

CLOSE THE CONTRACTOR FRAUD LOOPHOLE ACT

APRIL 22, 2008.—Committed to the Committee of the Whole House on the State of  
the Union and ordered to be printed

Mr. WAXMAN, from the Committee on Oversight and Government  
Reform, submitted the following

R E P O R T

together with

ADDITIONAL VIEWS

[To accompany H.R. 5712]

[Including cost estimate of the Congressional Budget Office]

The Committee on Oversight and Government Reform, to whom  
was referred the bill (H.R. 5712) to require disclosure by Federal  
contractors of certain violations relating to the award or perform-  
ance of Federal contracts, having considered the same, report fa-  
vorably thereon with an amendment and recommend that the bill  
as amended do pass.

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The amendment is as follows:

Strike all after section 1 and insert the following:

**SEC. 2. REVISION OF THE FEDERAL ACQUISITION REGULATION.**

The Federal Acquisition Regulation shall be amended within 180 days after the date of the enactment of this Act pursuant to FAR Case 2007-006 (as published at 72 Fed Reg. 64019, November 14, 2007) or any follow-on FAR case to include provisions that require timely notification by Federal contractors of violations of Federal criminal law or overpayments in connection with the award or performance of covered contracts or subcontracts, including those performed outside the United States and those for commercial items.

**SEC. 3. DEFINITION.**

In this Act, the term “covered contract” means any contract in an amount greater than \$5,000,000 and more than 120 days in duration.

**PURPOSE AND SUMMARY**

H.R. 5712, the Close the Contractor Fraud Loophole Act, was introduced by Rep. Peter Welch on April 3, 2008. The bill, as amended, mandates that the Federal Acquisition Regulation be amended within 180 days to require contractors to report violations of federal criminal law and over-payments on contracts over \$5 million, including contracts performed overseas and commercial item contracts.

**BACKGROUND AND NEED FOR LEGISLATION**

Each year the federal government spends billions of dollars to procure goods and services, making federal contracts one of the fastest growing components of the federal budget. In fiscal year 2006, the federal government spent over \$400 billion through contracts.

The steady increase in federal spending and recent high-profile criminal and civil matters involving federal contractors has heightened the need to detect, investigate, and prosecute fraud in overseas contracting. This Committee’s investigations have uncovered millions of dollars in wasteful and fraudulent spending on contracts overseas. To date, the Department of Justice (DOJ) has charged 46 individuals and companies for contract fraud relating to contracts in Afghanistan, Kuwait, and Iraq. However, overseas contracts were exempted from a proposed rule requiring fraud reporting by contractors.

On May 23, 2007, DOJ requested that the Federal Acquisition Regulation be amended to “require contractors to establish and maintain internal controls to detect and prevent fraud in their contracts, and . . . notify contracting officers without delay whenever they become aware of a contract overpayment or fraud, rather than wait for its discovery by the government.”<sup>1</sup> DOJ believed such a rule was necessary because few government contractors have complied with the existing voluntary disclosure program. DOJ proposed specific changes to the Federal Acquisition Regulation.

In response, on November 14, 2007, the Civilian Agency Acquisition Council and the Defense Acquisition Regulations Council published a proposed rule on “Contractor Compliance Program and Integrity Reporting.” This rule requires contractors to have a code of ethics and business conduct, to establish and maintain specific in-

<sup>1</sup> Letter from Assistant Attorney General Alice Fisher to Administrator for Federal Procurement Policy Paul Denett (May 23, 2007).

ternal controls to detect and prevent improper conduct in connection with the award or performance of government contracts or subcontracts, and to notify contracting officers without delay whenever they become aware of violations of federal criminal law with regard to such contracts or subcontracts.

However, the proposed rule on fraud reporting added two exemptions not included in the DOJ proposal: an exemption for contracts to be performed outside of the United States and a second exemption for contracts for commercial items.

On January 14, 2008, DOJ filed a comment on the proposed rule stating that “we do not agree with” the exemption for overseas contracts. According to DOJ, “[a]lthough these contracts may be performed outside the United States, the United States still is a party to these contracts and potentially a victim when overpayments are made or when fraud occurs in connection with the contracts. Under these circumstances, the government still maintains jurisdiction to prosecute the perpetrators of the fraud. Moreover, these types of contracts, which in many cases support our efforts to fight the global war on terror, need greater contractor vigilance because they are performed overseas where U.S. government resources and remedies are more limited.”<sup>2</sup> Another comment filed by the American Bar Association questioned whether the acquisition councils had statutory authority to create a fraud reporting requirement by regulation.

