

Senate Democratic Policy Committee Hearing

“An Oversight Hearing on Whether the Army Corps of Engineers Retaliated Against Whistleblowers Who Objected to Iraq Contracting Abuses”

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Thank you, Mr. Chairman, for the opportunity to address the Democratic Policy Committee on these pressing issues of procurement policy, in the wake of the horrific damage caused by Hurricane Katrina. Our public procurement law program at The George Washington University Law School is the leading program of its kind in the nation, and we appreciate the opportunity to review these important policy issues with the Committee.

Ironically, the problems that are emerging in post-Katrina contracting¹ in many ways echo the problems that emerged in Iraqi reconstruction contracting, and which Ms. Bunnatine Greenhouse has had to address.

On September 8, 2005, the President signed the second supplemental emergency appropriation of \$52 billion for Hurricane Katrina relief. That legislation included major changes to procurement law, including a provision that exempted Katrina-related procurement, up to \$250,000 per contract, from all normal federal procurement requirements.

This new exception means that Katrina relief procurements up to \$250,000 can be made without competition, and out of the public view. This new exception therefore raises serious concerns that the same problems that dogged U.S. contracting in Iraq – failures in competition, failures in transparency, and failures in integrity – will arise again in the Hurricane Katrina relief effort.

¹ See, e.g., Renae Merle, “Audit Teams to Monitor Relief Money,” *Washington Post*, Sept. 14, 2005, at D03; Ellen McCarthy, “Cleanup Cash Goes to Familiar Faces,” *Washington Post*, Sept. 12, 2005, at D01. House Democratic leaders reviewed some of these concerns regarding potential misuse of Hurricane Katrina relief funds in a September 13, 2005 letter to Comptroller General David M. Walker, in which the leaders asked for “[i]mmediate and intensive GAO oversight” of the funds being spent in the relief effort. See Letter to David M. Walker (Sept. 13, 2005), available at <http://www.democrats.reform.house.gov/Documents/20050913120920-64050.pdf>.

Extraordinary Procurement Exceptions Allowed as Part of \$52 Billion Second Supplemental Hurricane Katrina Emergency Appropriation

As noted, on September 8, 2005,² the President signed the second supplemental appropriation of \$52 billion for Hurricane Katrina relief.³ The bill had been introduced only the previous day, September 7, 2005. Included in the legislation were provisions which, with regard to “property or services determined by the head of an executive agency to be used in support of Hurricane Katrina rescue and relief operations”:

- Raise the micro-purchase threshold from \$2,500 to \$250,000, and
- Allow the use of simplified acquisition procedures for contracts up to \$10 million.⁴

Of the two exceptions, the radically increased micro-purchase exception has probably garnered the most attention (and criticism).⁵ Representative Henry Waxman criticized the proposed new exception as potentially dangerous in a September 8, 2005 letter,⁶ and Senators Charles Grassley, Susan Collins and Joseph Lieberman signed a letter opposing raising the micro-purchase limit, because of concerns regarding oversight and accountability for spending.⁷

In response to those concerns, the Administration has announced various protective measures,⁸ discussed further below. It appears, however, that those additional protections will not address the core problem with the new procurement exceptions: under the new law, agencies will be able to spend billions of relief dollars without any of the competition, transparency and other legal rules that normally protect our procurement system.

² On September 8, President Bush also issued a proclamation that suspended, indefinitely, application of the Davis-Bacon Act to federal contracts entered into across storm-ravaged counties in Alabama, Florida, Louisiana and Mississippi. (Available at <http://www.whitehouse.gov/news/releases/2005/09/20050908-5.html>.) AFL-CIO president John Sweeney promptly denounced the President's action as “outrageous.” See Thomas B. Edsall, “Bush Suspends Pay Act in Areas Hit by Storm,” *Washington Post*, Sept. 9, 2005, at D03. The President's proclamation means, in effect, that the wage guarantees of the Davis-Bacon Act will not apply to *any* federal contracts – whether related to reconstruction or not – across a broad swath of the South. Excepting federal procurement from wage rules such as the Davis-Bacon Act (or, for example, the Service Contract Act) reduces barriers to entry in the federal marketplace, but can have profound impacts on a labor market. My focus today, however, is on other procurement exceptions that have been enacted since Hurricane Katrina, which undermine the competition and transparency at the heart of the U.S. procurement system.

