorded to Billed Costs

a. Condition:

We found KBR does not periodically reconcile differences between recorded costs and billed costs on physically complete, but not yet closed contracts. The reconciliation is important to identify physically complete contracts which may be over billed. Our review disclosed that the Launch Operations Support Contract (LOSC) cost reimbursable contract number F08650-95-C-6038, which was physically completed in December 1998, is over billed by approximately $150,000

b. Recommendations:

We recommend KBR establish procedures and internal controls to ensure reconciliations of billed and recorded costs are performed on a periodic basis for all contracts, including physically completed contracts awaiting closeout. Also, KBR should ensure that final vouchers for physically completed contracts are submitted within 120 days after the settlement of the applicable final indirect rates. If billed costs exceed recorded costs, revised billings and refunds should be submitted within 30 days.

c. Contractor's Reaction:

Response dated March 5, 2004

KBR will formalize the DCAA's recommendation, in conjunction with the FY 2003 incurred cost submission preparation, as part of its billing procedure manual.

Rates for the year 1999 are the most current audited and negotiated final indirect cost rates. KBR has submitted adjusting invoices for the actual final un-audited years (FY 2000, FY 2001 and 2002) indirect cost rates.

d. Auditor's Comments:

KBR has proposed adequate corrective action. We will verify the corrective action in our follow-up audit scheduled in about six months.

Audit Report No. 3311-2002K11010001

7. **Lack of Adequate Contract Briefings**

a. Condition:

Our audit has found KBR does not properly brief its contracts and the associated task orders to identify terms impacting billings. KBR's Contract Policy & Process, CA-S-03, dated August 29, 2002 states the contractor "shall develop a contract post award summary and the DCAA contract brief" as soon as possible but no later than three business days after contract award. The policy continues on to state, KBR "shall update the DCAA Contract Brief or KBRSI Contract Billing Summary as needed (i.e., upon receipt of the contract modification but, no less than on an annual basis)."

During our audit we identified two contracts, N62470-00-D-0005 and DAAA09-02-D-0007 did not have a contract brief on each of the associated task orders. KBR prepares a contract summary which summarized the contract and the task orders. The contract summary included information such as performance period, brief description, and the cost of the contract or task order as modified. The contract summary does not identify special requirements, funding, and limitations nor does it identify the contract clauses relative to the specific task orders.

Inadequately briefed contracts result in incorrect billing to the government due to noncompliance with unique contract clauses requirements (i.e. period of performance, level of effort, unallowable costs, specials billing requirements, funding limitations, etc.).

b. Recommendation:

We recommend KBR brief each contract and task order as prescribed by its policies and procedures. We further recommend KBR include any special requirements or special limitations in each of the contract briefs.

c. Contractor's Reaction:

Response dated March 5, 2004

KBR will to the maximum extent practicable ensure that contract briefs include billing details, contract types and other pertinent data important for the billing process.

d. Auditor's Comments:

KBR has not proposed adequate corrective action. In March 2004, to further test KBR's actions we requested copies of contract briefs for three programs from the accountants responsible for submitting vouchers for those programs. The accountants for the RIO program did not have a copy of the contract brief; but indicated KBR's Government Compliance department could provide it. (Mr. Floyd Green, Government Compliance did provide a copy of only the basic contract brief). The Balkans accountants did not have copies of their contract briefs either, and indicated that Contract Administration would have a copy. The accountant for

the LOGCAP presented only a copy of the prime contract, and a summary of funding levels for the individual task orders.

The contract brief is a tool to ensure that government invoices are prepared in accordance with contract terms and conditions. KBR should ensure that the individuals responsible for preparing the billings have direct access to the contract briefs and review them for changes prior to preparing each billing. We recommend KBR take meaningful corrective action to ensure complete contract briefs are prepared and are available to those preparing contract billings.

8. Billing of Unallowable Costs

a. Prior Condition:

Our prior audit found KBR billed unallowable costs on Contract No. F04701-90-C-0080. FAR 31.201-6, Accounting for Unallowable Costs requires that costs that are expressly unallowable or mutually agreed to be unallowable, be identified and excluded from any billing, claim or proposal applicable to a Government contract.

KBR's final invoice included approximately $45,000 in costs which included overhead and G&A that had been determined to be unallowable by DCAA in Audit Report No. 3521-95D10160003, dated September 30, 1997, and agreed-to by the contractor. The contractor reduced interim vouchers for the questioned costs, but KBR did not reclassify the questioned costs to an unallowable account in its ledger. KBR prepared the final voucher from its accounting records which did not reflect the unallowable costs, resulting in billing the unallowable costs in its final voucher.

We believe the lack of written general billing procedures prescribing actions to take regarding costs determined to be unallowable under these or similar circumstances has contributed to this condition; which resulted in an over billing to the government.

b. Status of Corrective Action Taken on Prior Recommendations

The contractor developed and implemented KBR Government Operations Guidelines and General Billing Procedures for U. S. Government Contracts (billing procedures) dated November 1, 2002. We believe the billing procedures addressed the unallowable/unallocable costs criteria necessary for the billing system.

c. Contractor's Reaction

KBR concurs with the DCAA's position.

9. Inadequate Controls over Subcontract Billings

a. Condition

Our audit found KBR has inadequate controls over subcontract billings. We found KBR has no documented mechanism for subcontract administrators to monitor subcontract billings to ensure they comply with subcontract terms. KBR requires its subcontract administrators to prepare documents that state whether a subcontractor has delivered its goods or services in accordance with the subcontract terms. However, we found no such documents included in KBR's subcontract files, nor did we find any log of subcontractor payments.

The need to monitor subcontractor performance as part of the subcontract management function is well established. The Contractor Purchasing System Review (CPSR) guidebook Appendix B – Typical Content of Contractor Policies, Procedures and Forms states in summary that typical contractor policy and procedures include statements covering the following: "...(5) Subcontract award and administration...(iv) maintaining visibility of subcontracts in the areas of cost, schedule, and performance, (v) monitoring progress payments to subcontractors.

The advantages gained by prudent and capable efforts in planning and negotiating subcontracts can be dissipated through the failure of upper-tier contractors to administer their subcontracts properly. KBR's subcontractor invoicing and payments must be monitored for compliance with FAR 52.216-7, *Allowable Cost and Payment*. This clause requires higher-tier Subcontract Administrators to determine and/or approve subcontractor progress made; costs incurred, and ensure timely delivery of an acceptable product.

Policies and procedures should be in place to notify the government of potential significant subcontract problems that may impact delivery, quality, or price. The prime contractor's procedures related to cost controls should be directed to production and financial controls, with emphasis on those controls which ensure physical progress of production are commensurate with reimbursement.

KBR does not have a mechanism in place at the subcontract level to monitor the on-going physical progress of a subcontract or the related costs and billings. Procurement files do not contain a subcontract invoice/payment log for tracking the number of invoices received, the cumulative amount incurred and billed, or the available funding. The subcontract personnel on-site are required to verify subcontracts were being completed in accordance with the subcontract terms and that a vendor should be paid.

An example of a problem that can be caused by this condition is KBR's payment of DFAC subcontractor invoices that are not reasonable in amount and are not computed in accordance with subcontract terms and conditions. The subcontract required the subcontractor to create a billing format to include "meals served for each billing item." The subcontract indicates meals served will be the basis of the billed amounts as follows:

> "SUBCONTRACTOR will create a Subcontract billing format acceptable to CONTRACTOR, to be used for all payments. This form will include, but not be limited to the full name and address of the Subcontractor work performed, and meals served for each billing item; the previous billed amount; the 'to date' billed amount; the billing period, and the SUBCONTRACT number."

Only the on-site subcontract administrator is actually in a position to verify the billing format met the intended subcontract objectives and was acceptable to measure the performance occurring in the field. However, the billing format was not addressed until recently. One result of this lack of monitoring is the billing methodology did not consider actual meals served in determining the billing amount, despite the expressed terms of the subcontract.

The condition identified in the Operations Subcontract Management Audit contributed to the following irregularities with the billings process for DFAC costs in Kuwait and Iraq identified by the DCAA Iraqi Branch Office:

(1) Inadequate internal controls over payments to subcontractors;
(2) Payments to subcontractors that are unreasonable and not computed per contract terms;
(3) Missing published standard operating procedures for food service personnel
(4) Inadequate monitoring for compliance with prime contract and master agreement terms and conditions; and
(5) Improper segregation of duties for DFAC subcontract negotiator/approving officer.

The lack of controls has a potential of resulting in over billings to the government.

b. Recommendation

We recommend KBR prepare policies and procedures to document processes for ensuring subcontractor performance is monitored by all of its subcontract administration personnel. KBR should establish a process/mechanism for the subcontract administrators to have visibility into subcontract payments as well as monitor subcontract performance to specific subcontract terms.

KBR's subcontract/vendor payment procedures should include, but not be limited to, the following:

- Procedures for payments based on receipt of goods and/or services for a fixed price.
- Procedures for payments based on the percentage of work accomplished and dollars expended on a fixed price purchase order.
- Procedures for periodic payments for costs incurred and a percentage of fees earned monthly under a cost reimbursable contracts.
- Procedures for milestone payments based on measurable work progress on a fixed price purchase order. For example, work accomplished that can be

measured, such as meals served, camp operations running by a certain date, or services delivered.

- Appropriate invoice approval and payment forms and/or worksheets such as:
  - Invoice Approval for Cost Reimbursable Subcontracts
  - Invoice Approval for Milestone Payments
  - Invoice Payment Request
  - Invoice Approval for Progress Payments
- Procedures for tracking subcontractor invoice submissions, payments, and available funding along with the requirement for subcontract administrators to maintain a subcontract invoice log in the procurement file documentation.

c. Contractor's Response:

KBR's response, dated March 5, 2004

KBR's position is that the issues cited by DCAA in support of this Statement of Condition have been misquoted as well as misinterpreted. The end result is that a difference of opinion between DCAA and KBR regarding certain DFAC subcontract terms is now mischaracterized herein as a billing system control deficiency.

DCAA is aware that KBR established a Tiger Team that is actively researching and analyzing the facts and circumstances surrounding each of its DFAC subcontracts. This effort includes a thorough review and analysis of past subcontract payment practices, as well as, developing standardized subcontract practices for future DFAC subcontracts.

Thus KBR believes any conclusion at this time regarding KBR's billing procedures related to the payment of DFAC subcontracts is not only unsubstantiated but also premature.

d. Auditor's Comments:

KBR's response has not addressed the condition. KBR disagrees with our interpretation of the specific DFAC terms; however, adequate controls and management of the subcontract billing process would have allowed the issues currently under review to be addressed sooner. We recommend KBR address the systemic issues in the subcontract billing process. KBR has not yet responded to the Statement of Conditions and Recommendations from the DCAA Subcontract Management Operations audit.

10. <u>Management Oversight – Internal Audit</u>

a. Condition:

We have been unable to determine the adequacy of KBR's internal audit function to ensure compliance with established policies and procedures. A strong internal audit function is required in order to conclude that established internal controls can be relied upon to prevent or detect errors and misstatements in the processing of accounting transactions. We have requested

evidence that KBR's internal audit department is functionally and organizationally independent and sufficiently removed from management to ensure that it can conduct audits objectively and can report its findings, opinions, and conclusions without fear of reprisal. Such evidence includes organization reports, evidence that there is broad audit coverage, that audit recommendations are considered and addressed by management, that the internal audit department has regular communications with the Board of Directors or Audit Committee, and that the internal audit department participates in the development, modification and implementation of significant accounting system changes. It has been KBR's long established practice to restrict DCAA's access to the internal audit function. As a result – we can place no reliance on management's oversight to ensure that established policies and procedures and other related internal controls are routinely complied with.

b. Recommendation:

We recommend that KBR provide requested access to internal audit functions required to determine the adequacy of its oversight function in ensuring that established internal controls are adequate and complied with.

c. Contractor's Reaction:

The contractor's response is taken from a letter issued to our office on November 24, 2003 which stated KBR's position regarding all internal audits.

All internal audits are conducted by the Halliburton Company on behalf of the Halliburton Board of Directors Audit Committee, not KBR. The Audit Committee is independent of KBR and HES. Additionally, Halliburton Company has no legal or contractual obligation to share these reports with KBR or HES. The information contained in those reports and any actions that may result from the reports belong to the audit committee and are subject to the disclosure requirements and restrictions of Sarbanes Oxley and other laws and regulations applicable to publicly traded companies.

d. Auditor's Comments:

We will continue to pursue internal audit reports at KBR. We believe an adequate internal audit function is integral to a companies internal control structure. Without access to determine if this function operates effectively we are required to assume maximum risk on each audit test we perform.

CONTRACTOR ORGANIZATION AND SYSTEMS

1. Organization

Kellogg Brown & Root (KBR), also known as the Engineering and Construction Group (E&C), is one of the two operating subsidiary groups of Halliburton. The other operating subsidiary group is Halliburton's Energy Services, Inc. (HESI), also called the Energy Services Group (ESG). The legal structure of Halliburton is different from its operational structure. Halliburton owns all the stock HESI which owns all the stock of DII Industries, LLC (DII). DII in turn owns all the stock of numerous Halliburton legal entities including KBR. Halliburton's two operating subsidiary groups are organized around the products and services provided to the customers they serve.

- The ESG provides a broad array of products and services to upstream oil and gas customers worldwide, ranging from the manufacturing of drill bits and other down hole and completion tools and pressure pumping services to subsea engineering.
- KBR E&C deals with large-scale construction projects including construction and designing of oil and gas processing and refining plants, production facilities, and onshore and offshore pipelines. KBR's non-energy business meets the engineering and construction needs of governments and civil infrastructure customers. Operationally, KBR consists of five business lines – Offshore, Onshore, Operations & Maintenance, Infrastructure, and Government Operations. Government Operations consists of KBR Services, Inc. (KBRSI) and KBR Commercial entities that perform contracts for foreign countries. (KBRSI) is a new subsidiary formed in CFY 2002 as a result of KBR's reorganization due to its planned bankruptcy for asbestos litigation (see the Other Matters Reported Appendix). Most government contracts, signed under several legal entities, have been novated to KBRSI.

KBRSI consists of two operating business units that perform government contracts: Brown & Root Service Operations (BRSO) and KBR Civil Infrastructure (KBRCI).

- BRSO is the primary government segment that provides engineering, construction, operation, and maintenance services for the Air Force, Army, Navy, and NASA. It also provides logistical support services for the U.S. troops in foreign countries through contracts with the Army Corps of Engineers and Army Material Command. BRSO also operates as Management Logistics, Inc. (MLI) to perform projects with a union-represented work force.
- KBRCI, formerly Brown & Root Civil Engineering prior to 2002, provides consulting and civil engineering services primarily for commercial projects. Projects include highways, bridges, stadiums, aviation and water and wastewater infrastructure, facilities modification, and on-call construction.

KBR revenues were approximately $5.736 billion (B) in contractor fiscal year (CFY) 2002 and $5.235B in CFY 2001, or about 46 percent of Halliburton Company's total revenue of $12.572B for CFY 2002 and about 40 percent of $13.046B for CFY 2001. KBR's operating loss

for CFY 2002 was $685 million (M) and income for CFY 2001 was $111M. Halliburton's total operating loss for CFY 2002 was $112M and operating income for CFY 2001 was $1.084B.

BRSO's CFY 2002 costs incurred were approximately $573M and for CFY 2001 costs incurred were approximately $563M. For CFY 2003, estimated costs were $4.2 billion. In CFY 2001, BRSO had 95 percent federal-government participation, of which 63 percent was cost reimbursable, 30 percent fixed-price work, and 2 percent time and material. KBRCI reported CFY 2001 revenues of $95M with about 18 percent federal-government participation. Government participation was 10, 5, and 3 percent for cost reimbursable, time and material, and fixed-price contracts, respectively. The remaining 82 percent of KBRCI's costs was incurred on commercial contracts.

In CFY 2002, corporate home office expenses such as executive management, accounting, communications, human resources, information technology, legal, risk management, and taxes were allocated to operating segments using the three-factor formula. Effective January 2003, a majority of corporate expenses were specifically identified either to KBR or ESG. The only expenses currently allocated using the three-factor formula from the Corporate home office are HALCO 21 costs relating to SAP software implementation and state and franchise taxes. Specific Corporate costs now identified to KBR are charged into the Intermediate Management III (IM-III) Home Office. IM-III provides management support, accounting, and business acquisition functions for all of KBR's business units. The residual expenses in CFY 2003 for these services are allocated to the following business units using the three-factor formula: BRSO, KBRCI, Government Operations United Kingdom (UK) and Asia Pacific (AP), Commercial Infrastructure UK and AP, and KBR Other Commercial.

Government OPS Intermediate Management II (IM-II) Home Office provides global business unit management and accounting and sales and marketing functions. Residual expenses are allocated to BRSO and Government Operations UK and AP using the three-factor formula.

Government OPS Americas BRS Intermediate Management I (BRS IM-I) Home Office provides various functions including accounting, human resources, information technology, sales and marketing, government compliance, quality, and contract administration. The costs associated with these functions are allocated to only BRSO except for government compliance which is also allocated to KBRCI using the three-factor formula.

Infrastructure Intermediate Management II Home Office provides business unit management and accounting and finance to the Infrastructure business unit. Residual expenses are allocated to KBRCI and Commercial Infrastructure UK and AP.

The Americas Infrastructure Intermediate Management I Home Office provides business unit management, accounting and finance, and chief engineer functions to the America Infrastructure activities. Residual expenses are allocated only to KBRCI.

2. Systems

Billing System

Kellogg, Brown and Root Services Inc. (KBR) project controls prepares its invoices and voucher using its Guidelines and General Billing Procedures for U. S. Government Contracts dated October 2002. Project controls is responsible for compiling billings; accordingly, each project is governed by its own project-specific policies and procedures. Accounting is responsible for establishing the requirements for billings in the start-up phase of a project and ensuring the necessary client codes and bill-types are established in the accounting system.

KBR uses an information technology system to process government invoices. KBR employees convert and record contract costs such as labor, subcontracted services and purchases materials through various input systems. All contract costs recorded in the input systems ultimately flow to and are recorded into a KBR financial accounting system called the New Business System (NBS). The NBS is an IBM mainframe legacy system placed into production in 1983. NBS produces financial reports including a job ledger report and maintains accounts payable and accounts receivables sub ledgers. NBS is the book or original records for the corporation. Since 1983 various input and output systems have been added to enhance user interface to NBS. One such system was placed into production within the last two years is called the KBR Financial Application System. The NBS feeds the KBR Financial Application System with a daily file of contract costs.

The KBR Financial Application System is a read-only system for job ledger costs and the system allows accounting personnel to extract job ledger data for invoicing. Accounting personnel extract job ledger data into MS Excel spreadsheets as part of the invoicing process. Accounting personnel summarize job ledger data by job/work order, reconcile amounts to NBS reports, and remove un-billable amounts.

The accounting function determines whether the cost is billable or not during the processing phase of the cost. The bill-type field in the accounting system identifies whether or not a cost can be billed. . The costs are formatted and summarized to meet government billing standards. During the performance of the contract, project billing personnel are responsible for preparing payment vouchers and reconciling the booked costs to the billed costs on a monthly basis, with project accounting also independently performing monthly reconciliations

Audit Report No. 3311-2002K11010001

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AUDIT REPORT AUTHORIZED BY:

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Audit Report No. 3311-2002K11010001

AUDIT REPORT DISTRIBUTION AND RESTRICTIONS

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RESTRICTIONS

1. Information contained in this audit report may be proprietary. It is not practical to identify during the conduct of the audit those elements of the data which are proprietary. Make proprietary determinations in the event of an external request for access. Consider the restrictions of 18 U.S.C. 1905 before releasing this information to the public.

2. Under the provisions of Title 32, Code of Federal Regulations, Part 290.7(b), DCAA will refer any Freedom of Information Act requests for audit reports received to the cognizant contracting agency for determination as to releasability and a direct response to the requestor.

3. Do not use the information contained in this audit report for purposes other than action on the subject of this audit without first discussing its applicability with the auditor.

CONTRACTOR'S RESPONSE

KBR

Government Operations, 155 0 Wilson Boulevard, Suite 700, Arlington, Virginia 22209 (703) 526-7500
Fax (703) 526-7585

March 5, 2004

William F. Daneke Branch Manager Defense Contract Audit Agency Arlington Branch Office Arlington, TX 76006-6223

Dear Mr. Daneke:

The purpose of this letter is to respond to your draft audit report conditions and recommendations regarding the audit KBR's Billing System under Audit Report No. 33112002K11010001. Based on the comments contained in the report, KBR's responses are provided in Attachment A to this letter.

KBR appreciates the opportunity to respond to the various DCAA issues identified within this Statement of Condition. For ease of reference, excerpts from the Statement of Condition are presented in italics, followed by the KBR response in normal text.

If you have any question, please feel free to contact me at 713.753. 4931 or Todd W. Bishop at 713.753.4186, or by e-mail to bill.walter@halliburton.com or todd.bishop@halliburton.com.

Sincerely,

Director, Government Compliance

cc: Mr. Gary Catt, Supervisory Auditor, DCAA Mr. John Short, Supervisory Auditor, DCAA Ms. Catharina Ignacio, CACO, DCMA Mr. Al Neffgen, Chief Operating Officer, KBRSI Mr. Craig Peterson, Vice -President, KBRSI Mr. Pete Glynn, Director, Accounting & Finance

NOTE: This KBR Response to DCAA Audit Assignment No. 3311 -2002K11010001 contains proprietary and confidential information which is authorized to be withheld from the public . Disclosure would cause a foreseeable harm to an interest protected by one or more Exemptions of the Freedom of Information Act, 5 USC Section 552. Furthermore, it is requested that any Government entity receiving this information act in accordance with DoD 5400.7-R, and consider this information as being for official use only (FOUO), and mark, handle

and secure this information so as to prevent unauthorized access.

1. DCAA-Lack of Written Billing Procedures

a. DCAA Condition

1.1 KBR does not have written general policies and procedures covering the billing system. The contractor representatives assert due to the unique nature of the various contracts, generic billing procedures could not possibly cover the myriad of situations that would need to be addressed. However, KBR has project specific billing procedures for the various contracts it performs. Our review of ten of the project specific procedures indicated they do not address many of the criteria for adequate policies and procedures. This is a prior condition. We provided a complete description of this condition in Audit Report Number 3521 -2001D11010001. The contractor developed and implemented KBR Government Operations Guidelines and General Billing Procedures for U.
S. Government Contracts (billing procedures) dated November 1, 2002.
1.2 KBR does not have written policies and procedures for processing offsets. KBR stated that it does not process offsets. However, during our review, we noted instances where KBR processed offsets by reducing current requests for payment on contract billings. Examples of offsets processed by KBR include:

- *The Balkan Support Contract, contract number DACA78-99-D-0003, scrap sales proceeds are processed as offsets against current requests for payment;*
- *An Army contracting officer, contract number DABT-63-98-C-0060, advised KBR in July 2003 to offset a $17 thousand overpayment, as described in note 4 above, against current request for payment; and*
- *The Navy CONCAP contracting office, contract number N62470-00-D-0005, also advised KBR in July 2003 that the preferred method of processing overpayments or over-billed amounts was offsets on subsequent public vouchers or requests for payment.*

1.3 KBR has not developed formal, written procedures for processing contract cost data after extraction from the KBR Financial application system through invoice preparation. Written approved procedures will ensure compliance with management's assertions and allow for a consistent application for all contract billings.

b. DCAA Recommendations

KBR should establish and maintain procedures for (1) processing offsets and (2) processing contract cost data after extraction from the KBR Financial application system through invoice preparation.

KBR Response to Condition 1:

1. 1.1 As noted by DCAA, KBR developed and implemented KBR Government Operations Guidelines and General Billing Procedures for U. S. Government Contracts (billing procedures) dated November 1, 2002. This procedural Manual was developed in coordination with DCAA.
2. 1.2 Billing Procedures will be revised to incorporate the statement, "It is not company practice for Government Operations projects to create offset invoices unless directed specifically by the customer, procurement office, etc." Under the Balkan's support contract KBR was directed to record scrap sales as an offset.
3. 1.3 KBR is currently developing additional procedures and information for processing contract c ost data after extraction from the KBR Financial application system through invoice preparation.

2. DCAA-Failure to Adjust Billings Promptly

a. DCAA Prior Condition

KBR does not require its project managers to submit adjustment vouchers for any over or under billings of indirect rates and direct costs. We provided a complete description of this condition in Audit Report Number 3521 -2001D11010001.

b. DCAA Status of Corrective Action Taken on Prior Recommendation

The contractor's corrective action taken since the initial audit did not adequately address the condition reported in the prior audit. In performing our follow-up review, we found that KBR is not adjusting billings on all contracts. We reviewed adjustment vouchers on a test basis and documented the following conditions:

. *The contractor has not made the required billing adjustments on contract number FA2550-96-C-0003 for FY 2000 and 2001 and on contract number DAKF11-99-D-0006, task order LM05 for FY 2001.*

. *We also noted instances where the contractor did not make billing adjustments within the 45 days after final indirect rates were established as prescribed by its billing procedures.*

c. DCAA Recommendations

KBR should implement corrective action for the billing adjustments on all cost-reimbursable contracts for prior years so that the amounts of indirect costs reimbursed are as close to the certified amounts as possible;

KBR must ensure timely year-end adjustments are performed on all contracts within 45 days of determining its year-end indirect rates;

KBR should notify its billing personnel of any changes to the billing procedures to ensure compliance; and

KBR Government Compliance, who are responsible for the preparation of the incurred cost submission, should develop a procedure to communicate to the project managers the claimed costs for those projects to facilitate the adjustment process. This could be done at the same time as when KBR Government Compliance distributes the rate matrix.

KBR Response to Condition 2:

The two contracts referenced (FA2550-96-C-0003 for FY 2000 and 2001 and DAKF11-99-D -0006, task order LM05 for FY 2001) both were adjusted in August of 2002. This adjustment supporting data was provided to DCAA.

KBR has submitted adjusting invoices for the actual final un-audited years (FY 2000, FY 2001, & FY 2002) indirect cost rates. FY 1999 is the most current audited and negotiated final indirect cost rate.

In the past KBR Government Compliance has notified the projects of rate updates via e-mail. KBR will formalize this practice , in conjunction with the FY 2003 incurred cost submission preparation, as part of its billing procedure manual.

3. DCAA-Incorrectly Preparing Adjustment Vouchers

a. DCAA Condition

KBR incorrectly prepares its year-end billing adjustment vouchers. We examined adjustment vouchers on a test basis to determine if the vouchers were properly prepared, mathematically correct, and reconcilable to KBR's accounting records. While performing our evaluation, we noted that the contractor uses year-to-da te billed amount to calculate its adjustment voucher amount instead of claimed costs. This calculation is erroneous because of the significant difference between billed and claimed cost. The contractor employed this erroneous billing process on each adju stment vouchers we reviewed.

KBR's system should provide for the segregation of cost by year so that rate adjustments can be easily made and the rates used can be identified.
KBR does not have a sufficient level of control over its process for preparing adjustment year-end voucher, which we believe, can lead to significant over or under billing. Adjusting billing at year-end ensures that the amount of indirect costs reimbursed is as close to the certified amount (claimed cost) as possible.

b. DCAA Recommendation

KBR should develop procedures and controls to ensure that year-end adjustment vouchers are properly prepared. The process should provide for the segregation of cost by year so that rate adjustment can be easily made and the rates used can be identified.

KBR Response to Condition 3:

KBR will formalize the DCAA's recommendation, in conjunction with the FY 2003 incurred cost submission preparation, as part of its billing procedure manual.

1999 is the most current audited and negotiated final indirect cost rate. KBR has submitted adjusting invoices for the actual final un-audited years (FY 2000, FY 2001, & FY 2002) indirect cost rates.

4. DCAA-Lack of Appropriate Reviews and Approvals of Vouchers

a. DCAA Condition

KBR failed to follow its billing procedures when processing vouchers. We examined 14 interim vouchers prepared between April and August 2003 and found that the contractor had completed neither the project checklist nor the management checklist for two of the 14 interim vouchers. We also found that the contractor had not completed the management checklist on nine of the 14 interim vouchers. The deficiencies noted impact three major contracts, DACA78-99-D-0003, DABT23-01-C-0008 and DAKF11-99-D-0006.

KBR Government Operations Guidelines and General Billing Procedures for U. S. Government Contracts (billing procedures) states "The project business manager (sometimes called project accountant), or designee, must complete and sign the checklist entitled "Project Checklist for Reviewing Invoices before Submittal." The billing procedures also states "The project manager, or designee, must

complete and sign the "Checklist for Management Review of Invoice" before the invoice can be submitted for payment."

We believe cost-reimbursement contract represent an increased risk to the government when the contractor's billing system does not protect or detect against billing errors. It is vital that the contractor has controls in place to minimize the risk of over billing the government.

b. DCAA Recommendation

KBR should follow its billing procedures. KBR procedures state that the project business manager should complete both the project checklist and management checklist when processing vouchers.

KBR Response to Condition 4:

KBR has implemented corrective action and is monitoring the completion of the checklists in accordance with the KBR billing procedures

5. DCAA-Failure to Notify ACO of Refunds and Over Payments

a. DCAA Condition

During our audit, we determined that KBR did not notify the Administrative Contracting Officers (ACO) or the paying offices prior to submitting credit public vouchers. A $382 thousand credit public voucher for contract number N62470-00-D-0005, delivery order 003, invoice number 0208-304-UR651, dated August 27, 2002, was sent to the Navy CONCAP payment office without prior notification to the ACO or paying office. In another instance, a $17 thousand credit public voucher for contract number DABT-63-98-C-0060, voucher number 03034, was sent to the Army contract paying office without prior notification to the ACO or paying office. In addition, KBR did not include the checks due the government with the credit public vouchers. During 2001, KBR identified and reported to the General Accounting Office three overpayments totaling $53 thousand relating to contract numbers DAKF11-99-D0066 and FA2550-96-C-0003, but it did not refund the overpayments in a timely manner. Also, in September 2002, KBR identified a duplicate payment of $107 thousand for Army Corps of Engineers contract number DACA31-97-D-7000, which remains unresolved as of this date.

KBR's government billing procedures require contacting clients and/or the paying office to resolve issues regarding past-due invoices and any overpayments or underpayments within 30 days of identification of the issue and/or follow up as necessary until final resolution. Also, recently the Federal Acquisition Regulation (FAR) was amended to require the contractor to notify the contracting officer if the contractor becomes aware of an overpayment on a contract invoice (see FAC 2001-02).

KBR is not complying with its policies and procedures for resolving overpayments in a timely manner or within 30 days of identifying overpayment. KBR refunded the Navy contract overpa yment for $382 thousand on June 10, 2003, which was 490 days after the overpayment was made. The $53 thousand overpayment identified by KBR in 2001 was not resolved until September 2003 or about 845 days after KBR received the overpayment. The duplicate payment of $107 thousand identified by KBR in September 2002 on the Army Corps of Engineer contract has not been resolved as of this date.

b. DCAA Recommendation

KBR must comply with its polices and procedures for resolving overpayments in a timely manner or within 30 days of identifying an overpayment;

KBR must comply with its polices and procedures and FAR for notifying contracting officers and paying offices to resolve issues regarding past-due invoices and overpayments or underpayments within 30 da ys of identification of the issue and follow up as necessary until final resolution;

All significant overpayments/duplicate payments or over-billed amounts returned to the paying offices as refunds using credit public vouchers must be accompanied with checks for the amount of the credit voucher; and

KBR needs to ensure significant refunds are made only after notification and instruction from the contracting officer and/or the paying office.

KBR Response to Condition 5:

The duplicate payment of $107 thousand for contract number DACA31-97-D-700 was resolved with the client's directive in September 22, 2003 and the information was provided to the DCAA October 29, 2003.

KBR has implemented corrective action to comply with its procedure and is currently contacting the client and the paying office by correspondence within the 30 days after identifying an overpayment. After notification the resolution may extend beyond the 30 days, however, KBR will continue to work towards final resolution.

6. DCAA-Lack of Reconciliation of Recorded to Billed Costs and Submission of Final Vouchers

a. DCAA Condition

KBR does not periodically reconcile recorded costs and billed costs on physically complete (but not closed) contracts. Additionally, KBR is not submitting final or completion vouchers for closeout of physically completed contracts on a timely manner. Our review disclosed two contracts, which were physically completed in December 1998, that are in an overpaid status, i.e. billed costs are greater than recorded costs. The LOSC cost reimbursable contract number F08650 -95-C-6038, which was physically completed in December 1998, is overbilled by approximately $150 thousand. The NASA cost reimbursable contract number NAS9-18787, which was physically completed in December 1998, is over billed by approximately $28 thousand. Both of these overpayments are unresolved as of this date.

FAR 52.216 -7d requires a contractor to submit completion vouchers for closeout of physically completed contracts within 120 days after settlement of the final indirect cost rates for all years in which the contract incurred costs.

b. DCAA-Recommendations

KBR should establish procedures and internal controls to ensure reconciliations of billed and recorded costs are performed on a periodic basis for all contracts (including physically completed contracts awaiting closeout). Also, KBR should ensure that final vouchers for physically completed contracts are submitted within 120 days after the settlement of the applicable final indirect ra tes. If

billed costs exceed recorded costs, revised billings and refunds should be submitted within 30 days.

KBR Response to Condition 6:

Please see KBR Response to DCAA Condition 3 above.

7. DCAA-Lack of adequate contract briefings

a. DCAA Condition

KBR does not properly brief its contracts and the associated task orders. Specifically, contracts N62470-00-D-005 and DAAA09-02-D-0007 does not have a contract brief on each of the associated task orders. The contractor prepares a contract summary which summarized the contract and the task orders. The contract summary included information such as performance period, brief description, and the cost of the contract or task order as modified. The contract summary does not identify special requirements or limitations nor does it identify the contract clauses relative to the specific task orders.

KBR's Contract Policy & Process, CA-S-03, dated August 29, 2002 states the contractor "shall develop a contract post award summary and the DCAA contract brief" as soon as possible but no later than three business days after contract award. The policy continues on to state, KBR "shall update the DCAA Contract Brief or KBRSI Contract Billing Summary as needed (i.e., upon receipt of the contract modification but, no less than on an annual basis)."

b. DCAA Recommendation

We recommend KBR brief each contract and task order as prescribed by its policies and procedures. We also recommend that KBR include any special requirements or special limitations in each of the contract briefs.

KBR Response to Condition 7:

KBR will to the maximum extent practicable ensure that contract briefs include billing details, contract types and other pertinent data important for the billing process.

