

**CORRUPTION IN THE PROCUREMENT PROCESS/OUTSOURCING  
GOVERNMENT FUNCTIONS:  
ISSUES, CASE STUDIES, IMPLICATIONS**

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*[Shortened version prepared by W. Black]*

**REPORT TO  
INSTITUTE FOR FRAUD PREVENTION**



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## EXECUTIVE SUMMARY

This report presents a case study into procurement fraud and corruption in connection with ongoing U.S. programs in Iraq. The U.S. effort involves unprecedented reliance on private contractors to provide services and goods in a combat environment. The methods employed for this study combined interviews, site visits, collection and analysis of court documents, review of the literature and secondary data.

The report covers six primary topics. First, it shows why U.S. procurement for Iraq inherently took place in a criminogenic environment. Second, it explains how elite criminals act dynamically to take advantage of such environments and to change such environments to optimize them for crime. Third, it notes why effective controls are essential to limit procurement abuses. Fourth, it demonstrates that inadequate controls and other practices have made the environment even more criminogenic. Fifth, it summarizes why the procurement abuses have harmed national security. Sixth, it suggests policy reforms to reduce the abuses.

Procurement effort in Iraq is taking place in a strongly criminogenic environment. Transparency International (TI) notes that procurement is the leading environment in which “grand” (v. “petty”) corruption takes place. TI notes three procurement fields that account for the bulk of grand corrupt transactions: military, construction, and oil. The U.S. effort to reconstruct and pacify Iraq required success in each of these three inherently risky procurement fields. In such circumstances, it is essential to have in place the best possible controls to reduce fraud and corruption.

This report emphasizes what criminology teaches about fraud and corruption by elites that have substantial governmental power or economic power (typically as CEOs). Often, of course, they have both forms of power simultaneously. Elite criminals (what Black refers to as “control frauds”) have far greater ability than non-elites to act dynamically to optimize the environment for fraud while “neutralizing” their crimes psychologically and obtaining substantial impunity. The first level of dynamism is that elites are able to *choose* to operate wherever the legal, political, economic and cultural environment is most criminogenic and the payoffs to abuse the greatest. The second level is that elites are able to *change* the environment to increase the “asymmetries” and make it far more criminogenic. Normally, thieves face a fairly symmetrical environment: to steal more they have to take greater risks of detection, prosecution and sanction. But elites can often produce an environment in which engaging in massive fraud and corruption *increases* one’s political power and status and greatly reduces the risks of detection and prosecution. Elite criminals optimize by creating fraud networks that help them maximize this asymmetry of risk and reward.

Criminologists have long argued that, in addition to its economic and political injury, fraud and corruption kill. In Iraq, the success of the procurement effort was vital to the twin U.S. missions to pacify and reconstruct the country. Independent experts agree that the failures of the procurement effort have made the already horrendously difficult missions impossible. Indeed, Iraq may now be the most corrupt nation in the world. (TI’s Corruption Perception Index (CPI) for 2006 ranks only one nation – Haiti – as more corrupt than Iraq.) The corruption is believed to be a major source of funding of the insurgents. The U.S. CPI ranking has worsened since 2001 – from 7.6 (tied for 16<sup>th</sup> place) to 7.3 (20<sup>th</sup> best) in 2006. The Global Corruption Barometer 2006 for the U.S. has also fallen. Americans surveyed by TI hold the view that U.S. anti-corruption efforts are ineffective.

The report concludes with policy recommendations regarding the procurement process, revolving door practices, conflicts of interest and improved prevention, enhanced legitimacy, transparency and support of public trust.

The general policy implications from this study point to the following measures:

- Clarify the goals of procurement and procurement/ethics rules
- Balance priorities and values in view of available capacity and resources
- Simplify and streamline the procurement system
- Conduct a systematic and credible study into the extent of the use of contractors, the concrete problems posed by cohabitation and ways in which these can be minimized
- Create a central database of information
- Develop a normative framework through multi-stakeholder communications
- Ensure consistency of conflict of interest and other rules applying to government employees and private contractors
- Ensure oversight, transparency and openness – strengthen the capacity of the Office of Government Ethics to oversee private contractors
- Ensure that there is a fair and competitive bidding process
- Render the third party workforce visible to the public
- Sanction misconduct and improve accountability
- Encourage and reward integrity and mutual respect
- Raise awareness and renew public trust
- Provide for regular training and proper management of contractors

## Introduction and background

Procurement is an area that has long been recognized as being particularly vulnerable to fraud and corruption. This is true in the private sector, where the typical problem is kickbacks to the contract officer. It is also true in public sector procurement where the fraud can be initiated by either the public contracting official or the private supplier. The World Bank has estimated that roughly \$1.5 trillion in public contract awards are influenced by corruption. Procurement fraud is often associated with cartels. In Japan, for example, the *dango* has rigged the bids on public construction projects for many decades. The process is illegal but is carried on with impunity. Procurement fraud is a serious concern in advanced and developing nations.

Procurement in the context of the U.S. occupation of Iraq, therefore, would have posed a strong, inherent risk of fraud and corruption in the best of circumstances. The circumstances, however, were far from the best. Iraq was a dictatorship run by Saddam Hussein through the Baath party. The key leaders were disproportionately members of a religious minority in Iraq (Sunnis) from a particular region (Tikrit). The government, therefore, had little legitimacy and few credible institutions. The law enforcement personnel were repressive and had no popular support.

Gulf War I led to enormous destruction of Iraqi infrastructure, particularly communications, electrical generation and transportation. Hussein's unwillingness to comply with U.N. peace provisions after the first Gulf War led to a sanction regime that caused Iraq's infrastructure to deteriorate further and its economy to stagnate. His brutal suppression of Shia uprisings after Gulf War I increased Shia-Sunni animosity. The creation of a *de facto* Kurdistan increased Kurdish power and aspirations. Widespread corruption in the "oil for food" program created an international network of corruption.

Gulf War II shattered the Iraqi military. The looting caused a severe loss of U.S. prestige and devastated the already critically impaired infrastructure. It also provided insurgents with enormous stocks of weapons and explosives.

Therefore, the U.S. civilian authorities that attempted to restore Iraq were faced with a nearly impossible task. Some of the difficulties were inherent on the U.S. side. Americans were foreign occupiers from a non-Islamic nation that had twice humiliated the Iraqi military. Iraqis widely believed that the U.S. invaded Iraq to seize its oil. The U.S. military and diplomatic services have very few proficient Arabic speakers. The U.S. defense industry is heavily concentrated, making it difficult to obtain competitive bids.

Some of the inherent difficulties were on the Iraqi government side. It had no legitimacy in the eyes of most Iraqis. It had no rule of law. It had no democratic institutions. Its security forces were unpopular, corrupt, and untrained. The nation was fractured along ethnic, religious, and regional lines. Its infrastructure had largely collapsed. The most functional institutions in Iraq were robust networks of corruption. In sum, Iraq inherently posed an extraordinarily criminogenic environment for procurement fraud. In the best of worlds, U.S. and Iraqi post-invasion efforts would have had to struggle to reduce widespread procurement fraud.

This report concentrates on other policies that added materially to the problems of inadequate security, inadequate institutions and infrastructure, and procurement fraud in ways that are not commonly understood. Among criminologists, fraud experts and procurement experts there is a consensus that these errors include:

- The legal structure of the Coalition Provisional Authority (CPA)
- Hostility to procurement controls
- The unique reliance on private contractors to provide support for a military operation
- Inadequate insistence on, and monitoring of, contractor performance
- Increased toleration of conflicts of interest in the procurement process
- Exacerbating already severe “systems capacity” problems
- Exalting “loyalty”, tolerating abuse and easing “neutralization” of abusive conduct

The period in which the CPA operated was a particularly active time in which the international community adopted far tougher anti-fraud and corruption procurement standards. The U.S. had long urged the international community to adopt far more stringent controls designed to limit procurement fraud and corruption. Moreover, the U.S. was the leading supporter of an intense, contemporaneous, UN investigation by Paul Volcker of the Iraqi “oil-for-food” network of corruption and fraud under Hussein.

This report focuses on corruption within procurement processes and issues arising from the practice of relying on private contractors for governmental work. Although this practice is not new, it has recently increased significantly. Federal managers no longer rely solely on their employees for service delivery; more than ever, they rely on contractors who work together with federal employees but are subject to different conflict of interest rules and ethical standards.<sup>1</sup> Government’s increased dependence on contractors has created a number of problems that undermine the integrity and arguments in support of the expanding contracting process.

## **I. IRAQ WAS AN INHERENTLY CRIMINOGENIC ENVIRONMENT**

TI first included Iraq in its CPI in 2003. It was in the lowest quintile with a score indicating endemic corruption. Iraq was considered deeply corrupt under Saddam Hussein and the Volcker report demonstrates that it created an international network of corruption with elite institutions in many nations in order to abuse the UN “oil-for-food” program.

The second Gulf War and subsequent occupation made the environment even more criminogenic. Hussein’s security forces were poorly trained in legitimate police operations, were hated and feared by most Iraqis, and were shattered by the invasion and resulting vacuum of authority. Iraq had no rule of law, no democratic traditions, and no politically legitimate institutions. It was run as a dictatorship supported by a minority clan (Tikritis) that was widely unpopular in Iraq. It was split by ethnic and religious divisions.

The U.S. procurement effort was subject to inherent risks. The Defense Department led the government in outsourcing military tasks to private contractors. Those contractors would have substantial leverage in the effort to rebuild and pacify Iraq. First, the outsourcing was so vigorous, and the troop strengths committed to Iraq so low, that the private defense contractors were essential to the success of the military mission. Second, there were relatively few contractors willing and able to provide immediate, large teams in a war zone as dangerous as Iraq. Third, the situation was a military and humanitarian emergency. The combined effect was that competition and transparency were dramatically reduced. The combination increased the criminogenic environment for procurement fraud.

In his book *The True Size of Government* Paul Light has made clear that the size contract workforce is unknown to both the government and US taxpayers. He argues that contractors have become a “shadow of government” in a process whereby politically connected private actors are

taking over a growing slice of work from federal employees. This workforce has not been counted and its appropriateness remains unanalyzed. The federal government uses contracts and grants for more than just the procurement of goods and services. While the number of federal employees is now smaller, actually more people work for the government now than ever before.

