S. HRG. 100-1065

THE MAJOR FRAUD ACT, AND THE GOVERNMENT FRAUD LAW ENFORCEMENT ACT OF 1987

HEARING

BEFORE THE

COMMITTEE ON THE JUDICIARY
UNITED STATES SENATE

ONE HUNDREDTH CONGRESS

SECOND SESSION

ON

H.R. 3911

A BILL TO AMEND TITLE 18, UNITED STATES CODE, TO PROVIDE INCREASED PENALTIES FOR CERTAIN MAJOR FRAUDS AGAINST THE UNITED STATES

AND

S. 1958

A BILL TO ESTABLISH REGIONAL GOVERNMENT FRAUD LAW ENFORCEMENT UNITS FOR EFFECTIVE INVESTIGATION AND PROSECUTION OF FRAUD AGAINST THE GOVERNMENT

JULY 12, 1988

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CONTENTS

STATEMENTS OF SENATORS

CHRONOLOGICAL LIST OF WITNESSES

ALPHABETICAL LISTING AND MATERIALS SUBMITTED

H.R. 3911, THE MAJOR FRAUD ACT, AND S. 1958, THE GOVERNMENT FRAUD LAW ENFORCEMENT ACT OF 1987

TUESDAY, JULY 12, 1988

U.S. SENATE,
COMMITTEE ON THE JUDICIARY,
Washington, DC.

The committee met, pursuant to notice, at 9:42 a.m., in room SD-226, Dirksen Senate Office Building, Hon. Howard M. Metzenbaum (acting chairman) presiding.

Also present: Senators DeConcini, Grassley, Simon and Specter.

OPENING STATEMENT OF SENATOR HOWARD M. METZENBAUM

Senator METZENBAUM. This morning this committee addresses itself to the issue of the passage of the Major Fraud Act, H.R. 3911, and S. 1958, the Government Fraud Law Enforcement Act of 1987.

Elimination of government fraud, waste and abuse has been a campaign promise and policy goal of every modern administration, Democratic and Republican. It enjoys great popular support, and has been the object of countless commission studies, new anti-fraud laws, and reportedly intensified law enforcement reports.

But despite all the studies, all the talk, all the claimed accomplishments, the Pentagon scandal shows that procurement fraud, particularly in the military remains an epidemic out of control.

The corruption is massive and systemic. It will lead as it should to yet another round of debate on defense acquisition reform.

New measures will have to be considered and implemented. But that work will largely be done in the Armed Services Committee, and on the House and Senate Floors.

As we get into this subject, it reminds me of a time when Senators Armstrong, Warner and myself went down to see Secretary Weinberger, and Deputy Secretary Carlucci, to talk about the problems of procurement; not fraud, but just failure to use proper procurement practices.

And I remember after that there came out the 32 new initiatives of the Department of Defense for procurement.

And we had gone down to talk about using competitive bidding. And interestingly enough, they had made no improvement, suggested no improvement, as it pertained to competitive bidding.

And I called Mr. Carlucci at that time. He was deputy director. And I said to him, how come you didn't say anything about competitive bidding in the procurement process? Oh, it was an oversight. So then it went in.

And I remember also when Senator Goldwater and I sued the Navy by reason of their procurement practices in connection with a particular plane. And notwithstanding the fact that Senator Goldwater at that time was Chairman of the Armed Services Committee; notwithstanding the fact that we had gone to court to do something about it, we still could not beat the processes of the government, processes of the Navy, that didn't want to use anything except this one particular plane.

And so you get the feeling that you're swimming upstream when you're dealing with the Department of Defense in this area.

And one can't overlook the fact that it wasn't too many years ago when a number of defense contractors were suspended as far as their right to bid on contracts because of their involvement in defense and fraudulent practices and inappropriate practices; and then suddenly overnight the government reversed itself and said, well, we have nowhere else to get the equipment. And so they just forgot about it entirely.

And that reminds us, that when we take a look at what happened just yesterday, we find that, when the very same defense contractors who had been suspended, all of that is suddenly changed, and the Department of Defense reverses itself.

The job of this committee is not to reform the system, but to consider ways of deterring and penalizing the human behavior that corrupts it. For while the corruption is systemic, what lies at its root is old fashioned greed.

We cannot eliminate greed, but we can make it expensive; very expensive. We can beef up the government's ability to uncover and prosecute fraudulent schemes inspired by greed.

And we can consider tightening revolving door restrictions to reduce the financial temptations that incite greed and compromise the integrity of Federal procurement officials.

H.R. 3911, passed unanimously by the House—and I congratulate you, Congressman Hughes, for your leadership in this area—would establish a new Federal procurement fraud offense for major contracts.

As Congressman Hughes, its chief sponsor, will explain more in a moment, it would stiffen penalties, lengthen the statute of limitations, and strengthen incentives and protections for corporate whistle blowers.

I consider these whistle blower provisions to be essential, as effective detection and prosecution of complex procurement fraud is almost impossible without inside tips.

Unless workers are encouraged and freed to come forward, the battle against fraud and corruption is already half lost.

I look forward to today's testimony on these and other provisions. I would be willing to consider any necessary revisions.

I would hope we can move forward promptly with this legislation.

S. 1958, which would establish a regional enforcement program for government fraud, also merits serious consideration. For a fuller explanation of the bill, I will defer to Senator Grassley, coauthor with Senator Proxmire, whom we are fortunate to have with us today.

And I might say parenthetically that this body is going to be a lesser body when my good friend, Bill Proxmire, leaves us. Because he's been a voice of reason and a voice of outrage when there was a reason to be outraged over a period of many years.

And we will be a lesser body, and not nearly as effective in seeking out some of the issues to which he has addressed himself over the years.

And I might also say that my friend to my left here who is usually on my right, Senator Grassley, has certainly distinguished himself in so many ways by his willingness to speak out regardless of the politics of the matter when he's found ripoffs of the Federal Government, and I am looking to hearing from you very shortly.

But before we turn to Senator Grassley, let me emphasize how important I think it is that the Congress lead and act on this issue.

The American people, nearly 90 percent according to recent polls, are demanding that more be done to fight waste, fraud and abuse in government. While the Pentagon bribery scandal is not the immediate focus of this hearing, it is a vivid backdrop and a reminder of the crisis in our government procurement system, and of the threat of that crisis to our national security, and to public trust in government.

Unless the Congress and the administration act effectively and act now, these pillars of our democracy will suffer serious and lasting damage.

I think it is an indication of the determination of Congress to act in this area that the Armed Services Committee is conducting a hearing, I think at this very moment, along similar lines, although with respect to different phases of the problem as are we today.

Senator Grassley.

Senator GRASSLEY. Mr. Chairman, I thank you for your kind remarks about me; but more importantly, I want to associate myself with the remarks made on behalf of Senator Proxmire.

We need to remember that his leadership in this area goes back to protecting whistle blowers who were involved in the C-5A scandals.

Mr. Chairman, the current defense procurement investigation shows how widespread and potentially harmful this type of fraud can be to the national security and to the public trust.

The government has consistently been on the short end of the war against defense procurement fraud, despite pleas by the public and many of my colleagues in Congress to beef up government resources to fight this kind of fraud.

We're here today to put our money where our mouth is. The defense procurement fraud problem is insidious. It is characterized and driven by a set of values completely alien to the rest of America.

Competition, and its benefits, apparently are not a desired goal in the defense business. To win, you have to play the "insider" trading game.

Winning a contract seems to be based on who you know, not on what you can do. I call this "peek-a-boo" procurement; getting a peek at what it takes to win a contract.

What could be more anathema to the American way of life?

Now let's be very clear from the outset that the problem of defense procurement fraud is not a "Johnny-come-lately" phenomena. Defense procurement fraud is probably the world's second oldest profession.

There is enough history on defense procurement fraud over the centuries to fill an encyclopedia. Consequently, there is much to learn from history on the nature and the character of this type of fraud.

And from that learning, we can better understand what needs to be done if we're going to conquer it once and for all.

Let me read a quote relevant to a current investigation.

> Classified documents which are prohibited from ever leaving the DOD are regularly trafficked among private consultants; companies in the procurement industry; and military and civilian employees of the government.

This quote dates back to 1985 testimony delivered to this committee by a former DOD investigator named Robert Segal.

Mr. Segal's testimony related to the Justice Department's handling of the *GTE* case, of which Mr. Segal, who directed the investigation, was critical. According to Mr. Segal, the investigation included 25 major companies, not just GTE, and this point did not fall on deaf ears.

Now, lawyers for the defendants said that this was an everyday activity, that, "the government is attempting in this criminal prosecution to punish three individuals for engaging in conduct that was routine and pervasive, and that no one regarded as criminal at the time."

The *GTE* case resulted from a two-year investigation by the Defense Criminal Investigating Service (DCIS). Only recently did it become public that bribery was involved in that investigation, and that the DCIS investigation of 25 companies showed the same pervasive and potentially fraudulent activity as seen in the current probe.

But the Justice Department prosecuted only GTE, not fully understanding the magnitude of the case brought to them by DOD investigators. This is according to Mr. Segal and other investigators involved at that time.