8. DCAA-Billing of Unallowable Costs

a. DCAA Condition

BRS billed unallowable costs on Contract No. F04701 -90-C-0080. BRS's final invoice included approximately $45,000 in costs including overhead and G&A that had been determined to be unallowable by DCAA in Audit Report No. 3521-95 D10160003, dated September 30, 1997, and agreed-to by the contractor. The contractor reduced interim vouchers for the questioned costs, but BRS did not reclassify the questioned costs to an unallowable account in the ledger. BRS prepared the final voucher from its accounting records which did not reflect the unallowable costs, resulting in billing the unallowable costs in its final voucher. We believe the lack of written general billing procedures prescribing actions to take regarding costs determined to be unallowable under these or similar circumstances has contributed to this condition.

b. DCAA Status of Corrective Action Taken on Prior Recommendations

The contractor developed and implemented KBR Government Operations Guidelines and General Billing Procedures for U. S. Government Contracts (billing procedures) dated November 1, 2002. We believe the billing procedures addressed the unallowable/unallocable costs criteria necessary for the billing system.

KBR Response to Condition 8:

KBR concurs with the DCAA's postion.

9. DCAA-Inadequate Controls over the Dining Facility Subcontract Cost Billing Process

a. DCAA Condition: DCAA Condition

1.1:

KBR's internal controls over payments to subcontractors are inadequate. The existing process does not provide assurance that payments made to Dining Facility (DFAC) subcontractors and billed to the Governmentare adequately supported and computed in accordance with prime contract and subcontract terms and conditions. The LOGCAP III contract requires KBR to provide DFAC services in support of Government operations in Iraq and Kuwait. Since the inception of LOGCAP III in Kuwait and Iraq, KBR has awarded DFAC subcontracts to seven different subcontractors. The early subcontracts were awarded as stand alone subcontracts. Later DFACs were subcontracted under work releases to Master Agreements, which are similar to Basic Ordering Agreements.

KBR Response To 9.1.1:

KBR's position is that the issues cited by DCAA in support of this Statement of Condition (9.1.1) have been misquoted as well as misinterpreted. The end result is that a difference of opinion between DCAA and KBR regarding certain DFAC subcontract terms is now mischaracterized herein as a billing system control deficiency.

DCAA is aware that KBR established a Tiger Team that is actively researching and analyzing the facts and circumstances surrounding each of its DFAC subcontracts. This effort includes a thorough review and analysis of past subcontract payment practices as well as developing standardized subcontract practices for future DFAC subcontracts.

Thus, KBR believes any conclusion at this time regarding KBR's billing procedures related to the payment of DFAC subcontracts is not only unsubstantiated but also premature.

DCAA Condition 1.2:

KBR is paying DFAC subcontractor invoices that are not reasonable in amount and are not computed in accordance with subcontract terms and conditions.

The subcontract required the subcontractor to create a billing format to include "meals served for each billing item." The subcontract indicates that ***meals served*** *will be the basis of the billed amounts as follows:*

> *"SUBCONTRACTOR will create a Subcontract billing format acceptable to CONTRACTOR, to be used for all payments. This form will include, but not be limited to the full name and address of the Subcontractor work performed, and* ***meals served*** *for each billing item; the previous billed amount; the 'to date' billed amount; the billing period, and the SUBCONTRACT number."*

The actual billing methodology did not consider actual meals served in determining the billing amount, despite the expressed terms of the subcontract. Instead, as far as we have been able to determine, KBR relied on the undocumented "Mayor Cell Count," which was not authorized in the contract. We don't believe the "Mayor Cell Count" was a reasonably close app roximation of meals served. However, KBR stated that payments to its DFAC subcontractor were based on "Mayor Cell Counts" provided by one or more Non Commissioned Officers or in some cases, a warrant officer. The Mayor Cell Count was provided for planning purposes only and was never intended to be used for billing. The numbers that were provided to KBR for planning purposes can not be independently verified. KBR asserted that the number was provided verbally to them and could not be written down because it was considered classified. We found, however, that KBR wrote down and used this "classified" number in their billings to the Government. The use of the undocumented "Mayor Cell Count" as a basis for payment has resulted in billings to the Government for as much as three times the meals actually served.

KBR Response To 9.1.2:

Please see KBR's response to 9.1.1 above.

DCAA Condition 1.3:

The prime contract required KBR to develop, coordinate and publish a standard operating procedure for food service personnel to include instruction sheets for headcounters. Until December 18, 2003, KBR never issued a procedure addressing headcount procedures. Having a n adequate headcount procedure in place would have provided an accurate count of meals served for billing purposes.

KBR Response to condition 9.1.3:

Please see KBR's response to 9.1.1 above.

DCAA Condition 1.4:

KBR has not maintained adequate controls over the subcontract payment process for DFACs subcontracted under Master Agreements. KBR is not adequately monitoring subcontractor invoices for compliance with prime contract and master agreement terms and conditions. The subcontract payment terms state that the subcontractor will create a billing format that will include "the number of persons tha t actually ate breakfast, lunch, dinner, and midnight meals formulated from sign in sheets for each meal." KBR is not using sign in sheets across all master agreement DFACs. In addition, KBR has been billing at projected headcounts rather than actual meals served on at least one of the subcontracts. (This practice has recently been discontinued pending resolution of outstanding billing issues.) Despite repeated requests over two months, KBR has not been able to provide an adequate explanation or adequate documentation for the payments to any DFAC subcontractors. The limited documentation that has been provided shows, for example, that KBR has added "overage" factors of 10 to 35 percent to each bill for one of the subcontractors. We still do not have an adequate explanation of the "overage" factor. We saw a reference to a 10 percent factor as a "wastage" amount in the subcontract correspondence file, but no reference to a 35 percent factor.

A contractor should be able to provide supporting data for its billed costs when a routine audit inquiry is made. A system should be in place to provide such supporting documentation in a reasonable time frame. Our first request for supporting data was made as early as November 9 and followed up with several additional requests. On February 1, 2004, we did receive some supporting data, but it is far less than we requested. The fact that KBR has been unable to demonstrate the process for monitoring and paying subcontractor DFAC invoices shows that a significant internal control deficiency exists.

KBR Response to condition 9.1.4:

Please see KBR's response to 9.1.1 above.

DCAA Condition 1.5:

We identified an instance where the KBR DFAC subcontract negotiator was also one of three KBR representatives responsible for approving DFAC subcontractor invoices for the same subcontract he negotiated. This procedure does not represent adequate segregation of duties for internal control purposes. We believe that this could have been a contributing factor to the continued billing issues we identified on the DFAC subcontract for site 5a at Arifjan.

A different subcontract administrator from the one who negotiated the original subcontract should have been required to approve the billings. If this were the case, the billing issues could have been identified at an early stage and possibly corrected.

KBR Response to Condition 9.1.5:

Please see KBR's response to 9.1.1 above.

b. DCAA Recommendation:

DCAA Recommendation 1:

KBR should implement a standardized DFAC subcontract payment process. The procedures should require that subcontracts include clear and reasonable payment terms. The negotiated subcontracts should have a detailed level management review to identify any shortcomings. Appropriate personnel should review the billings to verify that the services have actually been provided and that the amounts invoiced are in accordance with payment terms. Authorization for payment should come from a KBR procurement official who was not involved in negotiating the subcontract.

KBR Response To Recommendation 9.1

Please see KBR's response to condition 9.1.1 above.

DCAA Recommendation 2:

KBR should perform an internal analysis of the billing issues we identified and determine the cost impact. Amounts which can not be supported for payment in compliance with prime and subcontract terms should be voluntarily withdrawn from billings until such support can be provided.

KBR Response To Recommendation 9.2

Please see KBR's response to condition 9.1.1 above.

DCAA Recommendation 3:

KBR should use actual headcount/meals served as a basis for their subcontractor's billings in accordance with the terms of the contract. Subcontracts with DFAC vendors should be renegotiated to reflect reasonable terms based on actual services provided.

KBR Response To Recommendation 9.2

Please see KBR's response to condition 9.1.1 above.

END OF DOCUMENT

NOTE: This KBR Response to DCAA Audit Assignment No. 3311 -2002K11010001 contains proprietary and confidential information which is authorized to be withheld from the public . Disclosure would cause a foreseeable harm to an interest protected by one or more Exemptions of the Freedom of Information Act, 5 USC Section 552. Furthermore, it is requested that any Government entity receiving this information act in accordance with DoD 5400.7-R, and consider this information as being for official use only (FOUO), and mark, handle and secure this information so as to prevent unauthorized access.

Audit Report

Federal Deployment Center
Forward Operations at the Kuwait Hilton

Report Number 04-003 **June 25, 2004**

Office of the Inspector General
Coalition Provisional Authority

Acronyms

AAFES	Army Air Force Exchange Service
ACO	Administration Contract Officer
CONUS	Continental United States
CPA	Coalition Provisional Authority
CRC	CONUS Relocation Center
DA	Department of the Army
DoD	Department of Defense
EXORD	Execution Order
FDC	Federal Deployment Center
FDC-Forward	Federal Deployment Center at the Kuwait Hilton
IDIQ	Indefinite Delivery, Indefinite Quantity
ITO	Iraq Theater of Operation
KBR	Kellogg Brown & Root, Inc.
LOGCAP	Logistics Civil Augmentation Program
RCO	Requirements Control Office
RSO&I	Reception, Staging, Onward-Movement, and Integration

COALITION PROVISIONAL AUTHORITY
OFFICE OF THE INSPECTOR GENERAL

June 25, 2004

MEMORANDUM FOR ADMINISTRATOR, COALITION PROVISIONAL AUTHORITY

SUBJECT: Report on Federal Deployment Center Forward Operations at the Kuwait Hilton (Report No.04-003)

We are providing this report for your information and use. We performed the review at the request of your office. We considered management comments on a draft of this report in preparing the final report.

Comments on the draft of this report were responsive to our recommendations and left no unresolved issues. Therefore, no additional comments are required. However, we will follow-up to ensure corrective actions are fully implemented by management.

We appreciate the assistance extended to the staff. Questions should be directed to Mr. Brian Flynn, (703) 343-8953 or Mr. William Whitehead, (703) 343-8954. Management may request a formal briefing on the results of this audit.

Stuart W. Bowen, Jr.
Inspector General
Coalition Provisional Authority

400 Army Navy Drive • Arlington, Virginia 22202

Office of the Inspector General
Coalition Provisional Authority

Report Number 04-003 **June 25, 2004**
(Project No. D2004-DCPAAO-0024)

Federal Deployment Center Forward Operations at the Kuwait Hilton

Executive Summary

Introduction: The Inspector General accomplished this review at the request of the Coalition Provisional Authority (CPA) Deputy Chief of Staff who had concerns about unauthorized personnel using the facility. The Federal Deployment Center (FDC) at the Kuwait Hilton (FDC-Forward) provides a location for reception, any further deployment training, and re-deployment of executive personnel. Total annual cost for this operation is over $11 million. The Department of the Army (DA) established FDC-Forward at the Kuwait Hilton as the reception location for, "...executive personnel deploying in support of operations in Iraq."

The Department of the Army issued an indefinite delivery, indefinite quantity cost plus award fee contract (DAAA09-02-D-0007), Logistics Civil Augmentation Program (LOGCAP), was issued to Brown & Root Service, a Division of Kellogg Brown & Root, Inc. to provide civil augmentation for base operations and support to the DA throughout the world. The DA issued Task Order 0063, on August 27, 2003, to provide deployment processing for federal executives deploying to the Iraq Theater of Operations.

Objective: The objectives of this review were to determine whether the CPA efficiently and effectively operated FDC-Forward. Specifically, objectives were to determine whether FDC-Forward (1) met the purpose for which it was established by Department of Army Execution Order and (2) established policy to limit the use of FDC-Forward facility to authorized personnel.

Conclusion: The FDC-Forward operation met the purpose established in the Department of Army Execution Order; however no CPA policy existed for usage, which led to inefficient use of CPA resources. Specifically, the CPA did not:

- Provide adequate oversight of the operation to ensure CPA costs were limited to those for authorized users.

- Have a defined policy identifying those persons eligible to use the FDC-Forward Kuwait Hilton facility. Without established policy, contractor employees allowed unauthorized persons to use the Kuwait Hilton at the expense of the CPA.

Recommendations: We made eight recommendations to the CPA Chief of Staff to improve the effectiveness of FDC-Forward operations.

Managements Actions: During the review period, the CPA Chief of Staff concurred with all recommendations and fully implemented seven of the eight recommendations. The Chief of Staff is in the process of implementing the remaining recommendation. Implementing the eight approved recommendations will result in a minimum annual potential monetary benefit of $3.6 million (32 percent of current annual cost).

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Background

The Inspector General accomplished this review at the request of the Coalition Provisional Authority (CPA) Deputy Chief of Staff who had concerns about unauthorized personnel using the facility. The Federal Deployment Center (FDC) at the Kuwait Hilton (FDC-Forward) provides a location for reception, any further deployment training, and re-deployment of executive personnel. Total annual cost for this operation is over $11 million. The Department of the Army (DA) established FDC-Forward as the reception location for, "...executive personnel deploying in support of operations in Iraq."

The Department of the Army issued an indefinite delivery, indefinite quantity (IDIQ) cost plus award fee contract (DAAA09-02-D-0007), Logistics Civil Augmentation Program (LOGCAP), was issued to Brown & Root Service, a Division of Kellogg Brown & Root, Inc. (KBR) to provide civil augmentation for base operations and support to the DA throughout the world. This is The DA issued Task Order 0063, on August 27, 2003, to provide deployment processing for federal executives deploying to the Iraq Theater of Operations (ITO).

The Coalition Provisional Authority (CPA) established the FDC-Forward to provide support and meet requirements outlined in the DA Execution Order (EXORD) for training, equipping, and processing of non-unit related personnel reporting individually for deployment to the ITO. Other deployment centers were established at Fort Belvoir and Fort Bliss. The EXORD for Deployment Centers specifically addresses employees such as U.S. military forces, federal civilian employees, contractors supporting the Department of the Army, Red Cross employees, Army Air Force Exchange Service (AAFES) employees, Department of Defense (DoD) civilian employees, and senior executive service employees. Each deployment center's required functions included: providing pre-deployment and post-deployment medical screening of health records and blood samples; reviewing inoculation records and providing any needed inoculations; issuing and accounting for personal protection equipment; briefing on security and local threat conditions; transport to and from the ITO; and providing other logistics for ITO transitioning.

The DA implementing EXORD directed certain categories of personnel (i.e., U.S. military, contractors supporting the DA, Red Cross employees, and AAFES employees) to process through the continental United States (CONUS) Relocation Center (CRC) at Fort Bliss, Texas and senior executives to process through the Federal Deployment Center (FDC) at Fort Belvoir, Virginia. Personnel supporting the CPA who processed through the FDC-Fort Belvoir are transitioned through Kuwait and lodged at the FDC-Forward. In Kuwait, personnel receive required briefings and await transportation to the ITO. The FDC-Forward (through the Contractor) presently leases office space and personal room space from the Kuwait Hilton.

Objective

The objective of this review was to determine whether the CPA efficiently and effectively operated FDC-Forward. Specifically to determine whether FDC-Forward met the purpose for which it was established by DA Execution Order and established policy to limit the use of FDC-Forward facility to authorized personnel.

Finding A. Operations of the Federal Deployment Center at the Kuwait Hilton

The CPA did not provide clear guidance on who is eligible to use of FDC-Forward. As a result, the contractor allowed all requestors supporting CPA's mission to billet and mess there, charging the cost to the CPA. Additionally, in the absence of adequate CPA oversight and guidance, the contractor procured billeting and office space beyond CPA requirements. Allowing unauthorized persons to use the FDC-Forward facility meant that the available bed space was limited and the contractor turned away authorized personnel. Also because available space was limited, the FDC-Forward medical, administrative, briefing, and equipment issue functions were performed in more expensive office locations in the main hotel. The resulting additional costs incurred under the task order amounted to $3.64 million annually. Specifically, the:

- Director for Reception, Staging, Onward-Movement, and Integration (RSO&I) leased an individual room in the main hotel costing over $101,000 annually and maintained an office in the main hotel costing more than $152,000 for the year. The RSO&I operation costs more than $253,000 annually.
- Medical and equipment issue functions were located in the main hotel costing CPA $171,000 annually. CPA also rented an office to conduct local threat briefings at a cost of $85,428 annually and an office for KBR to use for Material Control also costing $85,428 annually. These four offices cost over $342,000 annually.
- Contractor employees were lodged in the main hotel costing $2.85 million annually.
- Government is projected to reimburse the hotel $191,000 annually for laundry service in place of providing a washer and dryer in each villa.

The contract administration staff of the Defense Contract Management Agency did ensure that the contractor provided all services required under the terms of the task order. Contract administration staff saw to it that the contractor:

- Provided credentialed medical staffing to conduct medical screening for persons deploying to the ITO, as well as post-deployment processing, to include inoculations, and blood sampling;
- Issued and accounted for personal protection equipment such as protective vests, helmets, gas masks, canteens, desert camouflage uniforms, and boots;
- Conducted training briefings for security, local threat conditions, and personal protection (chemical environment, unexploded ordinance, etc.); and,
- Provided transportation (or assisted with arrangements) to and from the military air transportation location and the civilian airport.

However, the statement of work for the task order was written in generic terms and, in the absence of specified task order provisions, the CPA did not apply adequate oversight to ensure that operating costs were minimized; review and analyze the details of the cost reports provided from the contractor to identify opportunities to minimize costs; or establish clear limitations on the costs that the contractor could incur under the task order.

As a result of the limited task order oversight, additional costs incurred under the task order amounted to $3.64 million annually. Additionally, the contractor billeting records were insufficient to determine the appropriateness of some costs related to unauthorized individuals who were billeted at FDC-Forward. Without sufficient records, accurate costs for the inappropriate use could not be determined and refunds from unauthorized users could not be pursued.

Recommendations and Management Actions

A. We recommend that the CPA Deputy Chief of Staff:

1. Require the Administration Contract Officer (ACO) to conduct a detailed review of contractor cost reports.

   Management action. The Deputy Chief of Staff concurred with the recommendation and implemented corrective action. The Requirements Control Office (RCO) of the CPA now receives weekly billeting reports to review for authorized use. In addition, the CPA RCO directed the ACO to review detail level costs to determine whether costs are appropriate.

2. Relocate living quarters for the Director, RSO&I from an individual room in the main hotel to a room in a villa, saving $101,000 annually.

   Management action. The Deputy Chief of Staff concurred with the recommendation and implemented corrective action. The Director of RSO&I has relocated to living quarters in a villa.

3. Relocate the medical and equipment issue functions from the office locations in the main hotel to a room in a villa saving $171,000 annually.

   Management action. The Deputy Chief of Staff concurred with the recommendation and implemented corrective action. The Director of RSO&I coordinated with the contractor to relocate the medical and equipment issue functions to a villa.

4. Relocate Contractor employees supporting the CPA from individual rooms in the main hotel to rooms in a villa saving over $2,853,000 annually.

   Management action. The Deputy Chief of Staff concurred with the recommendation and implemented corrective action. The Director of RSO&I

coordinated with the contractor to relocate 28 contractor employees from individual rooms in the main hotel to rooms in a villa.

5. Relocate the FDC briefings, administrative office of the Director RSO&I, and the contractor's Material Control office from the main hotel to a room in a villa saving, at least, $323,000 annually.

   Management action. The Deputy Chief of Staff concurred with the recommendation and implemented corrective action. The Director of RSO&I coordinated with the contractor to identify a villa location for the briefings. The Director also coordinated with contractor representatives to relocate the Equipment Issue function and the Director's administrative office from the main hotel to a villa

6. Install a washer and dryer in each CPA rented villa and discontinue government reimbursement of over $191,000 projected annually for Kuwait Hilton laundry service.

   Management action. The Deputy Chief of Staff concurred with the recommendation and implemented corrective action. The Director of RSO&I coordinated with the contractor to procure additional washer and dryer machines already available under the Logistics Civil Augmentation Program contract to supply one pair each per villa and directed the use of the hotel's laundry service be discontinued.

Audit Response

The Deputy Chief of Staff's actions are fully responsive. We commend the Deputy Chief of Staff for prompt and aggressive action to establish management controls and reduce task order costs. However, because the Director, Reception, Staging, Onward-Movement, and Integration could not provide a date by which all corrective action would be implemented, we will follow–up to ensure that the corrective actions proposed in response to Recommendations A.3., A.4., A.5., and A.6. are fully implemented.

Finding B. Eligibility for Use of the Federal Deployment Center in Kuwait

The CPA did not have a defined written policy identifying those persons eligible to use the FDC-Forward. Specifically, the statement of work for the task order indicated that, "senior level personnel" were authorized to use FDC-Forward. However, the statement of work did not define senior level personnel. Also, the DA EXORD stated that, "executive personnel" would process through the FDC-Forward, again without defining executive personnel. Finally, CPA implementing guidance did not define what personnel categories (non-U.S. military, Department of State, other contractors) were to be supported by the contractor. Therefore, the contractor interpreted who was eligible to use FDC-Forward. Generally, the contractor allowed any person supporting the CPA to stay at the FDC-Forward facility and charged the cost to the CPA.

The initial Director for RSO&I gave the contractor representative verbal guidance that the FDC-Forward facility could be used by all categories of personnel for any purpose. However, the Director of RSO&I did not discuss this issue with the ACO to determine, based on the contract, what was allowed. As a result:

- U.S. appropriated funds were used for unauthorized guests;
- CPA inappropriately paid for contractor employee's use of the FDC-Forward facility for their rest and recuperation; and,
- CPA was not reimbursed for non-CPA personnel billeted at the FDC-Forward facility.

Without established written policy, CPA paid for unauthorized and unnecessary expenditures.

Recommendations and Management Actions

B. We recommend that the CPA Deputy Chief of Staff:

1. Establish and provide contractor representatives written policy defining who is eligible and the process for using the FDC-Forward facility.

   Management action. The Deputy Chief of Staff concurred with the recommendation and implemented corrective action. CPA Policy was issued on April 8, 2004, defining the reservation and use process. The policy clearly defined the category of users eligible to use the facility. The CPA Deputy Chief of Staff coordinated the policy with the ACO to ensure any action or changes to cost estimates for the contractor would be approved. Further, the CPA provided specific guidance to the Director for RSO&I identifying responsibilities and authority, as well as, instruction to address any unclear issues to the Director, RCO of the CPA for resolution.

2. Require the ACO to periodically monitor contractor performance, as well as, FDC-Forward requirements to ensure issues are interpreted using the contract or amending the contract as necessary.

   Management action. The Deputy Chief of Staff concurred with the recommendation and implemented corrective action by requiring the contractor to provide the RCO of the CPA with a copy of all contract issues and concerns raised to the Director of RSO&I. The RCO has been made responsible for reviewing and forwarding these issues and concerns to the ACO. Additionally, the CPA Deputy Chief of Staff required the ACO to periodically visit the site for personal observation of contract performance. The first such visit was made on May 10, 2002.

Audit Response

The Deputy Chief of Staff's actions are fully responsive. We commend the Deputy Chief of Staff for prompt and aggressive action to establish management controls and reduce task order costs.

Appendix A: Scope and Methodology

Audit Scope. The CPA Deputy Chief of Staff requested this review. Although we used audit techniques to review the objectives, only limited guidance existed to provide standards. When a standard did not exist, we applied best business practices as determined by the review team based on experience and comparable operations. We maintained close liaison with the CPA to provide immediate feedback on conditions and recommendations for possible management action.

Audit Coverage

- During the period from March 31 to April 4, 2004, with follow-up from April 17 to April 19, 2004, we conducted personal interviews with personnel at the FDC-Forward facility. Personnel interviewed included the contractor's Lead FDC Operations, Billeting Supervisor, Project Control Officer, and LOGCAP III Government Compliance Manager. We also interviewed the Government's Director RSO&I, CPA-RCO and the ACO for LOGCAP III, Task Orders 0044 and 0063 to obtain operational and cost information. We reviewed the contractor's billeting records to determine who and why persons billeted at the FDC-Forward, we then tested this through personal observation at airport arrival and hotel arrival. We used cost information from the January 2004 billing from the contractor based on Hilton Hotel billing to the contractor to determine operational costs.

- The audit reviewed the LOGCAP III, Task Order 0044 and 0063 FDC operations at the FDC-Forward location. The audit scope was limited to the FDC operations, more specifically, to the hotel, meals, and laundry costs associated with these Task Orders.

- The audit was conducted from March 31 through April 19, 2004.

- The only source document we relied on for specific information was the January 2004 contractor billing to the Government. The contractor Project Control Officer provided this document and stated to the best of her knowledge the information was clearly and accurately presented. The contractor Billeting Supervisor provided registration forms for the period of December 2003 and a recently created EXCEL spreadsheet for registrations from November 2003 through February 2004; however, most of these forms and registration entries were incomplete and lacked sufficient information. As a result, we could only draw general conclusions from this information.

- We provided the CPA Director, RCO a copy of the draft report on May 11, 2004.

- We evaluated general internal controls to determine whether only authorized users received the benefit of this operation. Specifically, we interviewed the KBR

Billeting Supervisor to determine rules and policy for room assignment, meal card provisions, and the registration process.

Sampling Methodology. We did not use statistical or judgmental samples or computer assisted auditing tools and techniques to analyze data or project results in this audit. While reviewing the registration forms, we included information from only those forms we found legible, complete, and understandable. Selection was not based on sampling, rather meeting the above criteria.

Data Reliability. We did not rely on computer-generated data to support our conclusions.

Auditing Standards. We conducted the audit in accordance with generally accepted government auditing standards.

Discussion with Responsible Officials. On April 6, 2004, we provided an out brief of our review to the CPA Deputy Chief of Staff, CPA Director RCO, and the ACO for LOGCAP III Task Orders 0044 0063. At that time the CPA Deputy Chief of Staff concurred with the audit conclusions and recommendations. Subsequent to the April 17 to 19, 2004 follow-up review, we provided a Memorandum for Record reiterating our conclusions along with completed management actions to the CPA Director of RCO.

Prior Audit Coverage. We did not find evidence of any prior audit coverage in this area.

Appendix B: Report Distribution

Office of the Secretary of Defense

Under Secretary of Defense (Comptroller)/Chief Financial Officer
Director, Defense Procurement and Acquisition

Department of the Army

Assistant Secretary of the Army, Acquisition, Logistics & Technology
Auditor General, Department of the Army

Other Defense Organizations

Administrator, Coalition Provisional Authority
Director, Coalition Provisional Authority Program Management Office
Department of Defense Inspector General
Director, Defense Contract Audit Agency

Non-Defense Federal Organization

Office of Management and Budget
General Accounting Office
Department of State
U.S. Agency for International Development
Department of Health and Human Services Inspector General
Department of Commerce Inspector General

Congressional Committees and Subcommittees, Chairman and Ranking Minority Member

Senate Committee on Appropriations
Senate Subcommittee on Defense, Committee on Appropriations
Senate Committee on Armed Services
Senate Committee on Governmental Affairs
Senate Committee on Foreign Relations
House Committee on Appropriations
House Subcommittee on Defense, Committee on Appropriations
House Committee on Armed Services
House Committee on Government Reform
House Subcommittee on Government Efficiency and Financial Management, Committee on Government Reform
House Subcommittee on National Security, Emerging Threats, and International Relations, Committee on Government Reform
House Subcommittee on Technology, Information Policy, Intergovernmental Relations, and the Census, Committee on Government Reform
House International Relations Committee

Appendix C: Audit Team Members

The Financial Management Division, Office of the Assistant Inspector General for Auditing, Coalition Provisional Authority, prepared this report.

John Betar
Brian Flynn
William Whitehead
Edward M. Terek

Mr. WAXMAN. Now, what you bring to this committee is a different perspective. The auditors come in after the fact and their conclusions are based on a review of the invoices, purchase orders, and billing records. But each of you worked inside the company and saw these problems happen in real time, so you are able to provide a completely new perspective to this committee. Some of the Members may not want to hear this perspective, but it corroborates what all these auditors had to say.

What I would like to do is ask you about some of the auditors' conclusions and see whether you agree with them and whether you observed the kinds of problems they described when you were on the ground in Iraq and Kuwait.

In the audit GAO issued yesterday, GAO found Halliburton had no spending limits for LOGCAP until the spring of 2004, a year after the end of the war. You were over there during this timeframe. I would like to ask each of you, from your perspective, do you think GAO is right when it says that Halliburton had no spending limit?

Mr. Warren, do you know?

Mr. WARREN. I don't know, sir.

Mr. WILSON. I wasn't involved in any of the contracting procedures. I couldn't honestly answer that question.

Mr. WAXMAN. Do you think they showed a concern about how well the money was being spent?

Mr. WILSON. At the camp that I was at with the supervisors that I had at that time, no, sir.

Mr. WAXMAN. Mr. Warren.

Mr. WARREN. Personally, it seemed like there was no end in sight for the money being spent. It was just nothing but the best.

Mr. WAXMAN. How about you, Ms. deYoung?

Ms. DEYOUNG. I was in Kuwait and these gentlemen were in Iraq. There was no regard for spending limits, but the priorities were backward. Luxuries, KBR came first, soldiers, the people in the field were second.

Mr. WAXMAN. People in the field?

Ms. DEYOUNG. KBR people. KBR people.

Mr. WAXMAN. The DCAA audit from May found systemic deficiencies in Halliburton's billing practices.

Ms. deYoung, you were working in Halliburton's subcontract office and were involved with billing issues. Based on your experience on the ground, do you agree with the auditors at DCAA that there were billing problems?

Ms. DEYOUNG. Absolutely.

Mr. WAXMAN. Halliburton argued to DCAA that these were isolated problems. DCAA disagreed and concluded that they were systemic.

Based on your experience, do you know who is right, DCAA or Halliburton?

Ms. DEYOUNG. DCAA was right. They were systemic because they were using manual systems rather than automated systems.

Mr. WAXMAN. What about the CPA Inspector General who found the overcharging at the Kuwait hotel? You found similar problems yourself at the five-star Kempinski Hotel in Kuwait; is that correct?

Ms. DEYOUNG. Yes.

Mr. WAXMAN. The chairman said in his opening statement that Halliburton wanted to move out of their five-star hotels and into the tents on the base; they wanted to move to the cheaper quarters.

This is the exact opposite of your testimony. You said the military asked Halliburton to leave the hotel, so there is a contradiction here. Can you explain this difference?

Ms. DEYOUNG. Halliburton wanted to build man camps, which are a cut above what soldiers were living in. Soldiers were living in tents. The Army, the DCAA was telling our management, come and live in tents with us. And when the man camps go up for soldiers, you can have man camps. But our manager said "no." We had a retired general over there as a manager who met for days with key staff and they couldn't come to an agreement; and he finally went up north to Iraq.

Mr. WAXMAN. Halliburton is going to come before us in this next panel, and Republicans seem to know some of the details of what they are going to say.

Chairman TOM DAVIS. Will the gentleman yield on that?

First of all, every briefing we have had, we have invited you. And second, there is testimony unlike Ms. deYoung's testimony, which she put out today after she appeared here. Their testimony was made available to the minority, and it's in our books and it's in your books. You have the same testimony.

I don't want to leave the impression that we know something about Halliburton that you don't. Every meeting we have had, you have been invited to, and their testimony is in the record books for the public to read today.

I want to clarify that.

Ms. DEYOUNG. Chairman Davis, please know that the extended statement I have is all based on documents that I have previously provided, that I understand both sides do have.

Chairman TOM DAVIS. And we have entered it in the record.

Mr. WAXMAN. When we hear from Halliburton and they say things that we may know about from their statement or we may hear for the first time, we will get a chance to ask some questions.

Do you have any suggestion for questions we ought to ask them?

Ms. DEYOUNG. To ask Halliburton? I would ask them why, if they knew that they could not handle the $7 billion—why did they sign up for a $7 billion contract which—from the day I was hired, they knew it was going to be $7 billion. That number was used up front, this is a $7 billion contract.

Why did they sign on—why, with 10 years of experience in LOGCAP, being a world class oil services company and government contractor, did they sign on with manual requisition systems, with individual data bases rather than an enterprise data system and with inadequate personnel? And if they made a decision to do this as a subcontract operation, which a number of Tiger Team managers did tell me that this is the wave of the future, why did they continue to hire all of these logistics personnel, operations personnel, when these things were being subcontracted out?

They should have hired a couple of hundred subcontract managers instead of people who do operations.

Mr. WAXMAN. That will be helpful.

Today's Washington Post had a couple of articles. On the front page, there is a story about the military might run out of money before the end of the year. The article says that one of the reasons is, "The Army is having trouble paying for the escalating costs of the logistics contract with Halliburton." This is why so many Members are concerned about the kind of waste and abuse that you have described.

And this is the headline, "War Funds Dwindling, GAO Warns." We are running out of money for essential military operations at the same time that companies like Halliburton are squandering millions by putting their employees up in five-star hotels and paying $45 for a case of soda.

Another article in the Washington Post recounts the experience of another former Halliburton employee, who is not testifying today, John Mancini. Mr. Mancini was a procurement supervisor in Halliburton's LOGCAP office in Kuwait, and according to the Washington Post, Mr. Mancini observed Halliburton employees pay inflated fees for cell phone services and buy hundreds of rolls of duct tape at $60 each. He concluded that no one at Halliburton was making sure that government money was wisely spent.

I want to make those comments so people don't think that you are just making all this up.

I yield to my colleague, Mr. Ruppersberger.

Mr. RUPPERSBERGER. Thank you, Mr. Chairman and Mr. Waxman. I think what is important here is that we follow the facts and review what has happened in the past so we can move forward and do things the right way.

You are talking about accountability of taxpayers' money. That's an important issue. More important than that right now are the resources we give to our troops, and that's what's important. So let's get into the area of fact.

Ms. deYoung, it's true you were a chaplain and an officer in the Army before you went to work for Halliburton?

Ms. DEYOUNG. That's correct.

Mr. RUPPERSBERGER. You have firsthand experience of Halliburton's subcontract management because you worked in the LOGCAP subcontracts department in Kuwait, correct?

Ms. DEYOUNG. That's correct.

Mr. RUPPERSBERGER. You have met with the committee staff and briefed them on the problems you found. You provided your observations and conclusions and supplied the committee with scores of documents to support your claims?

Ms. DEYOUNG. That's correct.

Mr. RUPPERSBERGER. I would like to walk through some of those with you. Let's talk about Halliburton's poor, what is alleged, poor subcontract management.

Is it true you and other employees were told to extend subcontracts and increase their value even though no one had determined if equipment or services were still needed?

If you're going to answer the question, stick to the facts.

Ms. DEYOUNG. Yes, that is correct. I will give an example: one contract, 23, people on the Tiger Team who had no background whatsoever in government contracts, accounting government work; contract 23 was for forklifts and other equipment, and there was

no evidence that these things had ever been used. And the Tiger Team auditor suggested that—no invoices had been paid—pay the invoices and extend the subcontract, as if this thing was actually operational.

Mr. RUPPERSBERGER. Were you instructed to pay the invoices even though no one could confirm the services were actually delivered?

Ms. DEYOUNG. Yes, exactly. And my point was, you don't do that. I sent a letter up to the Vice President saying, this is not the way to go. We need to go account by account, look at the documents, check with the end users, Is the equipment there?

Mr. RUPPERSBERGER. Who was the Vice President, and do you have a copy of that letter?

Ms. DEYOUNG. Yes, I do. And if I haven't forwarded that one, I'll be very happy to forward it. Vice President Burnell and also John Cowings were there.