This workforce has reached its highest level since before the end of Cold War.<sup>2</sup> In 2000, the federal government spent a little more than \$203 billion on contracts with private companies. By 2005, this spending reached \$377.5 billion. During this period, spending on these contracts grew at almost double the rate of other discretionary federal expenses. Half of the growth in discretionary spending between 2000 and 2005 is linked to increased expenditures on private contracting<sup>3</sup>. Notably, Department of Defense (DOD) officials awarded contracts worth more than \$200 billion for goods and services, in fiscal year 2004. As Light recently pointed out,

Fueled by nearly \$400 billion in contracts in 2005 and another \$100 billion in grants, the true size of the federal government now stands at 14.6 million employees, which includes civil servants, postal workers, military personnel, contractors, and grantees. The total is up from 12.1 million in 2002, and just 11 million in 1999. More than half of the 2005 total is composed of contract employees, which accounted for an estimated 7.6 million jobs. This number is up nearly 2.5 million since 2002, the last year the true size of the federal workforce was measured, and the most recent year for which complete data are available. As such, the growth in contract employees between 2002 and 2005 marks both the single largest absolute and percentage increase since 1990 at the end of the cold war, which produced sharp declines in the number of civilian, military, and contractor employees during the 1990s. All of the increase in contract employees is due to increased spending at the Department of Defense.<sup>4</sup>

The top five contractors were all military: Lockheed Martin, Boeing, Northrop Grumman, Raytheon and General Dynamics. The five collectively received \$80 billion in 2005, which amounts to more than 21% of total federal contract dollars. Lockheed Martin is the largest federal contractor. It received \$25 billion in 2005. Halliburton is the fastest-growing one as it surged from the 20th position it was in 2000 to reach in 2005 the 6th rank of government's stronger federal contractors, receiving \$6 billion<sup>5</sup>. Among the most outsourced agencies are also the Department of Energy and the Environmental Protection Agency.<sup>6</sup>

## **II. HOW ELITE CRIMINALS ACT**

Elite public criminals can use the power and apparent legitimacy of their office to extort bribes or direct procurement to entities they control or profit from. They can shape the environment, e.g., by increasing regulatory requirements, to optimize their gains from corruption. Private elites can indirectly achieve the same result by suborning public officials to modify the environment to benefit the private party, e.g., by going to a no-bid, sole-source contract.

Three traditional, generally legal, means of influencing the environment to aid private contractors are campaign and PAC contributions and lobbying. The Project on Government Oversight (POGO) found that more than one trillion U.S. dollars has been awarded to federal contractors since 1997. In FY 2002, the top ten contractors were received 35% of the money.<sup>7</sup> Moreover, "Since 1977, the top 20 contractors contributed over \$46 million in total campaign contributions, of which \$25 million was political action committee (PAC) contributions."<sup>8</sup> Additionally, the top twenty contractors spend nearly \$400 million in lobbying since 1977.

Some contractors take illegal actions to optimize the environment for fraud. Four case studies illustrate the variety of tactics alleged to have been used.

### **Case Study: Thomas Spellissy**

In this case, Thomas Spellissy consulted with companies seeking business with the US Special Operations Command (SOCOM). An indictment alleged that he formed Strategic Defense International as a company used to facilitate corrupt payments to William Burke who was employed by a private contractor and assigned to the SOCOM Special Operations Acquisition and Logistics Center, Management Directorate. In that capacity, Burke was acting on behalf of the United States government and the Department of Defense. Burke allegedly formed a company, Carlisle Bradford Enterprises, which received Spellissy's illicit payments in exchange for the preferential treatment of projects and companies represented by Spellissy. Invoices for "technical services" were used as the justification for those payments.

According to the indictment, Spellissy did "directly and indirectly, knowingly and corruptly, give, offer, and promise anything of value to any public official [William Burke] ... with intent to influence any official act [preferential treatment for awarding contracts to companies represented by Spellissy]." <sup>9</sup> Wire fraud and bribery counts were also included in that indictment. <sup>10</sup>

### **Case Study: Darleen Druyun**

The Chief Financial Officer of Boeing (Michael Sears) and the official in charge of Air Force contract acquisitions (Darleen Druyun) pled guilty to aiding and abetting acts affecting financial interest and acts affecting financial interest respectively. During the course of 2002 and 2003, Sears offered Druyun a high-level position within Boeing. At the time of this exchange, Druyun was overseeing contract negotiations between the Air Force and Boeing regarding the modification of the Boeing 767 aircraft for military use.

During the employment negotiations (including salary, compensation, and bonus) the two also discussed awarding the modification contract to Boeing. Upon Druyun's retirement from the Air Force, she accepted a high-level position within Boeing where she made upwards of \$250,000 not including benefits and signing bonuses. When questions arose about the connection between Druyun's awarding the contract to Boeing and her receiving a position with them post-retirement, Sears failed to disclose that he had met with Druyun while she was still an employee with Boeing in charge of contract acquisitions. Sears subsequently pled guilty to a single count of the aiding and abetting charge; his sentence is pending. Druyun received sixteen months.

The most disturbing element of this case was revealed in a 2005 story on *60 Minutes II*. During her sentencing, Druyun admitted she had swung Air Force contracts in Boeing's direction and was overly agreeable in meeting Boeing's price tags for projects. Specifically, during the Boeing 767 modification negotiations, the price tag was upwards of twenty-three billion dollars. Critics within the Air Force thought the price was much too high but Druyun sided with Boeing – not the Air Force. Druyun's position within the Air Force was specifically to determine the price tag for military projects that would be borne by the American taxpayers. Her other negotiations while with the Air Force are under investigation.

A Defense Science Board Task Force on Management Oversight of Acquisition Organizations noted the following contributing factors: "exceptional expertise in contracting; long tenure in her

position; gradual accretion of acquisition and personnel management authorities; little oversight because of no immediate supervisor (or her supervisor delegated acquisition authorities to her); abusive behavior to subordinates and contractors that was not apparent, or viewed as “tough, but fair” by supervisors; “behind closed doors” decisions; employment of her daughter and future son-in-law by Boeing.”<sup>11</sup>

### **Case Study: Randall Cunningham**

Randall Harold Cunningham (aka Randy “Duke” Cunningham) was a member of the United States House of Representatives for a congressional district in San Diego County, California. For a period of approximately five years, ending in June 2005, he conspired, along with four others, to commit a number of criminal offenses including bribery and fraud. In return for adjusting the performance of his official acts, Cunningham demanded, sought and received from his co-conspirators at least \$2.4 million in illicit payments and benefits in various forms such as cash, checks, meals, travel, lodging, furnishings, antiques, rugs, yacht club fees, boat repairs, moving expenses, cars and boats. Cunningham then used his office to influence appropriations in the awarding of defense contracts.<sup>12</sup> He ultimately pled guilty to conspiracy and tax evasion. The judgment was pronounced in November 2005 by the United States District Court, Southern District of California.

Cunningham attempted to conceal this conspiracy by various means. He used one-sided transactions through which his co-conspirators bought property from him at an above market price, paid money to him for the property that he continued to own and sold property to him at a below-market price. He also directed payments through multi-layered transactions involving corporate entities and bank accounts he and his co-conspirators owned and controlled. Notably, but not surprisingly, Cunningham failed to reveal these illicit payments in Financial Disclosure Statements to the United States House of Representatives and on his federal tax filings.

These misdeeds translated into the following criminal offenses, as committed by Cunningham and his coconspirators:

They engaged in bribery of a public official (Title 18 U.S.C. section 201(b) (2) (A)) as Cunningham and his coconspirators conspired and agreed he would directly and indirectly corruptly demand, seek, receive and accept items of value from them in return for being influenced in the performance of his official acts.

Cunningham and his co-conspirators engaged in “honest services mail fraud” (Title 18 U.S.C. sections 1346 and 1341) because they conspired and agreed to devise a material scheme to defraud United States of its right to his honest services, including his conscientious, loyal, faithful, disinterested, unbiased service, to be performed free of deceit, undue influence, conflict of interest, self-enrichment, self-dealing, concealment, bribery, fraud and corruption, and, in executing said scheme, to cause matters and things to be sent and delivered by the U.S. Postal Service and private and commercial interstate carriers. “Honest services wire fraud” (Title 18 U.S.C. sections 1346 and 1343) was committed because they conspired and agreed to devise a material scheme, again, to defraud the U.S. of Cunningham’s good services, this time, in executing said scheme, to transmit and cause to be transmitted in interstate commerce by means of wire communications, certain writings, signs, signals and sounds.

Cunningham and his co-conspirators conspired to willfully evade income tax payments (Tax Evasion, Title 26 U.S.C. section 7201) due and owed to the United States from 2001 to 2005 by



concealing and disguising illicit payments and benefits received by Cunningham through various ways. In 2004, he falsely declared that his joint taxable income was \$121,079, and he was due a refund of \$8,504, while he knew that his income was at least \$1,215,458, and there was a joint taxable income due and owing of at least \$385,077.

Moreover, members of Congress have announced they will investigate the \$21.2 million contract between the Department of Homeland Security and Shirlington Limousine of Alexandria, Virginia. Shirlington is a firm deeply implicated in the Cunningham scandal and obtained the DHS contract despite being headed by a man with a lengthy criminal record. The case raises questions about the contracting process as well possible security issues.<sup>13</sup>

### **Case Study: Custer Battles<sup>14</sup>**

The case of Custer Battles (CB) epitomizes many of these problems and is worth a closer look. CB and other defendants conspired to over-bill the CPA for tens of millions of dollars in services and facilities with respect to two contracts awarded to CB. The first one dealt with the provision of security, housing and related facilities and services at the Baghdad International Airport (BIAP). It also included the provision of armed security at the main gate and perimeter of the airport and a team of Transportation Safety Administration-approved security screeners. The second contract was assigned for the provision of security, construction and operational services to support the Iraqi Currency Exchange (ICE), which was charged with the replacement of the old Iraqi dinars with new ones.

In June 2003, the CPA solicited proposals to provide security and baggage screening services at the Baghdad International Airport (BIAP). CB submitted a fixed price proposal to the CPA and was awarded the contract. CB had made a security assessment of Kabul International Airport for Afghan aviation officials, but had never worked for the U.S. government or provided security services. At that point, Scott Custer offered counter-terrorism courses for public-utilities managers in Nevada. Battles contacted Robert Isakson, a former FBI agent whose security company had worked in Kosovo and Somalia, and asked him to join Custer Battles on the BIAP project. CB's bid was lower than those of established security firms, such as DynCorp and ArmorGroup. The CPA extended CB a contract and provided over \$2 million upfront.<sup>15</sup>

In its proposal, CB represented that it would provide over 138 security and related personnel, services and equipment. However, representations that CB would provide a fixed number of security personnel at the proposed BIAP contract price were false, as it intentionally declined to provide the required services. According to the original terms of the contract, the BIAP was to be fully operational by July 10, 2004; yet, on that date BIAP was only partially functional. CB had offered to provide these services for \$13,640,832, but later the contract price rose to approximately \$16,500,000.

Custer Battles assembled a staff and took over the airport, beginning cleanup of the terminal, which had been largely destroyed by retreating Iraqi troops. Within weeks, the CPA decided that the airport would not open, for security reasons, but gave Custer Battles another \$2 million in cash to continue to patrol the empty airport.<sup>16</sup>

Shortly thereafter, CB set up subsidiaries in the Cayman Islands and submitted a bid for the ICE contract.<sup>17</sup> The CPA created the ICE with the purpose to replace old Iraqi dinars bearing Saddam Hussein's picture with a new Iraqi currency. In August 2003, CB signed a contract with the CPA to construct camps and provide security and operational support for the ICE. The ICE contract

was awarded through a competitive bidding process. CB won with the lowest bid of \$9,801,550. The contract underwent a number of modifications, each of which resulted in an increase to the contract price. The contract itself identified two sources of funding: Seized Funds (\$3 million) and the DFI (\$12 million).

CB used shell companies in other countries through which items required under the CPA contracts could be billed, in order to inflate costs and create a mark-up in excess of that normally permitted under a cost-plus contract. The three intermediary companies used to inflate costs associated with the ICE contract were defendants SGD, MEL and Laru; Custer Battles controlled and owned either all of the stock or a majority of their stock. Under the ICE contract, Custer Battles was entitled to a fee of 25% over its costs. However, through the use of intermediary shell companies, the defendants artificially inflated Custer Battles' fee to 60% over its actual costs.