Today, 3 years later, Mr. Segal's testimony is just as relevant as it was in 1985. Had the Justice Department understood the significance of the case presented to it by DOD investigators, the apparent routine and pervasive activity could have been brought out and addressed 3 years ago.

Mr. Chairman, let me refer to an op-ed piece that appeared in Sunday's Baltimore Sun. It's an historic account of defense fraud in this country, written by David Morrison of the National Journal.

Morrison notes that defense procurement fraud dates back to 1782, when Congress directed the Secretary of Finance, Robert Morris, to investigate procurement abuses that occurred during the Revolutionary War.

Morrison recounts similar instances in 1861, during the Civil War; 1896, during the Spanish American War; 1934, following the First World War; 1941, with the Truman Commission, in the Second World War; the Fitzhugh panel of 1970, and the Packard Commission of 1986.

The problem has surfaced many times over the years, and many Commissions have come along suggesting the same remedy to the same problems.

This is clearly an historical problem, Mr. Chairman. But it makes us wonder why we can't seem to break the code on solving such a well-documented problem.

The reason in my mind that the Commissions often do not work is that they are sometimes intended as a large "valium" for the body politic.

Designed to tranquilize an outraged public, their solutions seldom cure the ills, because the prescription is to erode checks and balances in the defense management structure, rather than enhance those checks and balances.

With the Packard Commission, two examples come to mind. One is a self-policing policy by contract. Does anyone who has read the Morrison piece truly believe that self-policing will work?

The second example is the establishment of an acquisitions "czar". How can there be internal checks and balances when all the performance functions come under one office?

Without true independence among the functions responsible for monitoring performance, the system is ripe for manipulation and collusive fraud.

So what is the solution, Mr. Chairman? I would like to once again refer to the op-ed piece of David Morrison, who writes:

> An historical perspective suggests that there is little that is truly new in the scandal, and that eternal vigilance will always be the price of efficiency and of ethical practices in the $160 billion per year business for stocking the arsenal of democracy.

I would say, Mr. Chairman, that that means it's time to move government's resources to the front line, and fight fire with fire!

Today, this committee considers two bills that would be part of the process of constant vigilance. I welcome today's expert testimony, and trust that the committee will act expeditiously to respond to a problem that all of us are concerned about, and that we can certainly do something about.

Thank you, Mr. Chairman.

Senator METZENBAUM. Also we are very pleased to have Senator DeConcini with us this morning. Senator DeConcini is also one of those whose voice has been raised in ire and concern on so many occasions having to do with this very problem.

We are happy to have you with us this morning.

Senator DECONCINI. Mr. Chairman, thank you. And thank you for holding these hearings, and thank you Representative Hughes for your leadership in the House.

And may I compliment again, as you have so well pointed out, Senator Proxmire's leadership in this area. At times he has been a voice in the wilderness, but often has been heard, and certainly by this Senator.

The recent FBI investigation has made us all well aware of the issue of procurement fraud in the Department of Defense and procurement fraud in general.

Earlier this year the Government Accounting Office studied 148 open cases reported to the Secretary of Defense from April 1, 1985, to March 31, 1986.

The GAO estimated the losses due to procurement fraud in those cases alone at at least $387 million. In 1985, Deputy Attorney General Toensing testified before the subcommittee on administrative practices and procedures that 45 of the top 100 Department of Defense contractors were under criminal investigation.

Apparently not much has changed in these 3 years. In the last few weeks, it has been reported that 39 of the 46 defense contractors who had agreed to police their own compliance with procurement rules have come under investigation for fraud, including criminal fraud.

As a result of the recent investigation, the Justice Department has issued 278 subpoenas, 42 search warrants, and it is likely that even more will follow.

Defense Secretary Frank Carlucci has ordered a freeze on approximately $1 billion in defense contracts. The Senate Government Affairs Committee and the House Armed Services Committee recently held hearings on the procurement process.

The Senate Armed Services Committee is also holding hearings today on the issue.

Whatever the final outcome of these investigations, it appears that the current system of monitoring the procurement process is not working. We have before the committee legislation that attempts to address problems associated with Federal procurement fraud in contracts of $1 million or more.

The bill amends Title 18 of the United States Code by increasing penalties for certain major frauds against the United States. Specifically the bill provides jail terms, fines, and a whistle-blower provision in the event of procurement frauds in excess of $1 million.

The FBI probe into procurement practices appears to be serving as a catalyst for quick passage of this type of legislation. I would caution, however, that an objective approach to the problem must be taken.

Although I agree that we have to do something and steps are needed to combat procurement fraud, I would not want to overreact simply because the political winds are blowing in favor of the extreme measures.

Mr. Chairman, I want to compliment you for setting aside today with your busy schedule to review these two bills, S. 1958 and H.R. 3911. I think these are most significant pieces of legislation, and your leadership in getting them through the Judiciary Committee is going to be crucial.

Thank you, Mr. Chairman.

Senator METZENBAUM. Thank you very much, Senator DeConcini.

Before I call the first panel, I wish to place opening statements by Senators Thurmond and Hatch in the record.

[Prepared statements follow:]

STATEMENT BY SENATOR STROM THURMOND(R-S.C.) BEFORE THE SENATE JUDICIARY COMMITTEE, REFERENCE-FULL COMMITTEE HEARING ON H.R. 3911-MAJOR FRAUD ACT, AND S. 1958- GOVERNMENT FRAUD LAW ENFORCEMENT ACT, 226 DIRKSEN SENATE OFFICE BUILDING, TUESDAY, JULY 12, 1988, 9:30 AM.

Mr. Chairman:

I am pleased to be here today at this Judiciary Committee hearing on H.R. 3911, the Major Fraud Act, and S. 1958, the Government Fraud Law Enforcement Act. Both of these bills address the problems that have arisen with regard to fraud in the area of government contracting.

It is extremely disturbing as we continue to learn of instances of fraud in connection with government procurement contracts. In this time of belt-tightening and budget cutting, any waste of money, especially as a result of fraud, is inexcusable. The American people are the real losers in these situations because money which could be used for legitimate programs and purposes is being needlessly wasted. In 1986, Congress passed the False Claims Amendments Act and the Program Fraud Civil Remedies Act to strengthen the current laws with regard to such fraud in the procurement process. However, allegations of fraud in this area continue. Therefore, it is appropriate to consider whether additional legislation is necessary.

The two bills that are the focus of this hearing propose different approaches to this problem. H.R. 3911 establishes stiff criminal penalties for persons who defraud the government in connection with a contract for the procurement of property

or services. S. 1958 directs the Attorney General to establish regional task forces to investigate and prosecute program and procurement fraud. I look forward to hearing the testimony today on these bills. I am also interested in hearing the views of those present today as to how this legislation will work in conjunction with the laws enacted in 1986.

In closing, we must take strong, tough action which will stop abuse in the area of procurement in order to ensure the integrity of the contracting process of the Federal Government.

STATEMENT OF SENATOR ORRIN G. HATCH
HEARING ON MAJOR FRAUD ACT, H.R. 3911
GOVERNMENT FRAUD LAW ENFORCEMENT ACT, S. 1958
SENATE COMMITTEE ON THE JUDICIARY
JULY 12, 1988

Mr. Chairman, this morning we examine legislation to combat fraud against the federal government. Recent newspaper accounts of pervasive misconduct by contractors, consultants, and DoD officials against the federal government have once again fueled concern for assurance that these abuses of the system are fully and appropriately punished. Therefore, it is important at this time for the Committee to examine the adequacy of the law enforcement tools, criminal penalties, and civil remedies available to fight fraud against the government.

At the outset, it is useful to note the considerable body of law currently available to battle procurement fraud. In addition to suspension and debarment for government contracting, which is possibly the greatest deterrent to contractor fraud, there are some thirteen federal statutes and other remedies that could be applicable to the information release and trading alleged in the current Pentagon fraud scandal.

This Committee was active in negotiating and passing the False Claims Act Amendments in 1986 which raised both criminal and civil penalties for violations involving false claims, provided protections for "whistleblowers," and strengthened provisions relating to "bounty hunter" qui tam suits involving government fraud. This bill constitutes an important prosecutorial tool in fighting procurement fraud. In fact, we were told in recent Judiciary Committee hearings that the three major fraud bills passed in 1986, the Program Fraud Civil Remedies Act, the Anti-Kickback Enforcement Act, as well as the False Claims Act Amendments have proved successful in fighting fraud against the federal government. Moreover, in the Criminal Fines Improvements act of 1987, Congress enacted legislation that permits the imposition of fines of up to twice the gross gain to the defendant or twice the gross loss to the United States.

While there is general agreement that action must be taken to curtail procurement fraud, a number of criticisms have been raised with respect to the drafting of the Major Fraud Act, H.R. 3911. Given the volume of existing law applicable to procurement fraud, some have expressed concern that provisions of the Major Fraud Act are duplicative of existing law. Another concern raised involves the intent standard of "knowingly" found in the bill. Given that a violator could be imprisoned for ten years upon a guilty verdict, some have

argued that a specific intent standard such as "knowingly and willfully" is a more appropriate standard.

In addition, concern is raised that the bill would establish excessive penalties-- penalties that are not related to the severity of the underlying crime and not consistent with penalties imposed for other serious crimes. Finally, the bill extends the statute of limitations for procurement fraud actions from five to seven years and some argue that this extension is contrary to the government's obligation to investigate and act expeditiously on suspected criminal activity.