³ See H.R. 3673, now Public Law No. 109-62, available at thomas.loc.gov. See Appendix A, below.

⁴ As noted, the relevant legislative provisions are included in an appendix to this statement.

⁵ See, e.g., Yochi J. Dreazen, “No-Bid Contracts Win Katrina Work,” *Wall Street Journal*, Sept. 12, 2005, at A3.

⁶ Available at http://www.yubanet.com/artman/publish/article_24827.shtml.

⁷ See Peter Baker & Amy Goldstein, “Congress Approves \$51.8 Billion for Victims,” *Washington Post*, Sept. 9, 2005, at A01.

⁸ See, e.g., Amelia Gruber, “Procurement Provision in Hurricane Bill Raises Eyebrows,” *Government Executive*, Sept. 9, 2005 (available at www.govexec.com).

Micro-Purchase Threshold Normally \$2,500, Up to \$15,000 in Domestic Emergencies – New Limit of \$250,000 Never Previously Discussed

Traditionally the micro-purchase threshold rested at \$2,500, and certain critical procurements, such as those for contingency operations, had been subject to higher micro-purchase thresholds of \$15,000 (in domestic emergencies) and \$25,000 (for foreign emergencies).⁹ Until Hurricane Katrina, however, there was never any serious public discussion of raising the standard micro-purchase cap a hundred times over, to \$250,000.

The broadened micro-purchase exception, which reportedly was added at the request of the Administration,¹⁰ drew concern on the House floor during the bill's abbreviated debate. In practice, the increased micro-purchase exception will likely mean that most normal procurement requirements, including special protections for small-business contractors, will not apply to post-Katrina reconstruction contracts up to \$250,000.

Micro-Purchases Are Exempt From Almost All Procurement Rules – Thus, New \$250,000 Micro-Purchase Cap Threatens Competition, Transparency and Small Businesses and Other Socioeconomic Concerns

The radically increased exception for micro-purchases raises concerns for the small business community, which depends on the FAR's special protections for small businesses.¹¹ During House debate of the bill, Representative Donald Manzullo noted that, as chairman of the House Committee on Small Business, he was concerned that the law may, in effect, hurt small businesses' ability to "play a significant role in the recovery."¹²

Congressman Manzullo's concerns were sound – the new exemptions will indeed leave small businesses without any of their normal protections in federal procurement – but those concerns are also merely the tip of a much larger problem.

To understand why, it is important to remember that procurements under the micro-purchase threshold (traditionally, \$2,500) are generally exempt from all procurement requirements. (The current micro-purchase rules are set out in an Appendix to this statement.) As procurement expert Karen Manos has pointed out, **purchases of supplies or services at or below the micro-purchase threshold "are exempt from virtually all procurement laws, and do not require any clauses or contract provisions other than those necessary to make payment by electronic funds transfer."** As a result, "micro-purchases are not subject to CAS [Cost Accounting Standards], TINA [Truth in Negotiations Act], the cost principles, or any Government audit requirements."¹³ While the statutory exemptions for micro-purchases are somewhat skeletal,¹⁴ the regulations that implement the micro-purchase exception state explicitly

⁹ See FAR 13.201. As noted, the current Federal Acquisition Regulation provisions on micro-purchases are included in an appendix to this statement.

¹⁰ See Representative Waxman's letter, cited *supra*.

¹¹ See, e.g., "Small Business Contracting Provisions in H.R. 3673," *Congressional Record*, Sept. 9, 2005, at S9875 (criticism by Senator Snowe).

¹² See *Congressional Record*, at H7782 (Sept. 8, 2005).

¹³ Karen L. Manos, 1 *Government Contract Costs & Pricing* § 2:E:2 (West/Thomson 2004).

¹⁴ See 41 U.S.C. § 428.

that, though additional requirements *may* be imposed by the customer agency, micro-purchases are exempt from almost all the normal contractual provision and clauses.

By raising the micro-purchase exemption from \$2,500 to \$250,000, the new law likely means, in practice, that thousands of purchases across the federal government – so long as they are below \$250,000, and can be linked to the hurricane relief efforts – will be exempt from the normal panoply of procurement requirements. Those purchases will be exempt from competition, from small business and other socioeconomic requirements, and from many other federal procurement requirements. With one stroke, thousands of federal purchases, worth potentially billions of dollars, have been stripped out of the federal procurement apparatus.