The intermediaries SGD and MEL "leased" ICE contract facilities components, such as cabins, vehicles and heavy equipment used for lifting and transporting, to Custer Battles at an amount higher than the one charged by a third-party supplier. Then, Custer Battles invoiced the inflated amount as its supposed actual cost, and thus received a double mark-up over the true cost.

Moreover, Custer Battles also billed CPA with substantial sums for services and equipment that it failed to provide. CB also used Laru to create fictitious invoices to Custer Battles which then billed the CPA for non-existent costs. Battles decided to start a business in Iraq because "the fear and disorder offered real promise"<sup>18</sup>. During trial testimony, he said that he was writing a book entitled "Blood in the Streets: Finding Opportunity in Crisis."<sup>19</sup>

### *Troubling Signs along the Way*

The allegations that emerged in the Custer Battles case should have surprised no one. There was a repeated, egregious troubling pattern of behavior from the outset: the bidding and awards process. As indicated above, this was allegedly followed by contract modifications and increases without proper accountability, the use of separate, shell companies, the provision of services at inflated costs, and the submission of false leases and invoices.

### The Bidding Process

The Custer Battles contract was fraught with problems from the beginning. The contract was to be awarded through a competitive bidding process. Colonel Kibby, a contracting officer at the CPA, estimated Custer Battles proposal had the lowest price and represented the best value in relation to the proposals that were submitted by other contractors. However, the contractors' proposals could not have been compared on the basis of labor rates; Custer Battles in their proposal neglected to mention the labor rates, the term that allowed them to make profit.

Custer Battles was the only contractor that had agreed to build the camps by the CPA's deadline. Indeed, Ambassador Bremer who was assigned to head the CPA with the title of "Administrator" announced the ICE project in about the middle of July and wanted it completed by October. Custer Battles' proposal met the criteria of quick completion and low bid of \$9,801,550.00 and was awarded the contract.

### Contract Modifications and Lack of Accountability

Once the contract was signed the haggling began, as the ICE contract was not a firm-fixed price contract because the CPA determined that it would be inappropriate. In a meeting Custer had with a CPA contracting officer, he asked her to consider changing the contract type from a time and materials to a firm fixed price. The contracting officer denied the request as she was very suspicious of the reasons they wanted this change. Marc Stanislawczyk, Custer Battles' government contractor attorney, also informed the company they should account for this contract as a time and materials as the reference in modification 3 to a firm fixed price contract was not sufficient to convert the original contract.

The ICE contract was modified four times; each one resulted in an increase to the contract price. One of these modifications was the payment of \$3 million cash advance to Custer Battles, which came from the Seized Assets account, before the work was actually started, as the company needed the money to fund the project. They were expected to use that amount to hire people, purchase materials, labor and equipment for the execution of the contract. However, no document, record or receipt was provided to the CPA.

### Separate Companies or Shell Companies?

According to Custer's testimony, the company established five operating entities: Secure Global Distribution (SGD), their transportation and logistics entity formed in August 2003; Mideast Leasing, formed in September 2003; Custer Battles Levant which was their local procurement and operating company and was formed in June 2003; Secure Global Engineering, their construction and engineering company; and K-9 Associates, their canine explosive detection company. The last two did not perform work in conjunction with the ICE contract.

Custer testified that separate companies were established to create a corporate structure allowing them to make these organizations work. (They had liability and brand benefits.) Custer stated the companies were independent subsidiaries, not sham companies, and they didn't intend to hide the relationship between it and these entities. However, these companies were not independent. In fact, their ownership belonged to some of the officers of Custer Battles. Baldwin testified based on the information he received from Custer and Battles, SGD and MEL were owned half and half by them. Battles made presentations to the CPA about SGD where he said the reason why SGD was a good distribution company was because it was owned by Custer Battles. Custer and Battles with Muhammed Darwish owned Custer Battles Levant, which according to Custer was their regional company. Together with Murtaza Lakhani, Custer and Battles owned Laru.

Laru was a subcontractor with which Custer Battles had business. The first assignment was to complete the project for the construction of the life support camp at Baghdad Airport for which worked three subcontractors. Laru also worked for the ICE project. When Baldwin took on the responsibilities at the camp, Morris (the manager for Custer Battles in Iraq) told him to discharge the other two subcontractors and utilize only Laru as the primary subcontractor. However, Baldwin refused and used all three subcontractors to finish the project. Laru's price was 40% higher than the other two subcontractors, so he notified Custer and Morris; nevertheless, they directed him to use Laru because as they stated, they had a relationship with that company. Under the ICE contract Laru was contracted to provide catering services for the ICE camp in Baghdad Airport. There was also another company called Satco and suddenly it became Laru/Satco. Custer said he made a purchase in Laru, and they were partners.

The use of these shell companies permitted Custer Battles to increase its profits. They were controlled by Custer and Battles and served as intermediaries between the actual suppliers and CB creating the appearance of additional costs and thus more markups. The reason Custer Battles didn't make payments to SGD, MEL and Custer Battles Levant was that these subsidiaries were owned by them and were kept in one set of financial records. These companies did not seem to exist as registered companies; they had no offices, no employees and no bank accounts by the time the ICE contract was awarded.

#### Services Provided at Inflated Costs

Under the ICE contract, Custer Battles was required to a) provide security guards, b) construct and operate three camps for the security personnel and the personnel working for the ICE, c) provide trucks and vehicles for the transport of the currency, d) provide heavy equipment for the movement, storage and transport of the currency.

Custer Battles ordered in its own name to the supplier the items required and then purchased the items in the name of shell intermediaries SGD and MEL. The artificial inflation of the amount invoiced to the CPA as its true cost enabled Custer Battles to claim a double mark up.

Custer Battles ordered 65 to 100 cabins with the company Red Sea Housing Services Ltd. SGD issued the purchase order to Red Sea. Custer Battles then billed the CPA for these items at a higher price and when required to justify the high cost, it prepared a lease after-the-fact in an attempt to convince the CPA for the transaction's legitimacy. Red Sea did not do any actual work; it just sold the cabins to Custer Battles that then used their subsidiary SGD to lease them to CPA. Custer Battles bought certain things and then marked them up in the name of its subcontractors and provided them to the government. The same practice was repeated with a second purchase order for additional cabins from Red Sea by using MEL as an intermediary to create inflated costs under a non-existent lease. Custer Battles also purchased vehicles through SGD and heavy equipment used for lifting, transporting and storing, through MEL in the same manner.

All this was profitable as the ICE contract entitled Custer Battles to a fee of 25% over its costs. General Hugh Tant regarded all this as totally inappropriate: it exceeded the provisions of time and materials contract which allowed for a cost plus 25%; in his opinion, these were suspicious cases of fraud that had to be investigated. According to Baldwin's testimony, in a meeting Custer had with company employees, Morris informed him that he was able to get additional change orders approved by the ICE board that would generate extra profit; he said that was able to establish a higher profit than the 25% time and materials, in the 40% and 50% range on some items.

#### Submission of False Leases and Invoices

Custer Battles created leases that never existed, which were backdated to (on or about) September 17, 2003 when the camps were completed and occupied by the ICE employees, but they never existed prior to November of 2003. Baldwin testified that this couldn't make the leases false, but he believed it was not a good practice. Ihab Bashier, a new Iraqi employee of Custer Battles was ordered by Morris to sign the leases without reading the documents. The

signatures of the SGD leases were created by George Boustany a junior manager who worked under SGD, previously an employee of Custer Battles. He denied that he had signed any of them.

The leases were fraudulent and Custer Battles billed CPA for services and goods it never provided. Daniel Ray, a public accountant retained as an expert testified that defendants' own records strongly suggested they submitted invoices to the CPA that did not reflect the actual costs incurred for the ICE project.

The icing on the fraudulent cake was that Custer Battles didn't have any internal tracking procedures for its invoices. Some of the exhibits that were submitted to CPA could be easily generated from any word processing program. They were not accompanied by any documentation or any substantiation, although Custer Battles was required to maintain auditable records to include receipts with the names of individuals who provided work and all the money disbursed for the project. They were only photocopies. Some invoices didn't even identify the entity that sent it, and were nevertheless accepted. Custer asked for a SGD blank letterhead similar to the one used for invoicing and prepared the invoices. Yet, Custer and Battles denied ever having any direct involvement in invoicing.

The opportunity generated by the disorder offered Custer Battles was clear to CPA officials who felt powerless to act, even while CB's invoices started raising red flags. In his testimony, a CPA official stated that he believed that with more than 600 personnel "in the field" working on the ICE contract, dependent on CB camps, transportation and logistical support, "failure to execute that mission would have had a ripple effect through the currency exchange and the reconstruction itself ... disastrous impact."<sup>20</sup> The same term was used by Al Runnels, chief financial officer for the CPA, in a November 2003 memorandum about "potential irregularities" in CB invoices that had been turned over to the Defense Criminal Investigative Services for further exploration. Termination of Custer Battles for those irregularities, he said, would "have a disastrous impact on the success of the currency exchange program. The successful continuation of the program is of vital importance to the economic development of Iraq and to the overall progress of the Iraq Relief and Reconstruction Fund." He called for the DCAA to initiate an audit of the ICE program.<sup>21</sup>

In the context of the Iraq conflict, however, deterrents and strong controls were unavailable. As a *Washington Post* article noted:

If an official were to try to cancel a meal-service contract, for example, "some colonel is going to be on the phone to you ripping your lips off saying, 'Why aren't my troops being fed?' "Shaheen said.<sup>22</sup> The threat of canceling a contract "is normally the sharpest quiver in the bag of the contracting officer. But there's no arrowhead on it any more," Shaheen said. "So the checks and balances are gone. The system is broken."<sup>23</sup>

The system was not simply broken. Elites broke it in order to steal with impunity. They are able to steal vastly more than non-elites, yet face less risk of detection, prosecution and sanction than do common non-elite thieves.

### III. EFFECTIVE CONTROLS ARE VITAL TO LIMIT PROCUREMENT FRAUD

Experts in criminology, management, economic development, economics, political science, public financial management and procurement agree on several central principles about procurement fraud. First, procurement poses a substantial, inherent risk of creating a criminogenic environment. Second, it takes consistent, vigorous efforts to *reduce* procurement fraud in the best of circumstances where there is a firm rule of law, intense social disapproval of elite crimes, and adequate prosecutorial resources. Nations like France mocked the U.S. when it adopted the Foreign Corrupt Practices Act, but two decades later France joined the OECD Convention against bribery of foreign officials. The UN, the World Bank (and its sister organizations), and the International Chamber of Commerce have all come to the same conclusion that corruption causes severe harm and that stringent controls and enforcement are vital to reduce procurement fraud. This consensus has led to the adoption of international treaties that have specific provisions dealing with procurement fraud because of the magnitude of the losses it causes.

A wave of “control fraud” in the private sector has shown that similar controls are vital there to reduce fraud by some of the most elite U.S. corporations and professionals (Black 2005). Even major U.S. non-profits have displayed serious problems with fraud by their senior officials. Note that many of these provisions (e.g., the OECD anti-bribery Convention) were considered vital even though the overall environment in OECD nations (relative to most other nations) is minimally criminogenic. In the context of post-Gulf War II Iraq, the need for exceptionally stringent anti-corruption controls should have been clear.