With these concerns in mind, I intend to examine the testimony of the witnesses carefully. Procurement fraud is a serious problem and we must craft legislation that is both effective and workable.

Senator METZENBAUM. Senator Proxmire, with all those accolades you've had this morning, I don't know how you can do any better. We are delighted to hear you.

STATEMENT OF A PANEL CONSISTING OF HON. WILLIAM PROXMIRE, A U.S. SENATOR FROM THE STATE OF WISCONSIN, AND HON. WILLIAM J. HUGHES, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF NEW JERSEY

Senator PROXMIRE. Well, thank you very much, Mr. Chairman. I want to thank all you gentlemen for your very kind remarks.

And I want to also thank you for holding hearings on defense fraud, and I appreciate the opportunity to testify.

I am here primarily to testify on S. 1958, the government fraud law enforcement act, introduced by Senator Grassley and myself last December.

The purpose of this bill is to establish regional fraud law enforcement units within the Department of Justice to achieve greater effectiveness in the investigation and prosecution of fraud against the U.S. Government.

Now you three Senators have been concerned for years about abuses in defense contracting. There are many officials and experts who have insisted that the defense contract system is basically sound, and that the abuses have been uncovered.

And they represent only isolated cases of horror stories. This argument has been used to frustrate efforts to fundamentally reform the system, although Congress has succeeded in legislating important improvements in recent years.

The recent disclosure of widespread defense fraud confirm what some of us have been saying about the seriousness and pervasiveness of this problem.

As you said, Mr. Chairman, a little earlier, other committees are holding hearings on defense contracting. In fact, you pointed out that one is being held this morning by the Armed Services Committee.

Those hearings are important, and I would hope that the military committees will consider the consequences of the scandal for the defense contract system.

But important as those hearings are, the hearings of the Senate Judiciary Committee are more important at the present time, and I want to tell you why.

The defense contract system needs to be reformed because of a number of problems. There is waste; there is mismanagement; there is inefficiency as well as abuses such as fraud and bribery.

But you cannot solve the problem of defense fraud without tightening up the criminal laws, and strengthening the mechanism for their enforcement. No matter what is done to improve defense contracting the process will be fatally flawed so long as the criminal laws are inadequate or not properly enforced.

Unfortunately, greed and cheating are universal. The crooks will always be with us. We can control illegality in defense contracting, but it requires good law enforcement to do it.

We are losing the war against defense fraud because law enforcement is not good enough.

I support increasing the penalties for defense fraud, but it makes little sense to strengthen the criminal laws if we do not strengthen the enforcement of the laws.

Stiffer penalties would be meaningless without more effective prosecution and more convictions.

My conclusion that law enforcement needs to be strengthened is well considered. It is based on many years of oversight investigation of defense contracting in the Joint Economic Committee, and many years of experience on the Senate defense appropriations subcommittee, on which I've served for almost 30 years.

I have personally investigated every phase of the defense contracting process, and have been involved in the uncovering of waste and mismanagement in numerous weapons programs, including the C–5A, the 688 class submarines, the F–14 aircraft and M–1 tanks.

Several of my investigations turned up allegations and evidence of fraud, and in the mid-1970s I pressed the Navy to refer a group of cases involving ship construction to the Justice Department.

In each instance the Justice Department fumbled the ball. Investigations dragged on for years, and were eventually dropped with an announcement that there was insufficient evidence for prosecution.

In some cases the statute of limitations ran. Two cases involving Lockheed and Newport News Shipbuilding took 5 years for the Justice Department to investigate.

A case involving General Dynamics was declined after 3 years of investigation; it's been reopened and investigated for another 2½ years.

The case involving Litton took 7 years to get to trial, and by that time, witnesses' memories had faded, and the company was acquitted on a technicality.

In 1984 new evidence came to light about the General Dynamics and Newport News cases. My subcommittee, the Joint Economic Committee, began hearings in the General Dynamics case in July of 1984.

And in the fall of that year, Senator Grassley and I combined our two subcommittee to probe both General Dynamics and Newport News.

One of the documents we uncovered was an internal Justice Department review of Navy claims investigations, conducted by the Office of Policy and Management Analysis of the Criminal Division.

The review looked at the Justice Department's handling of the General Dynamics case and two others involving Lockheed and Bath.

The report was highly critical of Justice for not properly supervising the cases; for not understanding at the outset how large and complex they were, for turnover of attorneys and investigators; and for lack of coordination with the Navy.

To obtain an independent assessment of the delays and other problems in the investigation and prosecution of these cases, I asked the General Accounting Office, GAO, to look into them.

Senator Grassley asked GAO to evaluate the efforts of the Defense Department procurement fraud unit, established by the Justice Department several years earlier.

In 1987 Senator Grassley and I asked GAO to look more generally into the Justice Department's overall management of defense fraud cases. In addition last year the staffs of Senator Grassley's office and my joint economic subcommittee produced a staff study of Justice's investigation of defense fraud based on an in-depth analysis of the Newport News case and the facts concerning the defense procurement fraud unit.

This series of reports documents one of the most extreme cases I've ever seen of government mismanagement. The most serious problems can be summarized as follows.

The Justice Department does not devote adequate resources to defense fraud cases. Justice says it gives defense fraud a high priority but does not follow through with the assignment of resources.

Number two, the Justice Department does not efficiently manage the resources that are assigned to defense fraud. The current GAO report provides an extensive account of Justice's mismanagement in this area.

Number three, there is inadequate cooperation among the principal government bodies involved in defense fraud cases, the main Justice Department, the U.S. Attorneys' offices, the FBI, the investigative services of the Pentagon, and the military services.

Now, as a consequence of these shortfalls, major investigations often lapse, and large backlogs of cases are building up in a number of U.S. attorneys offices.

In some of the largest U.S. attorney's offices, only one or two attorneys are assigned to defense fraud.

One such prosecutor recently told my staff that his office is drowning in defense fraud cases. They are simply unequipped to handle the workload.

Frequently attorneys who work on defense fraud also have other responsibilities. I have no doubt that the cases that ought to be prosecuted are not being prosecuted because of the shortage of attorneys.

Furthermore, the government is unable to adequately handle large, complex cases involving the giant defense contractors because of weaknesses in the existing law enforcement structure. Resources for combatting defense fraud need to be concentrated in the large metropolitan areas where most of the defense fraud cases are pending, not just in or near Washington.

The bill that Senator Grassley and I have introduced recognizes that prosecution of government fraud, including defense fraud, involves a specialized area of law. Effective law enforcement in this area requires stable and identifiable resources, and the maximum amount of cooperation between investigators, prosecutors, civil attorneys, and government specialists.

The bill establishes within the Justice Department no fewer than five government fraud investigative and prosecutive units to be located in regions around the country responsible for prosecuting cases under both the criminal and civil laws.

The precise location and number of the units would be determined by the Attorney General. And they would supplement, not replace, the Justice Department's fraud section.

In closing I want to emphasize two things. First, this is not a partisan problem. The Justice Department's weaknesses with regard to defense fraud cases, especially large, complicated cases involving major defense firms, did not begin in the Reagan administration. They stretch back over several administrations, Democratic and Republican.

No administration has distinguished itself by its efforts to combat defense fraud.

Second, in no way am I criticizing the attorneys and investigators and others in the trenches, so to speak, engaged in the war against defense fraud. There are many dedicated civil servants doing everything they can to carry out their responsibilities, often with inadequate resources at their command.

We owe those who have stayed in the fight for honest government a debt of gratitude.

Let me say just one more thing, Mr. Chairman. About 2 years ago the FBI set up a sting operation in which their agents offered bribes to 106 contractors in New Jersey and New York. These were municipalities, where the local official would buy services for paving and for other local activity.

Of those 106 bribe offers, 105 were accepted; 105. Only one was not accepted. Why wasn't that one accepted? Because it wasn't big enough. It wasn't big enough.

The reason I raise that point is that the only way you get at bribery is to go after and penalize the people who offer the bribes. That's what we have to do.

And we have to have—and believe me, as you know, these are corporations that are very well staffed. They have the best lawyers that money can buy. They know how to delay cases.

And we have to have the manpower, the force, the skill, the professionalism, to stand up to them. That's what we don't have now. We're going to continue to have bribery cases. They're going to continue to plague this country and hurt our taxpayers and shame our country unless we act on the kind of proposal that Senator Grassley and I have proposed.

Thank you.

[The prepared statement of Senator Proxmire follows:]

Statement On Defense Fraud
Presented by Senator William Proxmire
Before the Senate Judiciary Committee
July 12, 1988

I want to commend Senator Metzenbaum and the Senate Judiciary Committee for holding hearings on defense fraud, and I appreciate being invited to testify. I am here primarily to explain S. 1958, the Government Fraud Law Enforcement Act, introduced by Senator Grassley and myself last December. The purpose of this bill is to establish regional fraud law enforcement units within the Department of Justice to achieve greater effectiveness in the investigation and prosecution of fraud against the U.S. Government. Before going into the details of the bill, I want to say something about the current defense fraud scandal, how this issue relates to defense contracting, and the events that led up to the introduction of the Proxmire-Grassley bill.