Mr. RUPPERSBERGER. Did you get a response to that letter?

Ms. DEYOUNG. John Cowlings eventually sent a little note saying thank you for your experience.

Mr. RUPPERSBERGER. That letter would be important as evidence. You testified that Halliburton site managers were denied subcontract documents?

Ms. DEYOUNG. I'm sorry?

Mr. RUPPERSBERGER. You testified that Halliburton's site managers were denied subcontract documents so that you could see what the subcontract was about and so you could manage it.

Ms. DEYOUNG. That is correct.

Mr. RUPPERSBERGER. How could they properly manage the subcontracts without these documents? How could anybody you work with do that?

Ms. DEYOUNG. They couldn't. I'll give you an example.

DCMA out at Camp Udairi, they were building the tower and there wasn't a contract in place. The construction managers who were overseeing couldn't get a copy of the contract. DCMA actually fought to get a copy of that contract so that the Camp Udairi staff would have production schedules, time schedules.

Mr. RUPPERSBERGER. Did you complain to upper level management about this?

Ms. DEYOUNG. All of us complained and finally Tom Crum promised——

Mr. RUPPERSBERGER. Who is Tom Crum?

Ms. DEYOUNG. He is the vice president of the Middle East.

When all of these things were becoming public and coming to a head, he finally, in meetings with the site managers in February, promised them we would get subcontracts. But I can send you e-mails that were as late as end of March and early April; people in Iraq who knew me were sending me e-mails because they still couldn't get copies of their dining facilities contracts.

Mr. RUPPERSBERGER. Were these isolated problems, in your opinion, or were they more of intimidation? What were these problems?

Ms. DEYOUNG. As far as——

Mr. RUPPERSBERGER. Isolated problems or—was this one or two incidents or was this a culture of what was occurring?

Ms. DEYOUNG. It was systemic.

Mr. RUPPERSBERGER. And what do you think the reason was that you did not receive their subcontracts?

Ms. DEYOUNG. In some cases, it directly was related to fraud. The people who have been terminated that we know were the perpetrators of fraud, their names are on them, and—for example, the laundry.

When I raised the questions about laundry, I kept telling the procurement managers who were above me, we have independent records to corroborate this. When our auditors put two and two together, they are going to say you weren't managing this properly.

I sent forward a copy of our daily operations report that has the amount of laundry that was listed. When I sent that forward and showed them that we have independent ways of corroborating this information, my immediate manager said, go get the data. I went out to the laundry personnel and got the data. And they said to me, for the year prior, they had tried to look at this and tried to have input, and the people in subcontracts refused to let them see it. They said they had no business getting involved. This is $1.2 million per month.

Mr. RUPPERSBERGER. You were an employee of Halliburton, and the DOD was responsible for managing Halliburton or hiring Halliburton to provide the resources and the services that were needed.

At any time, did you see anyone in the DOD and the Army get involved in this process or try to see what was occurring and whether we were getting what we were paying for?

Ms. DEYOUNG. DCAA was asking questions. And, Congressman, you are opening up a door here if I may explain something that is very frustrating to me. I have been subject to audits, when I ran Army day care centers. Auditors come in and they look at your books directly.

Mr. RUPPERSBERGER. The price of management, accountability.

Ms. DEYOUNG. And yet in this system here, with private contractors, all of the information is getting filtered through government operations people, and I think that is the first correction that needs to be made. These auditors need to be able to come right in and take a look at your books the same way they would if I was running an Army day care, an Army guest House or an Army chaplain fund.

Mr. RUPPERSBERGER. Based on your observations, are you saying that you didn't see the Army involved at all in any of these issues that you were concerned about?

Ms. DEYOUNG. I saw the Army asking the questions. And then the KBR, personnel who were in government operations, were trying to filter the information down. And I provided e-mail examples where managers were instructing me to filter down the information, only give them what they ask, which is not what they need to know in order to know whether or not waste, fraud and abuse has happened.

Mr. RUPPERSBERGER. Let me ask you this. During this process when you were employed by Halliburton and you were raising issues that you were concerned about, were you ever reprimanded for providing too much information?

Ms. DEYOUNG. I was verbally chastised.

Mr. RUPPERSBERGER. Who chastised you and what occurred?

Ms. DEYOUNG. The first example was the laundry incident, and I decided to just go ahead and put everything in writing, because that way I would have a record, and I sent the information forward anyway by e-mail. But the managers were basically saying, you are giving too much information.

DCAA started to ask about the transportation mission, and they wanted to have all subcontracts related to transportation to find out what the true cost would be. Once again, I gave them a whole list of everything that they would need, types of contracts.

I was told in that meeting, that's too much. All we want to do is give them this piece. What they needed to know was this much. And I was basically removed from that activity because I was providing too much information.

Mr. RUPPERSBERGER. Let's get into the laundry. Under one subcontract, Halliburton was paying a Kuwaiti company called La Nouvelle a fixed price of over 1 million a month to do laundry at one facility. And because there wasn't much laundry to be done, Halliburton was paying on average of about $100 a bag; is that correct?

Ms. DEYOUNG. That's correct.

Mr. RUPPERSBERGER. Is it true that laundry was much cheaper under other subcontracts even when the laundry came from Iraq rather than Kuwait?

Ms. DEYOUNG. That's correct, and that is with the same company. I was negotiating with them trying to get them to come to terms with that. And the original argument was that there was no data and no way of tracking it, it was a war. This contract was in Kuwait, it was not in Iraq. And when I was able to produce data that their own subcontractors had left with us, that was the point at which they could see that the discrepancy, that we had records to prove that this was a serious overcharge.

Mr. RUPPERSBERGER. Did Halliburton try to renegotiate the contract at that point?

Ms. DEYOUNG. They did not. And for an entire year—and that includes Tiger Team people—for an entire year on that one line item, there is only one letter saying, gee, your prices are too high generically.

Mr. RUPPERSBERGER. In your opinion, we were not getting what we were paying for?

Ms. DEYOUNG. Absolutely not.

Mr. RUPPERSBERGER. And there were other subcontracts that were a lot cheaper?

Ms. DEYOUNG. Absolutely.

Mr. RUPPERSBERGER. You were asked about soda and you discovered that La Nouvelle was charging Halliburton for 37,200 cases of soda per month, but only delivering 37,200 cans. I want you to testify to that because under examination before, there was a discrepancy. And I want you to be able to tell your story about it.

The way I look at it, Halliburton was paying an average of $45 for a case of soda.

Ms. DEYOUNG. That's exactly what they were paying. The concept of a hospitality table, it looks suspicious. Soldiers don't really get treated that well anywhere in the Army. And the contrast between how they live and how Halliburton lives would shock you. If your

son or daughter was over there, you would be very upset. But if we provide that and if everything worked out fine, OK.

The first evidence that I had was monthly bills, monthly invoices that said there were 37,200 cases. I thought this is a perfect contract, it's done well, there's supporting documentation.

I looked at the supporting documentation, and it's only 37,200 cans, no matter how I added, subtracted or divided. And for 4 months this thing was paid. It came out to the price of about $45 per case of soda.

Over there in the desert, I was in the desert, soldiers could get cans off the shelf for 30 cents. You could get a case of soda for $1 or $2. It made no sense to me that Halliburton was paying about $45 a case.

Mr. RUPPERSBERGER. When you informed Halliburton's investigative Tiger Team about this, what was their response?

Ms. DEYOUNG. They tried to make it look like I didn't know how to do these things. You know the old routine, you are a chaplain, you pray. You probably don't know anything about this business.

Mr. RUPPERSBERGER. I don't know the routine, but if that's what it is.

Ms. DEYOUNG. Well, here's the thing. When you are a parish minister or when you're a chaplain in the Protestant world—maybe not in the Holy Ghost church, but in the Protestant world, it is just the way the government should be. A year in advance, you plan out your expenses for your education, for all of those things. You plan out your expenses and then you have to live by that budget.

I said this to a number of managers. There is no reason in the world why Halliburton can't do real-time data management, because they already have a ROM where they estimate what their budget is supposed to cost. When I ran Army day care centers in the 1980's, every month I got statements saying this is what you are supposed to spend. Here's what percentage you have spent to date.

We didn't have that. And we should have had it 25 years later.

Mr. RUPPERSBERGER. I thank you for your testimony and your courage in coming here today. I know it is difficult. Hopefully, the committee will follow the facts and get to the results of fiscal accountability and getting the resources that we need for our men and women in Iraq.

Mr. RUPPERSBERGER. One thing with respect to you, Mr. Warren and Mr. Wilson, I think the question on the issue that was raised about these trucks is not what happened after the trucks were broken down, but the question is why they broke down to begin with.

And the first question is whether you feel it is the Army's responsibility or Halliburton's in what happened before the trucks even broke down. So we have to deal with this issue to begin with. Do you have an opinion?

Mr. WARREN. I am not for sure whose responsibility it was to make sure these trucks were maintained. But Halliburton, KBR, they had built garages in Camp Cedar II and Anaconda. They had these garages built with maintenance crews there onsite. And the whole time I was over there, these maintenance crews were just limited in what they can do. They wouldn't—all they would do is

just change a tire. They would do a little bit of electrical work and that was basically it. We had lots of mechanics over there.

Mr. RUPPERSBERGER. It seems to me it is an issue of management accountability and planning. Truck drivers' lives are at stake over in Iraq, too. And I want to thank you for your service to our country in Iraq.

Mr. WAXMAN. I want to yield to my colleague, Ms. Watson.

Ms. WATSON. I want to say to the three of you who are brave enough and courageous enough to come forth, do not be intimidated by the questioning. Just stick with the truth. When you distort or lie, you forget which one you told. So if you come with the quest of telling the truth, you will be OK.

Our responsibility here is for oversight. And my dear friends on the other side will come to the floor and talk about waste, fraud and abuse.

I was suspicious that the former company of the Vice President got a contract, sole source, unbid. We didn't know anything about it until they were on the ground in Iraq. So I come into this with great amount of suspicions. How did that happen?

I understand today we have spent $65 billion already in Afghanistan and in Iraq. And I understand that because of the budget crunch, it will have an adverse impact on our military.

I love our military. They are the best in the world. We need to treat them like that. And I find it outrageous that Halliburton would put its people up in a hotel. We can quibble how many were in the room, but by the fact that they were paying over $100 U.S. dollars per day and our fighting forces were in tents, there is something that really troubles me there.

Now, I listened very closely to the testimony of the drivers. You are not military men. You are not in on the command and command tactics; is that true, Mr. Warren? Mr. Wilson.

Mr. WARREN. That's true.

Mr. WILSON. Ma'am, as a convoy commander, I did discuss intelligence with my NCOIC, and we did make decisions on whether we would travel a particular route or not, together. And we worked well together.

I was very impressed by our military over there, and I was very happy to have the regular Army as my escorts over there; and they did an excellent job. Several times the decisions that we made saved lives because we decided not to take a route and wait it out, and other convoys did take that route and were attacked.

Ms. WATSON. I think it might have been Mr. Warren, just correct me if I am wrong—that your truck broke down because there was not a filter.

Mr. WILSON. That was my truck, ma'am. It was because of a plugged fuel filter that I had been asking to be replaced, and I was told repeatedly there weren't any replacements at that time for that filter on that truck and I kept running the truck to complete the mission until the truck actually stopped.

Ms. WATSON. Do I understand these are brand-new trucks?

Mr. WILSON. Yes, ma'am. The trucks that I ran when I originally started running the sustainer mission, we picked up in Kuwait and transported to Iraq with our personal effects in those trucks; and those were the trucks that we started the mission with.

Ms. WATSON. And you were traveling on very rough terrain, sandy, dry, scraggly terrain.

Mr. WILSON. The roadways, they actually had rather impressive roadways over there, but you were surrounded by desert and did get caught in dust storms. And probably our worst place to have the trucks operating was on the bases. In Cedar II, it is a dust bowl.

Ms. WATSON. Wise management would say, you need filters.

Mr. WILSON. The trucks need extra maintenance not less maintenance.

Ms. WATSON. The other point I didn't quite understand is why they took the spare tires off the trucks.

Mr. WILSON. Ma'am, I couldn't answer that for you, you have to ask KBR that. I know for a fact when I picked up those new trucks in Kuwait to go into Iraq to begin this mission, the first thing we did was take the trucks to Truckville. We pulled up beside a Conex and put those tires in the Conexes. I thought maybe they were going to ship them to Cedar in those Conexes, but I never saw those tires again.

Ms. WATSON. This is a question for all three of you.

Did Halliburton's Tiger Team do anything to correct these problems or to eliminate the waste? Anyone that would like to respond.

Ms. DEYOUNG. I think I may be the only one who worked with them.

No, they did not.

Chairman TOM DAVIS. Ms. Watson, your time has expired.

Ms. WATSON. Thank you very much, witnesses. Thank you Mr. Chairman.

Chairman TOM DAVIS. We now go to the 5-minute rule, where Members have 5 minutes. Are you all OK? We'll try to wrap it up quickly, because we have two more panels and we have votes that may cut this short.

But let me ask, Ms. deYoung, your allegation the DCAA can't look at private contractor records. Under the contract they are allowed to look at contracting. What do you mean by that?

Ms. DEYOUNG. What I mean is that all of this information—what was happening—DCAA, GAO, they would send information requests, it would go to a government operations team. Their request would come down——

Chairman TOM DAVIS. Government operations team are who?

Ms. DEYOUNG. KBR staff. And then they would send the request down to procurement management. The procurement management would try to gather the data. And the way that they would accumulate the data is where you have this breakdown.

Chairman TOM DAVIS. OK. But under the contract itself, if you read the contract, they are allowed—the government is allowed to come in and look directly at the books. Often they go to the contractor and say get us these answers. But I wanted to clarify that.

Ms. DEYOUNG. Oh, I appreciate that. And I'm suggesting—I'm here to fix problems. I'm not here to say KBR doesn't deserve that job. I'm just saying we need to fix the problems.

Chairman TOM DAVIS. Now, let me ask you this. I have an e-mail you sent to Mr. Lesar. Is that his name?

[The information referred to follows:]

Baran, Jeff

From: Marie DeYoung [Marie.DeYoung@halliburton.com]
Sent: Monday, May 17, 2004 11:05 AM
To: [redacted]
Subject: FW: Halliburton in the Press

[Unable to display image]

Marie E. deYoung

Subcontracts Administration

Kellogg Brown and Root

Khalifa D15

APO AE, 09366

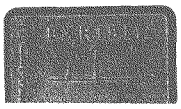
Cell Phone: 686-4481

-----Original Message-----
From: Marie DeYoung
Sent: Tuesday, February 17, 2004 8:02 AM
To: Dave Lesar
Subject: RE: Halliburton in the Press

Dave,

We just received the link to your commercial. Thanks for taking our story to the American public.

Marie



Marie deYoung

KBR Logistics Subcontracts Administration

Camp Udairi, Kuwait ☺

-----Original Message-----
From: Renee Westerman **On Behalf Of** Dave Lesar
Sent: Monday, December 15, 2003 10:19 PM
To: Marie DeYoung
Cc: Wendy Hall
Subject: RE: Halliburton in the Press

Thanks for your input....Dave

-----Original Message-----
From: Marie DeYoung
Sent: Saturday, December 13, 2003 11:54 AM
To: Dave Lesar
Subject: Halliburton in the Press

Dear Mr. Lesar,

As a former personnel officer and former chaplain in the Army, and as a relatively new employee, I am very grateful for your efforts to communicate your concerns about Halliburton to our staff. As a published author who campaigned against previous malignant press/political campaigns against army soldiers, I know that you are at a great disadvantage, because the political slurs are masked as legitimate public policy debate.

I only worked for the company three months in Kosovo, and so, I am not eligible for your employee contest to improve this great company. But, as a pretend contestant, I would like to give you feedback about the recent media slurs against Kellogg Brown and Root. if I could do one or two small things to improve this company, I would:

1. Scrub all personnel briefings, at headquarters and in the field, of references that "we're really in this for the money, right?" In Kosovo, and here in Houston, an extraordinary number of my peers are prior-service, with extensive experience in "contingency operations." Myself included. I am grateful for the money that Halliburton pays. It is too easy for frustrated workers, however, to become cynical when pay is cited as our primary motivation for serving Halliburton. To the extent that we can purge the image that our workers are only over there because we like the money, I believe we can turn recast our image as a service-providing company, not as a political kickback.

2. Capitalize on human motivation for excellence and service, as the military does. This company does the job right, the first time. I am sure that most prior service know the superior quality that KBR delivers, and they identify with this quality. We take the same pride in being KBR staff that we took in our assignments as 2ACR, 2ID or 4ID soldiers. Our friends are still wearing the uniform. We want to provide the best service support to our soldiers, our friends, and a number of us know that we can do this much more easily as a private company than as a government bureaucracy.

3. Get yourself out in front as the CEO of this company. If I were to do interviews or write op ed pieces, I would work to challenge this myth that Mr. Cheney is running KBR from his post as VP. I am grateful that Mr. Rumsfield is trying to set the record straight, but if the media and politicians are unfair in their publicizing of normal contract processes that you preside over, can you publicly challenge the constant linkage with Mr. Cheney, and challenge these folks to redirect their queries to you? That might kill the sensational press because we don't know who you are, what your political connections are, and hence, there doesn't seem to be a political scandal that would warrant the ink or air time.

I respectfully share these ideas because I have time on my hands while waiting for my flight to Kuwait. You have a wonderful crew of people excited to serve in Iraq, Kuwait, Afghanistan, D, and Uzbekistan, and you have a great staff that is working round the clock to get us over to our mission sites.

Thank you for your leadership. Have a peaceful holiday season.

Marie E. deYoung

Ms. DEYOUNG. Yes, sir.

Chairman TOM DAVIS. Where you note a couple of things. "As a former personnel officer and former chaplain in the Army, and as a relatively new employee, I am grateful for your efforts to communicate your concerns." "As a published author who campaigned against previous malignant press/political campaigns against army soldiers, I know that you are at a great disadvantage, because the political slurs are masked as legitimate public policy debate." And this was December 13th.

Ms. DEYOUNG. Yes, sir.

Chairman TOM DAVIS. "I only worked for the company 3 months in Kosovo." So I gather this is after you had left Kosovo?

Ms. DEYOUNG. Yes, sir.

Chairman TOM DAVIS. So, "I only worked for the company 3 months in Kosovo, and so, I am not eligible for your employee contest to improve this great company. But, as a pretend contestant, I would like to give you feedback about the recent media slurs against Kellogg Brown."

And you go on and on, but never in this do you offer any of the complaints that you are offering here. And you note in another e-mail, back in March, this is again after you had left, "Please know that KBR folks really do good work for the Army, because they care too. They are all doing a great job, and their spirit and determination is very strong."

Now, how do we reconcile all that with where you are today?

Ms. DEYOUNG. Very easy, sir. And there is nobody more disappointed than me. I had everything to lose by coming home and coming here. That letter was written the day before we flew—the day before Saddam's capture was announced and we flew over to Kuwait. And in the personnel briefings they talked about greed: Why are you taking this job? You want money, money, money. And that is why you are taking this job. And I suggested to him, as you can see in that letter, scrub that. Scrub that.

Second, I believed at the time—the folks on your side of the aisle there are assuming I'm a Democrat. Please do not assume that. I believed at the time that this was a political slur; OK? And I didn't—because what I saw and what I wanted to participate in was first-class support to the soldiers. And that's what Kosovo, even though it's very expensive, that was happening in Kosovo.

I get to Kuwait, and in the subsequent testimony, we are experiencing time and again situations where, for example, for over a month we could not repair a roof. A simple—you know, a simple temporary structure, a roof, because we didn't have screws and a ridge cap. A ridge cap costs about $30, and they could have been gotten off the economy.

Chairman TOM DAVIS. But these e-mails are long after you had left Kosovo. I mean, not Kosovo, long after you had left Kuwait. Excuse me.

Ms. DEYOUNG. The e-mail——

Chairman TOM DAVIS. These e-mails are after your experiences over there.

Ms. DEYOUNG. The e-mail to Dave Lesar is before I went to Kuwait.

Chairman TOM DAVIS. Well, one is dated April 1, 2004.

Ms. DEYOUNG. No, no, no. The original—it's about December 13th, the original. It may be a copy of how I sent it home to myself. But the original e-mail to Dave Lesar was on December 13th. It was the day before I flew.

Chairman TOM DAVIS. February 26, February 20. And you don't mention any of these issues.

Ms. DEYOUNG. And I had not—I went down to subcontracts. I was working in subcontracts on the outside until March 1st.

Chairman TOM DAVIS. Did you ever send any of this stuff to the President himself?

Ms. DEYOUNG. He came, and I went and shook his hand.

Chairman TOM DAVIS. But you never mentioned any of this in the e-mails? You had e-mails back and forth with him, of course, but did you ever mention this there, or did you just keep it down here and wait till later on to tell the committee?

Ms. DEYOUNG. Oh, no.

Chairman TOM DAVIS. Because you didn't tell government auditors. We know you didn't inform the government auditors.

Ms. DEYOUNG. The government auditors were trying to get the same information I was trying to provide them. They were trying to get that information, and I was trying to provide it. And when I saw internal shutdowns, that is why I came to this committee.

When Dave Lesar came, sir, and truck drivers, after the four men died, to include a guy who was in my cohort, named Fish, truck drivers were trying to tell him how unsafe it was. They were being shot at, and other instances were being discussed. And when that information was not considered, and when the information was not considered by the Vice President, whom I had sent e-mails to, that's when I made a decision.

I continued to receive e-mails until my last day, saying only give out this amount of information. You are asking too much. That's when I came to the committee.

Chairman TOM DAVIS. Ms. McCollum, you are recognized for 5 minutes.

Ms. MCCOLLUM. Thank you, Mr. Chairman.

Mr. Warren, you did call the CEO.

Mr. WARREN. Yes, ma'am.

Ms. MCCOLLUM. And in your conversation you tried to convey to him that there were problems, and you did show that there were problems with that. You reported that to him. What was his response to you?

Mr. WARREN. I had reached him when he just got out of a board meeting, and at that time when I called him, I was having problems in my own convoy. I was a very, very outspoken critic to safety, to my supervisors and to my foremen and to just about everybody, to the maintenance of the trucks.

I was involved in an accident while I was over there, and I felt like I was being pushed out the door because they just wanted me gone. And I wanted to speak to Mr. Randy Harrel and express to him my concern about my employment. And in the course of our conversation I brought up some of the problems we were having.

He thanked me for bringing it to his attention. He was very nice to me, and he just seemed like he was in a hurry; that he needed to go. And he promised me, he said, well, I assure you of one thing,

Mr. Warren, I won't leave you over the grease to burn. And I took that as a fair shake. I would get a fair shake, anything that pertained to me.

So after a couple of weeks I was transferred to Kuwait, thinking I was getting a new job assignment. And after 2 weeks in Kuwait, I was terminated.

Ms. MCCOLLUM. Did you ever see any evidence that someone had, from the company, come out and talked to the drivers and to others to say, you know, we need to do everything possible we can do to stop these thefts from occurring? Was there any difference in the amount of thievery you saw before or after your phone call?

Mr. WARREN. No. As a result, whenever I was called in to security, I thought they were going to address the concerns that I spoke to Mr. Harrel about. I thought they were going to talk to me in private. It wasn't nothing about that. It was about who have I seen run people off the roads? Or I was told that—they told me that they were in the know; they have some eyewitnesses that made statements that I know who was running them off the road, and they wanted me to give names.

Ms. MCCOLLUM. OK. Well, thank you, Mr. Warren.

Gentlemen, could I ask you, in your opinion, were any of the trucks that you saw that stopped functioning or that were torched due to the fact that the air filter gave out—I mean, you are experienced drivers. I'm sure you talked to the other drivers of the trucks. Was it air filters, just general maintenance, that was not being done in these areas?

Mr. WILSON. Yes, ma'am, there were problems in general maintenance. In particular, in my truck, when I was a convoy commander shut down because of filters. It wasn't air filters in my case, it was fuel filters. Diesel engines are sensitive to fuel filters. If the fuel filter stops up, the engine won't run. It will shut down.

Ms. MCCOLLUM. Thank you. Ms. deYoung, I know you were asked some questions about the different levels and all that. I have many years in retail management. I usually see things that, if they are contracts, it says "contract" on the top of the form, and if it is a purchase order, it says "purchase order" on the top of the form. And I am assuming Halliburton, being a private sector company, wouldn't be that different from the major companies that I worked for.

You can tell the difference between a contract and a purchase order, and you know how to match up to do basic inventory; is that not correct?

Ms. DEYOUNG. Absolutely. And because of my expertise in it or ability to do it, if I'm not certified, the subcontracts manager, who was the president of the National Contract Management Association, who is new there and trying to fix problems, he had me do investigations. He had me look at every single purchase order and subcontract to fill out reports for him.

Ms. MCCOLLUM. So it is easy to do when all the paperwork is there, to find out what came in and what went out.

I would just have one comment I would like to make. Thefts occur, and you did say in your testimony, and it was mentioned by one of the members here, that in times of war sometimes people come and purloin things. Well, in times of war, if you are deliver-

ing something to one of the units and they are counting on that being there, it makes a difference as to whether or not that piece of equipment arrives. So thefts should be prevented.

Mr. Warren, thank you for trying to make them stop that.

Mr. WAXMAN. Ms. McCollum, would you yield to me for 1 second?

Ms. MCCOLLUM. Yes.

Mr. WAXMAN. I just wanted to ask the two gentlemen, do you know of other drivers of trucks that worked with you that have similar stories?

Mr. WARREN. I have many friends that would be associates I worked with that would say the same thing.

Mr. WAXMAN. Well, if you have any of these names and phone numbers that you are willing to supply to the committee, we would appreciate it. Because we would like to see if others have experienced the same thing.

Chairman TOM DAVIS. The gentlewoman's time has expired. The gentleman from Indiana.

Mr. SOUDER. First, let me say that if I have ever heard a hearing where the forecast of what we were going to hear today and what we have heard are substantially different, it is this hearing. We have been hearing over and over about all these different allegations. Two of the five witnesses didn't show. The one I was supposed to question, which had this huge dollar amount there, when we actually get into the details and go over it from a business standpoint, quite frankly, he didn't realize, like the two gentlemen here with the trucks, that the military was making the decision, not Halliburton. He didn't realize that the cost he was projecting was incorrect, and he didn't have any proof that if there was a problem, it was Halliburton or KBR that had anything to do with it; that it was in fact inside his company, if there was a problem. So he begged off today not to come. We don't know why the other witness is not here.

And with all due respect, while it is very difficult for you to come forward, and quite frankly, I'm a little confused as to why the two of you were terminated in the truck incidents, because running Iraqis off the road, if you felt you were in danger, doesn't seem like much grounds for termination for such a lay observer. At the same time, you've acknowledged here under oath that you didn't realize that the military was making the decisions on how many trucks would go or whether they were empty. You didn't realize that the military was making the decision as to what was going onto the trucks. And your cases, really, in the big picture of things, are more or less irrelevant.

There are things that need to be dealt with that the military felt that they needed certain actions, and maybe we should be calling the military in, but what this hearing was hyped was that somehow Vice President Cheney is corrupt and President Bush is corrupt because contracts went to Halliburton, and Halliburton was enriching themselves. And not a single fact today showed that. In fact, Ms. deYoung, who actually makes what I believe are some fairly serious charges that we need to look into and they need to be continued to be looked at, because we need to make sure money is spent accurately and that the right bills are paid, but as you look at that, the fact is, as you said, you would not necessarily say that

KBR shouldn't keep the contract or that Halliburton shouldn't. What they need to do is correct errors in their process.

Furthermore, what we have heard today does not adjust for the fact that in the first days of that war, Members of this body, including critics of the administration, and people here today, were saying, oh, we have to make sure that the oil wells don't explode, and we have to make sure that money gets into the Iraqis flow. And then they say, well, there are too many guys standing around. In case something happened, the military wanted to make sure that they had the guys around. They said, oh, we need to make sure the electrical grid works. So the thing is, get everything you can, pay whatever price to get in there, even if it hadn't worked for a long time, and then we criticize the company because they paid too much to get the materials there on a rapid basis.

This body and the American people have been pushing the military and the contractors past even the point of safety, where we see them beheaded and captured and other types of things. Yes, they are making more money, but you know what, you can't pay most Americans enough money to go over there and risk the chance they are going to die, and without adequate protection. And so the contractors in my book are as much heroes as our soldiers, because they do not have the same security.

Now, a lot of what happened, and always happens, and it is happening around the world with our military in every zone there is, in the early days, quite frankly, speed is the most important thing. Second, we always have problems with maintenance, particularly in the first parts. And the reason we need auditors with integrity, who then match it up, is that after and as the mission changes, and as you get stabilized, you make sure there wasn't fraud in that process of overpaying; that indeed it was because there was a need to overpay, to maybe get the speed with a contractor that was relatively reliable because we couldn't spend the time checking out the normal low bidder that you would do in a normal situation with a retail store. I grew up in retailing, too.

You know, I had time and the ability to plan ahead. Here there isn't with these type of things. But as time goes on, if we are not correcting the maintenance questions, if we are not correcting the overbilling questions, if we are not doing better management to forecast the cost, if we find out that we are paying more than we should have paid, then those adjustments should occur. And to the degree that people like Ms. deYoung and you all help us sort that out, that is helpful to this committee. To the degree this becomes a witch hunt, which in fact this hearing has become—and that every time we seek out other people who have complaints so we can bring them up here and then find their complaints aren't valid.

Now, it isn't your complaints aren't valid that there are empty trucks, but the fact is we don't know. We don't know why the military asked for that, but it had nothing to do with Halliburton and the hearing. And even that last question for seeking information had the implication that somehow this has a tie back to the political arena.

Ms. DEYOUNG. Can I respond to that, sir?

Mr. SOUDER. This hearing would not be occurring if it wasn't politically motivated. That's the fact. We would have done it in a dif-

ferent way. We would have looked at the auditors. This show hearing, and the reason the press is here today, is because of the allegations made in the opening statements, not because of your information.

Yes.

Ms. DEYOUNG. Sir, I would like to respond to that. I understand, with my 10 years of tactical experience, I have been in all the combat units and trained with them, what the Congressman was talking about, about the military being in charge. But these gentlemen are absolutely understating the problem that Halliburton bought trucks, leased trucks, and they didn't have repair parts. All the European-made trucks have metric tools. They didn't have metric tools in country.

Subcontract administrators, if you put them under oath, they will tell you that. That's a fact. There are people who are trying to take pictures and trying to bring information back. The fact that the priorities were backward, taking care of luxuries for the people and the hotel staff, instead of getting armored trucks, instead of getting tools, fuel filters, that's a fact. It was a subcontract procurement problem.

Chairman TOM DAVIS. Thank you very much. The time has expired.

We have Mr. Duncan, 5 minutes.

Mr. DUNCAN. Mr. Chairman, I know we have votes going on, so I won't take the full 5 minutes. I don't have any questions, but I would like to make a couple of comments.

I think Mr. Souder made some good points. And I think it is ridiculously unfair to charge or imply that Vice President Cheney had anything to do with these problems, because all of these problems, if these allegations and charges are true, occurred while he was Vice President, long after he had left Halliburton. So it does appear to many people that some of this is being done purely for partisan political purposes.

Having said all that, I will say this, though. We didn't really have many of these problems like this when the government was small, the Federal Government was small. But when Federal spending exploded in the early seventies, we started hearing and reading about more and more examples of waste, fraud and abuse. And conservative Republicans have traditionally been the biggest critics of waste, fraud and abuse, whether it occurred by the government bureaucracies themselves or whether it occurred in government contracts.

Now, I can tell you this. Most of us have no connection whatsoever to KBR/Halliburton. If these charges are true, and if there are, as I heard on one national newscast, $166 million of overcharges, I want to put it on the record that conservative Republicans are almost more horrified by that across this country than anybody else would be. I don't want it to appear to anybody that conservative Republicans would defend any company that overcharged the government by many millions of dollars, or, as one witness said, had people not doing work and charging the government for it, or doing horrendous overcharges. I think it is terrible.

So I think if some of these charges turn out to be true—and they may not—but if they were, then these companies should be banned

from doing further business with the Federal Government and people should be prosecuted criminally.

Thank you, Mr. Chairman.

Chairman TOM DAVIS. Thank you very much. We have 10 minutes before the vote.

Mr. Platts, do you want to say anything before I dismiss the panel?

OK, then. Let me just thank the panel for being here. We will recess this part of the hearing. When we come back from votes, we will swear the second panel and move from there.

Thank you very much.

Ms. DEYOUNG. Thank you very much.

Chairman TOM DAVIS. The committee is in recess.

[Recess.]

Chairman TOM DAVIS. Thank you very much. We will reconvene, and if you would rise with me.

Our witnesses are Alfred Neffgen, Chief Operations Officer, KBR Government Operations, Americas Region; Mr. William Walter, Director of Government Compliance, KBR Government Operations; Mr. Charles "Stoney" Cox, vice president and past restore Iraqi Oil Project director; and Mr. Keith Richard, regional project manager, Theater Transportation Mission, LOGCAP III, KBR Government Operations.

It is the policy of the committee to swear all witnesses before you testify. Please raise your right hands.

[Witnesses sworn.]

Chairman TOM DAVIS. Thank you very much. Mr. Neffgen, we'll start with you and move straight down the line. We try to keep the testimony to 5 minutes and then we'll open it up to questions. Your entire testimony will be part of the record. Thank you, and thanks for patient and staying with us.

STATEMENTS OF ALFRED NEFFGEN, CHIEF OPERATION OFFICER, KBR GOVERNMENT OPERATIONS, AMERICAS REGION; WILLIAM WALTER, DIRECTOR OF GOVERNMENT COMPLIANCE, KBR GOVERNMENT OPERATIONS; CHARLES "STONEY" COX, VICE PRESIDENT AND PAST RESTORE IRAQI OIL [RIO] PROJECT DIRECTOR, KBR GOVERNMENT OPERATIONS; AND KEITH RICHARD, REGIONAL PROJECT MANAGER, THEATER TRANSPORTATION MISSION, LOGCAP III, KBR GOVERNMENT OPERATIONS

Mr. NEFFGEN. Thank you, Mr. Chairman and members of the committee. My name is Al Neffgen, chief operating officer for Government Operations, Americas Region at KBR, the engineering construction subsidiary of Halliburton. In this role, I oversee all work performed by KBR for the U.S. Government.

Mr. Chairman, there have been many criticisms of KBR this year. We are happy to be able to appear here today to tell the story of what KBR has done to support the military. When reviewing our activities, we think it is important you consider the environment in which we are serving.

Within hours of the beginning of the war in March 2003, KBR personnel joined the Army at the Iraq border and provided logistic support for the Army as it invaded and later secured Iraq. Over the

next 16 months, our people have been in harm's way. There are attacks on KBR personnel every day. Weekly, there have been anywhere from 40 to 80 incidents. We had not lost a single employee to hostile action in more than a decade of supporting U.S. troops in assignments in Haiti, Somalia, the Balkans, Afghanistan, and elsewhere. In Iraq, 42 employees and top-tier subcontractor employees, have lost their lives. Another 93 have been wounded. Some have been kidnapped, including Tommy Hamill, who later escaped. Two employees are still missing in action.