### IV. PROCUREMENT POLICIES HAVE EXACERBATED PROBLEMS

The CPA was structured in a manner that has raised the defense, e.g., to false claims act suits, that it is not an entity of the United States. The Custer Battles case provides a window into an environment, so-called postwar Iraq, that critics have labeled a “free fraud zone”<sup>24</sup> in which \$8.9 billion was unaccounted for in just the first eighteen months.<sup>25</sup> The legal battle raises serious doubts about the ability to police and punish fraud in such an environment.

#### *Custer Battles Case Trajectory and Overview*

The civil false claims act case was filed in August 2004, argued in February and March 2006 and subject to a surprising intervention by the trial judge in August 2006. The suit, filed by two former employees/subcontractors of Custer Battles LLC who worked in Baghdad, alleged that the company inflated costs billed to the Coalition Provision Authority (CPA), which was the de facto government of Iraq from May 2003 through June 2004. Under the FCA, a mid-19<sup>th</sup> century federal statute aimed precisely at war profiteering, individuals are permitted to sue on behalf of the U.S. government to recoup payments made because of fraud, with those filing the suit (“relators”) also receiving a hefty reward, plus reimbursement of legal costs.

The suit initially focused on Custer Battles’ August 2003 contract for \$9.8 million (later amendments raised the cost to more than \$21 million) with the CPA for the Iraq Currency Exchange program (ICE, also referred to commonly as “MX,” or “money exchange”). In the lowest of three bids<sup>26</sup> submitted to the CPA, Custer Battles agreed to build, provision and maintain three camps, in Baghdad, Basra and Mosul, and perform other duties to support the ICE program created to exchange old Iraqi currency for newer bills.<sup>27</sup> Relators William D. Baldwin,

the former ICE program manager for Custer Battles, and Robert J. Isakson, a former security contractor, alleged that Custer Battles fraudulently billed the CPA for \$3 million under that contract and severely underperformed in fulfilling its terms, amounting to an actionable claim under the FCA.<sup>28</sup> The ICE contract, according to CPA witnesses, was one for “time and materials” – that is, Custer Battles could pass along to the CPA all costs for workers’ time, plus the cost of materials obtained to fulfill the contract, with a 25 percent markup for profit. Baldwin and Isakson alleged that Custer Battles’ principals, Scott Custer and Michael Battles, set up shell companies, often in the Cayman Islands, that were subsidiaries of Custer Battles but were treated as subcontractors for the purposes of the ICE contract; inflated invoices were then created in the names of those subsidiaries for Custer Battles to pass along to the CPA for reimbursement.

CPA officials testified about Custer Battles’ performance and billing practices. The ICE contract manager, retired U.S. Army Gen. Hugh B. Tant III, under direct questioning by relators’ attorney, explained, for example, that four private security officers were injured using trucks provided by Custer Battles, because of “brake failure.” He testified that Battles told him the contract called for trucks but didn’t specify their condition. More dramatically, Tant testified about a spreadsheet left at CPA headquarters by Custer and Battles after an October 2003 meeting with contract managers, detailing the company’s actual costs and the inflated markup they planned to charge the CPA. He called the billing “totally inappropriate,” and said he referred it to CPA’s investigators because “it appeared to be fraud.”<sup>29</sup> Jeffrey Ottenbreit from CPA consultant BearingPoint, contracted to manage the ICE program, said his suspicions were raised because Custer Battles’ submitted invoices matched its initial contract estimates with “uncanny precision.” While declining to categorize them as fraudulent, he said, “they were certainly not what I would accept as, you know, bona fide invoices.”<sup>30</sup> Other allegations included that Custer Battles did not deliver enough sleeping cabins for the ICE workforce, and the company presented, and invoiced for old, repainted Iraqi forklifts as new forklifts leased from one of its subsidiaries.

Custer Battles’ defense (and that of respondent Morris, Custer Battles’ former “country manager” in Iraq), was manifold, but said essentially: there was no fraud; if there was fraud, it was committed by individual employees acting outside the scope of their work; and in any case, because the CPA is not a U.S. government entity, there can be no recovery under the FCA. Much was made of the hostile and alien environment of Iraq in 2003, and the confusion of operating in a war zone and with no clear direction from the CPA. Battles testified that when he first arrived in Baghdad in 2003, the CPA “was completely paralyzed,” and said the ICE contract “never clearly stated what we were supposed to do, and we struggled with that.”<sup>31</sup> Of any possible confusion about invoices, he said, “there are probably seven or eight layers of subordinate documentation behind each and every one of those. We subcontracted to someone who subcontracted to somebody else who subcontracted to somebody else who got nine guys named Ahmed that were their relatives to do stuff.”<sup>32</sup>

Documents and testimony in the case argued convincingly that, at the very least, Custer Battles’ business practices were shaky. Morris told investigators invoices were “best estimates” rather than actual bills from suppliers; “The invoices submitted were generated to reflect the cost of what we thought each line item to be.”<sup>33</sup> A November 2003 e-mail from Baldwin to Custer, Battles and others refers to the use of wholly owned subsidiaries as subcontractors as behavior that “crosses the line,” “is on the fringes” and “required questionable procedures,” and urged full disclosure of the relationships to the CPA.<sup>34</sup> A week later, Baldwin warned his superiors the company had “no financial systems as a foundation to manage from, track or control.”<sup>35</sup> Baldwin’s successor in Iraq, Derek Fox, found the ICE program “poorest run DOD (Department

of Defense) contract I've ever come upon ... most mom and pop stores would do a better job."<sup>36</sup> Fox warned, "I also don't want to/won't end up in some country club prison like Eglin for CB ... failure to disclose certain things can get you there ... accidental or not its (sic) a close call on this one."<sup>37</sup> A memo from Peter Miskovich, Custer Battles' ICE project manager, in March 2004, alleged Custer Battles submitted \$2 million "solely based on forged leases back in September 2003" to the CPA, and advised Custer Battles officials that "a clear criminal act had occurred and that I would not participate in perpetuating this fraudulent situation with the CPA."<sup>38</sup>

Still, underlying the entire suit was the question of whether Custer Battles could be held accountable under the FCA, which punishes for false claims presented to officials of the U.S. government, or caused to be presented to them. U.S. District Judge T.S. Ellis III called for pretrial arguments on two issues: Was any fraudulently obtained money, in fact, U.S. government money; and, were the CPA and its officers, for these purposes, standing in for the U.S. government? Assistant U.S. Attorney Richard Sponseller, et al., responded with a brief affirming "the United States sees the FCA as an important tool that should be available for any false claims presented to the CPA. ... Any dollar lost to fraud increases the burden on the U.S. taxpayer." Sponseller also noted, "It was clearly established that Ambassador (L. Paul) Bremer was the head of 'the authority' and that Ambassador Bremer was a U.S. government official and that he acted at the direction of and reported to the president through the secretary of defense."<sup>39</sup>

In his pre-trial opinion, Ellis explained the four funding sources available to the CPA: appropriated, vested, and seized Development Fund for Iraq ("DFI") monies. Briefly, "appropriated" funds were those directly appropriated by the U.S. Congress for use in Iraqi reconstruction; "vested" funds were claimed and held by the U.S. Treasury from Iraqi assets in the United States; "seized" funds were those taken from Iraqi accounts after hostilities and also held by the United States; and DFI was a pool of money created, under United Nations auspices, from Iraqi oil revenues and other national assets for use by the CPA in reconstruction efforts. Ellis ruled that "any request to the CPA for payment from seized or vested funds constituted a 'claim' within the meaning of the FCA," because they were controlled entirely by the U.S. government, but DFI funds were not covered; the ICE contract was paid mostly, but not entirely, with DFI funds, he noted. Addressing the second issue, Ellis opined that Custer Battles' claims for payment were apparently presented to U.S. government employees, on temporary duty with the CPA, or at least caused to be presented to the U.S. government for payment from vested or seized funds. But he left open a window for discussion: "Discerning the status of the CPA is not an easy task ... One should not too hastily conclude that because the United States was the CPA's principal controller and contributor that it necessarily follows that the CPA is an instrumentality of the United States."<sup>40</sup>

The jury returned on March 9 with a verdict against Custer Battles – nearly \$10 million, accounting for the treble damages allowed under the FCA for the \$3 million in overbilling, plus \$250,000 on Baldwin's claim of retaliation. In August 2006, however, Ellis struck down the FCA claim on the grounds he had hinted at earlier: that although "the CPA was principally controlled and funded by the U.S., this degree of control did not rise to the level of exclusive control required to qualify as an instrumentality of the U.S. government ... In fact, the evidence clearly establishes that it was created through and governed by international consent."<sup>41</sup> He did, however, concede that there was "ample evidence that the company had submitted false and fraudulently inflated invoices."<sup>42</sup>

The ruling, according to U.S. Senator Byron Dorgan (D-N.D.), was "a setback for accountability."<sup>43</sup> Perhaps anticipating the ruling, the Special Inspector General for Iraq



Reconstruction (SIGIR) noted in July 2005 that it “could be important to subsequent civil actions against companies doing business in Iraq ... To the extent that such options for recovery are limited by this initial decision, the SIGIR’s role in detecting and preventing fraud, waste and abuse in Iraq reconstruction will be more significant.”<sup>44</sup>

The ruling leaves wide open the question of what action can be taken against contractors alleged or proved to have committed fraud in Iraq. SIGIR opened as many as 50 criminal investigations for contracting fraud, waste and abuse, but no criminal charges have yet been filed against contracting companies.<sup>45</sup> Kubli points out that Bremer, in an early proclamation, said that contractors “have immunity from Iraqi law. And now (with Ellis’ ruling) they weren’t subject to U.S. laws – thanks, CPA.”<sup>46</sup> A United Nations panel formed to monitor the spending of Iraqi reconstruction funds has no authority to prosecute or punish misuse.<sup>47</sup> The Uniform Code of Military Justice, which governs U.S. troops abroad, does not apply, and U.S. civil courts have routinely dismissed cases for lack of jurisdiction. One judge said he could not “try a case set on a battlefield during wartime without an impermissible intrusion into powers expressly granted to the executive by the Constitution.”<sup>48</sup>

The CPA viewed anti-fraud controls on procurement as unnecessary and undesirable red tape. The CPA was sufficiently hostile to normal anti-fraud controls that it engaged in practices designed to evade applying even weakened procurement controls. In some instances, the CPA acted in the same way small-time money launderers seek to avoid reporting laws: ‘Smurfing’:

- The CPA avoided contract reviews of four projects by keeping contracts under \$500,000.
- In order to avoid review, the projects were structured through 20 contracts.<sup>49</sup>

The U.S. has recognized some of the increased risks of corruption that can come with increased reliance on private contractors. Executive policy letter 92-1 issued to the directors of executive agencies and departments addresses “inherently governmental functions,” and to avoid objectionable transfers of responsibility to contractors.<sup>50</sup> Here are some key excerpts:

#### 6. Policy.

(a) Accountability. It is the policy of the Executive Branch to ensure that Government action is taken as a result of informed, independent judgments made by Government officials who are ultimately accountable to the President. When the Government uses service contracts, such informed, independent judgment is ensured by:

- (1) Prohibiting the use of service contracts for the performance of inherently governmental functions (See Appendix A);<sup>51</sup>
- (2) providing greater scrutiny and an appropriate enhanced degree of management oversight (see subsection 7(f)) when contracting for functions that are not inherently governmental but closely support the performance of inherently governmental functions (see Appendix B);

#### 1. Guidelines.

(h) Degree of reliance. The extent of reliance on service contractors is not by itself a cause for concern. Agencies must, however, have a sufficient number of trained and experienced staff to manage Government programs properly. The greater the degree of reliance on contractors, the greater the need for oversight by agencies. What number of

Government officials is needed to oversee a particular contract is a management decision to be made after analysis of a number of factors. These include, among others, the scope of the activity in question; the technical complexity of the project or its components; the technical capability, numbers, and workload of Federal oversight officials; the inspection techniques available; and the importance of the activity. Current contract administration resources shall not be determinative. The most efficient and cost effective approach shall be utilized.”