Senator Metzenbaum, Senator Grassley, and other Members of Congress have been concerned for years about abuses in defense contracting. There are many officials and experts who have insisted that the defense contract system is basically sound and that the abuses that have been uncovered represent only isolated cases or "horror stories." This

argument has been used to frustrate efforts to fundamentally reform the system, although Congress has succeeded in legislating important improvements in recent years. The recent disclosures of widespread defense fraud confirm what some of us have been saying about the seriousness and pervasiveness of this problem.

Other committees are holding hearings on defense contracting in the wake of the recent scandal. Those hearings are important and I would hope that the military committees will consider the consequences of the scandal for the defense contract system. But important as those hearings are, the hearings of the Senate Judiciary Committee are more important at the present time.

The reason is this: the defense contract system needs to be reformed because of a number of problems. There is waste, mismanagement, and inefficiency as well as abuses such as fraud and bribery. But you cannot solve the problem of defense fraud without tightening up the criminal laws and strengthening the mechanism for their enforcement. No matter what is done to improve defense contracting, the process will be fatally flawed so long as the criminal laws are inadequate or not properly enforced.

Unfortunately, greed and cheating are universal. The crooks will always be with us. We can control illegality in defense contracting but it requires good law enforcement. We are losing the war against defense fraud because law enforcement is not good enough.

I support increasing the penalties for defense fraud. But it makes little sense to strengthen the criminal laws if we do not strengthen the enforcement of the laws. Stiffer penalties would be meaningless without more effective prosecution and more convictions.

My conclusion that law enforcement needs to be strengthened is well considered. It is based on many years of oversight investigations of defense contracting in the Joint Economic Committee and many years of experience on the Senate Defense Appropriations Subcommittee.

I have personally investigated every phase of the defense contracting process and have been involved in the uncovering of waste and mismanagment in numerous weapons programs including the C5A, the 688 class submarine, the F14 aircraft, and the M1 tank. Several of my investigations turned up allegations and evidence of fraud and in the mid-1970's I pressed the Navy to refer a group of cases involving ship construction to the Justice Department.

In each instance the Justice Department fumbled the ball. Investigations dragged on for years and were eventually dropped with an announcement that there was insufficient evidence for a prosecution. Two cases, involving Lockheed and Newport News Shipbuilding, took five years for the Justice Department to investigate. A case involving General Dynamics was declined after three years of investigations, then reopened and investigated for another two and a half years. A case involving Litton took seven years to get to trial and by that time witnesses memories had faded and the company was acquitted on a technicality.

In 1984 new evidence came to light about the General Dynamics and Newport News cases. My Subcommittee of the Joint Economic Committee began hearings into the General Dynamics case in July 1984, and in the Fall of that year Senator Grassley and I combined our two Subcommittees to probe both General Dynamics and Newport News.

One of the documents we uncovered was an internal Justice Department "Review of Navy Claims Investigations," conducted by the Office of Policy and Management Analysis of the Criminal Division. The review looked at the Justice Department's handling of the General Dynamics case and two others involving Lockheed and Bath. The report was highly

critical of Justice for not properly supervising the cases, for not understanding at the outset how large and complex they were, for turnover of attorneys and investigators, and for lack of coordination with the Navy.

To obtain an independent assessment of the delays and other problems in the investigation and prosecution of these cases, I asked the General Accounting Office to (GAO) look into them. Senator Grassley asked GAO to evaluate the efforts of the Defense Procurement Fraud Unit (DPFU), established by the Justice Department several years earlier. In 1987, Senator Grassley and I asked GAO to look more generally into the Justice Department's overall management of defense fraud cases. In addition, last year the staffs of Senator Grassley's office and my Joint Economic Subcommittee produced a staff study of Justice's investigations of defense fraud based on an in-depth analysis of the Newport News case and the facts concerning DPFU. This series of reports document one of the most extreme cases I have seen of government mismanagement.

The most serious problems can be summarized as follows:

1. The Justice Department does not devote adequate resources to defense fraud cases. Justice says it gives

defense fraud a high priority but it does not follow through with the assignment of resources.

2. The Justice Department does not efficiently manage the resources that are assigned to defense fraud. The current GAO report provides an extensive account of Justice's mismanagement in this area.

3. There is inadequate cooperation among the principal government bodies involved in defense fraud cases: the main Justice Department, the U.S.Attorney offices, the FBI, the investigative services of the Pentagon, and the military services.

As a consequence of these shortfalls, major investigations often lapse and large backlogs of cases are building up in a number of U.S.Attorney offices. In some of the largest U.S.Attorney offices only one or two attorneys are assigned to defense fraud. One such prosecutor recently told my staff that his office is drowning in defense fraud cases. They simply are unequipped to handle the workload. Frequently, attorneys who work on defense fraud also have other responsibilities. I have no doubt that cases that ought to be prosecuted are not being prosecuted because of the shortage of attorneys.

Furthermore, the government is unable to adequately handle large, complex cases involving the giant defense contractors because of weaknesses in the existing law enforcement structure. The resources for combating defense fraud need to be concentrated in the large metropolitan areas where most of the defense fraud cases are pending, not in Washington.

The bill that Senator Grassley and I have introduced recognizes that prosecution of government fraud including defense fraud involves a specialized area of law. Effective law enforcement in this area requires stable and identifiable resources and the maximum amount of cooperations between investigators, prosecutors, civil attorneys, and government specialists.

The bill establishes within the Justice Department no fewer than five government fraud investigative and prosecutive units to be located in regions around the country, responsible for prosecuting cases under both the criminal and civil laws. The precise location and number of the units would be determined by the Attorney General, and they would supplement not replace the Justice Department's Fraud Section.

In closing, I want to emphasize two things. First, this is not a partisan problem. The Justice Department's weaknesses with regard to defense fraud cases, especially large, complicated cases involving major defense firms, did not begin in the Reagan Administration. They stretch back over several Administrations, Democratic and Republican. No Administration has distinguished itself by its efforts to combat defense fraud.

Second, in no way am I criticizing the attorneys and investigators and others in the trenches, so to speak, engaged in the war against defense fraud. There are many dedicated civil servants doing everything they can to carry out their responsibilities, often with inadequate resources at their command. We owe those who have stayed in the fight for honest government a debt of gratitude.

Senator METZENBAUM. Thank you very much, Senator Proxmire. I had never heard that report about the 106 bribe offers, 105 of which were accepted.

Senator PROXMIRE. I'll be happy to make that available to you.

Senator METZENBAUM. I've asked my staff to follow through with you. I think that's just unbelievable and fantastic.

Senator PROXMIRE. It may be unbelievable, but it's true.

Senator METZENBAUM. Oh, I understand that. If it weren't you saying it, I would have difficulty with it. But it is incredible.

Congressman Hughes, you probably get some sort of accolade. My recollection is that your bill passed the House by some overwhelming margin. What was the count?

Mr. HUGHES. 419 to 0.

Senator METZENBAUM. Not bad. The others were home that day; they were not present.

Congressman Hughes, yours has been a voice of reason, logic and concern, and guts in Congress for a good many years. And I have had the privilege of working with you on some other areas as well.

I am just delighted to have you with us this morning. Maybe even apologize a little bit for the wordiness, starting first with myself and then all of my colleagues.

But my guess is, you've been around here long enough to understand that well.

STATEMENT OF HON. WILLIAM J. HUGHES, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF NEW JERSEY

Mr. HUGHES. Thank you, Mr. Chairman, and members of this distinguished committee for permitting me to testify on behalf of this bill, H.R. 3911, the Major Fraud Act of 1988, as it passed the House of Representatives.

H.R. 3911, which I introduced, passed unanimously at both the subcommittee and the full committee levels in the House Judiciary Committee, and on May 10, 1988, passed the House of Representatives by a vote of 419 to 0.

This bill grew out of hearings by the subcommittee on crime and a review of numerous other congressional, Department of Justice and Department of Defense investigations of procurement fraud over the last two decades.

I will not here reiterate the litany of successive scandals in spare parts, overhead overcharges, malfunctioning equipment, product substitution, and similar fraudulent acts that have been exposed in this testimony.

To say the least, it documents a story of greed, malfeasance and other fraudulent schemes that bilk the American taxpayers of billions of dollars and at the same time diminish our citizen's confidence in the executive branch's ability to efficiently administer essential governmental functions.

It was our feeling in the House that these investigations were not merely history lessons, but were a collection of facts that describe a relatively small, but extremely malignant blight on our society which is a continuing problem. Unfortunately, recent revelations indicate that we have not underestimated the seriousness of the problem.

While all of the details are not yet available, it appears that the current scandal within the defense industry may be the worst in the Pentagon's history. Among other things, that suggests to me that our current Federal statutes are not providing a sufficient deterrent to discourage such practices and that there is not enough information readily available to law enforcement agencies in order for them to discover and prosecute these illegal acts.

Even before the recent allegations surfaced, we in the House believed there was sufficient basis to justify H.R. 3911. For example, the GAO released a report in January of 1988 in which it estimated a loss due to procurement fraud of $387 million in but 148 open procurement cases reported to the Secretary of Defense from April 1, 1985, through March 31, 1986.