When we entered Iraq 16 months ago, we began work under intense pressure with inadequate infrastructure, with almost no communications, few phones, and little electricity. Our people slept in makeshift facilities and in the hallways of abandoned buildings. In these conditions, the military assigned us jobs, like bringing in millions of gallons of fuel for the military, feeding the troops, and transporting critical military supplies. In this situation, KBR employees were determined to get the job done and do it well. We are accomplishing this mission.

The challenges were expressed in an article in the New York Times in June 2003. It said, "KBR essentially took an entire army base out of containers and made it rise in the middle of the Kuwaiti desert 2 days ahead of schedule. To conjure Camp Arifjan in a twinkling, amid one of the most hostile environments on the planet, was by any measure a stunning logistical achievement."

Over the last 16 months, we have set up more than 60 camps for soldiers, helped restore oil flow to prewar levels 3 months ahead of schedule, delivered 463 million gallons of gasoline to Iraq to alleviate the very real possibility of civil unrest, and another 700 million gallons for the military.

Supporting the troops is an enormous logistics exercise. Every day we serve more than 475,000 meals to our troops, provide them more than 2.3 million gallons of water, wash almost 16,000 bundles of their laundry, collect nearly 10,000 cubic meters of trash. We did this with constant changes from the Army, the kinds of changes that are to be expected in a war zone.

The LOGCAP contract scope of work called for KBR to be prepared to support 25,000 troops, with an absolute maximum of 50,000. Within months, we were charged with supporting nearly 200,000 United States and Coalition Forces, as well as 11,000 others, a total of 211,000 people. Under these conditions, no one should expect the assembling and complicated logistics would be the epitome of pristine precision. These unanticipated requirements did tax and stretch our systems, but we placed continuous pressure on ourselves to do better. We identified problems and fixed them.

We have an elaborate system to detect improprieties, and when they occurred, we acted. Let me give you two examples of where we identified and fixed problems.

By late 2003, we were concerned about the overload to some of our procurement systems. We dispatched a special Tiger Team of seasoned procurement professionals that improved our systems. And when we discovered a billing irregularity that suggested a subcontractor may have improperly paid a kickback to a former employee, we investigated it, reported it to the Federal authorities,

and provided the government a $6.3 million credit, far in excess of the alleged kickback amount.

Despite all these challenges, KBR has constantly delivered on its promise to feed and house the soldiers and fuel and supply the military. In the end, that is our proudest accomplishment.

Facing all these realities, KBR undoubtedly made mistakes. But where we identified mistakes, we quickly moved to fix them. For example, earlier this year, a regular review showed some examples of splitting requisitions to keep them under $2,500. When it did happen, it was done to meet urgent Army need, not to avoid competition. When we found out about it, we put a stop to it. That is not the way we do business.

The other area where we find fault with ourselves is in subcontract documentation. These issues came about for a number of reasons: The huge ramp-up of LOGCAP, the need to utilize more than 200 subcontractors, and the speed needed to accomplish these jobs. Again, the goal was to provide service to the Army as quickly as possible. But it is an area where we could have done better, and we are doing so today.

In addition to our self-criticism, we are well aware of the external criticism, as typified by a few of our former employees. The company has long had procedures to encourage such complaints and criticisms and to address them. We encourage any and all employees to promptly report any violations of our company's code of business conduct, either by going to a supervisor or using our confidential ethics hotline and e-mail address for reporting any such concerns.

We take any allegations seriously and fully investigate. We are sorry that a few of these former employees failed to use these procedures. In any event, we believe their criticisms are mistaken and misinformed. We welcome the opportunity to speak to the facts on these and other issues.

Let me set out some of these: In the area of procurement, one former employee claims that people have been putting too many hours on their time sheets. Our policy strictly prohibits that. And if we learn of violations, they are dealt with very seriously.

Another employee claims to have read files and seen that we contracted to buy soda for $1.50 per case. That is just a little over 6 cents a can. Think about that premise: 6 cents a can. I don't know when you could buy soda for 6 cents a can.

We have also heard about what was called a $61 million fuel delivery overcharge, when in fact it is just the opposite. KBR's actions saved a lot of money.

Mr. Chairman, and members of the committee, I hope you will come away from today's hearings with three conclusions: first, never before has a contractor worked in as difficult and dangerous a situation as we do in Iraq; second, we have performed and performed well for our soldiers and for our country; third, we have performed our work within the law and consistent with Federal contracting requirements. There have been times when we made mistakes, and our systems were stretched, but we have identified mistakes and we have quickly moved to fix them.

Mr. Chairman, without question, the public has a right to expect that its tax dollars are spent wisely. All we ask is for a fair assess-

ment of whether KBR has done the best they could under the difficult and challenging conditions of operating in a war zone. We firmly believe we have met that challenge.

Thank you, Mr. Chairman, and members of the committee, and I look forward to your questions.

Let me now please turn it over to Bill Walter.

[The prepared statement of Mr. Neffgen follows:]

STATEMENT BY
ALFRED V. NEFFGEN
CHIEF OPERATING OFFICER,
KBR GOVERNMENT OPERATIONS, AMERICAS REGION

BEFORE THE

COMMITTEE ON GOVERNMENT REFORM
UNITED STATES HOUSE OF REPRESENTATIVES

July 22, 2004

Thank you, Chairman Davis. My name is Alfred V. Neffgen. I am Chief Operating Officer for Government Operations, Americas Region at KBR, the engineering and construction subsidiary of Halliburton. In this role, I oversee all work performed by KBR Government Operations, Americas Region, for the U.S. Government.

I appreciate the opportunity to share with the Committee the facts about our work in Iraq to deliver support to U.S. troops and to restore Iraq's oil infrastructure. KBR is proud of its achievements in Iraq. We have delivered support to our troops in a very difficult environment of unprecedented danger to our employees.

Ours is a mission defined by the Army, often in urgent terms. We are operating in a war zone where decisions are made in minutes, not months, because of the ever-changing conditions. Our mission affects the well-being, morale and even the lives of our troops. Working in this demanding environment, we put together a massive enterprise virtually overnight to do everything from feeding tens of thousands of troops to repairing oil infrastructure and delivering emergency fuels to Iraqi civilians.

Speaking for the thousands of KBR employees who are risking their lives in Iraq to support our troops, I am eager to present our views. The public without question has the right to expect that its tax dollars are spent wisely, and it is appropriate to carefully consider whether KBR has met that obligation.

In the end, all we ask is for a fair assessment of KBR's performance under the difficult and challenging circumstances of operating in a war zone. The contracting process under the Federal Acquisition Regulation (FAR) provides for regular and continuous scrutiny of the pricing of our services, and we are discussing these issues with the Department of Defense on a daily basis. In the end, while we have undoubtedly made some mistakes, we are confident that KBR has delivered and accomplished its mission at a fair and reasonable cost.

Mr. Chairman, my testimony today will first describe my company's history in working for the U.S. military and the U.S. troops. Following that, I will describe KBR's procurement, management and accounting systems, along with our company's Code of Business Conduct.

Later, I will talk in detail about two contracts.

The first is known as RIO, for Restore Iraqi Oil. Under RIO, KBR is helping repair and rehabilitate oil infrastructure at the request of the U.S. Army Corps of Engineers and the Iraqi Oil Ministry. KBR helped return Iraqi oil production to pre-war levels by December 2003, three months ahead of schedule. Under extraordinarily difficult circumstances and with only hours of advance planning time, KBR also developed a massive fuel importation program to prevent civil unrest and disorder after fuel stocks for the Iraqi people had dwindled dangerously low. This fuel program was a success. KBR followed Army guidance for sourcing fuel and worked to keep costs down – two topics I will address in detail.

The second contract is called LOGCAP, for the Logistics Civil Augmentation Program. Through LOGCAP, KBR serves the basic needs of America's troops in Iraq and Kuwait. KBR's priority is to make certain the troops have the food, shelter and tolerable living conditions they need while fighting in Iraq. KBR builds camps, delivers mail, services equipment, cooks meals, provides drinking water and fulfills many other missions. KBR's goal under LOGCAP is to accomplish its essential support mission, at the direction of the U.S. military, so that the warfighters can perform their mission. One of our important jobs under LOGCAP is to provide dining facilities, which has raised issues involving the billing for these facilities that I will also address in detail.

Sixty Years of Service to the U.S. Military

Dating back 60 years, our employees have a long and proud history of serving the needs of the U.S. military and U.S. soldiers during times of war and peace, in the harshest of climates, in the most remote locations, and under critical timeline and budget constraints. Working under both Democratic and Republican administrations, we pride ourselves on accomplishing our assigned tasks – whether at home, on humanitarian missions, on peacekeeping missions, in war-torn zones and, now, in the combat environment of Iraq.

In World War II, we built battleships and destroyers. When the war ended, Brown & Root was entrusted as the managing partner for the massive reconstruction of war-torn Guam. For the Korean War, we rebuilt 1,500 World War II tanks. In the 1960s, we helped build a massive air force base in Vietnam.

More recently, KBR has fulfilled urgent requirements in Somalia, Haiti, Bosnia, Saudi Arabia, Kuwait, Rwanda, Uganda, Marshall Islands, Turkey, the Balkans, the Philippines, and Afghanistan. We have also responded to hurricanes in Florida and South Carolina, and earthquakes in California.

For both the military and contractors alike, Iraq has posed a unique set of logistical and security challenges. In all of our contingency operations, we have not lost a single employee due to hostile actions. Iraq is different. Almost every day a report crosses my desk that catalogues new attacks on KBR personnel – everything from mortar attacks on a camp site to attacks on truck convoys. Over the last two months, the attacks ranged from 40 to 80 per week. For anybody who reads these reports, it is abundantly clear that Iraq remains a dangerous war zone with continuing sabotage and hostilities.

We are deeply aware that these are not just dry statistics. KBR's employees are on the front lines, putting themselves in harm's way to support U.S. soldiers in a war zone. As a company and as individuals, we mourn the fact that KBR employees have lost their lives in Iraq. As of July 19, forty-two (42) employees and top-tier subcontractor employees have died while working in Iraq. These colleagues included average Americans -- truck drivers, construction workers and food service personnel – who made the ultimate sacrifice to support American troops. As of July 19, another 93 employees and subcontractor employees have been wounded, and two are missing.

KBR has more than 34,000 direct and subcontractor employees working in Iraq and Kuwait and the surrounding region supporting our operations for the U.S. government. Of this figure, approximately 11,000 are KBR expatriate employees, including employees from every state and the District of Columbia. Another 14,000 are subcontractor employees. The remaining employees include a group of approximately 2,700 Iraqis. We manage subcontracts with more than 200 different companies.

The Rapid Growth of Our Mission in Iraq.

KBR has faced enormous challenges in meeting the Army's requirements. What has made Iraq challenging? It wasn't only because Iraq was a typically unpredictable war-time situation. It was also because the mission in Iraq mushroomed quickly and dramatically.

We began our work in Kuwait in the pre-war period, operating originally under the terms of the Scope of Work we had agreed to when we had won the most recent LOGCAP competition in 2001. That Scope of Work called on KBR to be prepared to support 25,000 troops, with an absolute maximum of 50,000, in seven base camps with 3,000 troops each, and a rear support area housing another 4,000 troops. This Scope of Work was appropriate for our previous assignments, even ones like the Balkans, previously our largest mission.

In Iraq and Kuwait our assignment quickly grew considerably beyond the original Scope of Work. The speed and volume of task orders accelerated, as the scope of work from the Army dramatically increased, along with multiple revisions of task orders. The pace of new requirements and changes to on-going missions greatly exceeded the original plans of both the government and of KBR. As a result, we now provide support for nearly 200,000 U.S. and coalition forces, as well as 11,000 others, for a total of 211,000 in more than 60 camps.

The rapid mobilization in Iraq beyond our initial Statement of Work required us to perform numerous jobs simultaneously – that is, to provide logistical support for a growing number of soldiers while simultaneously augmenting our own business management, accounting and personnel systems.

Thus, in an unpredictable situation, KBR mounted an enormous logistical operation that was distinctive for three reasons. It was many times larger than our previous logistical assignments that occurred concurrently in the Balkans and four other countries. It occurred according to the compressed timelines of a military force at war. And it was far broader in scope than we anticipated. Because of our substantial and unique experience in providing logistical support for the military, we adapted, adjusted, and modified our systems to meet the challenge.

In the earlier and smaller logistics missions, KBR had performed virtually all the tasks itself. In Iraq, it was difficult to find subcontractors in the Middle East who were knowledgeable about, and could comply with, U.S. regulations. It took time and effort to bring them up to standards. Thus, there were a combination of factors in Iraq – the speedy ramp-up, the ever-changing conditions dictated by wartime and the large scope of the assignment – that required us for the first time to build an extensive network of subcontractors, and assemble the people and systems to supervise them.

Facing these realities, did KBR make mistakes? Without question, we encountered difficulties in mounting such a large enterprise in a hostile, dangerous environment. Initially, given the dramatic ramp-up of responsibilities and constant changing of the Scope of Work, our business and subcontract management systems were stretched. No one at KBR would presume to say that our operation was flawless under these circumstances.

But while the rapid growth of our assignments and the demands of war taxed our systems, we placed continuous pressure on ourselves to do better. We worked hard to identify and fix problems. We worked equally hard with oversight teams from the Army and other DoD offices to correct problems they identified. We refined systems and improved our processes and performance – and we continue to do so. All the while, we worked within Army rules and regulations, supplemented by our own checks and balances and our Code of Business Conduct, which requires employees to conduct business honestly and ethically. I am confident that all this hard work – and the help of our oversight agencies – has led to success.

Let me give you two examples of where we identified problems and quickly fixed them:

- By late 2003 we were concerned about the overload that some of our procurement systems were facing. We subsequently dispatched a team of seasoned procurement and contract specialists to the theater to conduct an across-the-board review of our procurement processes, organization, systems, tools and training programs. As this group delved into its work, some shortcomings in our systems

came to light, such as the need to assemble documentation to expedite subcontractor payments. This group's work – it is often referred to as the "Tiger Team" – was quite successful. Its recommendations have resulted in multiple improvements to our business management systems, including six new manuals and a reorganization of roles and responsibilities. It also helped accelerate subcontractor payments.

- Another example occurred early this year when KBR identified a billing irregularity that suggested a subcontractor may have improperly paid a kickback to a former employee. Once it had identified the issue KBR immediately reported the matter to the Department of Defense Inspector General's office, the Department of Justice, and to the Army, turned it over to authorities and provided the government with a $6.3 million credit. The credit represented the amount of the money that KBR, in turn, billed to the government for the subcontracts in question – far in excess of the alleged kickback amount. When we detect a problem, we immediately investigate, self-report, and take corrective action.

Today, Mr. Chairman, the committee will hear from some former employees of KBR who were briefly employed in the theater and who are critical of the company.

Let me say that we take seriously the comments or criticisms of any of our current or former employees. We wish the criticisms had been raised in our hotline process to allow us to investigate directly and address them. Ultimately, we believe that their criticisms are off the mark and are not informed by the full facts.

Procurement Controls in Contingency Contracts

Both LOGCAP and RIO are "cost-plus" contracts. They often are referred to as contingency contracts, and with good reason. A contingency contract provides a flexible procurement tool for obtaining the necessary logistical support to deal with unknown contingencies – for military, peacekeeping or humanitarian missions around the world that might occur on very short notice – without requiring the military to carry the costs associated with full-time, long-term logistics support personnel capable of responding on a moment's notice. Because the military's needs for such services are as unpredictable as the course of world events, the form of contract must be flexible to account for unknown contingencies.

The Department of Defense made the proper determination that cost-plus contracts are the only realistic way to respond to the Government's urgent needs in time of war and conflict where uncertainty rules. The needs of the military must be met extraordinarily quickly and without the constraints required of traditional fixed priced contracts. Frequently, the size and duration of the required needs are totally unknown.

But this does not mean that there are no controls or accountability. In fact, because the use of cost-plus contracts is widespread in federal procurement – including by the National Aeronautics and Space Administration, the U.S. Agency for International

Development, the National Oceanic and Atmospheric Administration, the Social Security Administration and the Department of Energy – federal acquisition regulations provide detailed guidance and procedures for administering such contracts. These regulations guide the allowability of reimbursable costs, the methods of accounting for such costs, and procedures for setting ceilings on such costs. In KBR's case, its contracts are "cost-plus award-fee" contracts, in which the largest part of the fee is determined by assessing how well the contractor has performed its job, including the job of controlling costs.

In addition, it is important to note that the vast majority of our contracts and the vast majority of our subcontracts were competitively bid.

As part of complying with federal acquisition regulations, KBR maintains its own set of internal procurement policies and procedures. These policies and procedures are designed to ensure that KBR's procurement process operates with integrity, efficiency, effectiveness and accountability, and they include a number of checks and balances, accompanied by multiple layers of approval and oversight. One important part of KBR's checks and balances is that procurement compliance experts, whose sole purpose is to monitor the integrity of our procurement system, do not report to local project managers. Instead, to help maintain their objectivity, they report directly to a KBR corporate vice president of procurement.

Management oversight provides another layer of checks and balances. For example, procurement management regularly looks at process control, both on a transaction and trend basis. And periodic routine and random audits are conducted by four KBR divisions – Site Management, Internal Audit, Procurement Compliance and Government Compliance – as well as two federal agencies, the Defense Contract Audit Agency (DCAA) and the Defense Contract Management Agency (DCMA).

KBR maintains a comprehensive set of procurement instructions, procedures and policies. Our procurement policies are reviewed regularly by the government agency chartered with oversight responsibility, the DCMA. DCMA ensures that KBR complies with the FAR, and when DCMA identifies problems KBR makes corrections. Our procurement system is regularly reviewed and approved by the DCMA for compliance with federal law and regulation. Our most recent approval, which included a review of our in-theater procurement systems, was received in May 2003 and is valid for a period of three years. This validates that we operate in compliance with the guidelines set by the U.S. government for government contractors in the procurement area.

KBR trains its new employees in procurement processes, procedures, forms, ethics, company policies, compliance and site/project requirements. We also conduct a special Purchasing Supply Chain Academy to enhance the training and orientation for procurement new hires before they depart to the Middle East.

In addition, the Company for more than 20 years has had a policy prohibiting unlawful, unethical, and questionable conduct in its business affairs. Our Code of Business Conduct, which is distributed to each and every employee of the Company from the top

down, specifically requires employees to conduct business honestly and ethically; in fact, as part of the hiring process each new employee is required to sign a statement certifying that they have read and will comply with the Code. We maintain an "open door" policy that encourages employees to report any issues to their supervisor, or anyone in management. It requires Company employees promptly to report any violations of the Code and provides employees with a confidential ethics hotline and an e-mail address for that purpose.

The hotline is staffed by an independent company and is available 24 hours a day in multiple languages. The Code prohibits retribution against any employee for making a good faith report. There is simply no reason for any employee with a good faith question or concern not to report it to the hotline or by e-mail so that it may be promptly addressed.

Just this month the Inspector General for the Coalition Provisional Authority issued a draft audit report that reviewed the adequacy and effectiveness of corporate self-governance programs of contractors in Iraq. Our company was one of five corporations reviewed in areas like Code of Business Conduct, internal controls, and compliance with government contracting policy and procedures. The draft report concluded: "Each contractor we reviewed demonstrated a viable corporate governance program by taking actions to identify and eliminate liability creating conduct. Of the contractors visited, each designed and implemented their corporate governance policies in a unique approach to best meet the needs of their company."

Restore Iraqi Oil (RIO)

The goal of RIO, which is simple to describe and challenging to accomplish, is to restore Iraq's oil production and maintain the flow of fuel to the Iraqi people. Through RIO, KBR helped restore oil wells, pipelines and refineries – all with the goal of getting the oil flowing for both domestic use and export to enable Iraq to develop hard currency income for the benefit of the Iraqi people and their nation.

Iraq is a large country with a land mass a little larger than California. Superimposed over a U.S. map, it would cover an area east to west from Washington D.C. to central Indiana. North to south, it would cover Lansing, Michigan to Raleigh, North Carolina. As reported to OPEC and other sources, Iraq has 5,520 miles of petroleum pipeline in diameters ranging from 6 to 56 inches, 10 refineries and four export facilities.

With all this oil infrastructure, the potential for disaster during and after Operation Iraqi Freedom was enormous.

Before Operation Iraqi Freedom began, the Army Field Support Command issued KBR a planning task under the competitively awarded LOGCAP contract. This plan identified potential scenarios under which we were tasked to develop a classified scenario-based contingency plan that involved short notice, disaster management, and experience in oil infrastructure. Our selection for this highly sensitive and urgent task was based in part on

the fact that we had experienced personnel with the necessary security clearances and the experience in extinguishing oil well fires in the first Gulf War.

Later KBR was asked on a sole-source basis to help implement that plan to restore Iraq's oil infrastructure, an action that the General Accounting Office last month found was both legal and appropriate. As you know, federal law permits sole source contracts under specified conditions and they are widely used throughout the federal government. In its report the GAO said that "...the Army Corps of Engineers properly awarded a sole-source contract for rebuilding Iraq's oil infrastructure to the only contractor DOD had determined was in a position to provide the services within the required time frame given classified prewar planning requirements." [Page 4, GAO-04-605, "Iraq Reconstruction Contracting," June 2004]

The contingency plan was based on alternative scenarios. At the time the magnitude and nature of the conflict with Iraq was unknown, although it was a matter of history that Saddam Hussein's retreating forces had wrought significant damage to oil wells in Kuwait in 1991. Within the scenario's parameters, KBR was under contract to assess the condition of Iraq's oil infrastructure; extinguish and respond to oil fires and spills; restore oil infrastructure, including making necessary repairs to restart facilities damaged in war operations; and, finally, to support Iraqis with initial production and export operations.

KBR responded within a matter of hours. On March 21, 2003, the second day of the war, KBR engineers crossed into Iraq almost literally in the tracks of U.S. troops. On March 24, additional oil infrastructure experts left the United States, rolling into Iraq 48 hours after they landed at Kuwait International Airport.

Once our engineers began work, they found that many oil facilities were in complete disrepair due to decades of neglect, as well as recent looting and sabotage. Many pipelines in the south were damaged during battles. Wellheads were rigged with explosives, some of which were triggered, causing greater damage and again creating significant risk for our employees. These wells were assessed and extinguished in priority order.

We found that the Iraqi oil equipment was old, neglected and often desperately in need of repair. We found compressor stations where pump couplings were not available, and we found one site where technicians had improvised a coupling from pieces of leather. At fuel depots in and around Baghdad, brand new but poorly manufactured foreign-made pumps frequently broke down or simply performed poorly, putting our mission in jeopardy.

Before Operation Iraqi Freedom, there was little warning of the level of destruction that would be caused by continuing vandalism and sabotage. Almost immediately, our teams encountered bands of Iraqi men roaming the oilfields. Often they were armed, and often they stripped facilities of anything of value. They removed power generation equipment, tools, air conditioners, pumps, vehicles, valves – even furniture. Outside the facility, they

would use tractors or even donkeys to pull down power lines so they could scavenge and sell the inner copper core.

In July 2003, the Army Corps of Engineers, the Coalition Provisional Authority and the Iraq Ministry of Oil decided to pursue a study to determine the ideal end-state of the country's oil infrastructure. These three entities developed a "final work plan," with 226 projects spread over three phases. All of KBR's RIO work is at the direction of its client, formerly the Army Corps of Engineers and now the Project and Contracting Office.

KBR was one of several contractors that received taskings from the Army Corps of Engineers; specifically, we were given the job of overseeing seven key projects. KBR was directed to procure materials and equipment – some of which were readily available, some of which had to be manufactured and delivered months later by boat – for the maintenance staff of Iraq oil operating companies so they could make repairs. The Army was responsible for providing security for the Iraqi oil facilities infrastructure.

For example, at the Al Bakr Oil Terminal, we helped repair two of the four sets of marine loading arms. For the Ministry of Oil, we helped design, engineer, acquire and install a communications network. And, because reliable electric power is absolutely necessary for refineries to operate, we developed a plan to stabilize the power available to the refineries in Southern Iraq by procuring more than 300 mega-watts of power generation, enough to light most small cities in the United States.

In all, our team has made substantial progress in meeting or exceeding the milestones set by the Army Corps of Engineers. In earlier testimony to this committee, Major Gen. Carl Strock, director of Civil Works, the U.S. Army Corps of Engineers, said the Corps estimated before the war that it would take 12 weeks to reopen the oil fields. He added, "Due in large part to the hard work of Task Force RIO, its contractors, and especially the Iraqi experts in oil production, however, it took only about three weeks to get the oil flowing again."

KBR's work has directly affected the ability of Iraq to resume producing and exporting oil:

- After assessing about 600 oil infrastructure facilities, KBR identified 167 facilities that were critical to what we called "First Oil," the resumption of production. The first oil flowed from the southern oilfields on April 28, 2003.

- As production levels grew, exporting oil from the Al Bakr Oil Terminal became a reality on June 28, 2003, a day ahead of schedule.

- And on December 30, Iraq produced 2.4 million barrels a day – the pre-war production level – three months ahead of schedule.

Since exports restarted in June 2003, Iraq produced some $12 billion in revenue from oil sales in a year's time – oil revenues that the Iraqi people need to lay claim to their

nation's future, not only to finance modernization of its oil equipment but also to build new schools and libraries. Iraq continues to export more than two million barrels a day, although exports fluctuate due to sabotage and attacks on the infrastructure.

As you know, the Army Corps of Engineers earlier this year competitively selected two companies to assume the responsibilities for RIO project management and execution for northern and southern Iraq. The Parsons Worley Joint Venture assumed projects north of Baghdad. KBR now oversees projects for the southern Iraq section.

Finally, let me address the issue of the costs for oil field fire fighting equipment under the RIO contract. As early as November 2002, KBR participated in meetings with the Army to discuss plans to address oil well fires that were anticipated upon the launch of the Iraq war. Boots & Coots had already begun work with DoD planners prior to KBR's involvement and the Army expressed its preference that Boots & Coots perform this work.

On Feb. 12, 2003, the Army issued a classified task order under the LOGCAP contract (Task Order No. 42), directing KBR to purchase the fire fighting equipment. While typical lead time is 6 to 20 weeks to manufacture and obtain this specialized equipment, we were given just a couple of weeks to deliver equipment to Iraq. Boots & Coots was in a position to supply the required fire fighting equipment on an accelerated basis and so they were sent an RFP. Generally, this type of equipment is leased, not purchased, but given the potential long-term need for the equipment, KBR, with the Army's support, determined it was far more cost-effective to purchase rather than lease the equipment.

Boots & Coots agreed to a reduction from the commercial price list. Moreover, selling their customized equipment was something most companies would not agree to do. The government will also have the equipment for future use.

In addition, Boots & Coots substantially discounted its fire-fighting costs. Rather than charge its "list" prices of up to $15,000 per day per man, Boots & Coots agreed to substantially reduce its costs to $5,000 per day per man in Iraq and $3,500 per day per man in Kuwait.

These prices were fair and reasonable, particularly given the immediate, compelling and urgent nature of the government's classified task order. KBR received the Task Order on Feb. 12, and two weeks later, delivered by positioning the equipment by February 25.

Fuel Assignment

For much of what KBR is accomplishing in Iraq, it is vitally important to see our efforts in the context of the times when the Army has urgent needs. No better example exists than the mission to deliver fuel to Iraq so that Iraqi civilians could cook, heat their homes and drive their cars.

On May 3, 2003, the Army Corps of Engineers contacted KBR in Kuwait, stating that a civilian fuel shortage threatened to lead to civil unrest, posing a serious and imminent

danger to U.S. troops. In less than 100 hours, KBR had arranged the logistics so that the first trucks of gasoline and liquid natural gas were rumbling northward from Kuwait into Iraq.

Facing immense security and logistical challenges, KBR developed the fuel program from scratch under brutally difficult circumstances – responding to the Army Corps' requests to continually expand shipments to meet the mounting demand. The program eventually mushroomed from what was initially envisioned as a limited 21-day emergency program to a massive 11-month undertaking.

With your permission, I would like to set the record straight on three important issues related to the fuel assignment: the cost of fuel, the sourcing of fuel, and the security environment surrounding fuel delivery.

First, the price of fuel.

KBR did everything in its power to ensure that the Army's requirements were met at the lowest cost possible. One day after receiving the initial task order from the Army, we contacted more than a dozen firms to supply fuel and logistics support, including tankers and drivers. We received several written bids and chose the low bidder, a Kuwaiti company called Altanmia.

At the same time KBR, on its own initiative, sought alternative sources of fuel in Turkey to meet the Corps' urgent demand. The fuel market in Turkey was more competitive and the security risks associated with delivering fuel from the north were much lower. As a result, sourcing fuel from Turkey was much more cost efficient than sourcing fuel from Kuwait. By May 11, 2003, eight days after the Corps' initial request, KBR began delivering fuel from Turkey as well.

I want to emphasize an important point here about the so-called "overcharging" for fuel deliveries by Altanmia from Kuwait. DCAA, which examined the fuel pricing, took KBR's cost of delivering fuel from Kuwait, compared it to KBR's cost of delivering fuel from Turkey, calculated the difference between the two, and called it potential "overpricing." But that simple calculation fails to take into account a fundamental fact: It was impossible to get fuel to the entire country of Iraq from Turkey alone. Only the northern part of Iraq could be supplied through Turkey. Turkish delivery drivers refused to drive through the Sunni Triangle because of the danger of attack there. And the Army directed KBR to purchase particular quantities of fuel from Kuwait and Turkey. Certainly it was more expensive to obtain fuel through Kuwait than Turkey, but that is understandable given the greater dangers, the longer distances and other logistical difficulties involved in supplying through Kuwait. Everyone knew of these differences from the beginning.

Between May and October – when we rebid the fuel subcontracts – the Army Corps of Engineers provided funding for the fuel mission through a series of short-term incremental extensions without any assurance that longer-term funding would be available. In addition, KBR was often provided little notice of the Army's requirements

for future periods – in many cases, only a day or two. These constraints effectively prevented KBR from contracting with our existing supplier, Altanmia, for a longer period (and perhaps obtaining lower prices) or conducting an additional competitive procurement process.

In mid-October 2003, the Corps notified KBR that funding for the mission would continue through at least January 31, 2004. As a result, KBR sought competitive bids for a 90-day contract. KBR attempted to award the contract to the low bidder, the Kuwait Establishment Company. But this company could not prove that the state-owned Kuwaiti Petroleum Company (KPC) would provide it with fuel. Without proof, KBR had no other viable option than to award to the next qualified bidder, Altanmia. In fact, over the course of the contract, Altanmia has been the *only* company able to prove that it could obtain fuel from KPC. At this stage of the process, KBR sought – with success – to negotiate discounts from Altanmia, again with the goal of saving costs. In fact, at the end of the day, we were able to cut close to 20 percent off the price of delivery of the fuel.

The principal reason for the high fuel costs in Kuwait was the high cost of logistics, primarily because of the difficult security environment. When we structured the subcontracts, we anticipated that each tanker would make four round-trips per month from Kuwait to Iraq. Security-related conditions and other logistical challenges prevented that schedule. Tankers instead were only able to make fewer than two trips per month on average. Since tanker charges were a fixed price per month, this caused the price of delivered fuel to increase.

Had tankers been able to make four round-trips a month, the transport price per gallon from Kuwait would have been approximately $.82 rather than the $1.28 KBR paid. Thus four round-trips a month would have meant $.46 savings in the transport cost per gallon, or slightly less than a 20 percent savings on the total costs of fuel and delivery.

Second, I would like to discuss the sourcing of fuel from Kuwait and Turkey.

Initially, in the absence of directions from the Corps, KBR on its own initiative sourced fuel from both Kuwait and Turkey. After May 21, the Corps directed specific levels of fuel purchases from Kuwait and Turkey. As would be expected, KBR complied with these directions.

By the end of our involvement in the program, KBR had delivered a total of 463 million gallons of gasoline. Nearly three out of every four gallons came from Turkey. In all, 333 million gallons (72 percent of the total fuel delivered) was delivered from Turkey while 130 million gallons (28 percent of the total fuel delivered) came from Kuwait.

Third, I think it is important that the Committee understand the extraordinary, hazardous conditions we faced in delivering fuel.

Transporting the fuel was a dangerous and complicated mission. We and our subcontractors recruited and/or sourced hundreds of drivers, some 1,800 tankers, and supplied more than a hundred different download points across Iraq. It was nothing like transporting fuel in the United States. We leased every available tanker in Kuwait; when

we exhausted that supply, we leased tankers from elsewhere in the region. We were totally dependent on military escorts to provide security, and faced constant and real threats: our subcontractor lost approximately 200 trucks and five drivers in hostile and non-hostile incidents.

There were many logistical challenges along the way, such as delays in military escorts, mortar attacks, sabotage, closed supply routes, and last-minute changes in supply destinations. As I mentioned above, our convoys depended on military security escorts. Once convoys got going, stopping or slowing them created enormous risk to both military and contractor personnel. As a result, in some cases – including cases where a tanker broke down or even had a flat tire – a truck would be abandoned or destroyed to avoid life threatening risks from hostile attacks or the loss of military cargo to the enemy. But let me be clear: these decisions were made by the U.S. Army for security reasons, not by KBR. The Army told us what to deliver, when to travel, and what route to take, and provided convoys to ensure security. When a truck broke down, the decision about whether to repair the truck on the spot, abandon the truck and allow recovery personnel to come and pick it up, or to destroy it, was made by the Army. For good reason, these decisions were made by military personnel – only military personnel were in a position to calculate the security risk.

Logistics Civil Augmentation Program (LOGCAP)

Our largest contract with the U.S. government is LOGCAP, the Logistics Civil Augmentation Program. It is the modern-day equivalent of the U.S. military's reliance on civilian contractors to provide supplies and services – a reliance that began with the Revolutionary War.

LOGCAP is the U.S. Army contract first awarded to KBR in 1992 after a competitive bidding process. We frequently refer to that contract as "LOGCAP I." During this period, KBR provided support principally to contingency operations in Haiti, Somalia and the Balkans. KBR lost the contract to a competitor in the 1997 procurement competition ("LOGCAP II"), and won it again in 2001 ("LOGCAP III") as part of another open competitive procurement process. LOGCAP, our biggest contract, is not a "sole-source" contract at all, although it is frequently and erroneously referred to as such.

Under the LOGCAP contract, we are on call to provide a wide range of services to the U.S. military – all logistical in nature and designed to provide as much in the way of creature comforts to soldiers as possible. Many are familiar with our LOGCAP work today in Iraq and Kuwait. But through the LOGCAP contract, KBR today also supports contingency operations in Afghanistan, Djibouti, Republic of Georgia and Uzbekistan. We provide support whenever and wherever it is required.