These guidelines should have led the CPA to apply far greater oversight of private contractors, but the CPA did not comply with the guidelines. It provides inadequate oversight.

The CPA was found wanting in many respects by the SIGIR:

- CPA not effectively managed 907 contracts and 1,212 micro purchase contracts (part of the Rapid Regional Response Program; amount: \$88.1 million
- 158 contracts awarded without competitive bidding or lacked proper documentation
- 26 award files did not contain a signed contract
- Fully paid for 91 projects upon signing contract, not at completion
- Completion of projects never verified
- 11 projects overpaid
- Missing receipts or other documentation for hundreds of contract files (786 files did not contain a vendor invoice; 838 files did not have completion document)<sup>52</sup>

Even when some projects are completed, the final outcome may be far from satisfactory. As reported by the head of SIGIR:

- A. We visited five electrical substations in southern Iraq near Basra. There was quality workmanship, but there had not been feeder lines included in the contracts to provide the electricity to the immediate region...
- Q. They built the facility, but they weren't providing electricity to anyone?
- A. The contract only provided for the facility; there was not any provision for the provision of electricity out of those facilities.<sup>53</sup>

SIGIR's latest report notes the following:<sup>54</sup>

### Audits

From November 1, 2006 to January 30, 2007, SIGIR completed eight audits resulting in nine audit products; nine audits are underway. Those completed addressed topics including:

- A review of government property management controls by the U.S. Agency for International Development (USAID) and its contractor, Bechtel National, Inc.
- A review of improper IRRF obligations, the circumstances related to these obligations and subsequent actions taken or planned regarding the use of these funds
- A review of internal controls related to disbursements of IRRF apportioned to the Department of State (DoS), Department of Defense (DoD), and USAID
- A report on security costs as identified by design-build contractors on IRRF projects.<sup>55</sup>

Problems continued to result from a lack of a single entity responsible for the overall Iraq reconstruction program. In the last quarter, SIGIR has found a mixed record of management performance by IRRF-implementing agencies with some problems in accounting and protection of U.S. property investments, questionable obligations and failure to provide SIGIR access to certain financial records. SIGIR found poor contract administration by the Department of State Bureau for International Narcotics and Law Enforcement Affairs (INL) and the Office of Acquisition Management. Some \$36.4 million in weapons and equipment could not be accounted for, while the Joint Area Support Group-Central (JASG-C) and the Joint Contracting Command-Iraq/Afghanistan (JCC-I/A) made limited progress implementing previous SIGIR recommendations.<sup>56</sup>

### Investigations

At this point, SIGIR is working on 78 cases. Thus far, its work has led to 5 arrests and 4 convictions, while another 23 cases await prosecution at the Department of Justice. Together with the Major Procurement Fraud Unit, U.S. Army CID, DoS OIG Criminal Investigations Directorate, USAID OIG, Defense Criminal Investigative Service (DCIS) and the Federal Bureau of Investigation (FBI), SIGIR has established the International Contract Corruption Task Force (ICCTF). The task force identified 36 cases - SIGIR is working on another 37 cases for presentation to the task force. There are currently 78 open investigations. In the last quarter, SIGIR issued four Inspector General (IG) Subpoenas.<sup>57</sup>

Finally, SIGIR set up a Joint Operations Center at their Virginia headquarters to gather intelligence and disseminate information, which aims at enhancing the cooperation of case agents based in the US and overseas.<sup>58</sup>

SIGIR works with the Army's Legal Service Agency's Procurement Fraud Branch, which has suspended 14 individuals and companies based on allegations of fraud and misconduct connected to Iraqi reconstruction and Army support contracts. In addition, 12 other individuals and companies have been referred to the Army Suspension and Debarment Official, resulting in 8 debarments.<sup>59</sup>

The whole situation in Iraq has reached the point where industry consultants advise financial institutions to classify private contractors doing business there as "high risk":

Philip Bloom, an American defense contractor convicted of money laundering, bribery and conspiracy in an \$8.6M scheme involving rigged contracts, was sentenced this week to 46 months in Federal prison. The proliferation of contractor fraud cases being investigated in the US by several military and civilian law enforcement agencies has now resulted in our judgment that government contractors with operations in Iraq must now be considered high-risk for compliance purposes. There are reportedly dozens of ongoing criminal investigations of defense contractors active at this time, and contractor fraud in Iraq appears to be rampant and out of control. Bloom was involved with several high-ranking US Army officers, a Department of Defense contract employee, and corrupt local officials in Iraq. All aspects of the Iraq rebuilding scheme are being closely examined by the National Procurement Fraud Initiative, which prosecutes procurement fraud associated with contracting activities for national security and other government programs.<sup>60</sup>

Hostility towards procurement controls was not limited to the CPA. There was a concerted effort to eliminate SIGIR because of its effectiveness in rooting out corruption, fraud and non-performance by elites.

The U.S. was a leader in international efforts to take more vigorous action against procurement fraud, for example, the *United Nations Convention against Corruption (2003)*.<sup>61</sup> The Convention requires signatories to take adequate measures for the prevention of corruption in both the public and private sectors, including the establishment of anticorruption bodies and the promotion of transparency. Public servants should be subject to codes of conduct and disciplinary measures. It also calls its members to raise public awareness of corruption. The Convention demands the establishment of criminal and other offenses to cover the acts of corruption.

The Convention is the most comprehensive international instrument developed to date against corruption and related offenses. There are provisions relative to public administration, procurement, the role of the private sector and civil society.<sup>62</sup>

Similarly, the U.S. was the leader in the OECD negotiations that led to ratification of the anti-bribery treaty in 2001 (*Convention on Combating Bribery of Foreign Public Officials in International Business Transactions*).<sup>63</sup> The United States signed this Anti-Bribery convention which was adopted by the Organization for Economic Cooperation and Development in 1997, and adopted implementing national legislation, the International Anti-Bribery and Fair Competition Act of 1998, 15 U.S.C. para. 78dd. This Convention obligates parties to criminalize bribery of foreign public officials in the conduct of international business and proscribes the activities of those who offer, promise or pay a bribe. Member states are required to apply effective and proportionate penalties, establish criminal liability and take measures to prohibit such actions. Mutual legal assistance is regarded of most importance among states.

The U.S. also led the effort that produced the *Inter-American Convention against Corruption*.<sup>64</sup> Adopted by the Organization of American States, this treaty is designed to promote mechanisms that will prohibit corruption in the countries that are parties to the agreement. The U.S. ratified it in 2000.

## **VI. RECOMMENDED POLICY CHANGES TO LIMIT PROCUREMENT PROBLEMS**

As the World Bank wrote in its 2005 report on anticorruption policy, five areas are crucial to effectively combat corruption, four of which are discussed here: 1) increasing political accountability, 2) strengthening civil society participation, 3) creating a competitive private sector, and 4) institutional restraints on power.<sup>65</sup>

Ultimately, constraints must be placed on public officials by organizations with the power to sanction. Indeed, as accountability increases, the costs to public officials also increase and thus being involved in illegal behavior would be an irreparable stigma and the ultimate deterrent.

More oversight is needed in the rules governing party finance. Candidate participation in the electoral process should be affordable and accessible. If campaign finance is curbed, it will help reduce avenues for donations with strings attached. If campaign finance cannot be adequately curbed, then there must be complete transparency regarding donors. However, in order to increase accountability of political officials, there must be a motivated public ready to pay attention.

Thus, the public must be brought into the process and awareness of political and governmental behavior encouraged. Free and investigative media are essential for greater transparency. Also, freedom and access to information within the government is also necessary for an informed public and a vibrant civil society.

Powerful firms exert tremendous power on public policy making. This influence is not always negative, and thus, to ensure positive participation, enhanced competition is required to avoid single firm dominance. In order to enhance competition: 1) Barriers to entry must be lowered to decrease the presence of monopolies and oligopolies and 2) Greater transparency is needed in the ownership structure. This will contribute to public awareness and expose hidden agendas.

Perhaps the greatest need of the private sector in order to effectively combat corruption is transparency and cooperation in the international banking system. Proceeds from corruption are often laundered through the international banking system and the proceeds are often housed overseas. There must be an “International Collective Action” (international treaty).

An independent and effective judiciary is crucial and must underlie the whole system. In order to increase independence, the judiciary must be free from budget and management involvement from other branches of government. However, above all else, judges must evince integrity and manifest ethical behavior.

Furthermore, anti-corruption legislation must match the capabilities of law enforcement. These laws can vary based on a country’s cultures and mores, but the standard applications must be easily understandable and agreed upon. Equal resources must also be supplied to law enforcement in order to combat the massive resources used by entities engaged in money laundering.

The U.S. Merit Systems Protection Board made the following recommendations regarding the management of contracting officer representatives (CORs) “agencies need to fulfill the regulatory aspects of managing CORs to include formal delegation of authority, improved COR training, and strategic management of the COR workforce. Agencies also need to improve the day-to-day management of CORs. These day-to-day issues include improving COR selection

and assignment, ensuring CORs begin early in the contracting process, ensuring CORs perform critical pre-award technical contracting tasks, ensuring CORs have enough time to do their contracting work, rating CORs on the performance of their contracting work, and considering the other Federal employees who affect the COR's contracting work. Fulfilling the regulatory requirements for managing CORs and managing CORs more effectively day-to-day are significantly related to more positive contract outcomes. Taking these steps will help ensure that the over \$325 billion spent on contracting achieves effective and efficient results for the taxpayer."<sup>66</sup> Many of these suggestions are reflected below.

Legislation and policies to punish those who engage in corruption must be swift and proportionate. As Olaya (2005) writes, blacklisting or debarring of companies found to practice in corruption can serve a preventative and deterrent purpose. In order to be effective, however, the debarment policies must be easily understood and fairly applied so as to demonstrate their legitimacy. Furthermore, the outcomes of debarments should be made public and the active civil population is aware of the names of individuals who have engaged in corruption. (Otherwise, individuals can just rename the company.) Blacklists must include corporations and individuals.<sup>67</sup> Prison time, particularly for repeat offenders, may also be considered.