This report also noted that in fiscal year 1986 there were some 1,919 new fraud investigations as compared with fiscal year 1983, when there were 870 such investigations.

This GAO study, by the way, included only 32 product substitution cases which are a priority for DOD. In the product substitution area alone, cases where contractors deliberately provide inferior products on DOD contracts which can directly cost Americans their lives, investigations have increased to the point where there have been 85 indictments since January 1986.

As of October of 1987, the defense criminal investigative service was actively involved in another 231 product substitution cases. H.R. 3911 is fashioned to meet these problems, and to create new deterrents to criminal fraud.

It creates a new free-standing procurement fraud offense regarding contracts of $1 million or more, and is patterned after the Bank Fraud Act.

Under current conditions the bill would cover some 9,900 prime contracts. I know that the committee knows that we really don't have a free-standing fraud statute as such in the law at the present time. U.S. Attorneys have to use mail fraud, wire fraud, and the false statement provisions of title 18 U.S.C.

This bill would create a free-standing procurement fraud statute.

The maximum prison sentence that could be imposed under H.R. 3911 is 10 years. This is consistent with the maximum in comparable legislation.

The bill provides for a mandatory minimum sentence of 2 years if the offense involves foreseeable and substantial risk of personal injury. This is to cover those egregious situations, usually in product substitution cases, where a contractor provides such items as defective parachute cords; faulty jet ejection seat valves; or defective nozzles for fire-fighting equipment on ships.

These provisions should act as an additional deterrent to such life-threatening conduct.

The bill contains an alternate fine of up to $10 million, which should be a new deterrent to corporate fraud. It also would provide an extension to the statute of limitations in which prosecutions could be initiated to up to 7 years, rather than the normal 5 years, to accommodate the extensive investigations often required in this type of fraud.

In addition, the bill establishes a new system of rewards under which up to $250,000 can be paid from the criminal fine to individ-

uals who provide information leading to a conviction, as well as protection for whistle blowers, similar to provisions included in the false claims acts amendments of 1986.

The bill does set limitations on who can receive these rewards and it requires the DOJ to recommend and the court to approve such a reward. Those ineligible for rewards are as follows:

(1) Government employees performing their official duties.

(2) Workers who could have come forward with information to an employer at the formative stage of an offense, and could have prevented it or stopped it from occurring.

(3) And third, individuals who participate in the offense.

I believe that the Major Fraud Act of 1988 could become not only a major tool to fight procurement fraud, but an incentive for responsible individuals to come forward with information needed for the prosecution of major frauds against the government.

This latter aspect of the bill will be an additional deterrent to further illegal acts. I am very pleased that the Senate Judiciary Committee has moved so very quickly to consider the Major Fraud Act of 1988.

I look forward to working with you to secure its enactment into law this year.

I might say to this distinguished committee that this bill is not the final word in this area. We do have a major resource shortfall and as Senator Proxmire has so aptly stated, although the Justice Department has made procurement fraud and white collar crime a priority, our own subcommittee on crime, through the hearing process, has determined that that's a priority in name only, because we have not committed the resources.

We don't have the FBI resources, the investigative resources, to do the job that needs to be done and we don't have sufficient U.S. attorneys to pursue these crimes, or for that matter, many other areas of crime. We just haven't provided the resources in the U.S. attorneys' offices that is needed.

We just haven't made the kind of commitment that's needed. We also have a constant turnover of expertise and that undercuts our enforcement effort.

No sooner does an assistant U.S. attorney become conversant with a particular case, than he moves on to the private sector at a much bigger salary, and of course, we lose that expertise.

So we need to shore up the criminal justice system all along the line. But I would submit that this legislation would provide, I think, a new tool, an effective tool, that could certainly assist our law enforcement community.

The committee should consider one technical adjustment that might be made to H.R. 3911. It is possible to interpret sec. 1031(b) of the bill to allow a judge to only fine a defendant even if the offense involves a foreseeable and substantial risk of personal injury. Any sentence under those conditions would have to be a mandatory minimum of 2 years, but in reading sec. 1031(a) in conjunction with sec. 1030(b), the bill, as presently constituted, may not require any incarceration.

In order to clarify this matter, I would suggest that the Senate add in the first sentence of new section 1030(b) added to title 18 by the bill—

(1) Strike out "the term of imprisonment" and insert in lieu thereof "a term of imprisonment shall be"; and

(2) After "Subsection (a) of this Section" insert "and such term".

Another question has been raised as to whether the $10,000,000 cap imposed in new section 1031(b) would limit a fine imposed under 18 U.S.C. sec. 3571(d) which allows a fine equal to twice the gross gain or twice the gross loss. Since, however, the $10,000,000 cap is applied to those fines that ". . . may exceed the maximum otherwise provided by law", it is my reading of this bill that the $10,000,000 cap would not apply to a fine imposed under 18 U.S.C. sec. 3571(d).

I thank you.

Senator DECONCINI [presiding]. Thank you very much. Let me ask you one question that troubles me about both your legislation, S. 1958, and H.R. 3911. I don't see any penalty in it where the court could void a contract, or prohibit the contractor from participating for a period of time as part of the sentence.

I'm assuming that the contractor is found guilty. Did you pursue that, Representative Hughes, in your hearing, and if so, why did you rule that out?

Mr. HUGHES. Yes, we had some sentiment within the committee to deal with the debarment issue but that doesn't fall within our committee's jurisdiction.

As you know, we are very fragmented with jurisdiction. And frankly, we could not——

Senator DECONCINI. You mean that penalty wouldn't fall within the jurisdiction, as part of the penalty, assuming that guilt is proven and a verdict is rendered?

Mr. HUGHES. We would not have jurisdiction over debarment provisions.

Senator DECONCINI. How about you, Senator Proxmire? Do you have any thoughts on that subject matter?

Senator PROXMIRE. I think it's an excellent point. But I don't have any specific recommendations on it.

It seems to me that would make a good amendment to the Hughes bill. It is a superb bill. It is a great advance. But I think that what you suggest is something that the Senate might add.

Senator DECONCINI. It just seems to me the penalties apparently are not working, the million dollar penalties and what have you, and we are talking about increasing that substantially.

But it seems to me that if the contractor could face a disbarment and noncontractual basis, that that would be a great incentive.

Senator PROXMIRE. The difficulty, of course, is that we can apply none of the present penalties at all. Because all the cases seem to evaporate with time and delay.

And as both Congressman Hughes and I have pointed out, with the turnover of staff and the lack of resources.

Senator DECONCINI. Then coming to that question, Congressman Hughes, you mention a lot more needs to be done in addition to this legislation. I presume your position is, we'd be better off to pass this bit, even though it's not all of it. But don't we need to do something about career prosecutors in the Justice Department and investigators that are going to be able to be enticed to stay there for a period of time, more than 2 or 3 years?

Mr. HUGHES. I favor reviewing and increasing salaries to make them more attractive. I have always felt that it was important for us to develop certain commitments in exchange for employment; to retain that expertise for a period of time.

We need to do all those things. And I also favor the kind of targeting that is in the Proxmire bill, or Proxmire-Grassley bill, that would in fact develop expertise so that we can, on a regional basis, move a mobile team around the country.

Since we don't have resources to place them in every jurisdiction, it would be important to have a task force operation that we can move around the country to deal with these problems.

But your suggestion about debarment is a good one. Frankly, if we had had jurisdiction, I have no doubt we would have had provisions in here that would have dealt with the debarment issue.

Senator DECONCINI. Have either one of you worked on any language on disbarment over your experience?

Mr. HUGHES. No.

Senator DECONCINI. Thank you, Mr. Chairman.

Senator METZENBAUM [presiding]. One last question along that line about debarment.

I remember the Navy not too long ago that had debarred a general contractor and then withdrew the debarment because they said they didn't have anybody else to make the ships for them; there were no other places to go.

What do we do about that? I don't like that solution; in fact, I'm embarrassed by it for our own government. But what's the practical answer to that?

Senator PROXMIRE. As I understand it, the practical answer is that debarment is a Defense Department function. It has been, and it's up to them to do it. And I think we ought to do everything we can to provide, if necessary, legislation to encourage them to do it; require them to do it.

Senator METZENBAUM. Well, my point is that the Navy said that we need the ships, and there are no other shipyards that can make the ships.

Mr. HUGHES. I think the answer, Mr. Chairman, the answer is to diversify our procurement base. Unfortunately, we are hostage often to one particular source and unfortunately, that does in fact work against debarment.

The Department of Defense has no trouble debarring little contractors where they're not essential. It's when we get into the large sole-source providers that we have major problems.

The long term solution is to diversify that base so that we have more competition that we have today.

Senator PROXMIRE. Admiral Rickover had a tough proposal that's very hard for us to accept, but it made some sense. Where you do have only a single source, or an inadequate single source, he suggested that you use the government arsenal.

The government itself should step in. People say, oh, that's socialism. Well, if you have to have that kind of performance, competition, quality, that you're not getting, that's something that you ought to consider.

Senator DECONCINI [presiding].

Senator GRASSLEY. Thank you very much.

I don't know whether anyone has thought about it or not, but here you are, a famous budget cutter, proposing we spend more money on a government program, maybe for the first time in your career.

Does it trouble you any to break with this tradition?