H.R. 5712, the Close the Contractor Fraud Loophole Act, as amended, directs that the FAR be amended within 180 days to mandate a fraud reporting requirement for all contracts above \$5 million. This bill requires that the fraud reporting regulations apply to contracts performed outside of the United States and to commercial item contracts, and gives clear statutory authority to require reporting of violations of federal criminal law and overcharges in regulations.

#### LEGISLATIVE HISTORY

H.R. 5712, the Close the Contractor Fraud Loophole Act, was introduced by Rep. Peter Welch on April 3, 2008, and was referred to the Committee on Oversight and Government Reform.

The Subcommittee on Government Management, Organization, and Procurement held a hearing on H.R. 5712 on April 15, 2008. The witnesses were Paul Denett, Administrator for Federal Procurement Policy, Office of Management and Budget; Barry Sabin, Deputy Assistant Attorney General, Criminal Division, U.S. Department of Justice; David Drabkin, Acting Chief Acquisition Officer and Senior Procurement Executive, General Services Administration; and Colleen Preston, Executive Vice President, Professional Services Council.

The Committee held a markup to consider H.R. 5712 on April 16, 2008, and ordered the bill, as amended, to be favorably reported by voice vote.

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<sup>2</sup>Letter from Assistant Attorney General Alice Fisher to GSA Regulatory Secretariat (Jan. 14, 2008).

## SECTION-BY-SECTION

*Section 1. Short title*

The short title of the bill is the Close the Contractor Fraud Loop-hole Act.

*Section 2. Revision of the Federal Acquisition Regulation*

As amended, this section requires that the Federal Acquisition Regulation be amended within 180 days to include provisions that require timely notification by federal contractors of violations of federal criminal law or overpayments in connection with the award or performance of covered contracts and subcontracts of covered contracts, including those performed outside the United States and those for commercial items.

*Section 3. Definition*

As amended, this section defines “covered contract” as any contract in an amount greater than \$5,000,000 and more than 120 days in duration.

## EXPLANATION OF AMENDMENTS

Mr. Waxman and Mr. Davis offered an amendment, passed by voice vote, to implement a mandatory fraud reporting requirement through revision of the Federal Acquisition Regulation rather than directly by statute.

## COMMITTEE CONSIDERATION

On Wednesday, April 16, 2008, the Committee met in open session and favorably ordered H.R. 5712 to be reported, as amended, to the House by a voice vote.

## ROLLCALL VOTES

No rollcall votes were held.

## APPLICATION OF LAW TO THE LEGISLATIVE BRANCH

Section 102(b)(3) of Public Law 104–1 requires a description of the application of this bill to the legislative branch where the bill relates to terms and conditions of employment or access to public services and accommodations. The bill does not relate to employment or access to public services and accommodations.

## STATEMENT OF OVERSIGHT FINDINGS AND RECOMMENDATIONS OF THE COMMITTEE

In compliance with clause 3(c)(1) of rule XIII and clause (2)(b)(1) of rule X of the Rules of the House of Representatives, the Committee’s oversight findings and recommendations are reflected in the descriptive portions of this report.

## STATEMENT OF GENERAL PERFORMANCE GOALS AND OBJECTIVES

In accordance with clause 3(c)(4) of rule XIII of the Rules of the House of Representatives, the Committee’s performance goals and objectives are reflected in the descriptive portions of this report, including improving compliance with federal law.

## CONSTITUTIONAL AUTHORITY STATEMENT

Under clause 3(d)(1) of rule XIII of the Rules of the House of Representatives, the Committee must include a statement citing the specific powers granted to Congress to enact the law proposed by H.R. 5712. Article I, Section 8, Clause 18 of the Constitution of the United States grants the Congress the power to enact this law.

## FEDERAL ADVISORY COMMITTEE ACT

The Committee finds that the legislation does not establish or authorize the establishment of an advisory committee within the definition of 5 U.S.C. App., Section 5(b).

## UNFUNDED MANDATES STATEMENT

Section 423 of the Congressional Budget and Impoundment Control Act (as amended by Section 101(a)(2) of the Unfunded Mandates Reform Act, P.L. 104-4) requires a statement on whether the provisions of the report include unfunded mandates. In compliance with this requirement the Committee has received a letter from the Congressional Budget Office included herein.

## EARMARK IDENTIFICATION

H.R. 5712 does not include any congressional earmarks, limited tax benefits, or limited tariff benefits as defined in clause 9(d), 9(e), or 9(f) of rule XXI.

## COMMITTEE ESTIMATE

Clause 3(d)(2) of rule XIII of the Rules of the House of Representatives requires an estimate and a comparison by the Committee of the costs that would be incurred in carrying out H.R. 5712. However, clause 3(d)(3)(B) of that rule provides that this requirement does not apply when the Committee has included in its report a timely submitted cost estimate of the bill prepared by the Director of the Congressional Budget Office under section 402 of the Congressional Budget Act.