The existing legal regime should be better understood and used. For example, the 2000 Military Extraterritorial Jurisdiction Act has rarely been used despite the proliferation of contractor misdeeds. New legislation was passed in 2006 which extended the Uniform Code of Military Justice rules of conduct to contractors during contingency operations and in times of war.<sup>68</sup> One observer noted, "The scope of the new law could be made more clear; it could be either too limited or too wide, depending on the interpretation. While it is apparent that any military contractor working directly or indirectly for the US military falls under the change, it is unclear whether those doing similar jobs for other US government agencies in the same war zone would fall under it as well (recalling that the contractors at Abu Ghraib were technically employed by the US Department of Interior, sublet out to DOD)."<sup>69</sup>

When internal and external audits are conducted (e.g. by inspector generals) the findings must be backed by congressional committees. Otherwise, the result is the SIGIR report from 2004 – no hearings to speak of to change policies found to be ineffective or questionable. The audits must be undertaken by strong, independent, and credible professionals from multidisciplinary backgrounds. For example, those without engineering backgrounds should not be assessing the structural soundness of an infrastructure project.

There also needs to be a balance between speed and accountability. In times of war, speed is of the essence, and so normal procedures are abbreviated. Competitive bidding may take too long, and so a contract is established without too much investigation. Unfortunately, companies are able to take advantage of this by inflating the numbers. Without the time to check everything, there is no way for the government to realize this overcharging. Changes should be implemented to hold these companies responsible for this inflation. In fact, bills were proposed to criminalize war profiteering and to instate mandatory audits by the General Accounting Office for any contract over \$25 million.<sup>70</sup>

In sum, governments are often ill-equipped to police themselves. By classifying these types of concerns as matters of national security they effectively prevent full investigation and disclosure. Moreover, many people move in the same political and social circles, and it is hard to completely separate the two.<sup>71</sup> According to *The Washington Post*, in an article about Iraq, "Critics say that because of legal loopholes, flaws in the contracting process, a lack of interest

from Congress and uneven oversight by investigative agencies, errant contractors have faced few sanctions for their work in Iraq.”<sup>72</sup> Canceling contracts, however, can prove difficult because of military dependency on the service they provide. Regarding this latter point, an attorney for Greenberg Traurig LLP a law firm representing contractors said, “So the checks and balances are gone. The system is broken.”<sup>73</sup> A representative from an industry organization, the Professional Service Council blamed part of the difficulty of fixing procurement difficulties on partisanship and the “Gotcha.” attitude of Congress when problems do arise.<sup>74</sup>

The following represent a comprehensive but by no means exhaustive list of overarching recommendations to improve the public-private contracting system. These are followed by specific topical and steps that should also be taken.

1. Simplify and streamline the complex system.<sup>75</sup>
2. Ensure oversight, transparency and openness.<sup>76</sup>
3. Render the third party workforce visible to the public.<sup>77</sup>
4. Identify and share best practices, and question unusual practices and structures.<sup>78</sup>
5. Create an organizational culture for sharing knowledge and acquisition practices.<sup>79</sup>
6. Use mistakes and failures as case studies, and communicate them broadly.<sup>80</sup>
7. Require periodic self-assessments of acquisition organizations, practices, and processes, and expect continuous improvement.<sup>81</sup>
8. Government branches should work together to streamline nomination and confirmation processes.
9. The Department of Defense should modernize the Senior Executive Service (SES) performance management system by instituting 360° feedback; implementing a rotation policy; removing impediments from bonus and development systems, especially for those willing to rotate.<sup>82</sup>
10. Encourage and reward integrity and mutual respect.<sup>83</sup>
11. Raise awareness and renew public trust.<sup>84</sup>

## Topical Recommendations

With respect to the ‘cohabitation’ issue, there are good ideas for relatively small steps on which to build<sup>85</sup>. For example, the organizational conflict of interest rule currently in place (Subpart 9.5 of FAR) seems to cover contractor conflicts rather than conflicts of contractors’ employees. It has been suggested however, that one may rely on this provision to address employee conflicts as well. Subpart 9.5 of FAR could also be mended to ensure that conflicts of employees do not undermine the ability of a contractor to act impartially. In addition, agencies may issue supplemental FAR regulations to address questions particular to designated types of contracts. An illustration of this approach is offered by the Department of Energy’s regulations on employees of Management and Operating contractors.<sup>86</sup>

Specific clauses could be used to anticipate employee conflicts of interest. The Food and Drug Administration requires such a clause to be inserted in “all contracts to perform certain reviews of regulated products; this clause specifies that the contractor must have a ‘conflict of interest plan’ which must include, among other things, a requirement that all contractor employees execute a ‘COI/Nondisclosure Agreement’ governing such things as conflicting financial interests and abuse of non-public information.”<sup>87</sup> Such clauses can be attuned to agency and situation specificities; these could also be collected and made available as good practices covering a range of government areas and needs.

### *A. Contracting Process Recommendations*

#### 1. Full, open, fair and competitive bidding

Competition is the driving force behind outsourcing the delivery of services, so it is essential to establish a bidding process that is open to large and small contractors. Contractors’ offers must be fairly evaluated to ensure government receives the best deals and guarantee taxpayers have confidence in its integrity. Congress should restore the definition of “competitive bidding” by requiring at least two bidders.<sup>88</sup> Currently, the public knows who is awarded the contract, but there is no way to find out what companies bid.<sup>89</sup> Written documentation and justification of selection, along with feedback to bidders should be provided.<sup>90</sup>

2. Information about additional avenues for voicing concerns; e.g., ombudsmen and ethics offices should be made available.<sup>91</sup>

#### 3. Modify procurement practices and enhance oversight

Task and delivery orders that exceed \$25,000 must be made public. Although contractors consider it unnecessary, procurement contract oversight must be restored as agencies are effective in exposing misconducts.<sup>92</sup>

#### 4. Create a centralized database of information

This database should include information such as civil judgments, criminal convictions, settlements and fines as well as Superfund cleanup costs imposed on contractors. A federal agency should maintain the database, and it should be consulted before the award of any contract or debarment decision.<sup>93</sup>

#### 5. Contractor disclosure

Contractors are required to disclose current suspensions or debarments.<sup>94</sup>



## 6. Application of Federal Acquisition Act

Debarment actions should be taken equally against large and small contractors. A suspension or debarment would be mandatory for a contractor who more than once in three years is criminally convicted or has had a civil judgment rendered against.<sup>95</sup>

### ***B. Revolving Door Recommendations***<sup>96</sup>

#### 1. Simplify and clarify laws, regulations, and directives.

Create “a clear and consistent model rule of ethical conduct for the entire federal government;”

#### 2. Mandate time limits

Create a meaningful and realistic timeframe in which former senior level executives may not solicit employment with government contractors who significantly benefited from policies they formulated while in office.

#### 3. Create revolving door exit plans

Require binding revolving door exit plans to create awareness and accountability.

#### 4. Regulating the regulators

Ban government employees from overseeing or regulating previous private sector employers.

#### 5. Close revolving door loopholes

Eliminate the loophole permitting former federal employees to work for a department or division of a contractor different from that which they oversaw.

#### 6. Supervision of recusals and disqualifications

Legally require federal employees’ to report notification of recusal or disqualification to a supervisor;

#### 7. Better oversight of transitions

The Office of Government Ethics needs to better oversee those who move from the private to public sector.

### ***C. Conflicts of Interest***

1. Remove or modify conflict of interest and Freedom of Information Act exemption and waiver provisions for advisory board members and ensure that unclassified portions of board meeting minutes are publicly available.<sup>97</sup>

2. Enact Executive Branch-wide law requiring federal advisory committee members to recuse or disqualify themselves from any discussion on matters where they or their private employer or client have a significant financial interest. This disclosure or recusal statement, including name, title and employer should be filed with the Office of Government Ethics and made publicly available.<sup>98</sup>

3. According to the Office of Government Ethics, Congress should take a number of actions in order to update these statutes such as:

- issue narrowly tailored regulatory exemptions to the general prohibitions of 18 U.S.C. section 205, which bans both compensated and uncompensated representational activities.
- amend 18 U.S.C sections 203 and 205 so they apply to employees who “knowingly make, with intent to influence, any communication to or appearance before specified government entities on behalf of another person.”
- expand the current waiver provision of 18 U.S.C. section 207(j)(5) beyond permitting scientific and technological communications, or create a new exemption permitting communications that are in the national interest.
- amend the one year cooling off period for senior employees of 18 U.S.C. section 207(c) to also cover all members of the SES. Such an approach would provide clarity and uniformity in the treatment of SES employees and would eliminate the potential for gamesmanship within the pay system<sup>99</sup>.
- amend 18 U.S.C. section 209 to clarify that it doesn’t prohibit the acceptance of any items that employees are permitted to accept properly under gift rules and statutes.<sup>100</sup>

#### ***D. Training***

1. Contracting officers, program managers and contractors covered by conflict of interest and procurement integrity rules must receive adequate training and counseling to become aware of the issues and effectively perform their work, thus preventing misconduct<sup>101</sup>. Mistakes and failures should be used as case studies.<sup>102</sup>
2. “Regularly assess training and counseling efforts for quality and content, to ensure that individuals covered by conflict-of-interest and procurement integrity rules receive training and counseling that meet standards promulgated by the Department of Defense Standards of Conduct Office.”<sup>103</sup>
3. Department of Defense values and vision should be articulated at the top and flow-down to all employees should be ensured. Integrity, ethical behavior, and compliance with the letter and spirit of the law should be expected and required. An interesting question here is whether “should” ought to be replaced by “shall” making such programs mandatory.
4. Agencies may wish to consider also the possibility of a monitoring or assessment process to ensure that such ethics courses or programs are adequate – this could lead to the emergence and sharing of best practices by sector, policy, activity or specialization.

#### ***E. Contract oversight***

##### 1. Contractor management

Agencies need to efficiently manage contractors as they do their contracting duties. This involves actions by contractor supervisors and program managers so that contract outcomes would improve, thus meeting the public’s interest in getting a good return on the money spent on contracting.<sup>104</sup>

## 2. Ongoing auditing

After the contract is settled, there should be a continual auditing of costs as they come in, so that any egregious spending can be caught before it becomes excessive. Such audits may include itemized lists to prevent over-charging.