Senator PROXMIRE. Well Senator Grassley, I'm delighted you asked that, because that's right, I'm against spending money on anything.

I have tried to personify the great example of Ebenezer Scrooge. I think that's what we need in government.

However, in this case, it's a great way to reduce the deficit. You spent $8 or $9 million on what you and I are proposing, and there is no question in my mind it will bring in far, far more every year; no question. And it'll bring in fines and so forth, and also, in far better performance and lower cost.

So it is an excellent investment if you enforce the procurement law and prevent the kind of corruption which undoubtedly is increasing the cost of this, what is it, $300 billion a year that we're spending on defense procurement.

Senator GRASSLEY. I believe you were involved in the creation of the Foreign Corrupt Practices Act.

And as everybody knows, that act makes it illegal for U.S. companies to bribe foreign officials. What connections or insights do you see between the overseas bribery cases of the 1970s, and the current defense procurement investigation cases?

Senator PROXMIRE. I think there is a direct and explicit connection. The bribery there also involved defense contractors and weapons. It was the Lockheed Corporation that wanted to sell planes to Japan that paid a $1.4 million bribe to the Prime Minister of Japan.

He was convicted. He went to jail. For Lockheed, the bribe was great business. They made tens of millions of dollars of profits out of it.

Now, think of that for a minute. A $1.4 million bribe to the top elected official. It would be like the President of the United States accepting a million dollar bribe. A horrible shocking shame, for this country as well as Japan.

I am glad you raised that point, Senator Grassley, because I want to tell you something. The trade bill includes in it, unfortunately, a gutting of that Foreign Corrupt Practices Act that we passed in 1977.

If a trade bill passes in its present form, if we fail to amend it on the floor, it's going to mean that the one legislation that we have that has done an excellent job of preventing bribery, of stopping those scandals, is going to be gutted, repealed, and we're going to be once again shamed with enormous bribes that will be paid, because as I say, it is good business.

And incidentally, a study of that 1977 law showed that it did not inhibit exports. As a matter of fact, exports increased in 1978 and 1979, and the two following years are the best time to determine the effect of the law.

So that here is a law that the corporation executives of this country, to their discredit, have successfully lobbied into accepting. They inserted into a 1000-page bill a few lines that gut the law.

And we are going backwards rather than forwards in this area. And I hope that when the trade bill comes up before the Senate we can knock that language out.

Senator GRASSLEY. Congressman Hughes, I also compliment you for your leadership and involvement in this area. I have admired your commitment against waste and fraud since my service with you in the house.

If I could refer to some discussion of your bill that took place before the House Judiciary Committee, Rep. Hurtle recited over 10,451 allegations of waste, fraud and abuse in the Federal Government over a 6-year period, 55 percent of that related to Defense Department activity.

It seems to me to be disproportionate that just under 30 percent of our Federal budget is authorized for defense needs, and yet 55 percent of these cases relate to the Defense Department.

Do you believe that this apparent disproportion is due to the volume of activities that are involved in the defense of the nation?

Mr. HUGHES. I do not think there is any question. It is because of the volume involved, and often it is because of the pace that we were moving contracts out of the system, in the last 7 years in particular. We have put out billions and billions of dollars a day.

In fact, I remember debating just 4 or 5 years ago, amendments on the floor, that would permit a bypassing of the competitive bidding system because we weren't getting the money out fast enough.

Senator GRASSLEY. Do you believe that because of the turnover in those agencies charged with investigation and prosecution of fraud, waste and mismanagement in the government, such as U.S. Attorneys, there is a resource problem that must be cured before any meaningful oversight can be sustained?

Mr. HUGHES. I don't think there is any question that we have a serious problem of turnover within the Justice Department. It is not just in the procurement fraud area, but it is across the board. It has been a serious problem for a number of years, and we have not begun to deal with it.

Senator GRASSLEY. Your bill is very timely. I hope it will really turn the tide, not only in the short-term, but in the long run.

Mr. HUGHES. Well, you are kind to say that. You are one of the public officials, however, who have led the fight for a number of years in focusing attention on procurement fraud. And you are the one to be congratulated for your work and the work of your committee.

Senator METZENBAUM. Thank you very much, Senator Grassley. Thank you, Congressman Hughes, Senator Proxmire.

The Chair himself somewhat embarrassed that my staff, in their enthusiasm to permit everyone to be heard, has scheduled three separate panels.

The first three witnesses will come to the table, please. June Gibbs Brown, Inspector General, Department of Defense, accompanied by Derek Vander Schaaf, Deputy Inspector General; Victoria Toensing, Deputy Assistant Attorney General, Department of Justice, Criminal Division; accompanied by Anton R. Valukas, U.S. Attorney, Northern District of Illinois and Washington, D.C. both, I guess; and Richard Fogel, Assistant Comptroller General from the GAO.

The reason I am embarrassed is that we have that panel and we then have a panel from the U.S. Chamber of Commerce, electronic industries association, and aerospace industries; and then we have a fourth panel which has four additional witnesses.

It is 10:30. I had said that the government witnesses would have 10 minutes. I'd be grateful if you could do it in about seven. And it won't solve all my problems. But somehow I am going to try to move so that everybody has—so that we have a fair hearing out of this, and that nobody feels they have been prejudiced.

June Gibbs Brown, please proceed.

STATEMENT OF A PANEL CONSISTING OF JUNE GIBBS BROWN, INSPECTOR GENERAL, DEPARTMENT OF DEFENSE, ACCOMPANIED BY DEREK VANDER SCHAAF, DEPUTY INSPECTOR GENERAL, DEPARTMENT OF DEFENSE, WASHINGTON, DC; VICTORIA TOENSING, DEPUTY ASSISTANT ATTORNEY GENERAL, CRIMINAL DIVISION, U.S. DEPARTMENT OF JUSTICE, ACCOMPANIED BY ANTON R. VALUKAS, U.S. ATTORNEY, NORTHERN DISTRICT OF ILLINOIS AND WASHINGTON, DC; AND RICHARD L. FOGEL, ASSISTANT COMPTROLLER GENERAL, GENERAL GOVERNMENT DIVISION, U.S. GENERAL ACCOUNTING OFFICE, WASHINGTON, DC

Ms. BROWN. Thank you, Mr. Chairman.

My written statement addresses our comments on the Major Fraud Act of 1988, and the role of the Office of Inspector General, Department of Defense, in the investigation and prosecution of major fraud cases.

Senator METZENBAUM. Want to bring the mike a little closer, please?

Ms. BROWN. We enthusiastically support the bill, and have prepared a few comments on some minor revisions that have been addressed by the House. I have included those comments in my statement.

I have also included a description of numerous cases that have been investigated by my office, that may be important to consider in your deliberations on this bill.

I would also like to point out the attachments to my statement, which show some of the progress we have made in our enforcement of the laws, as they currently stand.

We've had very significant increases in monetary recoveries, and I have a graph to demonstrate that point. The first half of 1988 has witnessed a 50 percent increase over last year's total monetary recoveries. Those have been gained with the cooperation of the Department of Justice.

We also have a graph that shows the increase in suspensions and debarments by the Department of Defense since the Inspector General Act was created.

In 1981 there were a total of 80 suspensions and debarments. In the last 2 years, we have had almost 900 per year. This year we have had 467 already in the first half. So this is a very useful tool that Defense is using when some kind of contractor irresponsibility is identified.

There has also been a significant increase in the number of fraud trained investigators in the Department of Defense. I have included a graph which points that out.

I am not saying, of course, that we don't need more resources, and that we could not do a better job if we had them. But I would like to recognize the significant progress that has been made.

I would like to submit my full statement for the record, and I am certainly available for questions.

[The prepared statement of Ms. Brown follows:]

HOLD FOR RELEASE
UNTIL DELIVERY
EXPECTED 9:30 A.M.
JULY 12, 1988

STATEMENT OF

THE HONORABLE JUNE GIBBS BROWN

INSPECTOR GENERAL

DEPARTMENT OF DEFENSE

BEFORE THE

COMMITTEE ON THE JUDICIARY

UNITED STATES SENATE

ON THE MAJOR FRAUD ACT OF 1988

JULY 12, 1988

It is a particular pleasure to be here today to testify regarding H.R. 3911, "The Major Fraud Act of 1988," and the role of the Office of Inspector General, Department of Defense, in the investigation and prosecution of major fraud cases. My Deputy, Derek Vander Schaaf, shared these views with the House Subcommittee on Crime during their consideration of the Major Fraud Act and I am pleased to bring them to the Senate.

THE MAJOR FRAUD ACT OF 1988

We support the bill as passed by the House of Representatives. The amendments made by the House Committee will prove to be helpful in clarifying the purpose, intent and application of this legislation. We particularly like the language in the bill which extends the statute of limitations to seven years after the offense is committed. This is appropriate in light of the practical constraints on the Defense Contract Audit Agency auditors, who often cannot even commence incurred cost type audits until months or often years after the submission of contractor claims for payment. Once commenced these audits often take months to complete. It is from these incurred costs audits that the Defense Contract Audit Agency sometimes identifies indications of fraudulent accounting practices on the part of contractors. In such cases, it is not unusual, because of the unavoidable delays in scheduling the audits, for criminal investigators to first receive the allegations

well into the current five year statute of limitations. Given the complexity of accounting issues involved, the criminal investigations of these audit referrals often may require many months or years to complete. The consequence of this series of events is that it is not uncommon for our investigations to run to a point where the current five year statute of limitations becomes a pressure factor in the ultimate prosecutive decision-making process. Alleviation of this pressure through extension of the statute of limitations to seven years is a revision of current law which we therefore enthusiastically support. An extension of the criminal statute of limitations would further the efforts begun by Congress last year when the statute of limitations in the Civil False Claims Act was extended.