Higher Micro-Purchase Cap Encourages Government Purchase Card Abuse, and May Undermine Contract Enforcement

There is an even darker side to this micro-purchase exemption, as Congressman Waxman's letter of September 8 pointed out. Government purchase cards, which have often been misused, are now open to even more serious abuse.¹⁵ Until now, the low micro-purchase threshold (\$2,500) has capped the amount for which authorized users can purchase *and* pay for supplies using government purchase cards, outside the normal competitive procurement process. Now, with the cap lifted to \$250,000 for hurricane-relief purchases, authorized government credit card holders will be able, in one sitting, to purchase and pay for hundreds of thousands of dollars in goods, without any real check on their actions. The potential for abuse is staggering.

There is another long-term problem tucked away in this expanded micro-purchase exemption. Micro-purchases, because they are exempt from most federal procurement requirements, are also by definition exempt from most enforcement actions grounded in those requirements. This new, vastly expanded exemption may well entangle enforcement actions far into the future, for vendors subject to investigation and enforcement will likely argue that at least some of the contracting actions under review were hurricane-relief efforts that came under this high micro-purchase exemption. For years to come, therefore, federal contracting enforcement officials may be struggling with the unforeseen effects of Hurricane Katrina.

¹⁵ As my colleague, Professor Steven Schooner, noted in a recent op-ed piece in the *L.A. Times*:

A mountain of inspector general reports, Government Accountability Office studies and congressional hearings demonstrate that the government's management of its charge cards is abysmal. For the last decade, government agencies blindly chased rebates while ignoring the best practices of corporate charge card programs. Agencies affirmatively resisted investing in smart card technologies and transaction data mining. . . . Not surprisingly, numerous government employees misused their cards.

Steven L. Schooner, Commentary: "Fiscal Waste? Priceless," *L.A. Times*, Sept. 14, 2005, available at <http://www.latimes.com/news/opinion/commentary/la-oe-schooner14sep14.0,1567465.story>.

New Law Also Relaxes Competition Requirements Up to \$10 Million

Nor will the problems stem only from micro-purchases. Beyond the micro-purchase exemption, as noted the new law allows hurricane-relief procurements to use special “streamlined” competitive procedures. The new law allows any agency doing relief-related procurement up to \$10 million to use special emergency procurement procedures.¹⁶ Those special procurement procedures, which are set out in regulation in FAR Subpart 13.5, require minimal, if any, competition. This means, in practice, that agencies embarked on relief efforts will be able to make procurements up to \$10 million without what we would consider full and open competition – a marked departure from the competition requirements that are the cornerstone to our procurement system.

Were These Extraordinary Exceptions Necessary?

Did the federal government need these exceptions to clean up after Katrina? Probably not. The procurement reforms of the mid-1990s created a system with extraordinary flexibility, including streamlined competitions and task-order contracts that can be used to procure goods and services in minutes. The system was flexible enough to respond to the September 11 attacks,¹⁷ and it was in all likelihood flexible enough to respond to Hurricane Katrina. At the very least, it would have been impossible to tell, in the few days after the hurricane, whether these deep exemptions will be necessary over the coming years of reconstruction.

It is important to recognize that, in the days before the September 8 legislation was signed by the President, federal agencies were already using *existing* authority for flexible emergency procurement to respond to Hurricane Katrina¹⁸:

- On September 1, 2005, the Navy Supply Systems Command issued an order confirming more liberal contracting rules, as a result of the contingency operations to respond to Hurricane Katrina.
- On September 2, 2005, the Under Secretary of Defense for Acquisition, Technology & Logistics raised the limits for micro-purchases to \$15,000, and authorized commercial item streamlined procurements to \$10 million.

¹⁶ These special procedures are authorized by 41 U.S.C. §§ 428a(c) and 427(a)(2), and by 10 U.S.C. § 2304(g)(1)(B).

¹⁷ In the wake of the September 11, 2001 terrorist attacks, the federal government committed approximately \$20 billion in disaster assistance to the New York City area. See U.S. General Accounting Office, *September 11: Overview of Federal Disaster Assistance to the New York City Area*, GAO Rep. No. GAO-04-72 (Oct. 2003), available at www.gao.gov.