In Iraq and Kuwait, we build camps, cook meals, deliver mail, supply drinking water, provide a supply transportation infrastructure, and provide ongoing operations and maintenance of facilities. By fulfilling our mission, we allow the troops to fulfill their mission. The work of our employees frees the Army from having to maintain a large number of logistics support personnel on a continuous basis. Contracting like this has

been recommended over the years, including in 2001 by the U.S. Commission on National Security, known as the Hart-Rudman Commission, which encouraged the Secretary of Defense to establish a 10-year goal of reducing infrastructure costs by 20 to 25 percent "through outsourcing and privatizing as many DOD support agencies and activities as possible."

Iraq is not the first place we have provided these services – but it is the first one to occur in such a hostile environment with such difficult logistics challenges. We are extremely proud of our work there, which we have accomplished under incredible stress and in an extremely hostile and dangerous environment.

The challenges are immense, but our employees are delivering. Here is one description of our work, in a New York Times article by Dan Baum, "Nation Builders for Hire," June 22, 2003:

> *"KBR essentially took an entire Army base out of containers and made it rise in the middle of the Kuwaiti desert two days ahead of schedule: air-conditioned tents complete with 110-volt outlets for the soldiers' boom boxes, male and female shower blocks, kitchens, a laundry, Pepsi machines, a Nautilus-equipped health club with an aerobics room ("Latin Dance Thurs & Sat!"), a rec center with video games and a stack of Monopoly sets, a Baskin-Robbins and a Subway sandwich shop. . . .To conjure Camp Arifjan in a twinkling amid one of the most hostile environments on the planet was by any measure a stunning logistical achievement."*

As many officers and enlisted personnel have told us, LOGCAP has changed the way they live in the theater. Instead of lying on the ground they have shelter, and sleep on cots. Instead of eating MREs – meals, ready to eat – they eat hot meals. Instead of using a bucket of water to wash up, they have showers. Instead of using a bucket of water to wash their uniforms, they have laundry service.

The scale of providing these services to our soldiers would be challenging enough in even the most hospitable of environments. But we were called upon to do so without delay in areas that often lacked even the most rudimentary services, such as electricity, communications and potable water.

Every day in Kuwait and Iraq, often in hostile conditions, KBR:

- Serves more than 475,000 meals,
- Washes almost 16,000 bundles of laundry,
- Provides 2.3 million gallons of potable water,
- Hosts 40,000 patrons at Morale, Welfare and Recreation facilities,
- Collects nearly 10,000 cubic meters of trash, and
- Has as many as 700 trucks on the road at any time providing transport support to the military.

Let me repeat, Mr. Chairman and members of the Committee – that is what our people do for our troops *every day.*

We have faced a good deal of criticism for our LOGCAP contract. Even our critics agree that we have delivered the goods and services that the Army needed, and that the level of service we have provided has been excellent. The criticisms go to cost issues – KBR is criticized for supposedly being insensitive and inattentive to how much the LOGCAP and other contracts are costing the American taxpayer. We have faced a good deal of audit scrutiny, and that process has led us to make some changes in our systems and procedures. Their criticisms are just wrong. At the end of the day, the government will satisfy itself about the reasonableness of all our costs.

It is frequently said that, because most of the task orders under LOGCAP are "cost-plus," KBR lacks concern about running up costs to the Government because – so the criticism goes – the more the cost, the greater our fee. That is not the way it works. Under LOGCAP, the biggest part of our fee is the so-called "award fee," which is a maximum of two percent of the costs that have been defined and agreed upon, a step called "definitization" that involves final agreement on the scope and price of the work. The award fee is just what it sounds like – an "award" that the Army makes if it concludes that we have done a good job at controlling costs, meeting all our milestones and deliverables, and meeting and exceeding performance expectations. The potential award fee for RIO is five percent, and it is two percent for LOGCAP. If we do not control costs well, our award fee can be lowered.

Moreover, the Government has been operating with cost-reimbursement contracts for a very long time, and has developed a highly sophisticated body of regulations to make sure it is not overcharged.

People hear that the Army has proposed to withhold some 15 percent of our requests for reimbursement under the LOGCAP contract, and they assume that the Army must be accusing KBR of overcharging. That is simply not the case. The proposed withholding comes because KBR's Iraq task orders have taken a long time to "definitize," and the Army has applied a regulation that says the Government can only reimburse 85 percent until definitization has occurred. But, as GAO and DCAA have both recently noted, the big reason for slow definitization is the repeated scope changes to the LOGCAP task orders, and those scope changes reflect the fluid nature of the situation in Iraq. The Army has recognized that it would be unfair to hold back 15 percent under these circumstances, and has agreed to delay imposition of the withholding regulation while we work hard with DCAA and the Army to complete the definitization process.

We are experiencing a 15 percent withholding under the RIO contract. This means that approximately $50 million of our requests for reimbursement have been withheld. While we do not believe this withholding is appropriate, we are working with the DCAA and the Army to get the proposals definitized so we can be paid. Again, this withholding has nothing to do with any allegation of overcharging.

Some of our critics point to specific examples of allegedly wasteful procurement practices. Our contracts create incentives for cost savings, and we have a myriad of checks and balances and audit procedures. On top of this, the government closely scrutinizes every single cent we spend.

It is true that DCAA has made some criticisms of our billing and estimating systems. It has taken longer than normal to finalize cost proposals because of the unusual communication difficulties in Iraq, and constant customer changes in our Scope of Work.

While our systems have certainly been stretched by the enormous demands of the Iraqi operation, in the end, our systems work and we strongly believe that the Government has not been overcharged. We have made changes, including automation of our systems. Normally this process of give-and-take with DCAA occurs in a much less public environment, but we are continuing to work cooperatively to assure that our costs are properly documented.

Dining Facilities

One of our most important jobs is feeding the U.S. troops as well as other Coalition forces, government officials and contractor personnel. Through a rapidly changing series of task orders, we were directed to establish and operate more than 60 dining facilities in widely diverse geographical locations throughout Kuwait and Iraq, and serve three and in many cases four hot meals a day with no limitation on portions or take-out orders.

I am pleased to have the opportunity to set the record straight on the issue of KBR's supposed "overcharging" for dining facility services. It has frequently been alleged that KBR has improperly billed the government for meals that were never served. Again, these criticisms are mistaken. The Army directed us to build enormous dining halls and kitchens, to hire employees and procure food based upon an estimated number of personnel who would expect to be fed.

Our subcontractors got the job done, and asked us to pay them on the basis provided in the subcontracts, namely, those estimated numbers of troops to be fed provided by our customer at various intervals. This is a normal practice in the catering industry. DCAA has concluded that when the actual number of meals served fell short of the estimates, the actual number should be the basis for payment. But that is not what the agreements say, and we cannot, we believe, breach those agreements. The contractors deserve to be compensated for building a 4,000 person facility and hiring personnel to serve 4,000 people, even if only 3,500 show up at mealtime.

Because this issue has been so prominent, let me give you some history and a fuller explanation:

We were directed to set up the dining facilities as soon as possible after task orders were issued. We were told that time was of the essence and the failure to act quickly could affect the operational and personnel readiness of the U.S. troops. In the case of the V

Corps Task Order, the goal was to stand up and serve more than 120,000 troops in more than two dozen locations by July 4, 2003, a period of less than three weeks. Thus, the time frames were short and the conditions often harsh and dangerous. And in some cases, because this is war and troop deployments change, the U.S. Army Materiel Command issued revisions of our orders. For example, by June of 2003 the Army had formally modified the task order related to dining facilities at Camp Arifjan 15 times. This is not a complaint. Repeated revisions like this are just a fact of life in a war zone.

Most task orders specified a minimum number of people that each dining facility had to serve on a daily basis.

For example, a given task order might specify that the dining facilities should be ready to serve 4,000 people four meals a day (breakfast, lunch and dinner, as well as a late night meal/snack). At some dining facilities, the Army gave periodic and fluctuating projected headcounts -- changing troop movements caused some of this fluctuation. The minimum and headcount projections were designed to ensure that no soldier goes hungry, and that KBR prepare enough food so that the last soldier in line had the same selection as the first soldier served. The emphasis is on ensuring that U.S. troops are fed hearty, high-quality meals.

The task orders did not seek to control or limit the ability of soldiers to take extra helpings, or leave with extra meals for themselves or another soldier who was unable to come to the facility. As a result a significantly greater number of meals were served each mealtime beyond the actual number of persons who entered the dining facilities.

KBR determined that the best way to meet the immense time pressures to get the dining facilities up and operating was to utilize qualified, reliable subcontractors who could mobilize quickly, and we entered into a series of agreements with six principal subcontractors. Operating under brutal conditions and in the hostile environment, the subcontractors had to purchase and transport the materials necessary to build a dining facility; construct it; purchase and transport the equipment needed to prepare and serve meals to meet the estimated number of diners; hire, transport and house sufficient staff to serve the food; and purchase, transport and store the necessary food.

Taking on such a subcontract required a substantial investment on the part of the subcontractor. Frequently, subcontractors had to procure supplies and hire employees from outside Iraq and Kuwait. Often, they could not find regional sources for the goods and services the contracts required. Even when the subcontractors could find regional sources, they had to pay premium prices due to the limited supply and extreme demand.

Most subcontractors based their pricing on the minimum number that an individual dining facility had to be ready to serve each day. The contracts were relatively short-term, so they needed to calculate their bid so as to recover their significant start up costs within the life of the contract. A subcontractor who is directed to serve, say, 4,000 people a day must incur all of the costs to purchase and transport building supplies to build the facility, buy and transport the equipment, hire and transport sufficient staff and

purchase enough food to be ready to serve 4,000 people whether they all show up to be fed, or whether a lesser number arrive at the dining facilities on a given day.

The best analogy is catering a wedding. The first question that the caterer will ask is how many guests are expected. The caterer will then calculate a price to enable him to cover his costs and make a profit. The price the caterer will propose is based upon this estimate of attendees. If fewer guests show up, the caterer will still charge for the estimated amount. He still must prepare for the estimated number of people and be ready to cook for that number. He is unable to refreeze the food and use it for another day because of health standards. KBR and its subcontractors were in the same position as the wedding caterer – with the many significant additional challenges of operating in a war zone.

Despite the extreme time pressures, the war zone environment and the extreme scope of the challenge, the facilities have reliably provided high quality food. Indeed, the government has complimented KBR and its subcontractors on their food services on many occasions.

Questions and Controversies

As a government contractor, KBR is subject to numerous areas of oversight. We welcome this oversight. As is expected in the give-and-take of major government contracts, the oversight has sometimes resulted in various areas of disagreement between KBR and some oversight agencies.

The auditing process on large, complex government contracts always identifies issues, which are normally worked out quietly and professionally with the auditors. DCAA has identified some issues with which we agree, and some with which we disagree. This is the normal process, and we are working with them and the Army to iron out differences. In the meantime, however, the taxpayers' interests are fully protected.

In the case of dining facilities, the DCAA, while carrying out its responsibility of making audit recommendations, has raised questions about the billing methods of our dining facilities subcontractors. As you know, DCAA makes audit recommendations and provides audit reports, usually to the contracting officer. It is up to the contracting agency to decide whether the DCAA report findings and recommendations are valid or not – and whether the recommendations should be followed in whole, in part, or not at all.

DCAA has questioned whether any subcontractor billing methodology other than "boots through the door" or "meals served" is appropriate. In other words, it questions whether the subcontractors who were told to expect a minimum number of troops to be fed each day, and who calculated their proposed prices and made their bids to build, equip and operate a dining facilities based on that number, should be allowed to still bill for that minimum number if fewer than that minimum number visit their facility. The contracts require that subcontractors be reimbursed for these reasonable costs on the basis provided in their subcontracts.

It is important to note that the current difference of opinion over billing methods stems from subcontractor bills submitted to KBR for payment. There is no contention that KBR has sought reimbursement for dining facilities expenses that have not actually been incurred by it or invoiced by its subcontractors.

Soon after the DCAA raised these questions, KBR dispatched a team of contract specialists to Iraq and Kuwait to review contracts, invoices and supporting documentation at more than 60 dining facilities. When our review was completed, we reported these findings:

- No systemic billing irregularities were discovered (minor discrepancies are adequately addressed in the normal course of subcontract review and payment)

- The amounts invoiced by the subcontractors were fair and reasonable and in keeping with the terms of the LOGCAP contract, the dining facilities task orders and the individual subcontracts

- Where the Army furnished minimum personnel numbers for specific dining facilities it was reasonable for subcontractors to bill on the basis of such minimums, because they based their (mostly fixed) cost of operations and consequently pricing upon those numbers, which they would not recover if they were required to bill on the actual number of dining patrons

- In fact, the Army has relied on the exact same billing methodology as KBR – and with the exact same food vendor as KBR. This occurred when the Army contracted directly with a dining facility contractor to provide meals in Kuwait and Iraq. After contracting directly with this contractor, the Army turned the contractor over to KBR. Later the Army took back the contract and is managing the contractor. In all three situations the payment method was based on minimum personnel numbers, not on actual boots through the door.

Until this matter is resolved, slightly less than 20 percent is being withheld from KBR's dining facility invoices. KBR continues to work cooperatively with the DCAA and the Army to try to resolve this issue.

We should not be held to ideal peacetime standards during wartime realities. Any auditing of KBR's efforts and our business systems should take into account the chaotic and challenging nature of wartime contingency logistics contracting.

This dilemma was perhaps best described on June 24, 2004 by Michael Wynne, Deputy Undersecretary for Acquisition and Technology of the Department of Defense, testifying before the Readiness Subcommittee of the House Armed Services Committee on Contractor Support in Department of Defense:

"The Army is reporting absolute appreciation for the LOGCAP contract that is recently being questioned by the DCAA; the oil is, in fact, flowing extraordinarily well – on behalf of all the folks at Halliburton."

and

"There are two sides here. One is you must come up with a contract vehicle that, in fact, induces competition and induces people to actually want to perform on behalf of the American soldier in this condition, and on behalf of our national goals and objectives. That having been said, we are very hard to do business with. We have in our context, and contracts very stringent rules, regulations and follow up audit rights, that are rarely granted in any commercial activity. So when we have, in fact, induced commercial firms to help us, and many times these construction companies do not often do business with the Department of Defense under a cost-type schema. When they find out what the follow up is, usually, and in the case of even somebody as experienced as KBR, they find their accounting systems to be a little bit wanting, as it flows down to subcontractors.

"In the case of Iraq one of the most daunting features is cash payment. They have no banking system, so we don't write checks. As a result, a lot of contracts are, in fact, especially at the sub, sub level, are cash payments to get the job done. That having been said, it requires a certain accounting – our accountants love to – I mean, we're used to and our auditors are used to following up with some specific rationale for an expenditure of money across the board. And many times in the heat of the zone or trying to get a job done, you may not have exactly the kind of rationale that pleases a general auditor. And they get to look at it, if you will, under a little bit less trying circumstances than it may have been issued in the first place."

Conclusion

Mr. Chairman, the work in Iraq has been demanding and dangerous. Yet, when our employees were called upon to assemble a massive enterprise, they did so. The facts show that this enterprise has delivered and continues to do so. When the hostilities became intense, we did not close up shop. We instead delivered our mission – and with great pride we continue to deliver today. No other company in the world could have acted with such resolve and dedication to accomplish so much in such a short order.

Our challenge is to continue to meet the expectations of our customer, the United States Army, in demanding wartime conditions where time is often of the essence.

This was not easy work in the first hours after the U.S. soldiers entered Iraq, it is not easy work today, and it will not be easy work in the weeks and months ahead. But we have made a commitment to stay the course – a commitment we will keep to the U.S. soldier, to the Iraqi people, and to the American people.

Thank you.

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Chairman TOM DAVIS. Mr. Walter. Thank you.

Mr. WALTER. Mr. Chairman, and members of the committee, thank you for inviting me here today. My name is William Walter. I am the director of Government Compliance for KBR Government Operations. I welcome this opportunity in part because I am familiar with these issues from several perspectives.

Early in my career, I worked as an auditor for the Defense Contract Audit Agency. Next, I served as a consultant to government contractors, and as a teacher for George Washington University's government contracts program. Today at KBR, I currently spend about a quarter of my time in Kuwait and Iraq.

Let me make a few things clear at the outset about some assertions we have heard today. When I am in theater working with KBR procurement specialists, they are constantly trying to negotiate the best deals possible with vendors. I have never heard any guidance remotely close to "it's cost-plus, don't worry about it." Not once.

Before employees complete their time sheets, they are told they are responsible for their time sheets. We have heard that people have put too many hours on their time sheets. Our policy strictly prohibits such padding of hours, and if we find it is happening, we will deal with it directly.

We have also heard about our laundry contract. Early on in the deployment, the Army believed that the laundry from each soldier and facility would be considerably more than it turned out to be. But we had negotiated a fixed price based on the Army's higher estimate of laundry requirements. When it turned out there was less laundry, KBR renegotiated a lower price with the vendor.

Finally, we heard from Ms. deYoung that we overpaid for sodas for the troops. Our contract provided that our subcontractor should deliver a bag of sodas, ice, and cups to soldiers and provide a hospitality lounge at the airport. KBR, through its own auditors, discovered that the subcontractor was delivering only soda, without the ice and the cups. This was corrected. This investigation was undertaken by KBR before Ms. deYoung began to work as a logistics assistant in subcontracts.

Mr. Chairman, the common thread here is that KBR takes seriously the matters of controlling costs and providing the fiscal accountability the taxpayers expect. Contracting in Iraq poses greater and different challenges than those faced by a defense contractor building a weapons system, a contract that involves a permanent manufacturing plant and blueprints, even though the audit process is the same for both.

As a logistics contractor, we don't have a blueprint for a camp. We get the layout when a general points and says, let's put the dining facility here, and let's put the showers over here. There is always a clear sense of urgency. For example, we were asked to set up 26 dining facilities throughout Iraq in less than 3 weeks, and the requirements for dining facilities kept expanding so that soon it grew to more than 60. Requirements change on a daily basis. For example, one dining facility in Kuwait served 8,900 soldiers 1 day and the next day it served over 16,000 soldiers.

KBR's LOGCAP and RIO contracts are cost-plus contracts, the type of contract the government uses to meet urgent and unpredict-

able needs. As Major General Wade McMahon testified before this committee in March, it is important to note that the LOGCAP contract provides us the flexibility and agility to respond to unknown requirements over the unknown time lines and uncertain conditions.

Cost-plus contracts work like this: First, the Army issues a statement of work. This frequently involves a pressing assignment defined in broad terms, one that is later adjusted to fit changing conditions. KBR then develops a rough estimate of what it will cost. The Army then approves or modifies the estimate and issues a notice to proceed. The parties then work together to negotiate a final cost estimate. Once the costs are agreed to, this estimate serves as the basis for calculating KBR's base fee and our possible award fee pool.

Our base fee is very small, typically 0 to 2 percent. Our incentive is to obtain the award fee, the largest of the fees that can be earned. If our costs exceed the definitized amount, our base fee remains fixed. There is no additional fee if KBR were to simply rack up additional costs. Our award fee may be reduced or denied if we do not do a good job of controlling costs, one of the significant award fee criterion.

There are many reports in the media accusing KBR of running up costs to increase profits. This is not true. A contractor like KBR does not have an incentive to run up excessive costs. In fact, the opposite is the case. The review and the award fee process provides strong incentives for KBR to control costs. Our operations in Iraq and Kuwait are undergoing extensive and continuing government scrutiny and audits. This oversight is common for all cost-plus contractors and will ultimately assure that the costs charged will be fair and reasonable under the circumstances.

And all of this serves the best interest of our customer, the U.S. troops, and, of course, the U.S. taxpayer. The wartime conditions in Iraq have stretched our contracting systems, and there are a number of complicated issues of contract administration that we are in the process of resolving with the government. Many of these issues arise, we believe, because review mechanisms that are well suited for conventional contracting during peacetime have proven less well suited during a wartime environment.

In the wartime environment, subcontracts must be placed on an urgent basis. Even a simple task like assembling the necessary documentation is extremely difficult because of the hostile environment and the significant initial requirements. To address these unique issues, we are involved in a cooperative process with the Army, the Defense Contract Management Agency, and the Defense Contract Audit Agency to explore ways to bring these contracting processes in line to the wartime realities, based on our lessons learned, without sacrificing accountability.

We believe these contracting processes, oversight procedures, and our internal policies, taken as a whole, offer a system that is agile enough to serve the needs of the U.S. troops while also assuring the fiscal responsibility and the safeguards of the people's interests.

We are proud of our record as a Federal contractor and proud of our record of operating with business systems that assure absolute integrity, efficiency, and effectiveness.

Thank you for allowing me to talk about our procurement policies and practices, and I look forward to your questions.

Chairman TOM DAVIS. Thank you.

Mr. Cox.

Mr. COX. Mr. Chairman, and members of the committee, my name is Stoney Cox, and I am vice president of operations for the KBR's Governments Operations Unit. I returned last month, after 14 months in Kuwait and Iraq, where I served as the project director for KBR's Restore Iraqi Oil [RIO] project as it is called.

Prior to Operation Iraqi Freedom, the Defense Department decided that getting Iraq's oil flowing again was fundamental to the future of the Iraqi people. The RIO project was an outgrowth of that prewar planning. Our involvement began when the Army Field Support Command issued KBR a task order for planning under the competitively awarded LOGCAP contract that we hold. We were asked to develop a contingency plan to assess Iraq's oil infrastructure and how it could be returned to full production.

Later we were asked to implement that plan on a sole- source basis. And I know there has been a lot of criticism of the Army for giving KBR this contract without any competition, but I would point out that this matter was fully reviewed by the GAO and it was decided that it was both legal and appropriate, given the wartime conditions and the urgency of the mission.

Under RIO, KBR helped restore oil production and oil exports ahead of schedule, and imported fuels for the everyday use of the Iraqi civilians to cook, heat their homes, and drive their cars. On March 21, the second day of the war, KBR's engineers crossed into Iraq, following in the footsteps of the Coalition soldiers as they initially assessed the oil facilities. We faced mines, unexploded ordnance, booby traps, and roving bands of looters who actively targeted KBR personnel.

Operating under these harsh conditions, KBR helped the Army Corps of Engineers meet its goal of restoring Iraqi oil. The first oil flowed from the southern oil fields on April 23, 2003, just 5 weeks after we began the assignment. Exports started again in June 2003, and have produced some $12 billion in revenues for the Iraqi people in 1 year's time. And on December 30, 3 months ahead of schedule, Iraq reached its prewar production levels of 2.4 million barrels per day.

Mr. Chairman, any balanced examination of a contractor's work must take into account how it responds to the urgent demands of the military in the war zone. The perfect example of that for us is the emergency fuel mission. On May 3, 2003, the Army Corps contacted KBR in Kuwait and directed that we begin to procure and transport millions of liters of fuel for Iraq as soon as possible. The Army indicated to us that a fuel shortage for the Iraqi citizens threatened civil unrest and posed a serious danger to U.S. soldiers. As testified here before this committee, one soldier in fact was killed while trying to maintain order in a gas line in Baghdad.

Outside the war zone, a contractor might have months to develop such a complicated program. When the Defense Energy Support Center took over this mission, it had 3 months to complete the contract, compete it, and put it in place. We did it in 3 days. We simply did not have the luxury of time. We simply acted in 30 hours

and arranged for the logistics, and the first trucks of gasoline were rolling from Kuwait into Iraq. This eventually grew into a massive 11-month undertaking. We made almost 9,000 gasoline deliveries per month, delivering over 463 million gallons of gasoline to Iraq.

There are several important points I wish to make about this program.

First, It was a very dangerous mission. Our subcontractors have lost some drivers who have been killed due to hostile incidents, most of them from making deliveries from Kuwait.

Second, we did everything possible to ensure that the Army's requirements were met at the lowest possible cost, even given the urgency. Within 24 hours of being contacted by the Army, we had contacted several firms and had received several bids. We chose a low bidder, a Kuwaiti company named Altanmia.

A significant reason for the high cost of fuel in Kuwait was the high cost of logistics. We anticipated, when we began the mission, that each truck would be able to make four round trips per month from Kuwait to Iraq, but we were 100 percent reliant on the military-controlled convoy system. And because of the security situation and the many delays in getting the convoys going, tankers instead only averaged slightly less than two round trips per month, about half.

Since our tanker charges, our costs, were a fixed price per month, this caused the price of delivered fuel to increase. Four round trips per month would have been a savings of $0.46 a gallon, or less than 20 percent of the overall cost of the fuel delivered to Kuwait or Iraq.

The third point I would like to make is that at our own initiative, we saw alternative sources of fuel, namely from Turkey, which was—costs substantially less than the fuel from Kuwait. It was less costly because the vendors there deemed it less dangerous to deliver from Turkey and because there was a better competitive market for fuel, for that product, from Turkey. By May 11th, we also began delivering fuel from Turkey, and in the end, at the end of the mission, nearly 72 percent of the fuel that we delivered to Iraq came from Turkey rather than Kuwait.

Our critics often allege that we overcharged by some $61 million, and there is a new report out today that ups that to $167 million, but they allege that we overcharged by $61 million because simply we didn't buy all of the fuel from Turkey. A simple calculation. But it simply was not possible to do so, and we were not directed to do so. We were, in fact, directed where to purchase the fuel.

Now, why was that? Well, for one thing we needed two sources of fuel, two approaches, if you will. Turkish drivers often refused to drive through the Sunni Triangle because of the dangers there. And, in fact, Turkish drivers went on strike in November and shut down the Turkish fuel flow, and had we not had the Kuwait fuel flow at that time, we would have definitely been in trouble. We and our client would have been in trouble.

As I said, we are certainly aware of the minority's report that was issued yesterday alleging that we have overcharged $167 million compared to DESC current price for this mission. We strongly disagree that there was any overcharge, and we believe this report is flawed in several ways. For example, based on the rising spot

price, we believe today that DESC now pays a higher price for the gasoline than did KBR. Any difference, major difference, though, comes from the transportation cost.

We believe the report is flat wrong, and to compare our immense startup costs as we put the system in place to do this, for which DESC has reaped the benefit of this system, we believe that is wrong. I would welcome the opportunity, as we get into the Q and As, to further address those issues, but I think I will stop now. And thank you for allowing me to be here today and address these issues with the committee.

Chairman TOM DAVIS. Thank you very much.

Mr. Richard.

Mr. RICHARD. Thank you, Chairman Davis and members of the committee. My name is Keith Richard. I am the KBR government operations regional project manager for the theatre transportation mission in Iraq and Kuwait. In this role, I oversee all KBR LOGCAP transportation missions in Iraq and Kuwait.

I am pleased to address the committee on a key role that KBR is playing to help support our troops in Iraq. In addition to the trucks that you just heard about that supplied Iraqi civilians with fuel, KBR also wanted a separate program in Iraq to support military fuel, military parts, food and mail to coalition forces. Thus far these KBR trucks have driven nearly 40 miles and made more than 128,000 deliveries.

We operate a fleet of about 2,000 trucks, employ 1,700 drivers, 300 truck mechanics, along with logistics specialists, clerks and heavy equipment operators. In miles driven and fleet size, we are the equivalent of the fourth largest trucking company in the United States, and we set up that capability in a matter of months.

Let me take you through a typical trip, if typical is the right word. Our truck typically traveled from Kuwait to the central distribution center at Camp Anaconda and back. A distance of 1,100 miles round trip in a States trip, equivalent of travel from Richmond to Boston, would take 2 days, or 9 hours up and 9 hours back. But in Iraq it is almost a 5 or even a 6-day trip, and that's if all goes well. On the run to Camp Anaconda, the driver's day begins with a pretrip inspection of his truck in Kuwait followed by a meeting with the latest security briefing.

The mood is tense, and I certainly know that in trips I have made, my adrenalin is pumping. Trucks are joined by military escorts at the Iraqi border. From there they travel to Camp Cedar, a support center, where they overnight. The next day a new set of escorts joins in to head on to Scania, a massive truck stop where yet another escort awaits.

The third day is a straight run for Camp Anaconda. This is dangerous work for our drivers, and provides explosive devices, or IEDs, or a constant threat of rocket-propelled grenades, land mines, mortars, and small-arms fire and spikes in the road. On a recent trip a 25-truck convoy suffered serious damage to 17 windshields from rocks thrown in two particular hostile cities. That is not unusual.

Sadly, 14 drivers have been killed while carrying out this important mission. That's 14 drivers. One driver, Al Caton, was also a friend of mine, as you heard in previous testimony. Al was a real

leader and one of the nicest guys I know. Some of the other drivers were killed in the coordinated ambushes of convoys on April 8th and 9th, and two drivers are still missing from those tragic days. These drivers are a brave and courageous group of people.

But the danger does not end when the driving does. Even simply being at Camp Anaconda can be dangerous. In my 6 weeks in Anaconda this spring, there was virtually mortar fire every night, which means you get up, wait, go to the bunker and pray. At Anaconda I was asleep in my containerized housing when a mortar came flying just over my sleeping area and slammed into a KBR mail van parked 15 feet away.

Earlier this month at the same camp, a number of KBR employees had gathered for a July 4th celebration when two mortars hit. Twelve employees were injured, and three had to be evacuated to a combat support hospital. These close brushes with danger are not unusual for the men and women of KBR working in Iraq. It is simply a part of the job.

I also want to address some of the allegations made today. First was that we abandoned trucks because of flat tires or simple repairs. The Army provides all security, tells us what to deliver, when to travel and what routes to take. Contrary to some assertions, if a truck breaks down or is disabled, the decision to abandon or destroy a truck is made by the Army, not KBR. The Army makes a judgment based on their assessment of how best to save lives, not just equipment or trucks. KBR is the only contractor in Iraq with satellite tracking of its assets and personnel, and full recovery capability. Even a seemingly simple matter like changing a tire is at least a half-hour project.

So the Army must make difficult decisions. Let me repeat this. The Army, not KBR, makes all decisions regarding whether to halt the convoy, fix a truck or abandon it. We are operating in a war zone. The Army also provides records for driving, including security issues. We are told to run tight convoys and not allow intervening civilian vehicles, but the Army does not direct KBR to run civilians off the road. KBR, in fact, has disciplined several drivers who were found to have caused an accident by doing so. Several were terminated.

It has been said that we do not maintain our vehicles. That's not true. Today our teams of mechanics conduct routine preventive maintenance of each truck every 2 weeks. Current readiness rate is 81 percent and has never fallen below 75 percent.

While theft is not rampant, it is a problem. Protection of supplies from theft, it is the responsibility of the Army, and when thefts do occur, KBR promptly reports incidents to the Army. Cargo is tracked by radio frequency system making paperwork unnecessary.

Mr. Chairman, we are doing everything humanly possible to support our troops. I know you would be proud of us if you saw us in action.

Thank you for the opportunity to address you, and I look forward to your questions.

Mr. SCHROCK [presiding]. Thank you very much, Mr. Richard, and thank you all for being here.

As we did with the first panel, and we agreed upon, we will have 30 minutes per side. I think, Mr. Waxman, we agreed that we will proceed first.

We have heard from the so-called whistleblowers, and I would like for you KBR folks to respond to the allegations that were leveled here today. But, first of all, for the record, did KBR have a policy as it pertains to the LOGCAP contract that costs didn't matter because it was a cost plus contract? Any of you can answer that.

Mr. WALTER. Mr. Chairman.

Mr. SCHROCK. Yes, sir.

Mr. WALTER. We absolutely did not have a practice that costs did not matter. As I mentioned in my oral testimony, as I work with people, we are doing our best to make sure we do obtain the best value for the taxpayer and for the soldier in this environment.

Mr. SCHROCK. Any other comment? We heard from Ms. deYoung in the first panel, and I need to ask you first a question about her. Was Ms. deYoung hired as a contract or as a procurement specialist? Basically, what was she hired to do?

Mr. NEFFGEN. She was not hired as a contract specialist. She was hired in the logistics area as an administrative assistant. We have over 300 subcontract administrators on the LOGCAP contract, and every one of them is trained in that capacity and receives a warrant that authorizes them in writing to execute contracts, negotiate contracts, issue modifications to contracts. Ms. deYoung never had that warranty.

Mr. SCHROCK. Did she have signatory authority on any of the contracts?

Mr. NEFFGEN. She did not.

Mr. SCHROCK. None at all?

Mr. NEFFGEN. None at all.

Mr. SCHROCK. Concerning the Kempinski Hotel, can you elaborate on your decisionmaking process for housing your employees, and specifically any communication your company had with the Army in that effort?

Mr. NEFFGEN. Yes, sir, I would be glad to do so. When there was a buildup the latter part of 2002, there was a scrambling for accommodation within the country of Kuwait. We tried to get our people, as many people as possible, on Marfan in Kuwait. The Army chose priority for placement of troops inside Arifjan. We had some folks that live there and live in tents and Conex containers. But we were forced to search for any accommodation.

Our first priority in seeking accommodations on the outside in hotels like the Kempinski is security, and the hotel was gracious enough to accommodate our security concerns. It is a hotel that is off the beaten path. It is securable, and that was a primary concern.

I do have some pictures that I would like to show of some of our living accommodations to give you an idea.

We have 14,000 expatriate personnel on our payrolls living in Kuwait and Iraq; 88 percent of them either live in tents such as you see here, or they live in Conex containers. They are not the greatest living condition. It is the same as our troops live in in both locations. I personally requested Brigadier General Bob Radin, the

senior logistitian at Camp Arifjan, the senior representative of our customer in the LOGCAP, contact the Army Materiel Command to allow us to move people out of the hotels in Kuwait onto the camp, Camp Arifjan, and for us to build Conex living accommodations. This occurred in April of this year. He said he would support that request. However, there is an implication. There is a dispute with the landowner of the property going on. Until that is worked out, they couldn't allocate us a designated area within the complex of the camp to do so. He said he would support that request at the appropriate point in time when they have it all cleared up on where it is going to go.

We have had repeated discussions between senior members of our company and senior officers in the Army to allow us to move on to secured military camps and get out of these hotels. In the hotels we put people—we fill every bed that we lease in the hotels. We pay a daily rate for the room, and if it has one bed in it, we put one person; if it has two beds, we put two people per room; if it has five, we will put five in that room. So we have people doubled, tripled, quadrupled and quintupled up at the various hotel accommodations.

Our average cost per man per room per hotel a day in Kuwait is running $45 a night. Now, that compares to the government's per diem rate for allowable expense of government personnel living in a hotel room in Kuwait of $258. So it is only 20 percent of the allowable cost.

Mr. SCHROCK. The living conditions sound remarkably like what I experienced when I was on a ship in the Navy.

Mr. NEFFGEN. I can imagine.

Mr. SCHROCK. Yes. Concerning Ms. deYoung's allegations regarding a subcontractor, did that company overcharge for sodas under the contract that was questioned by Ms. deYoung?

Mr. Walter.

Mr. WALTER. Sir, the perception of waste in this matter is incorrect. The facts show that KBR actually did our best in this case to try to protect the government from waste.