Another provision which the Office of the Inspector General endorses is the reward provision which permits payment of up to $250,000 to any individual who furnished information leading to conviction under the provisions of this legislation. This mechanism, as contrasted to the qui tam provisions of the Civil False Claims Act, provides for a more direct means of rewarding true whistleblowers whose information leads to a conviction under this section. We do believe, however, that requiring a whistleblower to first report his allegations to his employer--who may be the ultimate defendant in a resulting Government action--can only act to deter the sort of good citizen involvement the Bill is supposedly designed to encourage. We certainly hope that most

contractor employees are able to raise concerns about questionable business practices to their employers. But we also understand the real world. While we support self-policing by industry, we should also encourage Government contractor employee's to report suspected fraud directly to the Government when they fear retribution by company officials or have concerns over the company's willingness to take appropriate action. In addition, further clarification is needed regarding the rights of Government employees to obtain a reward under the Act. We believe that Government employees, whose official duties are in no way involved with the audit and investigation of the fraud, or with the program which is the subject of the fraud, should not be automatically precluded in sharing in the reward. The Attorney General should be provided sufficient flexibility to determine eligibility through implementing regulations.

Another important provision of H.R. 3911, which we strongly endorse, is the mandatory mandatory minimum incarceration of two years for defendants convicted for product substitution when the offense involved a forseeable and substantial risk of personal injury. Historically, punishments for crimes of this kind against the Department of Defense have not been appropriate to the egregious nature of such crimes.

I would like to point out an additional concern regarding maximum fines under existing law. As you are aware, with the

November 1987 implementation of the Federal Sentencing Guidelines, there is an element of uncertainty regarding the maximum allowable fine for violation of Title 18 of the United States Code. While Congress moved swiftly to rectify this problem, I am concerned that one element of existing law may have been unintentionally nullified. Under Section 931(a) of the Department of Defense Authorization Act of 1986 (Public Law 99-145), Congress increased the criminal penalty for a violation of the False Claim Act (18 U.S.C. 287) on Department of Defense contracts to a maximum fine of $1 million. This provision has never been codified. Our discussions with the staffs of Congress, the Department of Justice, and the Sentencing Commission have resulted in a concern that both the Federal Sentencing Guidelines and subsequent clarifying legislation may have overlooked this provision. Therefore, its current status is open to question. We are strongly in favor of the $1 million maximum penalty per claim for false claims on Department of Defense contracts, particularly as it applies to claims by corporations. I urge this Committee to provide clearer guidance in this area.

We are also concerned that the Bill should not require proof of a specific intent to defraud in order to obtain a conviction. Currently, most fraud cases are prosecuted under the False Statements Act (18 U.S.C. 1001) and the False Claims Act (18 U.S.C. 286, 287). The majority of courts have held that these statutes penalize the provision of false, fictitious or

fraudulent claims and statements. If the indictment only alleges that false or fictitious, and not fraudulent, information was knowingly submitted to the Government, then the Government is not required to show a specific intent to defraud. Specific intent is often impossible to provide. The House Report on this Bill contemplates that "knowing" include deliberate ignorance or "willful blindness" of the facts which form the basis of the fraud. We concur and would further include the concept of "reckless disregard." Thus, the Bill should clearly state that specific intent need not be proven in order to establish liability under the Act. The House Report on the Bill clearly states that specific intent is not required. Such an interpretation from the U.S. Senate would be consistent with the amendments which were passed by Congress last year which clarified that specific intent need not be proven in order to establish liability under the Civil False Claims Act, and the Program Fraud Civil Remedies Act.

THE ROLE OF THE INSPECTOR GENERAL, DEPARTMENT OF DEFENSE IN PROCUREMENT FRAUD

Over the past few years, Congress has clearly been responsive in providing the executive branch with more tools and remedies to combat fraud. The best example of such congressional initiatives was the passage of the Inspector General Act of 1978, and the Department of Defense amendments thereto in 1982. The DoD was

not included among the agencies covered by that original IG legislation. Rather, the Secretary of Defense was asked to staff a study group to determine how best to attack fraud and waste in the Department. The group concluded that a senior official, reporting directly to the Secretary, was required to coordinate the overall effort to achieve economy and efficiency in Defense programs. Secretary Weinberger followed that recommendation in April 1981 by creating the position of Assistant to the Secretary of Defense (Review and Oversight).

Because, in large part, of the success of the Review and Oversight Office, and the perceived need by the Congress to arm that organization with full investigative tools. The Fiscal Year 1983 Defense Authorization bill contained language which created a statutory Inspector General for the Department of Defense and consolidated under that official the Defense Audit Service, the Defense Criminal Investigative Service, the Inspector General for the Defense Logistics Agency, and the audit policy function formerly held by the Office of the Comptroller. The new Inspector General further created an office for Audit Followup and one for Criminal Investigations Policy and Oversight, the latter of which issues investigative policy applicable to all criminal investigative organizations within the DoD and generally oversees the Department's effectiveness in conducting fraud investigations. Special emphasis has been placed on ensuring the effective coordination of all available criminal, civil and

administrative remedies for fraud, and in coordinating voluntary disclosures of fraud by Defense contractors.

As the Inspector General function grew in DoD, so did its paybacks. While the organization has doubled in size since 1982 to meet the increasing challenges of watching over tax dollars entrusted to the Department, the monetary benefits and cost avoidance identified by the Inspector General auditors alone have averaged 25 times the cost of supporting the entire Department of Defense Inspector General organization.

We have also built an impressive record in pursuit of criminal allegations against those who seek to defraud the DoD.

In partnership with the Department of Justice, we have aggressively pursued prosecutions of procurement fraud and corruption. Our top priorities are offenses involving product substitution, mischarging of costs, and fraudulent defective pricing, as well as schemes which undermine the foundation of our integrity based system of contracting, such as bribery, kickbacks, and antitrust matters.

From Fiscal Year 1984 through Fiscal Year 1987, the Defense criminal investigative organizations (DCIOs) have had a major impact on contract fraud. The DCIOs are the four criminal investigative organizations within the DoD that are responsible

for contract fraud investigations: the Army Criminal Investigation Command, the Naval Security and Investigative Command, the Air Force Office of Special Investigations, and the Defense Criminal Investigative Service, which is the criminal investigative arm of my office. Together, these offices are responsible for over 1,250 convictions and the return of over $400 million to the United States Treasury in criminal fines, civil fraud judgments, and other forms of recoveries. Attached to my statement is a chart which shows the rise in criminal fines, restitutions, and other recoveries such as False Claims Act judgments.

I should also note that in order to achieve these results, my office has encouraged each of the Defense investigative organizations to increase the number of agents who are dedicated to fraud investigations. Another chart attached to my statement shows that in Fiscal Year 1982, the Department of Defense fraud agent strength was 375. As of the end of Fiscal Year 1987, that number had risen to almost 1,000.

Product Substitution. Our number one priority has been, and will continue to be, product substitution. Product substitution is when a contractor deliberately provides an inferior product on a DoD contract. It is that offense which can most directly cost service members their lives. Substandard, defective, or counterfeit goods in our weapons systems have no

place on the battlefield and can only lead to horrendous consequences.

Since January 1986, the Defense Criminal Investigative Service has obtained indictments against more than 100 individuals and contractors who were found to be involved in product substitution schemes. Currently, the Defense Criminal Investigative Service is carrying over 225 open product substitution investigations. Let me provide you with some representative samples of our most successful product substitution cases:

Spring Works, Incorporated - This company deliberately provided defective springs which were ultimately installed in critical assemblies of the CH-47 helicopters, the Cruise Missile, as well as the F-18 and B-1 aircraft. The company falsified testing and inspection certificates. Two corporate officials were convicted, fined, and imprisoned.

Diversified American Defense - This company had a scheme to provide defective fins to be installed on 60 millimeter mortar rounds. The defective fins caused the mortar rounds to veer off target. The vice president of the company ordered company employees to pack and ship defective parts, then falsified testing documents to show that the fins were in compliance with the contract. The company and the vice president were convicted. The vice president was imprisoned

for one year, and the vice president and the company were fined over $900,000.

MKB Manufacturing - This company deliberately provided defective gas pistons which were to be installed in the M60 machine gun. Once installed, the defective part would cause the machine gun to jam. One corporate officer was sentenced to serve 18 months, while another was sentenced to provide a few hundred hours of community service.

Waltham Screw Company - This company engaged in a pattern of deliberately providing defective flash suppressors for the M16 rifle. A corporate officer, when informed of the damage which could be caused by a defective rifle, stated that if one soldier was killed, there would be more around to complete the job. This official and the company were convicted. The company was fined $125,000, and the official was given a year in jail.