¹⁸ Acquisition Solutions, Inc., a leading consulting firm in government procurement, has prepared a very thorough summary of agencies’ special procurement authority in responding to national emergencies. See Catherine Poole & Bob Welch, “Responding to Hurricane Katrina: Contracting in an Emergency Situation,” *Acquisition Directions Advisory* (Sept. 2005), available at <http://www.acqsolinc.com/emergencycontracting/docs/adv05-09.pdf>. The agencies’ notices regarding emergency procurement authority are gathered at various websites, including the Defense Acquisition University website, https://acc.dau.mil/simplify/ev.php?ID=84072_201&ID2=DO_TOPIC, and at the Acquisition Solutions Research Institute’s “Emergency Contracting” site, www.acqsolinc.com/emergencycontracting/.

- On September 2, 2005, the Acting Director of Defense Procurement and Acquisition Policy issued a memorandum which in effect raised the micro-purchase threshold to \$250,000 for Defense purchases – *but which retained the traditional array of federal procurement requirements on those purchases.*¹⁹
- By memorandum of September 6, 2005, the Office of Federal Procurement Policy noted that agencies were already using their emergency procurement authorities, but asked for ideas for any procurement reforms that would eliminate “any obstacles to the recovery effort.”
- On September 6, 2005, the General Services Administration issued internal guidance on more liberalized contracting rules, to respond to the Katrina emergency.²⁰
- On September 7, 2005 – the day before the legislation was passed – the Civilian Agency Acquisition Council issued guidance noting that civilian agencies had expanded procurement flexibility, under traditional authorities, to respond to Hurricane Katrina.²¹

Again, all of these agency initiatives were based on existing law and existing flexibilities. Despite these agency initiatives, however, the Administration requested the additional legislative exceptions, including the new \$250,000 micro-purchase exception. In essence, the September 8 legislation expanded the existing Defense Department micro-purchase flexibility (from September 2) to the entire government. In doing so, however, the new legislation abandoned the many procurement protections that were tied into the Defense Department’s September 2 initiative.

Now that the new exceptions are in place, and there has been criticism from many quarters, the Administration has issued guidance on use of the new exceptions. On September 13, 2005, the Office of Management and Budget (OMB) issued guidance on implementing the new legislation.²² While the OMB guidance noted that traditional criminal laws would continue to apply to the new, expanded micro-purchases, and the new guidance called for careful controls on purchase cards, nothing in the new OMB guidance restored the competition and transparency, or the socioeconomic requirements, which normally inform federal procurement.

¹⁹ http://www.gsa.gov/gsa/cm_attachments/GSA_BASIC/KatrinaDeviation_R2-y-gAY_0Z5RDZ-i34K-pR.doc (deviation); http://www.gsa.gov/gsa/cm_attachments/GSA_BASIC/2005-00005%20final1Atch11v3_R2-y-gAY_0Z5RDZ-i34K-pR.doc (laws still applicable, even under deviation).

²⁰ http://www.gsa.gov/gsa/cm_attachments/GSA_BASIC/Alert200505_R2-y-gAY_0Z5RDZ-i34K-pR.PDF.

²¹ http://www.gsa.gov/gsa/cm_attachments/GSA_BASIC/EmergencyProcurements-2005-04_R2-y-gAY_0Z5RDZ-i34K-pR.pdf.

²² http://www.gsa.gov/gsa/cm_attachments/GSA_BASIC/MemoforCAO-CFOreIncreasedMicro-PurchaseforHKatrinaRescueandRelief_R2-y-gAY_0Z5RDZ-i34K-pR.pdf.

Conclusion and Recommendations

A successful procurement system rests on three basic principles: competition, transparency and integrity.²³ Under the supplemental appropriation for Hurricane Katrina relief, among other things, procurements up to \$250,000 can be made without *any* competition or transparency. This is a formula for disaster, for where there is no competition or transparency, the risk rises exponentially that the system's integrity will fail, as well. Congress may, therefore, want to consider the following:

- Imposing a “sunset” date on the recently enacted exceptions.
- Requesting a study by the Government Accountability Office, or another reviewing organization, to assess whether in the days after the storm there were, in fact, unreasonable obstacles to Hurricane Katrina relief under traditional procurement rules.
- Assessing whether additional procurement flexibilities are needed now, or may be needed in future emergencies.
- Ensuring that any contracting reforms reasonably preserve competition and transparency, and recognize the government's broader socioeconomic commitments in federal procurement.