The allegation that we contracted for soda at $1.50 per case is wrong. I heard Ms. deYoung's testimony. She said it was $45 per case. Nowhere in the documentation that I have reviewed for the subcontract have I come up with that number. What I have come up with in the contract is a $45 KD, or Kuwaiti dinar, price per package. And the package is two cans of soda, ice and a cup and a plastic bag, and the cost of delivering it, and the cost of cleaning up afterwards when the soldiers get on their plane to fly wherever they have to go.

As Ms. deYoung began working a procurement. She was assigned to assist, provide administrative support for one of our subcontract administrators. That subcontract administrator was already working on this particular issue and had already identified the problem in February, and KBR had made the decision that we were going to withhold payment of over $100,000 to the vendor until we could remedy the situation.

Mr. SCHROCK. With respect to the sodas, again, what exactly did KBR contract for with respect to the sodas? We heard earlier that it was a bag of two sodas, ice and I think nonbreakable cups. Was

La Nouvelle also responsible for setting up and breaking down the area where these bags would be handed out as well as clearing out the trash?

Mr. WALTER. That is my understanding, yes, sir.

Mr. SCHROCK. Concerning laundry, that's a lot of laundry they do over there. Please walk this committee through what was being charged, what is being charged today, and why it is different than your local laundry down the street.

Mr. WALTER. Thank you, Mr. Chairman. I would be happy to try to clear up this misconception.

During the testimony this morning, it was identified that $28 a bag for a 15-pound bag would be more reasonable than paying $100 per bag. What happened in this case was KBR, as I mentioned during my testimony, got a statement of work. In the statement of work it said, provide laundry services for 6,200 soldiers.

We took the statement of work and we provided that to our various vendors, and our subcontractor looked at that requirement, and it also had an open requirement, because included in the laundry charge is the laundry for the medical facility as well as the sleeping bags for the soldiers to get them laundered as well. What we did was we provided that to our subcontractor, and they put together a quote of $1.2 million per month to do all of that laundry.

If you calculate the number of soldiers, that comes out to $24 a bag for the soldiers' laundry, but that also includes the cost of laundering all of the medical laundry out of the hospital as well as the sleeping bags.

Once again, during the progress of this particular task order, KBR identified that the volume of troops were not coming through the airport facility, which is where this contract was located. As a result of that, KBR negotiated with the subcontractor to get a per-soldier-per-bag price for laundry that was, I believe, $24 per bag, and that is what the price is today.

Mr. SCHROCK. How big are the bags?

Mr. WALTER. I'm sorry, sir?

Mr. SCHROCK. Like a seaman's bag? How big a bag?

Mr. WALTER. It is a 15-pound bag, I believe, of laundry.

Mr. SCHROCK. Is La Nouvelle still subcontracting?

Mr. WALTER. La Nouvelle is subcontracting in a very minor way with us. They are no longer doing laundry services.

Mr. SCHROCK. Typically with that subcontractor and other subcontractors, do you believe you have sufficient administration in place to oversee these contracts?

Mr. WALTER. I believe we do.

Mr. SCHROCK. Ms. deYoung has commented that she thought subcontracts were being closed out in order to avoid government contracts. Could you discuss KBR's policy on closing out subcontracts? In your experience, were closed subcontracts immune from government audits?

Mr. WALTER. I would like to clear that point up very readily. As my job with KBR, I am the director of government compliance. I work on a daily basis with the defense contract agency auditors in Houston and in theater, and in no way, shape or form do they allow us to get by by trying to close out a file so they do not have to audit.

I receive over 1,200 requests per month for supporting documentation as the auditors are going through their transactions, and one of the key elements they are looking for right now is the documentation to support a lot of the payments that we made in the 2000, 2001 and 2002 timeframe. And what they are doing is they are looking at these files, many of which are closed, to make sure that we have the adequate supporting documentation in place.

Mr. SCHROCK. Was Ms. deYoung a member of the so-called Tiger Team?

Mr. WALTER. No, sir, she was not.

Mr. SCHROCK. Could you explain in a little more detail the purpose in the mission of the Tiger Team?

Mr. WALTER. I would be happy to.

Mr. SCHROCK. I don't know, and I would like to know.

Mr. WALTER. Toward the end of 2003, we found that there were a number of our vendors that were not getting paid. And in reviewing that, what we found was that our company's internal controls were working. If a subcontractor invoice does not have the adequate supporting documentation, it will not be able to be paid by our accounting and finance group. So what we were doing is we worked with our accounting and finance people and found that this was an issue.

During a wartime situation, when we have immense buildup, a lot of our procurement people start out on the task order. They have a cell phone, a stubby pencil and a piece of paper, and they start making the requisitions, and they start getting the goods in place. The documentation for some of these things, the complete documentation package, sometimes will take a while to get in place.

What happened here, as Ms. deYoung was involved, she was helping the subcontract administrator pull together documentation for subcontracts that were issued back in 2002 and earlier in 2003 as the campaign was building significantly.

Today what we have done is—one of Ms. deYoung's statements is KBR is not like a company that has all of these things tied together in a nice electronics package. One of the things that was not available during the startup of this mission was communications. So, that is why our people were working with very heavily manually intensive systems. We did not have communications. And even today as I try to get ahold of people throughout the theater to get my questions answered for the government auditors, we have a very difficult time getting hold of them. E-mail is intermittent at best in many locations, so trying to get a very sophisticated communications system in place that links all of these things electronically was not possible at the time. So what happened was our procurement people would put together spreadsheets for the different camps, and that is how they were tracking their information.

Toward the end of 2003 we started to have improved communications. During 2003, we implemented a procurement tracking system called Procurement Plus. We now have all of our camps up and running on that with current procurements, and we are trying to get caught up with the few remaining older subcontracts that are out in place.

Mr. SCHROCK. Let me go to the testimonies of Mr. Warren and Mr. Wilson. This will be kind of a rapid-fire series of questions. In terms of convoys and trucks in both the RIO and LOGCAP, who was responsible for those convoys?

Mr. RICHARD. From the LOGCAP perspective, the military.

Mr. SCHROCK. Who supplied security for the convoys?

Mr. WALTER. The military.

Mr. SCHROCK. Did the convoys always carry spare tires?

Mr. RICHARD. Yes, they did.

Mr. SCHROCK. Did KBR ever destroy a tractor-trailer because of the need of a spare tire?

Mr. RICHARD. No, sir.

Mr. SCHROCK. Who made the decision to destroy trucks?

Mr. RICHARD. The military.

Mr. SCHROCK. Did KBR conduct regularly scheduled maintenance on the fleet? I think we heard.

Mr. RICHARD. Yes, we did.

Mr. SCHROCK. Did KBR advocate the stealing of goods off of these convoys?

Mr. RICHARD. No, we did not.

Mr. SCHROCK. When it comes to the drivers, what was KBR's policy concerning the drivers; are they responsible for keeping looters at bay? Who is?

Mr. RICHARD. It is the military and the Army's responsibility.

Mr. SCHROCK. Strictly?

Mr. RICHARD. Strictly.

Mr. SCHROCK. What is KBR's policy for drivers running people off the road in order to maintain convoy integrity?

Mr. RICHARD. We hold all of our personnel to the highest standards. If they are involved in any type of theft at all, those issues are investigated, and actions are taken.

Mr. SCHROCK. Nobody ever told them they could run people off the road?

Mr. RICHARD. No, sir.

Mr. SCHROCK. With respect to Mr. Warren, was he himself ever accused of stealing from the convoys, and could you elaborate on that?

Mr. RICHARD. That has not been proven, no, sir.

Mr. SCHROCK. Why were Mr. Wilson and Mr. Warren terminated?

Mr. RICHARD. For violating code of business conduct and running Iraqi civilians off the road.

Mr. SCHROCK. Tom, do you want to come back?

Chairman TOM DAVIS [presiding]. We still have 15 minutes on our side, and in 5 minutes I am going to recess for a few minutes as we vote on a subpoena, and then we will come back.

Any questions here, Mr. Platts?

Mr. PLATTS. Thank you, Mr. Chairman.

Mr. Cox, you talked about the field contracts in Kuwait versus Turkey, and the process of that decision of having the two sources, and what went into the time-sensitive nature, especially the beginning of getting the fuel in place?

Mr. COX. Well, the situation on the ground in Baghdad in late April rolling into the early May was characterized—can be charac-

terized by long lines at gas stations, fuel stations there due to the lack of the gasoline. The Iraqi refinery and gasoline production was simply not back up to speed, and so there was no gasoline being produced in country at that time.

So the situation was very, very urgent that we start providing and importing gasoline, particularly that product, immediately, and that is how it was put to us. We need this immediately. Can you start hauling tomorrow?

We took a few days to get it going, and we are under the whip the whole time to start making it happen. We took that mission. We contacted vendors in Kuwait, which is where our offices were at the time, and began the process of soliciting that gasoline and the transportation to take it forward.

Kuwait is a very small country, essentially a large city, and there were very few trucks there and assets to haul the gasoline. The Kuwaiti Government agreed to sell the fuel to us, or to the U.S. Government, and so we ended up with very quickly in a couple of days getting three vendors who quoted.

We took the lowest vendor. We took the lowest vendor. We did an examination. We had worked with this guy before on some other things—not transportation and not fuel—and determined that he had the wherewithal to buildup and start this mission coming out of Kuwait pretty rapidly.

We also were required—we required—when I say we, the Army—sent a letter to the Kuwait petroleum company validating that this guy was an official. We were buying this for the U.S. Government basically. The Kuwaiti Government wanted that, so it wasn't KBR and Altanmia doing this. So very rapidly we put that in place and started moving the fuel.

Almost immediately, the discussions in the staff meetings with our client were, you know, this may not be the only avenue of approach. We are coming into Baghdad from the south, and there are some download points south of Baghdad that we need to service. But there are also some north of Baghdad, and it seemed with the unrest in Baghdad that it was not wise to try to haul through Baghdad to the north.

At the same time, we, KBR, had a small office in Turkey had been put in place to support the flow of troops through Turkey. That didn't occur, and they were getting ready to fold their tents and go home. And we got in contact with them and asked if they could procure and ship fuel to Turkey. As you heard in my oral, by May 11th they were doing so, and so they put contracts in place there, and so they were coming at it from two directions.

Mr. PLATTS. Was it a similar process in—as far as soliciting different competitors?

Mr. COX. Absolutely. It was competitively done there also. A little bit different market conditions there. In Kuwait, of course, you have one source to purchase the fuel from. Turkey is larger, more sources, more competition, more trucks, quite frankly, than in Kuwait.

Chairman TOM DAVIS. I thank the gentleman. We will suspend for now.

We still have 11 minutes left on our side. What I would like to do is yield back the balance of my time, but maybe reserve a couple

minutes for clarification at the end if we need to say something. But they will get their 30 minutes to say something.

I am going to suspend now, recess, and go back to the business meeting for the vote on Mr. Waxman's amendment. The hearing will be in recess.

The committee will now consider the postponed motion offered by the ranking minority member. The motion has already been entered. The gentleman's motion would authorize the chairman to issue a subpoena for documents relating to communications between the DOD and the Vice President's Office regarding Halliburton contracts. The question occurs on the motion. All those in favor, signify by saying aye. Aye.

Opposed, no. All opposed say no. No one said no. Come on, no. No.

Chairman TOM DAVIS. The ruling. The chairman knows how to ask for roll call. A little off script there.

Mr. WAXMAN. Mr. Chairman.

Chairman TOM DAVIS. Yes. You have a roll call.

Mr. WAXMAN. Mr. Chairman, if I might ask a unanimous consent on this. Some Members thought we would complete the hearing before they come in. Some were told that they should be here at 2. I would like to request that we keep the roll, that Members can come and let your staff know how they wish to vote, and then we will tally the vote.

Chairman TOM DAVIS. With unanimous consent, during the hearing I may suspend for a moment during Q&A as a Member comes in to let them record their vote as they come in and let them go, I think keeping it open for the next hour or so. Is that amenable?

Mr. WAXMAN. At least until the hearing is over.

Chairman TOM DAVIS. Which should take about hour. Thank you very much.

The clerk will call the roll.

The CLERK. Mr. Davis.

Chairman DAVIS OF VIRGINIA. No.

The CLERK. Mr. Davis votes no.

Mr. Shays.

[No response.]

The CLERK. Mr. Burton.

[No response.]

The CLERK. Ms. Ros-Lehtinen.

[No response.]

The CLERK. Mr. McHugh.

Mr. MCHUGH. No.

The CLERK. Mr. McHugh votes no.

Mr. Mica.

[No response.]

The CLERK. Mr. Souder.

Mr. SOUDER. No.

The CLERK. Mr. Souder votes no.

Mr. LaTourette.

Mr. LATOURETTE. No.

The CLERK. Mr. LaTourette votes no.

Mr. Ose.

[No response.]

The CLERK. Mr. Lewis.
Mr. LEWIS. No.
The CLERK. Mr. Lewis votes no.
Mrs. Davis.
[No response.]
The CLERK. Mr. Platts.
Mr. PLATTS. No.
The CLERK. Mr. Platts votes no.
Mr. Cannon.
[No response.]
The CLERK. Mr. Putnam.
[No response.]
The CLERK. Mr. Schrock.
[No response.]
The CLERK. Mr. Duncan.
[No response.]
The CLERK. Mr. Deal.
[No response.]
The CLERK. Mrs. Miller.
Mrs. MILLER. No.
The CLERK. Mrs. Miller votes no.
Mr. Murphy.
[No response.]
The CLERK. Mr. Turner.
Mr. TURNER. No.
The CLERK. Mr. Turner votes no.
Mr. Carter.
[No response.]
The CLERK. Mrs. Blackburn.
[No response.]
The CLERK. Mr. Tiberi.
[No response.]
The CLERK. Ms. Harris.
[No response.]
The CLERK. Mr. Waxman.
Mr. WAXMAN. Aye.
The CLERK. Mr. Waxman votes aye.
Mr. Lantos.
[No response.]
The CLERK. Mr. Owens.
[No response.]
The CLERK. Mr. Towns.
[No response.]
The CLERK. Mr. Kanjorski.
Mr. KANJORSKI. Aye.
The CLERK. Mr. Kanjorski votes aye.
Mr. Sanders.
[No response.]
The CLERK. Mrs. Maloney.
[No response.]
The CLERK. Mr. Cummings.
[No response.]
The CLERK. Mr. Kucinich.
[No response.]

The CLERK. Mr. Davis.
[No response.]
The CLERK. Mr. Tierney.
Mr. TIERNEY. Yes.
The CLERK. Mr. Tierney votes aye.
Mr. Clay.
[No response.]
The CLERK. Ms. Watson.
Ms. WATSON. Aye.
The CLERK. Ms. Watson votes aye.
Mr. Lynch.
[No response.]
The CLERK. Mr. Van Hollen.
[No response.]
The CLERK. Ms. Sanchez.
[No response.]
The CLERK. Mr. Ruppersberger.
Mr. RUPPERSBERGER. Yes.
The CLERK. Mr. Ruppersberger votes aye.
Ms. Norton.
[No response.]
The CLERK. Mr. Cooper.
[No response.]
The CLERK. Ms. McCollum.
Ms. MCCOLLUM. Aye.
The CLERK. Ms. McCollum votes aye.

Chairman TOM DAVIS. No other voters at this point. I would ask the clerk to stay close, and we will resume our hearing.

Gentlemen, you can come on back, and we will resume the hearing.

Members who are recorded will stay recorded. We don't anticipate followup votes.

Do you have other questions or not?

I am going to recognize Mr. Souder for—if we can get Mr. Souder back in the room. Here is Mr. Souder.

Mr. Souder, you are recognized.

Mr. SOUDER. Thank you, Mr. Chairman.

I wanted to reinforce, I thought, the question on the oil. I had the same reaction listening to the testimony, that I hope the corrections get in the record as much as the inflated charges get in the record. In fact, had we had just one source, it could have been a disaster, and that is the whole challenge that you face in these types of contracts between cost and urgency, because an error would be so catastrophic to delivery of services that sometimes cost is not the primary variable, and I hope that the American people can understand this.

Second, I had a particular question. We heard about these truck convoys and empty trucks, and my understanding from your testimony and from what we understood previous is that the military makes those decisions. But do you know why there would have been convoys and empty trucks?

Mr. RICHARD. Yes. When the military plans a mission, they plan a mission to pick up supplies, say, from point B. But in the case of the Iraq-Kuwait theater, they plan a mission from Kuwait to

Camp Anaconda to pick up supplies. So, therefore, they move empty flatbeds to Kuwait to Camp Anaconda to pick up supplies. But everyone has to remember, we are operating in a war zone.

Chairman TOM DAVIS. Would you suspend for just a minute? Ms. Norton, you are not recorded. Would you like to vote aye?

Ms. NORTON. I would like to vote aye.

Chairman TOM DAVIS. Thank you, sir. Go ahead.

Mr. Tiberi.

Mr. TIBERI. No.

Chairman TOM DAVIS. Mr. Tiberi is no. Thank you.

This is very informal, but we are trying to—I don't think we have done this before, but it is the most efficient way in an inefficient process.

Go ahead.

Mr. RICHARD. I was on a roll there. But on a 3 or 4-day trip, things change. We are operating in a war zone.

Chairman TOM DAVIS. Mr. Clay, the gentleman, you are not recorded. You would like to be recorded——

Mr. CLAY. Aye.

Chairman TOM DAVIS. Thank you. We will try to let people finish their sentence.

Mr. RICHARD. Thank you. I was on a real roll there.

Chairman DAVIS. One more time, Mrs. Maloney.

Mrs. MALONEY. Aye.

Chairman TOM DAVIS. Ms. Sanchez.

Ms. SANCHEZ. Aye.

Chairman TOM DAVIS. We will get you back on that roll. You are doing well?

Mr. RICHARD. We are operating in a war zone, so on a 3 to 4-day transit to Camp Anaconda, things change. The military may need the supplies that we were scheduled to pick up. If they need the supplies, therefore we have to return that empty equipment back to Kuwait.

Mr. SOUDER. Thank you, Mr. Chairman.

I just have one other comment. I thought in Mr. Neffgen's testimony KBR provided to Somalia and Haiti and the Balkans as well and done services in other areas, because sometimes reading news media accounts and listening to news media, the only way you get an impression of an account is if Vice President Cheney called up the company. If I recall, he wasn't Vice President during those 8 years where you received many contracts. Is that correct, that you had many government contracts under both Presidents, and it doesn't always take a call for your company to get a contract?

Mr. NEFFGEN. That's correct, sir. We have dozens and dozens of government contracts. We have been a government contractor for 60 years starting in World War II and Korean War, Vietnam War, and up to the current day. We have won contracts with both Democratic and Republican administrations. I have never been aware of an elected official that awards a government contract. It is always government contracting officers that do so.

Mr. SOUDER. Thank you.

Chairman TOM DAVIS. If you read the Means of Ascent and you read the Lyndon Johnson trilogy, Brown & Root were the largest

funders of President Johnson back when it was a Texas firm. They have been around for years.

We have a number of Members who have not been recorded. I will start on my right. Mr. Towns.

Mr. TOWNS. Aye.

Chairman TOM DAVIS. Mr. Towns votes aye.

Mr. Cooper.

Mr. COOPER. Aye.

Chairman TOM DAVIS. Mrs. Davis.

Mr. Lantos.

Mr. Deal.

Mr. DEAL. No.

Chairman TOM DAVIS. Mr. Mica.

Is there anyone else? Oh, yes, the gentleman from Maryland.

Mr. Cummings votes aye.

Thank you. At this point, I would like to reserve a minute or so. I am ready to go to Mr. Waxman in your half hour.

Mr. WALTER. Mr. Davis, if I could interject one thing?

Chairman TOM DAVIS. Please.

Mr. WALTER. During my testimony on the laundry, I mentioned 45 KD. What I meant to say was 0.45 KD, which is about $1.50.

Chairman TOM DAVIS. Before we start our yield and Mr. Waxman's time—keep our time running—we talked about a laundry contract, which is a firm fixed price, and after it looked like the government had made a number of assumptions that were not true, you were gouging him in terms of the results. You came back on your own and renegotiated, is that right? You were not forced to renegotiate that point. You were locked into a contract?

Mr. WALTER. Sir, we did it because it made sense to provide the best values to the taxpayer.

Chairman TOM DAVIS. Contractually the government was really up for more money had you enforced it.

Mr. WALTER. Had we not changed it, but, yes, we would have changed it.

Chairman TOM DAVIS. One of the most prominent charges of KBR in the May 13th DCAA report rates the Iraqi-Halliburton contract. DCAA indicates you are not billing on the proper standards, but instead billing the government for a number of meals far in excess of that amount. Could you give us the company's position on that?

Before you answer, I want to record Mr. Cannon. You get to vote. OK. Mr. Cannon votes no.

Go ahead. Thank you. Go ahead. Go ahead.

Mr. WALTER. Once again, I appreciate the opportunity to clarify this. We have read quite a bit in the media. What has happened in this case, as we provide the dining facilities services to the government, we get a statement of work that identifies how many troops need to be served, and that's what we prepare for.

Chairman TOM DAVIS. Thank you very much.

We have a couple of other Members. Ms. Ros-Lehtinen.

Ms. ROS-LEHTINEN. No.

Chairman TOM DAVIS. Ms. Harris.

Ms. HARRIS. No.

Chairman TOM DAVIS. Thank you.

Mr. Waxman, you are recognized for half an hour.

Mr. WAXMAN. Thank you, Mr. Chairman.

Mr. Neffgen, Mr. Walter, Mr. Cox and Mr. Richard, I want to thank all of you for being here today. I think it is important for us to have a chance to hear your perspective and to have an opportunity to ask questions. Given the size of your contracts, the two biggest contracts in Iraq, there's really no way we can do our oversight without hearing directly from you.

When the public hears about Halliburton and Iraq, there are two major questions on people's minds. The first question is was there special treatment when the administration gave Halliburton a sole-source, no-bid contract worth up to $7 billion for oil infrastructure work in Iraq? And the second is has Halliburton been engaged in profiteering; has the company taken advantage of the war to overcharge the U.S. taxpayers?

These are the two issues I want to focus on in my questioning of you. I want to start with the special treatment issue. For over a year we heard that there was no special treatment because a decision to choose Halliburton was made by career procurement officials. On August 28, 2003, for example, your spokeswoman, Wendy Hall, said Halliburton's work in Iraq was awarded "not by politicians, but by government civil servants under strict guidelines." I have a chart over here with her actual quote.

We learned recently at our last hearing this wasn't true. We discovered that the decision to choose Halliburton and the decision not to allow other companies even to submit a bid was made by a political appointee. The decision was made by Michael Mobbs, who works for Douglas Feith, the Under Secretary of Defense for Policy. And we learned that there was a deputies committee, which is made up of a senior White House and departmental officials, that signed off on that decision.

Does your company still maintain that career civil servants made the decision to choose Halliburton for this work?

Mr. COX. Congressman, I will be happy to field that. We have no knowledge whatsoever of how the decision was made, other than what has been published, which is the sole source justification document, which we have seen. We do not know who made the decision specifically. We received our marching orders from the procuring, contracting officer. I am not aware of any political appointee deciding who got the contract.

Mr. WAXMAN. You don't know?

Mr. COX. We do not have insight to that.

Mr. WAXMAN. You don't know the facts?

Mr. COX. No, sir. We do not.

Mr. WAXMAN. Is that true of all you?

Mr. NEFFGEN. That's true.

Mr. COX. Yes, sir.

Mr. WAXMAN. You need to speak.

Mr. RICHARD. Yes.

Chairman TOM DAVIS. May be true of all four of your, but your spokesperson made a statement that was quite uneqivocal.

Mr. Waxman, would you suspend for one moment?

Pardon me. Would you like to vote?

Mr. SANDERS. Yes, I would.

Chairman TOM DAVIS. How do you vote?

Mr. SANDERS. Mr. Waxman, what do you suggest?

I vote yes.

Chairman TOM DAVIS. The gentleman is recorded. Thank you.

Go ahead.

Mr. WAXMAN. We have a statement from your spokesperson and the four of you, are unable to give any further information about that. Mr. Mobbs said he gave Halliburton the task order to plan for the takeover of Iraq's oil fields. And he knew at the time that Halliburton would therefore get the sole-source contract to put out the oil fires and restore the oil fields. So he was obviously in a position to know. You are not. Your representative spokesperson said something to the contrary.

One of the justifications we have heard for awarding these contracts to Halliburton without any competition is that Halliburton was the best-qualified company to do the work. So let me ask about Halliburton's experience and qualifications.

Chairman TOM DAVIS. Will the gentleman suspend?

Mrs. Davis, would you like to be recorded?

Mrs. JO ANN DAVIS OF VIRGINIA. No.

Chairman TOM DAVIS. Thank you.

Mr. WAXMAN. Mr. Chairman, may I suggest that the Members record their votes without interruption? They could be on the record.

Chairman TOM DAVIS. I would like to have the Members record their votes without interruption. But what I would like them to do is get the assent that both you and I hear or see them, a Member from each party as opposed to just registering with the clerk or making signals or something, without objection.

Mr. WAXMAN. That's fine.

The major rationale that Halliburton gave for why Halliburton was the best qualified is that you had put out oil well fires after the first Gulf war.

On March 24, 2003, you issued a press release announcing the award of the Iraqi oil contract. That press release said the following: "In 1991, Halliburton crews brought 320 wells in Kuwait under control. More than 190,000 work hours were incurred. Halliburton's crew extinguished 90 percent of the blowouts within 1 year."

This press release stated that Halliburton crews put out more than half of the 650 oil well fires in Kuwait. Obviously such experience would be extremely relevant. But my staff has investigated these claims, and they don't appear to be true. The company that had the contract to put out the oil well fires after the first Gulf war was not Halliburton, it was Bechtel. And by all accounts Bechtel's performance was excellent. Yet Bechtel was not even allowed to bid on the contract to put out the oil well fires this time.

And I have an article here about Terry Farley, who was the individual who led the effort to put out oil well fires after the first Gulf war, and according to Mr. Farley, Halliburton "put out no fires. Zero." Now, how do you gentlemen respond? Who was the prime contractor in charge of putting out the oil well fires after the first Gulf war, Halliburton or Bechtel?

Mr. NEFFGEN. I don't have the specific information on 1991 on who put out the oil fire. What I can tell you is the LOGCAP contract was competitively awarded to us in 2001. There was several other offers that submitted proposals in that solicitation, and when we were awarded the contract, nobody protested.

The original task order that we were issued under the LOGCAP contract for the planning, the advance planning for the potential oil fires if an invasion occurred was issued under the LOGCAP contract, and then it was the Army's decision to transfer that from the Army Materiel Command, who is our client for LOGCAP, to the U.S. Army Corps of Engineers.

Mr. WAXMAN. I understand all of that. We will get to some of the questions about that, but do any of you have any information about who actually put out the fires after the first Gulf war?

I think it is fair to say that none of you have further information to give us.

Well, my understanding is that after the first Gulf war, Bechtel deployed 1,000 engineering and construction professionals. The company oversaw a work force of 16,000 nationals from 35 countries. Bechtel brought in 200,000 tons of equipment, the largest airlift since World War II, and reportedly capped over 650 oil well fires.

In contrast, I have here an April 7, 2003, article in which your spokesman Ms. Hall said only 60 Halliburton employees were on the scene. That's quite a difference.

Here is the problem as I see it. Bechtel had the most relevant experience because it did most of the work after the first Gulf war. Yet this time Bechtel was not even allowed to submit a bid. Instead, the contracts were awarded to Halliburton without any competition. That's not the way our system is supposed to work.

The other rationale for giving Halliburton this contract was that the Pentagon could do it quickly as a task order under the existing LOGCAP contract that you are referring to, Mr. Neffgen. But this explanation is also suspect. It does not appear that Halliburton was uniquely positioned to work with DOD. Bechtel does a lot of work for the military. In fact, Bechtel historically has done at least as much military work as Halliburton, if not more. There should have been no question about Bechtel's ability to work for the military or to have the necessary clearances.

In fact, I understand that Bechtel also had an existing preawarded indefinite contract with the Pentagon. This contract is the cooperative threat reduction integrating contract. Under this contract there's not one preapproved company, but five. Bechtel is one. Halliburton is also preapproved under this contract. So if DOD had decided to use this contract as the vehicle for the task order, DOD could have gotten bids from both Halliburton and Bechtel. But DOD didn't use this vehicle. DOD used the LOGCAP contract, which excluded everyone but Halliburton. Is that correct, Mr. Neffgen?

Mr. NEFFGEN. Yes, for the planning task order.

Mr. WAXMAN. I recognize it might have been a stretch to use the cooperative threat reduction contract, but it would have been no more of a stretch than using the LOGCAP contract. As we learned at last month's hearing, both GAO and the procurement attorneys

responsible for LOGCAP determined that the Halliburton task order was outside of the scope of LOGCAP. There is a strong presumption again awarding contracts without competition.

That's the point I really want to emphasize. There's a strong presumption against it for the very simple reason is that competition protects the taxpayers. But in this case there was no competition, and there don't appear to be compelling reasons for failing to let other qualified companies like Bechtel compete. That's what we call the definition of special treatment.

Now, in fact, the award of this contract, is only one example of how the Bush administration sheltered Halliburton from competition. You were also sheltered during the implementation of the contract. Ten task orders were issued under the oil contract worth a total of $2.25 million, yet my understanding is that Halliburton did not have to compete for any of these task orders. There were five task orders given to import fuel from Kuwait and other countries into Iraq. These task orders were worth over $1 billion. Did Halliburton have to compete for any of these task orders, and did DOD ever put this out for bid and allow other companies the chance to show that they could bring in the gasoline for a lot less than Halliburton?

Chairman TOM DAVIS. Will the gentleman yield for just a moment?

Mr. WAXMAN. Well, I would like to see if we can get an answer to the question.

Mr. NEFFGEN. It was an Army decision to award us the sole-source contract, and we were pleased to see it and be in a position to respond quickly and appropriately. I believe the GAO has done an analysis on the—both the issuing of the task order for the planning under the LOGCAP, and it had some questions on that, but that was resolved by the DOD's General Counsel's Office that deemed it was appropriate use of LOGCAP to give us that planning task order.

And also the GAO has reviewed the decision to give us the sole-source award for the RIO and ruled that appropriate.

Mr. WAXMAN. These other task orders.

Mr. NEFFGEN. Once you have a contract, then the client issues task orders for work that they think is important to be executed under it. And typically task orders within a contract are never competed.

Mr. WAXMAN. Thank you.

Chairman TOM DAVIS. My only question was, I think, in a sense, they are the wrong people to ask. We had the military and everyone here last week. We can always review that. But they are the wrong people to ask on this because they weren't in the decision mode in terms of how these vehicles and which one to choose.

Mr. WAXMAN. It shouldn't be a surprise. We have questions about how the contract was awarded to Halliburton. This has been in the news for some period of time. We have raised it over and over again. Finally, we have representatives from Halliburton here. I would have hoped that we would have had people who could answer these questions.

But this highlights what is fundamentally wrong with the administration's contracting approach. There was no competition at

the front end when the political appointees gave Halliburton the work. There was no competition at the back end when billions of dollars' worth of task orders were issued.

I now want to examine the other major question: Have there been overcharges? Let me first ask about the hotels in Kuwait where Halliburton employees have been staying for more than a year. According to Marie deYoung, who testified earlier today, the U.S. taxpayers paid Halliburton $10,000 a day to house Halliburton employees at a five-star hotel in Kuwait, but in the op ed in the Wall Street Journal, David Lesar, the CEO of Halliburton, denied this. I want to put up his quotation. He said, "Our Halliburton employees live in the same conditions as the troops."

I would also like to show you some pictures that we have of the hotels where Halliburton employees have been staying. These are pictures of the five-star Hilton Hotel in Kuwait and the five-star Kempinski Hotel, also in Kuwait. I see one of them, and I will assume that is also one of them.

Do our troops stay at five-star hotels with maid service and complementary fruit baskets like this?

Mr. NEFFGEN. There are other government agencies staying in these hotels.

Mr. WAXMAN. But the quote was "our Halliburton employees live in the same conditions as the troops." Do you know of any of the troops that got to stay at these kinds of hotels?

Mr. WALTER. We would like to make sure that it is understood that 87 percent of our 14,000 employees that are there are staying in conditions with the troops, on the sites with the troops. We tried to get onto these bases. We continue to this day to try to get onto these locations. There is not space to do so.

So as we have to do that, we have to try to find locations where we can stay in a secure location, and a hotel is the host that will have the most availability of rooms in a location that is securable. So that is why these locations have been selected. But we are trying our best to get out of them.

Mr. WAXMAN. You answered a question earlier. You were asked to put in the camps in April of this year; is that correct?

Mr. NEFFGEN. Yes.

Mr. WAXMAN. That doesn't contradict about what Ms. deYoung had to say, because she was talking about a time preceding April of this year.

Mr. NEFFGEN. Last fall, a year ago, we also had discussions about building a 1,000-man camp of Conex containers at Camp Arifjan. We were not able to go through with that deal. The best we can get is a 5-year lease for property, and our task orders go 3 months to 6 months in duration. We cannot obligate government money beyond that period of time.

Mr. WAXMAN. Her testimony is that they wanted to put them in the tents.

Mr. NEFFGEN. Same thing. We have to get space designated available for use to put tents up. We were not given that space.

Mr. WAXMAN. I think it is important to recognize that Marie deYoung's allegations have been confirmed by independent auditors a few weeks after she made these allegations and they first surfaced. The inspector general for the CPA confirmed that Halli-

burton was billing the taxpayers to house people at the five-star Hilton Hotel in Kuwait. According to the IG, the taxpayers could have saved $3.6 million on an annual basis if these individuals had been moved to other quarters.

Mr. WALTER. I would like to address that audit report, sir. That audit report was not accusing Halliburton of overspending and waste. What that report was doing was focusing on the CPA itself. The CPA would present people to Halliburton. We were tasked by CPA to maintain a forward deployment center so that their—diplomats and others coming into theater could be processed, given their flak jackets and all of their equipment that they need and their training so they could be sent up to Iraq to their particular location.

The points made in the inspector general's report were that if the CPA were more diligent in how they would assign people and who should get what type of facility, then the taxpayer would be able to save money. That was not a criticism of Halliburton, sir.

Mr. WAXMAN. The CPA said it included contractor employees that were being put up there.

Mr. WALTER. Sir, since the FDC is located at the Hilton, we do have to put our employees there. We follow the direction of the CPA where our employees are. There are two types of facilities there. There are rooms that—one or two people to a room. Then there are what are called villas, larger facilities that can—I believe they have four to five bedrooms, and downstairs is used for office space. We will go wherever the CPA asks us to put our people.

Mr. WAXMAN. I appreciate your comments. I just put it in contrast to what your own representative said about employees living in the same conditions as the troops.

Mr. WALTER. Like I said, sir, 80 percent of our employees are living in the same conditions as the troops. And as we can get more people onto the sites, we will.

Mr. WAXMAN. Who were the elites that got to stay in the hotel?

Mr. WALTER. I don't agree that the term would be elites per se.

Mr. WAXMAN. Who got to stay in the hotel?