BUDGET AUTHORITY AND CONGRESSIONAL BUDGET OFFICE COST  
ESTIMATE

With respect to the requirements of clause 3(c)(2) of rule XIII of the Rules of the House of Representatives and section 308(a) of the Congressional Budget Act of 1974 and with respect to requirements of clause 3(c)(3) of rule XIII of the Rules of the House of Representatives and section 402 of the Congressional Budget Act of 1974, the Committee has received the following cost estimate for H.R. 5712 from the Director of the Congressional Budget Office:

APRIL 18, 2008.

Hon. HENRY A. WAXMAN,  
*Chairman, Committee on Oversight and Government Reform,*  
*House of Representatives, Washington, DC.*

DEAR MR. CHAIRMAN: As you requested, the Congressional Budget Office has prepared the enclosed cost estimate for H.R. 5712, the Close the Contractor Fraud Loophole Act.

If you wish further details on this estimate, we will be pleased to provide them. The CBO staff contact is Matthew Pickford.

Sincerely,

PETER R. ORSZAG.

Enclosure.

*H.R. 5712—Close the Contractor Fraud Loophole Act*

H.R. 5712 would amend the Federal Acquisition Regulation primarily to require certain contractors working outside of the United States to notify the government of any criminal violations of U.S. laws or any contract overpayments that occur while performing such contracts. According to the Office of Management and Budget and the General Services Administration, the Administration is in the process of implementing similar requirements. Thus, CBO estimates that implementing H.R. 5712 would have no significant impact on agencies' spending.

Enacting the legislation could increase revenues from civil and criminal fines that could be imposed on those who violate the amended regulations. Collections of civil fines are recorded in the budget as receipts (that is, revenues) and deposited into the general fund of the Treasury. Criminal fines are also recorded as receipts, which are deposited in the Crime Victims Fund and spent in subsequent years. CBO expects that any additional revenues or direct spending associated with civil and criminal fines would total less than \$500,000 each year.

The bill contains no intergovernmental or private-sector mandates as defined in the UMRA and would not affect the budgets of state, local, or tribal governments.

The CBO staff contact for this estimate is Matthew Pickford. The estimate was approved by Peter H. Fontaine, Assistant Director for Budget Analysis Division.

CHANGES IN EXISTING LAW MADE BY THE BILL, AS REPORTED

No changes to existing law are made by H.R. 5712, as reported.

## ADDITIONAL VIEWS

I had serious concerns about H.R. 5712 as originally introduced. The bill would have provided that a knowing failure to report violations of criminal law and overpayments related to a federal contract can be a cause for debarment or suspension for all firms, including those holding contracts performed overseas and contracts for commercial items. It was an attempt to “strengthen” an ethics compliance program currently under development by the Administration.

In actuality, the bill as introduced did not make as significant a change as intended to the substance of the proposed revisions to the acquisition regulations. Even without H.R. 5712, the proposed regulations would have applied the enforcement of debarment and suspension for failure to report to all firms, including those holding contracts performed overseas and contracts for commercial items. The problem was the bill leapfrogged the statutorily-designated process for writing acquisition regulations and would have encased in statute a new reporting scheme yet to be thoroughly vetted.

The concept of mandatory reporting by contractors of possible criminal violations based on “reasonable grounds” is unprecedented and controversial. The rule was the subject of more than 70 comments. As expected, many of the firms subject to the rule expressed serious and legitimate concerns about the concept and the wording of the proposal.

During the one hearing held by the Subcommittee on Government Management, Organization and Procurement, none of the agencies providing testimony, including the Department of Justice, nor the contractor community, supported H.R. 5712 as introduced. Instead, the stakeholders suggested the well-established regulatory drafting process should be allowed to continue to completion. They favored this approach because it would allow all interested parties the opportunity to submit comments and have those comments considered in the deliberative process.

The amendment adopted by the Committee ensures the Federal Acquisition Regulation is revised to include a requirement that federal contractors notify the government of violations of federal criminal law or overpayments in connection with the award or performance of contracts or subcontracts—and it will ensure the regulation is applicable to all contracts, including those performed overseas and those for commercial items. The key is the amendment does not mirror the proposed regulation’s preliminary language but will leave the precise wording to the regulation writers. The stated purposes of H.R. 5712 ultimately will be accomplished—but accomplished through the more appropriate acquisition rulemaking process.

These changes make H.R. 5712 a better bill, but not a bill I believe should be pursued. All interested parties would be better

served if the Committee had spent its time attempting to improve the operation of the federal acquisition system—in order to better acquire the best value goods and services the government so desperately needs. Furthermore, the Committee should have allowed the regulatory process to go forward without any interference at all. Nonetheless, under the circumstances, I accept this bill as an adequate solution.