Thank you, again, for the opportunity to address the Committee. I would be glad to take any additional questions you may have.

²³ See, e.g., Steven L. Schooner, “Desiderata: Objectives for a System of Government Contract Law,” 11 Pub. Proc. L. Rev. 103 (2002), available at www.ssm.com.

APPENDIX A:

**EXCERPT FROM HURRICANE KATRINA
SECOND EMERGENCY SUPPLEMENTAL APPROPRIATION**

PUBLIC LAW No. 109-62

SECTION 101: PROCUREMENT EXCEPTIONS

SEC. 101. For procurements of property or services determined by the head of an executive agency to be used in support of Hurricane Katrina rescue and relief operations –

(1) the emergency procurement authority in subsection 32A(c) of the Office of Federal Procurement Policy Act (41 U.S.C. 428a(c)) may be used; and

(2) the amount specified in subsections (c), (d), and (f) of section 32 of the Office of Federal Procurement Policy Act (41 U.S.C. 428) shall be \$250,000.

This Act may be cited as the `Second Emergency Supplemental Appropriations Act to Meet Immediate Needs Arising From the Consequences of Hurricane Katrina, 2005`.

APPENDIX B:

CURRENT FEDERAL ACQUISITION REGULATION

SUBPART 13.2: MICRO-PURCHASES

Federal Acquisition Regulation Subpart 13.2—Actions At or Below the Micro-Purchase Threshold

13.201 General.

(a) Agency heads are encouraged to delegate micro-purchase authority (see 1.603-3).

(b) The Governmentwide commercial purchase card shall be the preferred method to purchase and to pay for micro-purchases (see 2.101).

(c) Purchases at or below the micro-purchase threshold may be conducted using any of the methods described in Subpart 13.3, provided the purchaser is authorized and trained, pursuant to agency procedures, to use those methods.

(d) Micro-purchases do not require provisions or clauses, except as provided at 4.1104 and 32.1110. This paragraph takes precedence over any other FAR requirement to the contrary, but does not prohibit the use of any clause.

(e) The requirements in Part 8 apply to purchases at or below the micro-purchase threshold.

(f) The procurement requirements in the Resource Conservation and Recovery Act (42 U.S.C. 6962) and Executive Order 13101 of September 14, 1998, Greening the Government through Waste Prevention, Recycling, and Federal Acquisition, apply to purchases at or below the micro-purchase threshold (see Subpart 23.4).

(g)(1) For acquisitions of supplies or services that, as determined by the head of the agency, are to be used to support a contingency operation or to facilitate defense against or recovery from nuclear, biological, chemical, or radiological attack, the micro-purchase threshold is —

(i) \$15,000 in the case of any contract to be awarded and performed, or purchase to be made, inside the United States; and

(ii) \$25,000 in the case of any contract to be awarded and performed, or purchase to be made, outside the United States.

(2) Purchases using this authority must have a clear and direct relationship to the support of a contingency operation or the defense against or recovery from nuclear, biological, chemical, or radiological attack.

13.202 Purchase guidelines.

(a) Solicitation, evaluation of quotations, and award.

(1) To the extent practicable, micro-purchases shall be distributed equitably among qualified suppliers.

(2) Micro-purchases may be awarded without soliciting competitive quotations if the contracting officer or individual appointed in accordance with 1.603-3(b) considers the price to be reasonable.

(3) The administrative cost of verifying the reasonableness of the price for purchases may more than offset potential savings from detecting instances of overpricing. Therefore, action to verify price reasonableness need only be taken if—

(i) The contracting officer or individual appointed in accordance with 1.603-3(b) suspects or has information to indicate that the price may not be reasonable (*e.g.*, comparison to the previous price paid or personal knowledge of the supply or service); or

(ii) Purchasing a supply or service for which no comparable pricing information is readily available (*e.g.*, a supply or service that is not the same as, or is not similar to, other supplies or services that have recently been purchased on a competitive basis).

(b) *Documentation.* If competitive quotations were solicited and award was made to other than the low quoter, documentation to support the purchase may be limited to identification of the solicited concerns and an explanation for the award decision.