Mr. WALTER. The people who are currently at Camp Arifjan are the people who are working on Camp Arifjan. The people who are not able to stay at Arifjan or the support functions and other types of roles, they can either do the job on Arifjan or off Arifjan.

Mr. WAXMAN. Let me turn to fuel importation. You consistently said you delivered gasoline at the best value, the best price and the best terms. Yesterday Representative Dingel and I released a report comparing Halliburton's gasoline prices from Kuwait with those of the Pentagon's own fuel delivery unit, the Defense Energy Support Center.

Your average price of gas from Kuwait was $2.68 per gallon. On April 1st the Pentagon took this center away from you and gave it to the Energy Support Center. That job pays just $1.57 a gallon to import gasoline from Kuwait. As that chart over there illustrates, the military is now doing the identical job for $1 per gallon less. How can you say that your price was reasonable?

Mr. COX. I would like to address that, if I may, sir. First, it is interesting to note in the report that we released to say this is an apples-to-apples comparison. I submit to you that it is not. Quite

frankly, our costs are all in, after the job has been done, and, you know, the three components of our price are what they are.

The DESC costs that are presented in the report, I think, need to bear some scrutiny, and—but in a general sense, we are comparing what KBR did at one point in time, almost a year ago, a little over a year ago now, to what DESC was able to accomplish 9, 10 months later, given a 90-day ramp-up period. DESC came to theater in December, worked side by side with us from December until April 1st when they took over the mission.

Turning to the three components of the price, our understanding, and we understand—and I do not have insight as to their contracts or whatever, but I understand that they were paying for fuel a price, a certain amount of money. It is a fixed price with economic adjustment, meaning that they pay the spot price plus I think it is $0.16 per gallon is what they are paying. Today I am told that——

Mr. WAXMAN. But they were buying it from the same company you were buying from.

Mr. COX. They were buying from DESC.

Mr. WAXMAN. Did they get a better deal than you?

Mr. COX. No, sir, I don't think they did, and I will tell you why. We had a fixed price with a subcontractor. No matter what the spot market did, we had the price locked in. In December and January we know that the spot price—we know he was losing money providing fuel to us because of the fixed price he gave us. DESC's fixed price of $0.16 over the spot market. If you look at that today, that's—around July 16th, that was $1.04. The spot market plus 16 is $1.20. We only paid $1.14 per gallon. So right now my understanding is DESC is paying more per gallon as we did.

Mr. WAXMAN. As I understand it, yours was 32 cents over the spot price, and the DESC was 16 cents over the spot price. So the spot price can change, but if you have that——

Mr. COX. But in my case it doesn't matter what the spot price does. I had a fixed price of $1.14 a gallon. Today I would be paying $1.14 a gallon. They're paying $1.20.

So I think, sir, we need to look inside some of those numbers.

Mr. WAXMAN. Well, we need to haul them in here and find out why they are charging us less. We need a hearing on this.

But Halliburton's prices stayed extraordinarily high for month after month, and there was no major price drop until the DESC came in and took over. And then there was a price drop. They are using the same supplier, they are picking up the gasoline in Kuwait from the same supplier, they are transporting it to Iraq. It's the same service, yet they are able to do it at a lower price.

We consulted with independent experts, and they have a very different view than Halliburton. Phil Verleger, a California oil economist, said it's as if they put the gasoline on the Queen Mary and took it around the globe before they delivered it.

Jeffrey Jones, the former Director of the DESC, said, I can't construct a price that high. One oil expert from the region said simply, "it's highway robbery." Based on what we know now, that may not be a bad description.

You dispute that?

Mr. COX. Sir, I do dispute the overcharge allegations. If I may, I would also disagree with the statement we didn't achieve any cost savings over the course of our contract to deliver fuel. We reduced the cost of trucking by approximately 20 percent through renegotiation.

We were not able to renegotiate the fuel prices, but I think if you look—the biggest difference that has been identified is the cost of the transportation. The cost in the report, as issued for DESC, states that it's based on three round trips per month per truck. We only achieved about two round trips per truck, and I am told that is all DESC is achieving also. So maybe there is a premise or assumption of three round trips that needs to be reevaluated before we start comparing those.

I would also make the point on transportation that DESC is benefiting from the system that we put in place. Altanmia's startup costs were already paid for in our contract. They had a fleet already on the scene for DESC to utilize, and we built staging facilities under our contract that DESC is using.

So, in essence, it's not surprising to me that Altanmia is giving them a lower price than we got. I think you find that in many of our contracts, where when we first go on scene, the cost comes down from that because we build the facilities initially. Those are capitalized in 6 months or so.

Mr. WAXMAN. You might say it was a startup cost, but Halliburton's costs remained high for month after month. And the only time the price was dropped is when DESC took over.

Mr. COX. Sir, that's not factually correct. There was a change in the price of the transportation. The cost of the trucks went down in about the October timeframe.

Mr. WAXMAN. Let me ask you about another aspect of your prices: fees and overhead. For the gasoline from Kuwait, these totaled over $31 million, and I have a chart over there that shows this is 40 times greater than DESC's overhead costs. Why should the U.S. Government pay Halliburton $31 million when the Pentagon can do this work itself and get a better price?

Mr. COX. Well, first of all, the 24 cents per gallon, let me explain what is in that; 13 cents of that is an award fee that I have not earned yet, have not been awarded yet, haven't gotten yet. The remaining 11 cents is pretty reasonable per gallon. That covers our overhead management cost from top to bottom. Staff back here in Arlington, the staff in Houston that support us all comes from that cost.

And when I look at the DESC costs, sir, it seems very low to me, and I would want to ensure that they have included the cost of the DESC office back here in Washington that supports those DESC troops in the field, if you will. Having been involved in a couple of outsourcing decisions for the government, I know it is very difficult for the government to capture all its cost and do an apples-to-apples comparison. And I personally feel like we don't have that here yet.

Mr. WAXMAN. Well, the whole rationale for using private contractors is supposed to be to save the taxpayers money, but in Halliburton's case, the exact opposite seems to be happening. The taxpayers are paying millions more for something apparently this

government can do a lot cheaper, and that doesn't make sense to me.

I want to go into a different subject. The GAO also released a report yesterday on Halliburton's other major contract for work in Iraq: LOGCAP. As in the gasoline report, GAO found that when the military removed Halliburton from the equation, it saved money. Here is the example GAO gave.

Prior to the war, a Kuwaiti company called Tamimi was feeding our troops in Kuwait. Last year, DOD terminated that contract and gave the contract to Halliburton, but because Tamimi had been doing a good job, Halliburton was instructed to subcontract the feeding contract to Tamimi. So here, as in the case of the oil contracts, you were simply a middleman. All that has happened was that Halliburton went out to Tamimi, they continued to feed the troops, but Halliburton got to take its own cut of the expenses.

Finally, somebody in DOD decided to examine the situation, and earlier this year DOD eliminated Halliburton as the middleman. And here is what happened. Overnight the cost to the taxpayers were reduced by 43 percent at 6 dining facilities in Kuwait without a loss of service or quality. And according to GAO, the total savings to the taxpayers from getting rid of Halliburton was $31 million.

Halliburton had a chance to review GAO's report, but you didn't object to GAO's findings, did you?

Mr. WALTER. No, sir, and I'd appreciate the opportunity to discuss that point.

What we have here is, once again, an apples-to-oranges comparison. Tamimi was not at these facilities at the time. It was a new task order at a new location, and the government asked us, in fact directed us, to use Tamimi to do the dining facility services.

As we did that, we required Tamimi to get all of its up-front costs, to hire all the personnel, to get the kitchens and generators and everything they needed to put into place to run that dining facility. At the end of the year, we would then renegotiate a lower price with Tamimi, because they would have their mobilization costs and all the rest of these costs taken care of.

Now, what happened is as this contract was winding down, the government did go back to Tamimi, and the government directed us not to continue negotiating with any of our other vendors. We had already opened up a competition for the Kuwait dining facilities. And our Iraq dining facilities, after the initial 6-month term for those, we were able to negotiate significant savings after the contractors had their initial let's get everything in place, let's get the dining facilities up, let's serve the troops in the wartime environment. We have RPG rounds. We have pictures of all sorts of things that are happening that are causing a lot of mayhem and confusion in this area.

But once it's in place, once the people know what's happening, they have a little bit better idea of what the scope is going to be, we are identifying those significant cost savings, and we are passing them directly back to the taxpayer.

Mr. WAXMAN. And one of the cost savings was to eliminate you as a middleman and go to them directly.

Mr. WALTER. Well, sir, in the cases of the dining facilities that we've been able to cut out, we've been able to cut out prices that

exceed 45 percent. So I think we would be able to identify even more savings to the government, possibly.

Mr. WAXMAN. I appreciate that.

I want to clarify a matter. In the previous panel I said that I was concerned the majority was working with Halliburton in preparing for this hearing, and that the majority was receiving information that was not being shared with the minority. In response, Chairman Davis said that all the information the majority had received was in the written testimony.

In fact, that doesn't appear to be true. In Representative Blackburn's questioning, she asked about conversations between Ms. deYoung and her managers at Halliburton. We asked Ms. deYoung about this after she testified, and she said these were conversations with Tom Quigley.

This was not in any of your written testimony, and it wasn't shared with the Democrats. So my question is: Did any of you or anyone at Halliburton share information with the Republicans that wasn't shared with the Democrats?

Mr. NEFFGREN. Congressman, we've been working with your staff as well as the majority staff for months and sharing information, telling the story, telling the facts, and everything else. I have no direct knowledge of any communication between Tom Quigley, who is actually in Kuwait——

Mr. WAXMAN. No, no, my question is not about that. You talked to our staff, and you talked to their staff. But my question is: Did you share some information with their staff that you didn't share with us?

Mr. NEFFGREN. Did not.

Mr. WAXMAN. You did not. So she did some terrific research in finding out about things that weren't within your written statements.

Mr. NEFFGREN. Did not share anything with her; correct.

Mr. WAXMAN. Did anybody from Halliburton?

Mr. WALTER. I did not, sir.

Mr. COX. No, sir, I did not.

Mr. RICHARD. No, sir, I did not.

Mr. WAXMAN. So none of you individually did. Do you know whether anybody in your company has?

Mr. NEFFGREN. I'm unaware of anybody else in my company doing that.

Chairman TOM DAVIS. The gentleman's time has expired, but let me try to explain it.

To my knowledge, and I have staff who I just rechecked with, and I know that our staff put together a briefing memorandum for our Members that we didn't put together for yours based on documents available to both parties, just as you do the same for yours. But I'm not aware of any ex parte communication.

We tried to work this with you, and there were a lot of documents that we got back and forth that we drew certain conclusions that I don't think were shared with you. But the documents were available to you as well. We just put them up as talking points for other side, as I'm sure you do for yours.

I think that clarifies it.

Mr. WAXMAN. I appreciate that clarification.

Chairman TOM DAVIS. I have yielded back. I would just make one comment.

Mr. WAXMAN. We never got those documents.

Chairman TOM DAVIS. I think you did get the documents.

Mr. WAXMAN. My staff is telling me that, for the record, we never got documents that would have been the basis for that question. We will review it again. It could be just a misunderstanding.

Chairman TOM DAVIS. We will go over it with staff.

We have had two hearings with DOD witnesses to explore the rationale for awarding the planning task order and RIO contracts to Halliburton. We marched everyone up here, and the government, I think, made their case at the time. And after a certain amount of time, where they felt they were able to, they went out in a competitive way.

In wartime you don't always have that luxury. So I think we have already explored those issues with appropriate witnesses.

It is interesting that we mentioned Bechtel should have been permitted to compete. Bechtel didn't complain. They didn't protest. In fact, Bechtel also has multibillion-dollar contracts with Iraq through USAID.

Also, the incident that the ranking member mentioned concerning Altanmia and GAO was not in the final report. It was in a draft report. And as so often happens in these issues, GAO might have changed their mind when the facts are learned. Often with these reports you go back and forth with people you are investigating, and that is the difficulty when you move forward with tentative reports. But it was an issue that was raised, and I think an appropriate question he raised to you.

I don't have any other questions at this point for the gentlemen here, except that we will continue to exercise vigorous oversight of every contractor. That's our job up here. But from my perspective, we appreciate the job you are doing, your company is doing, and the people in the field. You have lost a number of employees over there, had others injured, and people there in harm's way as well. From our perspective, we appreciate the job that they are doing.

Mr. NEFFGREN. Thank you.

Chairman TOM DAVIS. Mr. Waxman, any other questions?

I guess we have the 5-minute rule, so we can go down the road and let your Members have a shot.

Mr. Ruppersberger.

Mr. RUPPERSBERGER. Thank you, Chairman Davis.

First thing I want to say is that your role is to help manage Halliburton. I think each one of you are doing the best that you can. We know it's difficult. But you have a sole-source contract because you are considered one of the best, and we can expect no less from you.

Our job is to investigate issues and allegations that are relevant to the subject matter, that being were there overcharges; was there a possibility of bad management. So we need to follow the facts. I know you are in a defensive mode because certain allegations are made, and that is why we are here, and then we have to determine that.

So in that regard, first, Mr. Neffgren, for several months we have been trying to get information about Halliburton employees you

identified as taking up to $6.3 million in kickbacks from a Kuwaiti subcontractor. Representative Lynch in particular has asked questions about this on two previous committee hearings. We have not yet received any information about this.

I know in your invitation letter to come here today to testify that the chairman directed you to address this issue. Will you please let us know who the employees were involved in the $6.3 million kickback?

Mr. NEFFGREN. I am sorry, sir. There is an ongoing investigation with the Department of Justice and the DOD IG. I am not permitted to provide that information.

Mr. RUPPERSBERGER. I know there is an ongoing criminal investigation, and we have an investigation going on, too. These are issues where we are asking for the two employees so that we can determine from our investigative point of view. Have you been ordered not to disclose any of that information by the Justice Department?

Mr. NEFFGREN. I have been advised by counsel not to mention the people.

Mr. WALTER. I will answer that, sir, though. We have provided all the files, all of the procurement files, to the Department of Justice so that they can complete their review. We are working, our legal department is working very closely with the Department of Justice on that.

Mr. RUPPERSBERGER. So you're saying that we don't have the information we have asked for, but you have given that to the Justice Department. Not arguing with you, just asking as a fact.

Mr. WALTER. I believe that is true.

Mr. NEFFGREN. Yes, that's correct.

Mr. RUPPERSBERGER. Let me ask you this: Have you made any comments to the media, or anybody from Halliburton, involving these two employees?

Mr. NEFFGREN. Personally, no.

Mr. RUPPERSBERGER. You are not aware of anybody at Halliburton having comments with the media about this incident and these two employees for the subcontractor?

Mr. WALTER. When this was initially mentioned, there was a press release, and there is a notification in our financial statements that identify that there is an issue. But I believe that is as far as it goes.

Mr. RUPPERSBERGER. Were these two employees managers?

Mr. NEFFGREN. No, they weren't.

Mr. RUPPERSBERGER. They were not managers? Do you know what their positions were?

Mr. NEFFGREN. Administrative people.

Mr. RUPPERSBERGER. They must have been in some kind of management capability or they wouldn't be involved with $6.3 million.

Mr. NEFFGREN. Let me clarify. Senior subcontract administrators.

Mr. RUPPERSBERGER. How many of those did you have in Iraq at that time?

Mr. NEFFGREN. We have about 300, 350 right now.

Mr. RUPPERSBERGER. What is the name of the subcontractor that paid the bribes?

Mr. WALTER. Sir, there is no statement that they have paid bribes. That is under investigation. It is an allegation of a kickback.

Mr. RUPPERSBERGER. Then I take that back.

What is the name of the country where there was alleged bribes to have been paid?

Mr. NEFFGREN. Kuwait.

Mr. RUPPERSBERGER. In Kuwait. But what's the name of the company, the subcontractor?

Mr. NEFFGREN. I've been advised by counsel that I can't disclose that.

Mr. RUPPERSBERGER. Have you had other contracts with this Kuwaiti company over and beyond what this incident was dealing with, with respect to the two contractors, the $6.3 million kickbacks?

Mr. NEFFGREN. We have provided information to the Justice Department on this specific incident, and then all of the documentation pertaining to the subcontractor and to the employees that potentially received the kickback.

Mr. RUPPERSBERGER. You did pay back money to DOD; did you not?

Mr. NEFFGREN. Yes, sir.

Mr. RUPPERSBERGER. Now, as a result of that, at this committee's hearing on March 11, Dov Zakheim, the Pentagon's comptroller, reported that KBR has paid the government $6.3 million for the estimated impact of the kickbacks. He then said, the DCAA, Defense Contract Auditing Agency, has requested supporting data from KBR to validate that sum.

At our June 15th hearing, Halliburton had still not provided the information DCAA requested. And, according to the testimony of William Reed, the Director of DCAA Halliburton, Halliburton failed to provide data necessary for DCAA to verify the accuracy of that amount.

I would like to know whether or not you or anybody else at Halliburton is under any legal requirement to withhold this information from us.

Mr. NEFFGREN. I'd be glad to answer that question. When we provided the $6.3 million refund to the government, that was the full value for the task order that was subcontracted. It was a 100 percent reimbursement for the prior billings under that task order. So, in effect, the government has not paid for the services received by them. Therefore, at the time of the request in March, there was nothing for DCAA to audit because the government had not paid for anything.

We have had subsequent communications with DCAA.

Mr. RUPPERSBERGER. OK. My 5 minutes are up.

Mr. WALTER. But we have provided information to DCAA and we continue to provide it in accordance with what our legal counsel advises.

Chairman TOM DAVIS. Let the Chair just say that under the voluntary disclosure policies, when we encourage companies to come forward if they think there has been an act of fraud committed, if congressional committees then go in there and start reaching out, nobody is going to disclose anything. There has to be confidentiality

to encourage companies when they find something wrong to come forward with it. That is why we have not pursued this after discussions with Justice. We are satisfied that these are being investigated by investigators who have teeth to make the appropriate enforcement mechanisms. At least that is my position as chairman of the committee.

Ms. Watson. We do have one more panel, so I would just caution Members, but I don't want to deprive anybody of taking their time. Ms. Watson.

Ms. WATSON. Thank you, Mr. Chairman, for your consideration, and I want to thank the witnesses for being here.

I want to turn to trucks, because earlier, in the first panel, we heard testimony, and I would like to reiterate some of that testimony.

It says that KBR brought its new trucks, usually Mercedes or Volvos, with virtually no mileage on the odometers. And they said that in a convoy, one of the trucks got a flat. "since we didn't have any spares, we had to leave the truck on the side of the road."

Who's responsible to perform the maintenance on the trucks; is it the military, or is it Halliburton? And why would Halliburton remove the spare tires?

Mr. RICHARD. Ma'am, thank you for allowing me to clarify that issue. It is KBR's responsibility to provide maintenance for all of our assets, and all of our convoys have spare tires. I do want to clarify that issue. All of our convoys have spare tires available.

When a convoy is out on MSR, it is the military's responsibility to provide protection for that convoy. But no truck has been abandoned, no truck has been lost due to a spare tire.

Ms. WATSON. Let me ask you this: Are you saying that the gentleman who testified in front of the committee before your panel was not telling the truth?

Mr. RICHARD. Ma'am, what I'm saying is that gentleman did not testify that a truck was lost or abandoned.

Ms. WATSON. Let me phrase my question clearly. The testimony was that there were no spare tires available. The spare tires were taken. "And since we didn't have any spares, we had to leave the truck on the side of the road."

I didn't say, and he did not say, the truck was destroyed. Why were there no spare tires if these were new vehicles, Mercedes and Volvos?

Mr. RICHARD. I want to clarify two points, ma'am. All convoys had spare tires. His truck may not have had a spare tire, and I will clarify that point, but all convoys have spare tires. A convoy consists of 25 trucks.

The issue of spare tires. We are in and amongst several hundred other trucks while we are in a staging area in Iraq. We only represent 20 to 30 percent of the total convoy movement in Iraq. There are several other contractors direct-hired by the military to support the effort. Many of those drivers are foreign nationals. Many of those drivers are from other countries. They don't have the same type of equipment KBR has. They are not as well equipped as our trucks. So, therefore, at times, they do take equipment from our trucks.

And I would like to reiterate for my testimony that it is the Army's responsibility to provide security for our equipment. But sometimes those tires are taken from our trucks. But we do replace those tires, and all convoys have spare tires.

Ms. WATSON. Is this not a true statement? This is a gentleman who has been driving for 13 years, and he stated in front of the committee that "KBR removed the spare tires from the trucks on my convoys. I don't know why they did this, but on one convoy, one of the trucks got a flat tire. Since we did not have a spare, we had to leave the truck on the side of the road." Is that not a true statement?

Mr. RICHARD. That truck may not have had a spare, but the convoy, other trucks in the convoy, could have a spare tire. All convoys have spare tires, ma'am.

Ms. WATSON. It said "but one convoy," they didn't have a spare tire. Well, then, if they did, then why would they leave the truck on the side of the road?

Mr. RICHARD. That's a military decision, ma'am, based on the level of hostility.

Ms. WATSON. Oh, OK. It was the military that made that decision?

Mr. RICHARD. It's the military's decision to abandon a truck, yes, ma'am.

Ms. WATSON. Also, Mr. Wilson and Mr. Warren that used to work for Halliburton testified on the first panel that they lost an $85,000 truck because they didn't have a spare tire. Then we heard later that they were told to destroy the trucks so that the enemy could not get them, strip them, and use them.

Mr. RICHARD. The Army makes a decision to destroy a truck based on the level of hostility and the insurgents that are in that particular area. Again, the Army has command and control of the convoy. It is their responsibility to provide protection for our employees and for the trucks.

We have lost 14 civilians, ma'am, and it is their responsibility to provide that protection.

Ms. WATSON. I didn't ask about protection. I'm asking about the maintenance.

Mr. RICHARD. Yes, ma'am.

Chairman TOM DAVIS. The gentlewoman's time has expired.

I am going to go to Mr. Ose and recognize him for 5 minutes.

Mr. OSE. Mr. Chairman, I won't take 5 minutes. As I understand it, during the delay in my getting here, you had a vote that was transpiring, and that is left open?

Chairman TOM DAVIS. Correct. Still open.

Mr. OSE. How am I recorded?

Chairman TOM DAVIS. You are not recorded.

Mr. OSE. And this is the vote on the subpoenas for documents that may represent communication between the Office of the Vice President and the Department of Defense?

Chairman TOM DAVIS. Correct.

Mr. OSE. And I am recorded in what way?

Chairman TOM DAVIS. You are not recorded.

Mr. OSE. I am opposed to that. I would vote no on issuing such a subpoena.

Chairman TOM DAVIS. OK. The committee is noticed.

Would the gentleman like to make any other comments.

Mr. OSE. No, I just want to talk to committee counsel here.

Chairman TOM DAVIS. OK, thank you.

The gentleman from Massachusetts.

Mr. TIERNEY. I thank the chairman and I thank the witnesses for their testimony here today. I know we have been talking mostly about particular accusations of charging or overcharging, things of that nature, but I want to broaden it out just a little bit to talk about some of the planning aspects on this.

I want to ask you a little about the planning that was done with respect to Iraq's oil infrastructure on the one hand and the planning done to provide basic support for the troops on the other.

My understanding is that your company was involved with the planning efforts for both of those through the LOGCAP contract; is that correct?

Mr. WALTER. Yes, sir, that's correct.

Mr. COX. Yes, sir.

Mr. TIERNEY. Now, Michael Mobbs, who is an adviser of Under Secretary of Defense Doug Feith, told our committee staff that contingency planning for the reconstruction and operation of Iraq's oil infrastructure began months before the war. It was a deputies committee setup of all the deputies of the relative departments and agencies.

Mr. Mobb said that he was charged by them to work on a plan during the summer of 2002, and then Halliburton was issued a task order in November 2002 to do the planning; is that correct?

Mr. COX. I believe that's correct, sir.

Mr. TIERNEY. Now, from the information we have from previous hearings, we were told that a career lawyer from the Army Materiel Command wrote a memorandum saying that the LOGCAP contract couldn't be read to encompass contingency planning for the operation of Iraq's oil infrastructure, and that then one of the Army's Deputy General Counsel for Procurement agreed with that memo, and then eventually, apparently, it was overturned when one of the Department of Defense's general counsel made an overriding decision. But GAO has since then indicated that it also thinks that it was beyond the scope of that contract to have LOGCAP's contract read to encompass the contingency planning for the oil.

Did anybody in your company raise that issue during that time, that you know of? Anybody in your company indicate that this may not be the appropriate vehicle by which to take this contingency planning contract?

Mr. NEFFGREN. No. We feel it was appropriate under the LOGCAP contract. The LOGCAP contract has a component that is a planning component. We have full-time planners that do scenarios for all different countries in the world and all different type of potential events, and that is their full-time job. So it would only be appropriate for them to be involved in this type of a scenario-planning exercise.

Mr. TIERNEY. So you think the GAO is incorrect in their determination?

Mr. NEFFGREN. No. You asked my opinion.

Mr. TIERNEY. I'm not trying to debate with you, I want to know if that is your opinion.

Mr. NEFFGREN. I do. I think it was a legitimate task order to a planning mechanism within the LOGCAP program.

Mr. TIERNEY. The final version of the plan was completed in February 2003?

Mr. COX. That's correct.

Mr. TIERNEY. Is that about the same time that Halliburton also started making the deals with subcontractors to implement the plan and to start their prepositioning of the equipment? Would it be about that time?

Mr. COX. About that time, during the planning phase and when we were notified to start getting ready, we put together a proposal, if you will, to do that. At that time we put together our team to execute the contract.

Mr. TIERNEY. My point on this only indirectly affects you, so you're going to get a little relief here for a second. The point I'm trying to make is if I compare this to the planning for the troops, under LOGCAP you were supposed to provide for the essential support services to our troops, the meals, the water, the housing, and the other essentials of life for the servicemembers; is that correct?

Mr. NEFFGREN. Yes.

Mr. TIERNEY. OK. Now, when GAO issued yesterday's report on LOGCAP, one of their key findings was that the planning for the use of LOGCAP's contract to support the troops in Iraq did not begin until after the fall of Baghdad. You looked at that report and didn't make any objections or corrections, so we are assuming that is an agreeable statement with you? That is when the planning started, after Baghdad fell?

Mr. WALTER. For the work in Iraq, yes, sir.

Mr. TIERNEY. So it is a little astonishing to me, and I think to others, the planning for what is going to happen to our troops, their meals, their water, their housing, the essentials of life, their protection, all of that doesn't even begin to happen until May 2003, after Baghdad falls, but in the meantime the administration had your company planning for Iraq's oil infrastructure months before it had a plan how to support our troops.

The GAO report also indicated that the Army failed to follow its own guidelines. The Army's guidance recommends a comprehensive statement of work be developed in the early phases of the contingency planning. Can I take it that you were never charged by the Department of Defense to start the planning with respect to the support of the troops; and that it wasn't a case of your delaying it on your own?

Mr. WALTER. In Iraq, yes. We were already involved in the planning in many other areas, in Kuwait, in Afghanistan, in Djibouti and other locations. So we have been working with the Army in many other locations.

Mr. TIERNEY. So despite the contact that you had with them, they never asked you to start the contingency planning for the troop situation in Iraq until May 2003?

Mr. WALTER. To the best of my knowledge, yes.

Mr. TIERNEY. I think it is just disturbing, when we look at these priorities, that we have troops living in tents, eating MREs through

August 2003, because there hadn't been adequate prewar planning for dining facilities and housing. We have heard reports over and over again that our troops didn't have enough body armor or armored vehicles.

I have one family in my district that lost a son, who wrote home that he was scared every time his troops went out because they didn't have armor for their vehicles. And it was a matter of a week or two that the family learned that he had, in fact, been killed because an RPG went through his unarmored vehicle.

It seems to me that these shortfalls all could have been prevented with some proper planning, and that this whole timing consequence is just a misplaced priority of this administration. They put oil planning ahead of planning for our troops' safety and for their support. They placed no spending limits on the LOGCAP work done by your company in Iraq. Yet we find over here they are shortchanging veterans' health care. They issue monopoly contracts to private companies in Iraq, but they don't adequately fund education in this country.

This isn't a statement of your performance or anything like that, it's just a general observation. We have gone over the overcharging hearings, and we've gone back and forth, and I don't have much else to add on that, but I do have just an abhorrence here for the fact these priorities were so out of line and so out of whack that in the summer of 2002 we had an administration focusing on planning for oil, but not until May 2003, and after Baghdad fell, would they even begin to ask your company to start planning for how to take care of our troops and how to protect them and how to service them.

So I thank you for your testimony, but those are questions I think we will have to address back to the administration on a broader scale.

Mr. MICA [presiding]. Mr. Lynch, if you have questions.

Mr. LYNCH. Thank you, Mr. Chairman.

Gentlemen, again, thank you for coming here to help the committee with its work.

I just want to say that, first of all, we had a discussion recently with Bill Reed over at the Defense Contracting Audit Agency, and also I think we had General Kern at the same time, and I asked them this question about the whole bribery issue with these two Halliburton employees.

Can you tell me whether you provided information to this committee and to others regarding the bribery under this Voluntary Disclosure Act?

Mr. WALTER. Sir, under the Voluntary Disclosure Act and the regulations, it says that you make a voluntary disclosure to the inspector general or to the Department of Justice. We went to both of those groups with this information. To the best of my knowledge, they are performing an investigation.

I have talked to our counsel. They said that we have been providing information to them.

Mr. LYNCH. Well, apparently, there is some inconsistency here, and I want to get to the bottom of this. On Tuesday we learned that was, in fact, not true, that the Pentagon IG said the information was not provided to the Pentagon under this program, and

that even if it was provided under this program, matters of bribery would not be protected; that the information would still have to come forward to this committee.

I just want to give you another example. We had a woman, Mary Robinson, who was also in the midst of a criminal investigation, who came before this committee even though there was an active ongoing criminal investigation, came forward and provided information that was helpful to this committee. Actually, it was helpful to the administration, and she came forward and testified.

So what I'm trying to get to the bottom of is why are we not being told at least the names of these employees, the names of the contractors? What level—if you can't tell us the individuals involved, what level of Halliburton's administration and company hierarchy, what level were these two individuals at; and were they, in fact, overseeing other government contracts in other countries as well?

Mr. NEFFGREN. They were not officers of the company. They were employees of KBR. They were low-level supervisory people, senior subcontracts administrators were their titles. They are no longer with the company. And all the contracts that they have touched while they were employees of the company have been provided to the Department of Justice for their review and investigation. There is an ongoing Justice Department investigation.

Mr. LYNCH. OK. Let me just ask you to pause there. We were once told that one of these Halliburton employees involved in the payoff scheme was the procurement materials and property manager of Halliburton/KBR in Kuwait, and that he was in charge of a very large number of contracts and purchase orders.

Are you telling me now that testimony before, which was also provided under oath, was false? Are you telling me that?

Mr. NEFFGREN. I have been advised that the employee's title was a senior subcontracts administrator, not the manager of PMP.

Mr. LYNCH. OK. Mr. Chairman, I yield back.

Mr. MICA. Thank you.

Other Members?

Ms. McCollum.

Ms. MCCOLLUM. Thank you, Mr. Chairman.

If you have a truck and you don't maintain it by replacing the filters on it routinely, and then the truck breaks down in a convoy and it has to be either abandoned or destroyed, who is responsible for the loss of that truck in dollars, the American taxpayer, or does your company assume the responsibility for not keeping up the maintenance?

Mr. RICHARD. Ma'am, we're not aware of any trucks that have been lost due to lack of maintenance.

Ms. MCCOLLUM. So the truck drivers that were speaking to us before were lying?

Mr. RICHARD. You'll have to repeat that, I didn't hear you.

Ms. MCCOLLUM. The truck drivers with years of experience, the one gentleman who even described how he on his own cleaned out the filter on his truck, he was lying to us then under oath?

Mr. RICHARD. No, ma'am, I do not disagree that truck drivers periodically have to perform maintenance on their trucks as well. We operate in a very substandard environment.

Ms. MCCOLLUM. I understand that, Mr. Richard, but he said that the trucks weren't being placed on a regular log of maintenance, just like we do with our cars. I realize you are in a war zone, but I also realize that some of the filters, carrying with and having at both ends—so you have maintenance logs on every single truck?

Mr. RICHARD. Yes, we do. We currently perform routine maintenance every 2 weeks on our trucks.

Ms. MCCOLLUM. That's fine.

Mr. WALTER. But, ma'am, just to clarify one point. He did not state the vehicle was abandoned by the side of the road. It broke down outside of a facility, and he pulled it into the Scania facility, I believe.

Ms. MCCOLLUM. I wasn't talking about that particular truck. Thank you, though.

I'm trying to understand how these contracts work a little better. So you have a master contract, and then you do a subcontract. The cost plus cost, is that the subcontractor? Do they also have the ability to do the cost plus cost?

Mr. WALTER. No, ma'am, they do not. What we do is a majority of our subcontracts are awarded on a fixed price or a fixed unit price basis.

Ms. MCCOLLUM. So the Kuwaiti oil company, Altanmia, you have all the documentation for what they charged through you?

Mr. COX. Yes, ma'am.

Ms. MCCOLLUM. For their prices?

Mr. COX. Yes, ma'am, we do.

Ms. MCCOLLUM. Is that available to the committee?

Mr. COX. It has been provided in the last month, I believe, ma'am, since I returned. We provided every contract document for the Kuwaiti fuel mission and the Turkey and Jordan. The total fuel mission has been provided to the Department of Defense, I believe, at the request of this committee. But I do not know if they have provided it to you or not.

Ms. MCCOLLUM. Well, I will ask Mr. Waxman to yield in a minute.

I have one other question. Payroll. You have two ways in which you pay, like I am sure you are salaried employees, but you have two ways in which you are paying some of your employees in Iraq and Kuwait. One is 8-hour, and one is 12-hour; is that correct?

Mr. WALTER. No, ma'am, that is not correct. Our employees are paid for the hours they work. If there is a case where an employee cannot do something, for example, they are in a convoy that does not have the security and cannot leave, or they are at a location where they cannot get to their activity, there is a standby pay, which is a maximum of 8 hours a day. That means they are ready to go, but because of the conditions they are not allowed to go.

Ms. MCCOLLUM. I don't disagree with that.

Mr. WALTER. But everything else is based on the hours worked. So if an employee works 10 hours in a day, they record 10 hours on their time sheet, and get paid for 10 hours. If they work 12 hours a day, they will record 12 hours and be paid for 12 hours.

Ms. MCCOLLUM. And when you advertise for a job, do you advertise based on the 8 hours? We hear things on the news that so-and-so is being paid so much to drive a truck. That is based on 8 hours?

Is that based on 8 hours standby? Is standby a lower rate than when you are actually in the convoy driving?

Mr. WALTER. The compensation can be very flexible, depending on what is happening. All of that is described to the employees when they are given their compensation packages. There is no promise of a 12-hour day. The only guarantee is if you are going to be over there and not able to work, you will get a minimum of 8 hours per day on standby.

Ms. MCCOLLUM. And they sign their time cards. Does a supervisor have to sign each time card, validating them?