## 3. Detection of misconduct

It is essential to improve efforts to detect ethics violations and conflicts of interest by current or former agency officials. Special agents and prosecutors should collaborate at early stages of procurement fraud investigations to assure successful prosecutions and civil recoveries.<sup>105</sup>

## 4. Monitoring and reporting on ethics violations

Ensure ethics officials monitor and report on the status of alleged misconduct to the military services and defense agencies head ethics officials.<sup>106</sup>

## 5. Review contractor ethical standards

Assess, as appropriate, contractor ethics programs in order to facilitate awareness and mitigation of risks in DOD contracting relationships.<sup>107</sup>

## 6. Monitor senior acquisition personnel performance and tenure.

## 7. Department of Defense organizational change

The GAO made the following recommendation regarding oversight of DOD contractors working in support of deployments:

The Secretary of Defense [should] appoint a focal point within the Office of the Under Secretary of Defense for Acquisition, Technology, and Logistics, at a sufficiently senior level and with the appropriate resources, dedicated to leading DOD's efforts to improve contract management and oversight. The entity that functions as the focal point would act as an advocate within the department for issues related to the use of contractors to support deployed forces, serve as the principal advisor for establishing relevant policy and guidance to DOD components, and be responsible for carrying out actions, including the following six actions:

- oversee development of the joint database to provide visibility over all contractor support to deployed forces, including a summary of services or capabilities provided and by-name accountability of contractors;
- develop a strategy for DOD to incorporate the unique difficulties of contract management and oversight at deployed locations into DOD's ongoing efforts to address concerns about the adequacy of its acquisition workforce;
- lead and coordinate the development of a department wide lessons-learned program that will capture the experiences of units that have deployed to locations with contractor support and develop a strategy to apply this institutional knowledge to ongoing and future operations;
- develop the requirement that DOD components, combatant commanders, and deploying units (1) ensure military commanders have access to key information on contractor support, including the scope and scale of contractor support they will rely on and the roles and responsibilities of commanders in the contract management and oversight process, (2) incorporate into their pre-deployment training the need to identify and train contract oversight personnel in their roles and responsibilities, and (3) ensure mission

rehearsal exercises include key contractors to increase familiarity of units preparing to deploy with the contractor support they will rely on;

- develop training standards for the services on the integration of basic familiarity with contractor support to deployed forces into their professional military education to ensure that military commanders and other senior leaders who may deploy to locations with contractor support have the knowledge and skills needed to effectively manage contractors; and
- review the services' efforts to meet the standards and requirements established above to ensure that training on contractor support to deployed forces is being consistently implemented by the services.<sup>108</sup>

## 7. Contractor transaction monitoring

World Check stated “Whilst we do not ordinarily pronounce blanket assessments that certain classes of clients should be classified as high-risk, the large number of unfolding fraud cases involving American defense contractors who operate in Iraq demands that compliance monitoring of such customers be upgraded,” and recommended monitoring the following for banks with clients/customers involved in Iraq reconstruction efforts:

- Wire transfers to countries not involved in the clients' contracting operations.
- Financing of, or cash purchases of consumer items not associated with the clients' business activities.
- Requests for large amounts of US dollar currency, when the client does not pay its people in the field in cash.
- Payments for building construction, improvement and renovation in the US that are far afield from the clients' location.
- Any kind of major business activity that is clearly inconsistent with the clients' trade or business.<sup>109</sup>

## *F. Checks on Undue Influence*

### 1. Limits on campaign contributions

The pre-1976 prohibition on contractor campaign contributions should be reenacted.<sup>110</sup>

### 2. Extension of lobbying ban

The one-year ban on lobbying for congress and their senior staff regarding authorizations or appropriations power should be increased.<sup>111</sup>

### 3. Require contractor consultants to register with the Office of Government Ethics.<sup>112</sup>

The Defense Industry Initiative on Business Ethics and Conduct (DII) presentation before the Acquisitions Advisory Panel in May 2005 offered suggestions on initiatives to be followed by firms in the private sector. It included the following:

#### Principles

- Have and adhere to written Codes of Conduct;
- Train employees in those Codes;
- Encourage internal reporting of violations of the Code, within an atmosphere free of fear of retribution;
- Practice self-governance through the implementation of systems to monitor compliance with federal procurement laws and the adoption of procedures for voluntary disclosure of violations to the appropriate authorities;
- Share with other firms their best practices in implementing the principles, and participate annually in “Best Practices Forums”

#### Expectations for contractor standards of conduct:

- A written code of Business ethics and conduct and ethics training.
- Periodic review of internal controls for compliance with standards of conduct and the special requirements of Government contracting.
- A method for employees to report suspected misconduct, and encouragement to make such reports.
- Internal and/or external audits, as appropriate.
- Disciplinary action for improper conduct.
- Voluntary disclosure to appropriate Government officials of suspected violations of law.
- Cooperation with Government investigation or corrective actions.<sup>113</sup>

## FOOTNOTES

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<sup>1</sup> National Academy of Public Administration, Academy Initiative, “Managing federal missions with a multisector workforce: Leadership for the 21<sup>st</sup> century.” November 16, 2005.

<sup>2</sup>

<sup>3</sup> United States House of Representatives, Committee on Government Reform-Minority Staff, Special Investigation Division, June 2006, “Dollars not sense: Government contracting under Bush Administration”, prepared for Rep. Henry A. Waxman.

<sup>4</sup> Light, 2006, p.1; see also Light Paul “Fact Sheet on The New True Size of Government”, Center for Public Service, The Brookings Institution, Wagner School of Public Service, New York University..

<sup>5</sup> United States House of Representatives, Committee on Government Reform-Minority Staff, Special Investigation Division, June 2006, “Dollars not sense: Government contracting under Bush Administration”, prepared for Rep. Henry A. Waxman.

<sup>6</sup> Marc Davis, “The Government is Already Over-outsourced,” March 3, 2003. available at <http://home.centurytel.net/BehindTheCurtain/Talking%20points%20OverOutsourced%20030727.htm>

<sup>7</sup> Project on Government Oversight (POGO), *The Politics of Contracting*, June 29, 2004, <http://www.pogo.org/p/contracts/c/co-040101-contractor.html#ExecSum>.

<sup>8</sup> Idem.

<sup>9</sup> United States Department of Justice, “Former SOCOM Official Indicted,” press release, November 8, 2005, [http://www.dodig.mil/IGInformation/IGInformationReleases/Spellissy\\_Indictment\\_110805.pdf](http://www.dodig.mil/IGInformation/IGInformationReleases/Spellissy_Indictment_110805.pdf). These acts violated Title 18, United States Code, Sections 201(b)(1)(A) and (B) and 2.

<sup>10</sup> The wired amounts in this case were of a total of \$6,000 (ibid.).

<sup>11</sup> Defense Science Board, *Management Oversight in Acquisition Organizations*. Washington, D.C.: United States Dept. of Defense, Office of the Under Secretary of Defense For Acquisition, Technology, and Logistics, 2005, page 1, [http://www.acq.osd.mil/dsb/reports/2005-03-MOAO\\_Report\\_Final.pdf](http://www.acq.osd.mil/dsb/reports/2005-03-MOAO_Report_Final.pdf).

<sup>12</sup> *U.S. v. Cunningham*, U.S. Dist Ct, SD CA, Plea Agreement, November 23, 2005.

<sup>13</sup> Ken Silverstein, “The Loss of Goss – Why Did the CIA’s Chief Resign So Abruptly,” *Harpers*, May 8, 2006, <http://www.harpers.org/sb-loss-of-goss-3025720.html#>.

<sup>14</sup> Unless otherwise noted, the sources for this part of the report are primarily the court documents, trial transcripts and exhibits in a False Claims Act action.

<sup>15</sup> Chandrasekaran, R. (2006). *Imperial Life in the Emerald City: Inside Iraq's Green Zone*. New York: Alfred A. Knopf, pp. 136-139.

<sup>16</sup> ibid., pp. 139-140.

<sup>17</sup> ibid.

<sup>18</sup> Chandrasekaran, R. (2006), p. 136.

<sup>19</sup> Battles testimony, Feb. 24, 2006. He testified that the book was inspired by the history of Argentina.

<sup>20</sup> Ottenbreit testimony, Feb. 21, 2006.

<sup>21</sup> “Memorandum for record,” Al Runnels, Nov. 6, 2003, entered as Exhibit 115.

<sup>22</sup> F. Shaheen is a lawyer who represents defense contractors

<sup>23</sup> Griff Witte, “Contractors Rarely Held Responsible for Misdeeds in Iraq,” *Washington Post*, Nov. 4, 2006, p. A12; [http://www.washingtonpost.com/wp-dyn/content/article/2006/11/03/AR2006110301585\\_pf.html](http://www.washingtonpost.com/wp-dyn/content/article/2006/11/03/AR2006110301585_pf.html) .

<sup>24</sup> Alan Grayson and Victor Kubli, “Iraq’s Free Fraud Zone,” *The European Lawyer*, November 2006, pp. 70-71.

<sup>25</sup> “A New Truman Committee,” U.S. House of Representatives Appropriations Committee, Democratic staff report, March 8, 2006, pp. 3-4.

<sup>26</sup> Perhaps as much as \$20 million under the next-highest bidder, according to Joseph Morris in his interview with the Defense Criminal Investigative Service, Jan. 15, 2004, a transcript of which is entered as Exhibit 158.

<sup>27</sup> This narrative of the ICE case, and subsequent quotations from witnesses, is based on testimony as reported in transcripts provided by relators’ attorneys.

<sup>28</sup> Baldwin filed a separate claim for personal damages, alleging he was a “whistleblower” against whom Custer Battles illegally retaliated

<sup>29</sup> Tant testimony, Feb. 16, 2006.

<sup>30</sup> Ottenbreit testimony, Feb. 21, 2006.

<sup>31</sup> Battles testimony, Feb. 24, 2006.

<sup>32</sup> Ibid. In subsequent questioning he clarified he had spoken figuratively, and he had no personal knowledge that “nine guys named Ahmed” worked on any Custer Battles projects in Iraq.

<sup>33</sup> Morris interview, op. cit.

<sup>34</sup> Baldwin e-mail, Nov. 6, 2003, entered as Exhibit 114.

<sup>35</sup> Baldwin e-mail, Nov. 12, 2003, entered as Exhibit 119.

<sup>36</sup> Fox e-mail to Battles, Nov. 21, 2003, entered as Exhibit 130.

<sup>37</sup> Ibid. “Eglin” refers to Eglin Federal Prison Camp in Florida, often nicknamed “Club Fed.”

<sup>38</sup> Interoffice memo by Pete Miskovich, March 1, 2004, entered as Exhibit 166.

<sup>39</sup> Brief of the United States, April 1, 2005.

<sup>40</sup> Judge T.S. Ellis III, Memorandum Opinion, July 8, 2005.

<sup>41</sup> Renae Merle, “Verdict Against Iraq Contractor Overturned,” *The Washington Post*, Aug. 19, 2006, p. D1.

<sup>42</sup> Ibid.

<sup>43</sup> Ibid.

<sup>44</sup> SIGIR, July 2005 Quarterly/Semiannual Report.

<sup>45</sup> House Appropriations Democratic staff, op. cit., p.4. Though some individuals have been prosecuted; see below.

<sup>46</sup> Kubli interview.

<sup>47</sup> Farah Stockman, “U.S. Firms Suspected of Bilking Iraq Funds,” *The Boston Globe*, April 16, 2006.

<sup>48</sup> Griff Witte, “Contractors Rarely Held Responsible for Misdeeds in Iraq,” *The Washington Post*, Nov. 4, 2006, p. A12

<sup>49</sup> SIGIR 05-023Jan. 23 2006 at [http://www.sigir.mil/reports/pdf/audits/05-023\\_DFI\\_Contracts-FINAL\\_Report.pdf](http://www.sigir.mil/reports/pdf/audits/05-023_DFI_Contracts-FINAL_Report.pdf)

<sup>50</sup> Office of Management and Budget, Policy Letter 92-1, September 23, 1992, [http://www.whitehouse.gov/omb/procurement/policy\\_letters/92-1\\_092392.html](http://www.whitehouse.gov/omb/procurement/policy_letters/92-1_092392.html),

<sup>51</sup> An illustrative list of inherently governmental functions includes the following:

1. The direct conduct of criminal investigation.
3. The command of military forces, especially the leadership of military personnel who are members of the combat, combat support or combat service support role.
4. The conduct of foreign relations and the determination of foreign policy.
5. The determination of agency policy, such as determining the content and application of regulations, among other things.
6. The determination of Federal program priorities or budget requests.
7. The direction and control of Federal employees. (ibid.)
8. The direction and control of intelligence and counter-intelligence operations.