Mr. WALTER. Yes, they do.

Ms. MCCOLLUM. And all that information is available, and everything is documented where everybody is?

Mr. WALTER. Yes, ma'am.

Ms. MCCOLLUM. Do you follow that on your subcontractors? How often do you audit those time clock records?

Mr. WALTER. If a subcontractor has timekeeping requirements, for example, we do subcontract some labor, their time cards are included with their invoices.

Ms. MCCOLLUM. I would like to yield to Mr. Waxman.

Mr. Waxman, have you been given all the information on this Kuwaiti contract? I understand we had some difficulty getting some information. We were told that Kuwait couldn't provide it.

Mr. WAXMAN. Well, I am not sure I can answer that at this time, but let me, for the record, clarify it.

And then, also, I want to ask these gentlemen some further questions, but I prefer to do it in writing and have them respond in writing, for the record, if they will all agree to that.

I see them indicating in the affirmative.

Mr. MICA. Without objection, the ranking member will submit additional questions to the panelists, and you can respond in writing, and it will be made a part of the record.

Has there been an agreement on keeping the record open?

On a time agreeable to the majority and minority, without objection, so ordered.

I want to thank you gentlemen for participating today and for your assistance with the committee. We will excuse you at this time, and we will now move to our third panel and final witness. And that witness is a single individual on this panel, Dr. Steven Kelman. Dr. Kelman is a Weatherhead professor of public management at Harvard Kennedy School of Government and former Director Of the Office of Federal Procurement Policy under the Clinton administration.

Dr. Kelman, if you will stand and raise your right hand.

[Witness sworn.]

Mr. MICA. Let the record reflect that the witness answered in the affirmative.

Dr. Kelman, you are recognized. The custom is we give you about 5 minutes. You are the only witness on this panel. I guess we could be a little lax.

Mr. KELMAN. I was actually told since I'm a panel, I get a little more. We'll see what happens. I know it's late.

Mr. MICA. Any lengthy statement or material you would like to be made part of the record, you can do so through a request of the Chair.

With that, Dr. Kelman, you are recognized.

STATEMENT OF STEVEN KELMAN, WEATHERHEAD PROFESSOR OF PUBLIC MANAGEMENT, HARVARD UNIVERSITY, JOHN F. KENNEDY SCHOOL OF GOVERNMENT

Mr. KELMAN. Congressman Waxman and Congressman Mica, and particularly my fellow Massachusettsan, Congressman Lynch, it is a pleasure to have an opportunity to speak before the committee today on some of the broader issues for the health of our procurement system that the oversight of Iraqi contracting raises. I am not an expert on Iraqi contracting. I am going to limit myself to some of the broader issues.

And what I would like to do is start with some quick vignettes, and you might say, what does this have to do with these hearings? So please be a little patient, and I will explain what they have to do with the hearing in a minute.

The first vignette. I was teaching an executive education program recently at the Kennedy School for some senior government managers and military officials, and we were discussing another subject, performance measurement in government. And a woman from the Defense Logistics Agency, in the context of that discussion, got up to talk about the efforts that DLA has been making over the last decade to improve its customer service, to be more customer-oriented and so forth, and how they had used performance measures for that.

She was standing or sitting at one end of the class. After she talked, a gentleman raised his hand at the other end of the class, who it turns out is the wing commander at Minot Air Force Base in North Dakota, and he said to her, in front of the class, thank you very much. I have noticed as a customer, as a wing commander, I have noticed that the procurement system is serving us better. We are getting things more quickly, you are more responsive, the procurement system is doing a better job.

At lunch I talked with him in more detail, and I have more of that in my written testimony, but I asked him more about that, and he just said there has been a real change in attitude, and then he added on, in addition to that, on the planes that he flies, they are able to upgrade them technologically, you know, technological refreshment on planes, much faster than they used to be able to.

So that is vignette one.

Vignette two. I had breakfast recently with a long-time career information technology manager at the Bureau of Labor Statistics, who is now in the private sector, and when he asked me to breakfast, he had experienced the procurement changes over the last 10 years at the end of his government career, and he said, how are they going, Steve? And I said, well, they are under some challenge now, whatever. He said, gee, that's too bad. And then he told me, again, a number of stories, but I will only share one with you.

He talked about a situation where he was the program manager for an IT contract in the late 1980's; that is to say, the time of the old procurement system. The vendor was performing terribly. He

went to his assistant administrator to say, the vendors aren't performing, we have to get rid of them. And the assistant administrator said, look, if we get rid of this vendor, it will take 2 years to get on contract again, and then 6 months for bid protest. Just live with it. And he had to.

Vignette three. Two of my students at the Kennedy School just did a study, did a lot of things, but let me share the thing I want to share with you. They looked at a sample of information technology services contracts at GSA and asked the government customer how satisfied they were with the contractor's performance and the contract, how good a job the contractor had done; 1 to 10 scale; 10 was the best, 1 was the worst. The average satisfaction, and this is now, 9.4 on a scale of 1 to 10. Very satisfied.

I did a similar survey in the late 1980's, same question, same kinds of contracts, again among government customers, how satisfied they were then, the old procurement system; 6.9 on a 1 to 10 scale. So it's moved from 6.9 to 9.4.

So what's the relationship between these vignettes and oversight of Iraqi contracts, you might ask? The relationship is that each of these vignettes illustrates how we are doing a better job than before in focusing the government's procurement system on its primary goal, which is to deliver the best value to taxpayers. What we have been trying to do over the last decade is to switch the focus of the procurement system from simply avoiding doing bad things to trying to do good things.

What do I mean by that? Let me illustrate as an example as a Member of Congress. We have all sorts of rules, as we should, ethical rules for standards of conduct among Members, and we expect people to comply with them. But imagine a Member of Congress who spends 20 years in Congress, and they have never violated the rules, but that's all. No legislation, no oversight, they haven't done anything else. And they say, I never violated a rule of Congress. They have done nothing wrong, but they haven't accomplished anything. They haven't done anything right.

And that's the distinction I'm trying to draw with what we're trying to do with the procurement system. We have ethical standards for contractors, saying they shouldn't be cheating the government, government officials should be observing the rules in awarding contracts, and so forth. But a contractor could have a spotless record of never having cheated the government and still done a terrible job in all their contracts in terms of their substantive performance. A government official can always follow all the rules and still have done a terrible job of asking for the right things in the first place or putting the right performance measures in the contracts, or whatever.

And, traditionally, the government procurement system was almost completely focused on trying to prevent people from doing the wrong thing, rather than, in addition to that, saying, you have to do the right thing as well. What we have tried to do, mostly in a bipartisan way over the last decade, is to refocus the system toward saying, your job is not done when you follow the rules. You need to be oriented toward the mission of the organization and use your head to come up with innovative solutions.

I present this history, and will finish up shortly, because experienced government contracting people remember the old days. And given this history, it is very easy for our procurement work force to get the message from the headlines that we want them to go back to those old days of just being the procurement police. I know no member of this committee has this intention, and I know many members of this committee are advocates of the Federal work force. Chairman Davis and Congressman Waxman are cochairs of the Congressional Public Service Caucus, for which I really admire both of you for what you do on that. But I think it is important to understand, and I want to emphasize, that I think it is unintentional, nobody means to be doing this, but I will tell you from talking with career folks in government that a lot of these headlines about Iraqi contracting and a whole bunch of things going on are really demoralizing and even terrorizing the government work force.

Now, you don't intend it, but they are getting the message, the unintended message, that there is no downside to asking for another review; to say no to the customer, to the military customer, whatever; to slow down the process; to just be the police. That is the message they are getting. I know you are not trying to send it. So what I am begging the committee to do is to work to counteract that message that I know you do not intend to send.

I urge you to do two things. One is I would urge, and we really need to repeat over and over again to our contracting work force and to contractors, that you believe that their responsibility is provide best value for the taxpayer; not just to avoid doing things wrong, but to do the right things. Their job isn't done when they follow the rules.

Second, I would urge the committee to hold a hearing where you bring in career government employees to talk about—not an Iraq contract; a hearing just in the general, Committee on Government Reform, on innovative business solutions that they have been working on to try to improve the value that contracting gives the government. And by doing that, you will send a message that you care about that kind of behavior and performance as well.

So that is my message, and I appreciate your time.

[The prepared statement of Mr. Kelman follows:]

TESTIMONY OF DR. STEVEN KELMAN,
WEATHERHEAD PROFESSOR OF PUBLIC MANAGEMENT
HARVARD UNIVERSITY
JOHN F. KENNEDY SCHOOL OF GOVERNMENT
BEFORE THE HOUSE COMMITTEE ON GOVERNMENT REFORM,
JULY 21, 2004

Chairman Davis, Congressman Waxman, and members of the Committee, I appreciate the invitation to speak before the Committee on the broader issues for the health of our procurement system that relate to the Committee's oversight on Iraqi contracting.

I believe that Congressman Waxman, by pursuing this issue, and Chairman Davis, by working in a bipartisan manner despite the special challenges of an election year, are doing taxpayers a service by conducting oversight on these issues. One of my heroes, Harry Truman, came to national attention with his oversight work, while a Senator, on contracting issues during World War II – work he undertook though that war was far less controversial than the Iraq War and though his own political party held the White House.

Let me note at the outset I have no special knowledge of the details of various Iraq military support or reconstruction contracts, and am therefore not in a position either to say anything or answer any questions about specifics of Iraq contracting.

I would make some very general observations. First, the kinds of support activities being contracted out under the LOGCAP contract – and I am here not referring to some other contracts, such as for interrogators – are very appropriate to contract out. A general view in the commercial sector is that one should keep one's core competencies inside one's organization, while contracting out non-core activities, so as to economize on management attention and hand over one's own non-core activities to organizations

that can make these their area of expertise. The LOGCAP contract meets that test. Serving meals, delivering letters to soldiers, and building base camps are not the core competency of the military. Another reason to contract out rather than providing a service in-house is that the organization's demand for a service is expected to experience wide swings. Under these circumstances, it doesn't make sense to staff one's organization based on the maximum expected demand, but rather to contract for surge needs, because it is less disruptive to an organization to avoid staffing itself for non-recurring peak demands and then need significantly to adjust the organization's size. Third, training soldiers is very expensive, and what costs so much money is training them to wage war. It generally does not make sense to use very expensively trained soldiers for tasks that could be performed by people with much less expensive training.

Second, under normal circumstances, one would wish and expect that many of the kinds of services the LOGCAP contract provides on a cost-reimbursable basis – such as serving meals – would be performed on a fixed-price or fixed-price per unit basis. Fixed-price contracts provide greater incentive for cost-control than cost-reimbursement ones. Unfortunately, it is often impossible to provide these services in a war zone on a fixed-priced basis, because of unknown security costs and other issues. This means that there is inherently less incentive for cost-control than in with fixed-price contracting. It should be noted, however, that, contrary to some press accounts, costs plus a percentage of cost contracts are illegal once a contract is definitized – a fixed fee is established based on the expected contract value, which may be supplemented by incentives that include cost-control performance. Thus, it is not the case that a contractor would make a higher profit, the higher their costs are. Indeed, in a cost plus fixed fee environment, the lower the

contractor's costs, the higher the profit as a percentage of sales and the higher the return on investment. Furthermore, were the operation performed in-house, it would also be on a cost basis with in-house employees, so there would be no greater incentive for cost control there either. However, as I understand it, the Defense Department has often been slow to definitize contracts, and until definitization occurs, contracts can take on a cost-plus-percentage-of-cost element. The Committee should therefore, in my view, encourage the Defense Department to move promptly to definitize cost-reimbursement contracts.

Third, there has been some discussion of whether more of the Iraq task order contracts should be multiple-award rather than single-award contracts. A statutory preference for multiple-award contracts when an agency awards task order contracts was established, with bipartisan support, in the Federal Acquisition Streamlining Act of 1994. That was an excellent provision, because it allows combining competition, quality, and timely service. I believe this principle should be applied to the maximum feasible extent in Iraq, but there is a difficulty that needs to be kept in mind. Say a multiple award contract is given to two large information technology companies in Washington. With many hundreds of employees and many local contracts active at any one moment, they can bid on new tasks based on people they expect to be available if they win the task, without taking them off other work. In Iraq, by contrast, the risk would be that employees of companies competing for tasks might not have other work to do when they don't win a task, and they might simply end up waiting around doing nothing. This would have a big impact on prices contractors would need to bid, and might vitiate the advantages of multiple award competitions.

I present these general remarks for the Committee's consideration. But the main topic I wish to talk about today is how the oversight being conducted on Iraqi contracting – including not just Halliburton but also, for example, out-of-scope task orders for interrogators awarded under GSA IT services schedules – should be conducted in the context of the ongoing efforts over the past decade to improve the ability of our procurement system to deliver the best value to agency missions and taxpayers.

I would like to present a number of vignettes, that members of the Committee might initially think have nothing to do with oversight of Iraqi contracting. I ask you to listen anyway, because in I believe there is an important connection.

Recently, I was teaching in an executive education program at the Kennedy School for GS-15 level (and uniformed equivalent) federal managers. During a class discussion of public-sector performance measurement, a woman from the Defense Logistics Agency spoke about how her organization had used performance measures as a tool in their effort to re-orient the agency towards a greater results-orientation and customer focus. Having listened to her account, another participant across the room raised his hand to identify himself as a customer of the Defense Department supply system. He had noticed the difference. The system was serving him better, he said.

The customer was a wing commander at Minot Air Force Base in North Dakota. He is not in acquisition or contracting. He flies planes (currently, B-52s to be precise).

I pursued the wing commander's in-class observation over lunch one day after class. "There has been a cultural change in the supply system that serves us," he told me. "People are more motivated to do the right thing and to make things happen. Before, we were stovepipes. It used to be that if we had a supply problem, we filled out a form.

Now, if we have a problem, a supply technician or supervisor can pick up the phone and reach a person at the Air Logistics Center who's responsible for us. When I pick up the phone, I don't feel like I'm bothering them. I feel they are there to solve the problem."

"Routine supply functions better than it used to. Our suppliers have worked hard to improve their processes and culture so they serve our Air Force better. Also, we get problems and issues resolved faster, both with the Air Logistics Center and with suppliers. When we're deployed, we have the same phone number to call. The last time I was deployed, we were able to maintain a higher number of mission-capable aircraft available than we used to."

Were there other ways the supply chain had become more responsive, I asked him? "Now we can update our planes with new technology much faster than previously. The Air Force recently added a new radio to the B-52 – we chose what we wanted; the Systems Program Office approved the contract modification and tested its compatibility quickly; then we used it in combat – well before it could have been fielded under the old system. We're currently integrating a new laser pod into the B-52's very quickly, in much the same way. This is important, because we have to have the ability to modify our systems faster to better enable us to dominate emerging threats."

Another vignette: I recently had breakfast with a long-time career information technology official in the Bureau of Labor Statistics, now working in the private sector. He asked me whether the procurement reforms he had experienced in the last years of his government career were still in place. I told him they were, but they were under challenge. "Too bad," he said, and then gave me a feel for his experience of the procurement system prior to the changes of the past decade.

"I was program manager for an IT contract in the late eighties, and the vendor was doing a terrible job. I went to the assistant commissioner and asked that we terminate the contract. 'Don't even try,' I was told. 'If we terminate this contractor, it will take two years for us to award a new contract, and then another six months for a bid protest. Just make do.'"

A recent study by two Kennedy School students of the satisfaction of the government customer with vendor performance on IT contracts shows an average satisfaction level of 9.4 on a 1-10 scale, compared with an average satisfaction level of 6.9 on the same scale in the late 1980's that I had found in research I did then.

What's the connection between these vignettes and oversight of Iraqi contracting?

The answer is that each of these vignettes illustrates how we are doing a better job than before focusing the procurement system on its primary goal – to deliver best-value products and services to our agencies and for the taxpayer. We have been engaged over the past decade, largely in a bipartisan way, to change the focus of the procurement system from simply avoiding doing bad things to trying to accomplish good things.

What's the distinction? Let me illustrate with an example from the career of a member of Congress. Congress has established, and rightly so, a number of ethical standards governing the behavior of members. We expect members to abide by these standards, and we punish members who do not.

But imagine a member who spends a 20-year career in Congress and, having no legislative achievements to his or her credit, is able only to say: I have obeyed all the ethical rules of the House.

That member has done nothing wrong. But the member has failed to accomplish anything. Few of us would judge such a career to have been a success.

Similarly, we establish ethical standards for contractors and government officials in the procurement system. Contractors shouldn't cheat the government. Government officials should observe rules about awarding only work within a contract's scope.

But a contractor can have a spotless record of never having overbilled the government or cheated the government in any way – and still have performed poorly on the substantive work of the contract.

A government official can have a spotless record of never having violated the procurement rules – and still have awarded contracts that require the contractor to do silly things, or done a poor job giving contracts to contractors most likely to perform well, or failed to provide a good incentive structure to encourage good performance, or been so insensitive to mission needs that contracts have taken years to award.

Traditionally, our procurement system was far more oriented towards preventing contractors and government officials from doing the wrong thing than in encouraging them to do the right thing. Indeed, we did little to orient our contracting workforce to the need to be sensitive to program customers and mission needs at all.

The thrust of the efforts we have been making for the last decade to improve the procurement system has been to redirect procurement towards satisfying mission needs, and to get out the message that the job of government contracting officials is not done when they have complied with, and assured that others have complied with, the rules. Rather, we expect them to use their brains to think of innovative ways to serve agency missions and taxpayers.

I present this history because experienced contracting people remember the old days when their job consisted mostly of policing government program officials and contractors to make sure nobody did anything wrong. Given this history, it would be very easy for our procurement workforce to get the message from the headlines that we want them to go back to that focus.

I know that no member of this Committee has that intention. Conducting contracting oversight of such a high-visibility effort is a duty of this Committee. And I know that a number of members of this Committee are advocates of the federal workforce – including Chairman Davis and Congressman Waxman, who are co-chairs of the Congressional Public Service Caucus. But I wish to call the attention of members of the Committee to potentially unintended consequences of your efforts. I believe that the various headlines about Iraqi contracting have demoralized and even terrorized many in our governmentcontracting workforce. Though you don't intend it, they are getting the message that you want them to spend all their time preventing every last ounce of wrongdoing, that there is no downside to saying "no" and to requesting another review, even if this significantly delays the ability to accomplish the mission. They are getting the message that you want them to go back to the old days.

What can you do to counteract this unintended message? I would make a number of suggestions. First, I would repeat over and over again to the contracting workforce -- and to contractors -- that you believe their responsibility is to provide best value for the government and to give program customers timely service, while obeying the rules. I would applaud the efforts to provide mission support and emphasize that we should learn

from honest mistakes made in an effort to support the mission, not execute those who have made them.

Second, I would urge this Committee to hold a hearing – perhaps working with the nonpartisan Council for Excellence in Government and the Partnership for Public Service -- on the topic of innovative business solutions in government contracting, focusing on and celebrating efforts to develop creative ways to get better value from contracting. Bring in some career civil servants who have come up with new ways to serve the public interest, and try through your hearing to help such innovative practices spread. I am not naïve enough to believe there will be any television cameras at such a hearing. But I would hope there would be significant attendance by members of this Committee, in the best tradition of this Committee's mandate to work for good government.

Thank you for your attention.

Mr. MICA. Well, thank you, and I am going to yield immediately to the ranking member for questions. Thank you.

Mr. WAXMAN. Thank you, Mr. Kelman, for your testimony, and we value what you have to say on these issues because we know you are an expert in this area, and I appreciate the key message you are bringing to us.

But I want to ask you about a certain situation. In Iraq there seems to be a pattern of awarding monopoly contracts, splitting up the geographical areas for electricity contracts in one area or oil contracts in another area of Iraq, and the contractor gets a monopoly, and then they do not compete for that. They will go out and hire—or they may even compete, but there is no opportunity for competition in it. For the over 2,000 discrete projects.

As a procurement expert, don't you think it would be better to have competition on the discrete projects so that we can get the benefit of competition, rather than a monopoly, with which it is hard to get the market forces to work?

Mr. KELMAN. That is a very, very good question. In fact, while I was in the government, we passed the Federal Procurement Streamlining Act of 1994, which did just what you said. It recognized task order contracting and set up a preference for multiple awards so there could be ongoing competition.

So as a general matter, I am in favor of using that whenever it is feasible, and actually had some conversations with your staff and others about it because I thought you were raising a very good issue.

And I want to emphasize I do not know very much about Iraq, but I asked a fairly senior person at the Defense Department, a career civil servant, hey, what about this suggestion? Why aren't you guys doing this more? Because I think, as a general matter, it is a very, very good idea. What the person told is, you've got to be careful, and I think you should continue to look at this issue, because I think as a general policy matter, I agree with you 100 percent, but what this person told me she was worried about was if you award a multiple contract here in Washington to IBM and Computer Sciences Corp. and KPMG, or whatever, they have all these employees who are working on a lot of projects at one time. So you bid them on an individual task order, and if they don't win that task order, they are working on something else, and so you switch to this other. It's just a lot of work to sort of share around.

This career DOD person—and again I'm putting it in the mix. I agree with the direction you are going, but this career person said to me, our concern would be that it's not like these, if you did a multiple award in Iraq, that they have a lot of other things to do. If they do not win an individual task order, they will just sort of sit around and do nothing, and might that not increase the price? That was her worry.

But I would be curious for your reaction to that.

Mr. WAXMAN. Well, all the major companies are in Iraq. Bechtel's there, Halliburton's there, Parsons is there, and there is no reason why they shouldn't be able to compete with each other on a task order and then get the job based on the competition.

Mr. KELMAN. What I would say——

Mr. WAXMAN. And their whole strategy with this administration is to carve out these monopolies, and then let them make the decision on the subcontractors.

Mr. KELMAN. What I would say is I would hope, if possible on a bipartisan basis, but have you been asking DOD about this?

Mr. WAXMAN. From the very beginning. See, the original contract was to Halliburton to run the oil fires infrastructure. They said they were going to put out oil first, but then they were given the monopoly to run the oil sector, and we asked, well, why were they given a no-bid contract? Other companies might have competed. And they came through with a series of reasons.

Mr. KELMAN. What I would say is continue to push this issue. I believe, as a matter of procurement policy, and it is reflected, as I say, in the procurement reform legislation in the 1990's, the idea of a multiple awards and task order contracting is a good idea.

A person whom I trust at DOD has argued to me, and she is a career person, there are reasons not to do it here, but I would continue to push. Unless you are satisfied with the answer, keep pushing them, because I think as a general matter it is a very good idea.

Mr. WAXMAN. Thank you. I appreciate your testimony, and I see we have a vote on.

Mr. MICA. Additional questions?

Ms. McCollum.

Ms. MCCOLLUM. No.

Mr. MICA. Well, we do have a vote.

Now, you come before the committee as a pretty experienced witness and on the subject in particular of acquisition. You have probably reviewed some of what took place with the awarding of the contract that is under question with Halliburton and this LOGCAP. It is my understanding that this was let initially some time ago under the previous administration.

Given what you know about the previous contract and then the situation we found ourselves in, do you think generally the way they proceeded in allowing this to be an extension of an existing contractor, sort of an add-on, was the appropriate way?

And then I think the ranking member raised the question of breaking these up into smaller parts. Just one quick general question.

Mr. KELMAN. Yes. I think I am going to—all I really know about this is what I have read in the newspapers. There is a lot of stuff back and forth, so I don't really feel like I am an expert on how these contracts were awarded and so forth. I do know just—I feel pretty confident before I read the newspapers. Actually the original LOGCAP contract was awarded the first time in the first Bush administration, was repeated in the Clinton administration and then repeated.

Mr. MICA. A long-time contract. But when you get into a situation where you need services ASAP and have an existing contract——

Mr. KELMAN. The——

Mr. MICA. Not just in general.

Mr. KELMAN. The whole reason for a contract in this situation—and it was an innovation and a good innovation in the first place—

in order to be able to gear up quickly for things in battlefield situations, you can't gear up quickly unless you have a contract in place before you do it.

Now, the debates about what was in scope, what was out of scope, that really goes beyond what I know enough about having an opinion. But the general idea that we should be setting up these vehicles in advance, I think, is a very good one. Indeed, there are other examples of them done by very progressive—our most innovative career people.

You know, Defense Logistics Agency in Philadelphia, the way they changed during the 1990's the way they buy medical supplies and uniforms, where they moved to what is called a prime vendor distributor. And what they did was some smart guy who got the message, your job is not over when you have obeyed the rules, you have to think creatively, he came up with the idea when they awarded those contracts for medical supplies—they have sort of a normal distribution, you know, during peacetime. The contract that's prenegotiated says, in the event of war, you have to be ready to send us X percent more. That's part of your contract. And so that is in place before a military action starts.

That is very intelligent contracting. That's the kind of thing we want our work force, our career work force, to be thinking more about and using their heads. That is the whole idea behind the procurement changes of the last decade.

Mr. MICA. Thank you. I may have additional questions, too, to submit.

We are running a little bit out of time. I do appreciate your being patient with the committee.

Mr. KELMAN. You have been very patient.

Mr. MICA. Well, you have been very patient to wait to be our final witness.

Mr. WAXMAN. Mr. Chairman, would you permit me to ask the gentleman to extend my best wishes to his father-in-law?

Mr. KELMAN. I will be seeing him very shortly. Thank you so much.

Mr. MICA. Thank you.

Without objection, wishes will go to your father-in-law.

We have one item of unfinished business. We have had a rolling vote here. The clerk will report the tally on the open vote on the ranking minority member's motion to authorize a subpoena.

The CLERK. Mr. Chairman, I have 19 ayes and 23 noes.

Mr. MICA. There being 19 ayes and 23 noes, the motion is not agreed to.

Mr. WAXMAN. Mr. Chairman, might I point out that this was a straight party-line vote?

Mr. MICA. Well, I thank the gentleman for recognizing that there is still a Republican majority on the committee and in the Congress.

There being no further business to come before the committee, the committee stands adjourned.

[Whereupon, at 3:33 p.m., the committee was adjourned.]

[The prepared statement of Hon. Dan Burton and additional information submitted for the hearing record follow:]

Opening Statement
The Honorable Dan Burton
Committee on Government Reform Oversight
Title: "Contracting and the Rebuilding of Iraq: Part IV"
Date: July 22, 2004
Time: 10:00 A.M.
Room: 2154 Rayburn House Office Building

Mr. Chairman, thank you for holding this hearing today. This is the fourth hearing the Committee has held to examine coalition efforts to rebuild Iraq after the fall of Saddam Hussein's despotic regime.

One year after Coalition forces liberated Iraq, Iraqis are fully engaged in the enormous challenge of rebuilding their country after decades of neglect. Let's remember that Saddam Hussein spent decades frittering away his Nation's vast wealth on himself and his Baath party thugs, while little to nothing was spent to meet the urgent needs of the Iraqi people.

There is ample evidence that our Coalition forces are helping the Iraqi people: electricity is now more equitably distributed and more stable, instead of, as during Saddam Hussein's rule, being supplied to Baghdad at the expense of the rest of the country; water supply in many areas is now at pre-conflict levels, Iraqi hospitals are up and running, and healthcare, previously available only for Ba'athist elite, is now available to all Iraqis; repairs and modernizations are being made to the

antiquated and neglected oil production and distribution systems; repairs to roads, airports, bridges and other critical infrastructure have improved access and mobility for the Iraqi people.

Mr. Chairman, I know that you have twice visited Iraq to observe first-hand the reconstruction efforts in order to gain a better understanding of the vast network of government agencies and contractors who are literally risking their lives to perform the critical work on the ground.

Earlier this year, I also had the great honor to witness first-hand the outstanding job our men and women in uniform, as well as our civilian workforce, are doing over in Iraq. I can tell you that everyone I talk to has a clear understanding and appreciation not only of the dangers, but also for how important their mission is; and every single person wanted to get the job done and done right. I can also tell you from my conversation with the Iraqi people that they were very grateful to Coalition forces for liberating them from their former tyrannical, murderous dictator, Saddam Hussein.

Despite the mammoth task, our troops and civilian contractors are accomplishing so much on a daily basis, yet a disheartening silence remains in the media about the dramatic improvements underway in Iraq.

Even more disheartening is the steady drumbeat of criticism and negativity stemming from my colleagues on the other side of the aisle. At every turn, for partisan political reasons, they have chosen to criticize the rebuilding efforts, and distort the facts to emphasis the negative and downplay the positive.

Even in this Committee, Mr. Chairman, as you worked tirelessly to conduct responsible oversight of Federal reconstruction contracts, our Democratic colleagues chose to practice their own oversight by press releases, leaked draft reports, and confidential briefings; even going as far as making publicly unwarranted accusations about improper contact between the Vice President's office and Department of Defense contracting officials. Despite the fact that in briefings arranged by the staff of this Committee, DoD officials unequivocally stated that they had not experienced inappropriate influence from the Vice President or anyone in his office.

This is rather like Senator Rockefeller's repeated allegations that the White House pressured intelligence analysts to doctor evidence on Iraq's Weapons of Mass Destruction programs while at the same time endorsing his own Intelligence Committee report that found no evidence of any such pressure.

These extremist statements simply fly in the face of common-sense and fall completely apart under serious scrutiny. Yet that doesn't stop the partisan drum-beat of negativity and insinuation.

Let us be honest, this has not been an easy transition, but we must remain committed to the task at hand – the task of delivering the Iraqi people from oppression and tyranny to democracy and freedom. The successful transfer of sovereignty has paved the way for meaningful equity for Iraqi citizens in the process of shaping their future, and generated renewed hope for prosperity and democracy. We should not let partisanship derail our efforts to finish the job we started.

And, I commend you Mr. Chairman for avoiding getting swept up into the partisan circus, and for continuing to conduct a fair, constructive, and

transparent series of oversight hearings on this very complex subject. Throughout these hearings, we have managed to separate fiction from fact and truth from partisan rhetoric; and, I think we have helped make sure that the contract process in Iraq is improved in such a way as to ensure success and safety.

No one will dispute that mistakes have been made in Iraq. Government contracting is difficult under normal circumstances and especially challenging in a war zone. The Federal contracting process is rarely pretty, and problems with cost estimating, accounting and documentation practices are not out of context. But, the vast majority of contracts in Iraq were done properly. Where problems have been identified, solutions and improvements have been found.

The rebuilding of Iraq will take time – after all, Nations are not built in a single day. Mistakes will still be made and this Committee will continue to do its due diligence in oversight.

So, thank you again, Mr. Chairman, for holding this hearing. I look forward to hearing the testimony of all of our witnesses today. I, like many members of the Committee, have some tough questions to ask of our

panelists, but by the end of the day I hope that we all will have a better understanding of the accomplishments – as well as the ongoing concerns – of those brave men and women involved in the enormous and daunting task of rebuilding Iraq.

Motion to Subpoena Documents from DOD
Offered by: Mr. Waxman
Motion Failed
7-22-04

COMMITTEE ON GOVERNMENT REFORM
108TH CONGRESS – **2nd SESSION**
ROLL CALL

Name	Yeas	Nays	Present	Name	Yeas	Nays	Present
MR. DAVIS (VA) (CHAIRMAN)		X		MR. WAXMAN	X		
MR. SHAYS		X		MR. LANTOS	X		
MR. BURTON		X		MR. OWENS	X		
MS. ROS-LEHTINEN		X		MR. TOWNS	X		
MR. MCHUGH		X		MR. KANJORSKI	X		
MR. MICA		X		MR. SANDERS	X		
MR. SOUDER		X		MRS. MALONEY	X		
MR. LATOURETTE		X		MR. CUMMINGS	X		
MR. OSE		X		MR. KUCINICH			
MR. LEWIS (KY)		X		MR. DAVIS (IL)	X		
MRS. DAVIS (VA)		X		MR. TIERNEY	X		
MR. PLATTS		X		MR. CLAY	X		
MR. CANNON		X		MS. WATSON	X		
MR. PUTNAM				MR. LYNCH	X		
MR. SCHROCK		X		MR. VAN HOLLEN	X		
MR. DUNCAN		X		MS. SANCHEZ	X		
MR. DEAL		X		MR. RUPPERSBERGER	X		
MRS. MILLER (MI)		X		MS. NORTON	X		
MR. MURPHY		X		MR. COOPER	X		
MR. TURNER (OH)		X		MS. MCCOLLUM	X		
MR. CARTER		X					
MRS. BLACKBURN		X					
MR. TIBERI		X					
MS. HARRIS		X					

Totals: Yeas 19 Nays 23 Present ____

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Alfred V. Neffgen
Chief Operating Officer
Americas Region

July 27, 2004

Representative Thomas M. Davis III
Chairman
Committee on Government Reform
U.S. House of Representatives
Room 2157
Rayburn House Office Building
Washington, D.C. 20515

Dear Chairman Davis:

We want to thank you for the opportunity to testify before your committee last Thursday. We felt it was a good opportunity to clarify the record on a variety of issues. We appreciate the opportunities we had to meet with both your staff and the staff of the ranking Minority member, Congressman Henry Waxman, and we will continue to work with you and the Minority on these issues.

There are two matters I would like to correct for the record regarding the hearing.

The first matter concerns questions raised by Mr. Waxman about Halliburton's role in extinguishing oil well fires in Kuwait following the first Gulf War. This was used to question whether KBR/Halliburton had the most relevant experience to be given the firefighting task order under LOGCAP. Assertions were made that need to be corrected.

Halliburton in 1991 entered into a contract with the Kuwait Oil Company. This contract, among other things, required Halliburton to provide both manpower and equipment to assist in extinguishing the oil well fires that were then ravaging Kuwait.

As a result Halliburton deployed its personnel and both pumping and jet cutting equipment to directly support the firefighting effort. The crews and equipment directly contributed to shortening the length of time necessary to extinguish the well fires. These same types of crews and technology were recently employed in Iraq.

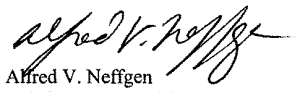
In 1991, Halliburton crews and equipment worked directly at the wellhead in fighting well fires in concert with such firefighting firms as: Red Adair, Boots & Coots, Wild Well Control, CNPC, (a Chinese firm), and several other foreign firms. It was because of the efforts of our crews and our technology that 320 of the burning wells were extinguished.

The company and the employees who risk their lives in this dangerous work think it is important that these facts be on the record. It is an important part of our company's history and it is expertise that makes us proud.

The second matter concerns questions raised about two former employees who are currently under investigation by the Department of Justice and Department of Defense relating to allegations that they received payments from a subcontractor. In order not to jeopardize the investigation, KBR declined to provide details as to the allegations. However, I testified from memory that the two former employees were "senior subcontracts administrators."

Further research has indicated that the proper titles of the two employees' last positions at KBR were "global manager – procurement" and "manager – procurement," and I wanted to be certain to correct this for the record. I would also like to reiterate that this is a situation in which KBR learned of certain discrepancies, investigated and self-reported to the Department of Justice and the Department of Defense Inspector General's office. Thank you.

Regards,



Alfred V. Neffgen
Chief Operating Officer
KBR Government Operations, Americas Region

cc: Rep. Henry Waxman