<sup>52</sup> SIGIR Management of Rapid Regional Response Program Contracts in South-Central Iraq, 05-023, Jan. 23 2006 at [http://www.sigir.mil/reports/pdf/audits/05-023\\_DFI\\_Contracts-FINAL\\_Report.pdf](http://www.sigir.mil/reports/pdf/audits/05-023_DFI_Contracts-FINAL_Report.pdf)

<sup>53</sup> Special Inspector General Stuart Bowen interviewed by Robin Wright, *The Washington Post* November 9, 2005; <http://www.washingtonpost.com/wp-dyn/content/article/2005/11/08/AR2005110801514.html> .

<sup>54</sup> Special Inspector General for Iraq Reconstruction, “January 30, 2007 Quarterly and Semiannual Report to Congress Report,” January 30, 2007, [http://www.sigir.mil/reports/quarterlyreports/Jan07/pdf/Report\\_-\\_January\\_2007.pdf](http://www.sigir.mil/reports/quarterlyreports/Jan07/pdf/Report_-_January_2007.pdf).

<sup>55</sup> Idem at 135.

<sup>56</sup> Idem, at 136.

<sup>57</sup> Idem at 201.

<sup>58</sup> Idem at 202.

<sup>59</sup> Idem at 203.

<sup>60</sup> Kenneth Rijock, “Are American Defence Contractors Working in Iraq Now High Risk?” World-Check, February 17, 2007, <http://www.world-check.com/articles/2007/02/17/are-american-defence-contractors-working-iraq-now-/>.

<sup>61</sup> United Nations Guide for Anti-corruption policies, UN Office on Drugs and Crime November 2003 pages 1-4

<sup>62</sup> See Legislative Guide for the implementation of the UN Convention against Corruption at [http://www.unodc.org/pdf/corruption/CoC\\_LegislativeGuide.pdf](http://www.unodc.org/pdf/corruption/CoC_LegislativeGuide.pdf)

<sup>63</sup> United States Department of Commerce, International Trade Administration, “Addressing the Challenges of International Bribery and Fair Competition 2004”, The Sixth Annual Report under Section 6 of the International Anti-Bribery and Fair Competition Act of 1998.

<sup>64</sup> Fighting corporate and Government Wrongdoing: A research Guide to International and U.S. Federal Laws on White-Collar Crime and Corruption www.llrx.com

<sup>65</sup> World Bank, *Anticorruption Report*, 2005, <http://web.worldbank.org/WBSITE/EXTERNAL/TOPICS/EXTPUBLICSECTORANDGOVERNANCE/EXTANTICORRUPTION/0,,menuPK:384461~pagePK:149018~piPK:149093~theSitePK:384455,00.html>

<sup>66</sup> U.S. Merit Systems Protections Board, “Contracting Officer Representatives: Managing the Government’s Technical Experts to Achieve Positive Contract Outcomes,” December 2005, p. i, [http://www.mspb.gov/studies/cor\\_abridgedpdf.pdf](http://www.mspb.gov/studies/cor_abridgedpdf.pdf).

<sup>67</sup> J. Olaya, “Blacklisting Corrupt Companies,” *Global Corruption Report*, 2005, [http://www.globalcorruptionreport.org/gcr2005/download/english/intel\\_finance\\_and\\_corruption.pdf](http://www.globalcorruptionreport.org/gcr2005/download/english/intel_finance_and_corruption.pdf).

<sup>68</sup> Jenny Mandel, “Military Justice Code Now Covers Some Contractors,” January 9, 2007, GovExec.com, [http://www.govexec.com/story\\_page.cfm?articleid=35830&printerfriendlyVers=1&](http://www.govexec.com/story_page.cfm?articleid=35830&printerfriendlyVers=1&).

<sup>69</sup> P.W. Singer, “The Law Catches up to Private Militaries, Embeds,” Defensetech.org, January 3, 2007, <http://www.defensetech.org/archives/003123.html>.

<sup>70</sup> Adam Davidson and Mark Schapiro, “The Spoils of War.” Center for Investigating Reporting, April 22, 2004, [http://muckraker.org/pg\\_one\\_investigation-1193-2-0-Spoils%20of%20War.html](http://muckraker.org/pg_one_investigation-1193-2-0-Spoils%20of%20War.html).

<sup>71</sup> M.J. Hogan, M.A. Long, P.B. Stretesky, and M.J. Lynch, “Campaign Contributions, Post-war Reconstruction Contracts, and State Crime,” *Deviant Behavior*, 27(3), 2006.

<sup>72</sup> Griff Witte, “Contractors Rarely Held Responsible for Misdeeds in Iraq,” *The Washington Post*, November 4, 2006, p. A12.

<sup>73</sup> Ibid.

<sup>74</sup> Nina Gregory, “Homeland Security’s ‘Procurement’ Predicament,” Homeland Security National Imperative or Business as Usual News Initiative, July 25, 2006, [http://newsinitiative.org/story/2006/07/25/homeland\\_securitys\\_procurement\\_predicament-oultn](http://newsinitiative.org/story/2006/07/25/homeland_securitys_procurement_predicament-oultn).

<sup>75</sup> Defense Science Board, *Management Oversight in Acquisition Organizations*. Washington, D.C.: United States Dept. of Defense, Office of the Under Secretary of Defense For Acquisition, Technology, and Logistics, 2005, page 2, [http://www.acq.osd.mil/dsb/reports/2005-03-MOAO\\_Report\\_Final.pdf](http://www.acq.osd.mil/dsb/reports/2005-03-MOAO_Report_Final.pdf).

<sup>76</sup> Jenny Mandel, “Panel Aims to Increase Competition for Services Contracts,” GovExec.com, July 25, 2006, www.govexec.com.

<sup>77</sup> Dan Guttman, “Who is Doing Work for Government? Monitoring, Accountability and Competition in the Federal and Service Contract Workforce” Testimony before the U.S. Senate Committee on Governmental Affairs, March 6, 2002, <http://www.senate.gov/~govt-aff/030602guttman.htm>

<sup>78</sup> Defense Science Board.

<sup>79</sup> General Accounting Office (GAO), “Highlights of a GAO Forum – Federal Acquisition Challenges and Opportunities in the 21<sup>st</sup> Century,” October 2006, GAO-07-45SP, <http://www.gao.gov/new.items/d0745sp.pdf>

<sup>80</sup> Defense Science Board.

<sup>81</sup> Idem.

<sup>82</sup> Idem.

<sup>83</sup> Defense Science Board, page 3.

<sup>84</sup> Karen Rutzick, “Lawmakers Move to Extend Ethics Requirements” GovExec.com, April 7, 2006, www.govexec.com.

<sup>85</sup> These are based on interviews with OGE officials and M. Glynn’s comments before the Acquisition Advisory Panel in May 2005, available at <http://www.acquisition.gov/comp/aap/documents/05%2017%2005%20Panel%20Meeting%20Minutes.pdf>

<sup>86</sup> See 48 CFR 970.0371, [http://a257.g.akamaitech.net/7/257/2422/12feb20041500/edocket.access.gpo.gov/cfr\\_2004/octqtr/pdf/48cfr970.0371-6.pdf](http://a257.g.akamaitech.net/7/257/2422/12feb20041500/edocket.access.gpo.gov/cfr_2004/octqtr/pdf/48cfr970.0371-6.pdf)

<sup>87</sup> M. Glynn comments before the Acquisition Advisory Panel in May 2005. See FDA AS No. 1337 (Section H), 11/30/99



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- <sup>88</sup> Evelyn Bandoh, "Outsourcing the Delivery of Human Services," <http://www.win.com>; and Project on Government Oversight (POGO) "Federal Contracting and Iraq Reconstruction," March 11, 2004, <http://www.pogo.org/p/contracts/co-040301-iraq.html>.
- <sup>89</sup> M.J. Hogan, M.A. Long, P.B. Stretesky, and M.J. Lynch, "Campaign Contributions, Post-war Reconstruction Contracts, and State Crime," *Deviant Behavior*, 27(3), 2006.
- <sup>90</sup> Defense Science Board.
- <sup>91</sup> *Idem*.
- <sup>92</sup> *Idem*.
- <sup>93</sup> Project on Government Oversight (POGO), "Federal Contractor Misconduct: Failures of the Suspension and Debarment System," May 10, 2002, <http://www.pogo.org/p/contracts/co-020505-contractors.html>.
- <sup>94</sup> *Idem*.
- <sup>95</sup> *Idem*.
- <sup>96</sup> Summarized and near verbatim. POGO, "Federal Contractor Misconduct," Recommendations, <http://pogo.org/p/contracts/c/co-040101-contractorb.html#pogorecommendations>.
- <sup>97</sup> Project on Government Oversight (POGO), "Presentation Before the Interagency Ethics Council," April 6, 2006, <http://www.pogo.org/m/cp/cp-POGOEthics-04062006.pdf>.
- <sup>98</sup> *Idem*.
- <sup>99</sup> Tom Shoop, "Ethics Office Seeks to Extend Post-employment 'Cooling Off' Period to All of SES," January 27, 2006, <http://www.govexec.com>.
- <sup>100</sup> Office of Government Ethics, Report to the President and to Congressional Committees on the Conflict of Interest Laws Relating to Executive Branch Employment, January 2006, pages 39-40.
- <sup>101</sup> Government Accountability Office (GAO), "Defense Ethics Program: Opportunities Exist to Strengthen Safeguards for Procurement Integrity: Report to Congressional Requesters," Washington, D.C.: U.S. Government Accountability Office, 2005.
- <sup>102</sup> Defense Science Board, page 2
- <sup>103</sup> GAO, "Defense Ethics Program."
- <sup>104</sup> U.S. Merit Systems Protection Board, "Contracting Officer Representatives: Managing the Government's Technical Experts to Achieve Positive Contract Outcomes," December 2005, page 50, [http://www.mspb.gov/studies/cor\\_abridgedpdf.pdf](http://www.mspb.gov/studies/cor_abridgedpdf.pdf).
- <sup>105</sup> U.S. Department of Justice 2006, "Combating Procurement Fraud: A National Initiative to Increase Prevention and Prosecution of Fraud in the Federal Procurement Process" Federal Bureau of Investigation; available at <http://www.usdoj.gov/criminal/npftf/pr/speeches/2006/oct/10-10-06npftfinitiative.pdf>
- <sup>106</sup> GAO, "Defense Ethics Program." Near verbatim.
- <sup>107</sup> *Idem*.
- <sup>108</sup> General Accounting Office, "High-Level DOD Action Needed to Address Long-standing Problems with Management and Oversight of Contractors Supporting Deployed Forces," December 2006, GAO-07-145, pp. 36-7, <http://www.gao.gov/new.items/d07145.pdf>.
- <sup>109</sup> Edited, verbatim bullet points from Kenneth Rijock, "Are American Defence Contractors Working in Iraq Now High Risk?" World-Check, February 17, 2007, <http://www.world-check.com/articles/2007/02/17/are-american-defence-contractors-working-iraq-now/>.
- <sup>110</sup> POGO, "Federal Contractor Misconduct," Recommendations. Near verbatim.
- <sup>111</sup> *Idem*.
- <sup>112</sup> *Idem*.
- <sup>113</sup> Defense Industry Initiative on Business Ethics and Conduct presentation before the Acquisition Advisory Panel in May 2005, available at <http://www.acquisition.gov/comp/aap/documents/05%2017%2005%20Panel%20Meeting%20Minutes.pdf>