As you can see, while these criminal schemes are often life threatening and can have a disastrous effect on the ability of our troops to complete their mission, we have not received a significant sentence on most of these cases. A recently completed study by my office concluded that more information must be provided to the court at time of sentence which will identify the adverse safety and mission impact of product substitution schemes. My

office and the Department of Justice are working on procedures to implement this recommendation. Furthermore, based on our recommendation, the recently enacted sentencing guidelines provide for an increased criminal sentence for product substitution cases.

Cost Mischarging/Defective Pricing. As representatives of my office have testified before the Senate Armed Services Committee and elsewhere, the investigation of cost mischarging and defective pricing by contractors is a top priority of our agents. Those cases represent two of the most common and serious abuses found in public contracts. They are also among the most complex investigations, with a myriad of cost allocation systems and procedures to be untangled, and the need for expert audit assistance. Not only do those schemes undermine our procurement process, but the impact is always greater than the actual dollars lost to misallocation or overpricing. For example, when direct labor costs are intentionally overcharged, so are the associated overhead and administrative expenses. Since those costs often exceed 100 percent of the labor costs, such mischarging ultimately results in greater than double the loss to the Government.

Let me share with you some of the mischarging and defective pricing cases which we have completed:

Cost Mischarging:

TRW - An investigation conducted by the Defense Criminal Investigative Service and the Defense Contract Audit Agency concluded that TRW had mischarged cost overruns on fixed price contracts on to DoD cost type contracts. TRW pled guilty in September 1987 and has repaid over $12 million in fines and restitution.

AVCO - An investigation conducted by the Defense Criminal Investigative Service and the Defense Contract Audit Agency concluded that AVCO had improperly charged Independent Research and Development and Bid and Proposal costs on to DoD cost type contracts. In June 1987, AVCO pled guilty to criminal charges and agreed to pay over $6 million in fines and recoveries.

Rockwell International - An investigation conducted by the Defense Criminal Investigative Service and the Defense Contract Audit Agency concluded that Rockwell had engaged in cost mischarging on Air Force radio contracts. Rockwell pled guilty and repaid over $1.2 million in criminal fines and recoveries.

Defective Pricing:

JETS, Incorporated - An investigation conducted by the Army Criminal Investigation Command and the Small Business Administration Inspector General resulted in the racketeering conviction of the contractor who submitted false cost estimates on numerous DoD laundry contracts. The contractor and its officers were sentenced to repay over $12 million in criminal fines and forfeitures.

Hayes International - An investigation conducted by the Air Force of Special Investigations, the Naval Security and Investigative Command, and the Federal Bureau of Investigation resulted in the conviction of an aircraft maintenance contractor for a consistent pattern of deliberate overstatement of labor costs. The contractor repaid over $2 million in fines and civil penalties.

Litton Industries - A Defense Criminal Investigative Service and Army Criminal Investigative Command investigation proved that the Clifton Precision subsidiary of Litton Industries had repeatedly overpriced Army contracts. Litton officials would add a "chicken fat" factor on to legitimate costs in order

to overstate prices. Litton pled guilty and paid over $10 million in fines and recoveries.

Harris Corporation - An investigation by the Defense Criminal Investigative Service and the Federal Bureau of Investigation resulted in the conviction of the Harris Corporation for a pattern of submitting false cost estimates on Army and NASA contracts. Harris paid over $9 million in fines and restitutions.

I would like to particularly emphasize the fact that many of these investigations were prosecuted in the offices of the United States Attorneys in whose jurisdiction the offenses occurred. Our ability to work directly with local United States Attorneys is an important complement to our effective relationship with the Defense Procurement Fraud Unit at the Department of Justice in Washington, D.C.

Coordination of Remedies. As I mentioned earlier, a high priority of the Office of the Inspector General, through the Office of the Assistant Inspector General for Criminal Investigations Policy and Oversight, has been to ensure that all available civil, criminal, contractual, and administrative remedies are appropriately considered and used in each case.

We are very proud of our record in this regard. Early on, we recognized a number of areas where the Department clearly needed to enhance its procedures to effectively resolve issues involving fraud. One of those was suspension and debarment -the procedures whereby corrupt contractors can be barred from doing business with the Government.

In a report issued in 1984, the Inspector General concluded that more positive steps were required to improve the effectiveness of these tools. More information from criminal investigators was recognized as a vital element to enhance suspension and debarment activity. All three Services and the Defense Logistics Agency concurred, and the DoD record on suspension and debarments has subsequently improved.

Since 1982, the number of DoD suspension and debarment actions has increased by over tenfold. A chart attached to my statement demonstrates the dramatic rise in suspension and debarment actions over the last eight years.

While we believe that we have demonstrated success in many of our antifraud initiatives, we are constantly aware of the need to improve the framework of laws under which we seek to attack major procurement fraud. For this reason, we have supported legislation such as amendments to the Ethics in Government Act to tighten "the revolving door," the Program

Fraud Civil Remedies Act, the 1986 amendments to the False Claims Act and the proposed Major Fraud Act of 1988.

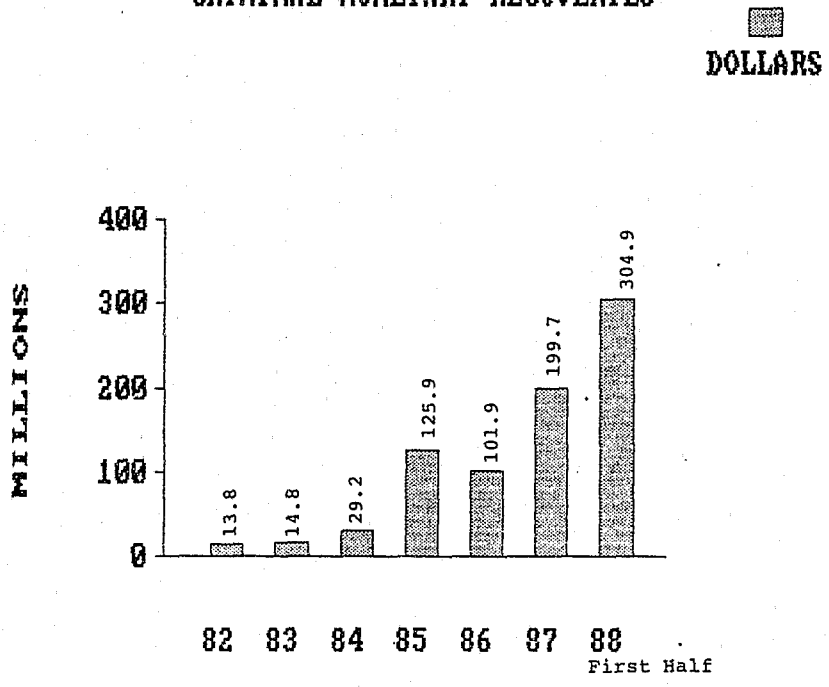
Mr. Chairman, that concludes my statement. I would be glad to answer any questions you may have.

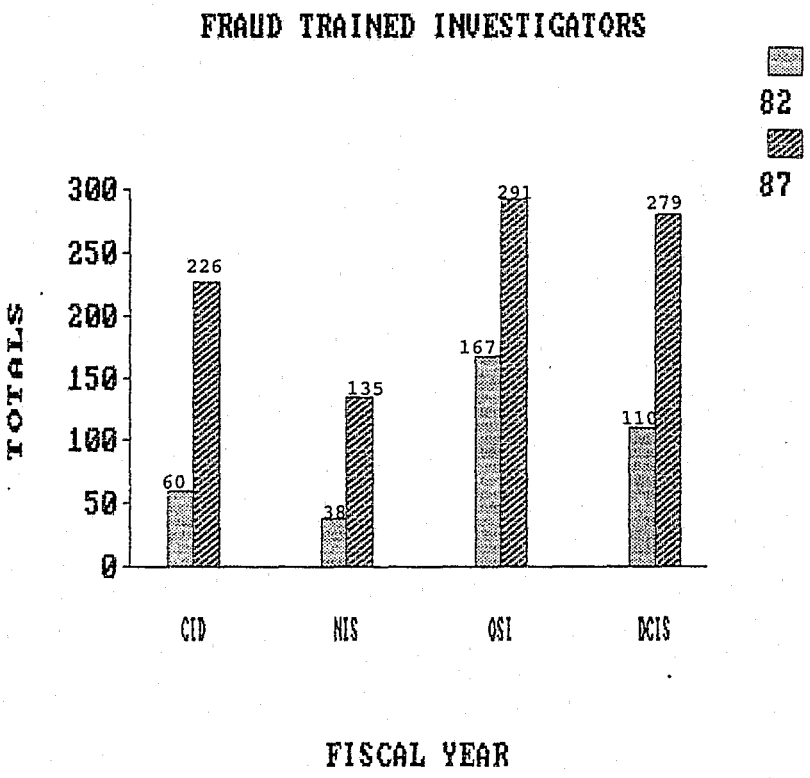
Increased Suspensions and Debarments

FY	Suspensions	Debarments	Totals
1981*			80
1984	134	268	402
1985	225	357	582
1986	470	415	885
1987	393	505	898
First Half 1988	173	284	457

*Data collected on a calendar year basis from 1981 through 1983.

CRIMINAL MONETARY RECOVERIES




FRAUD TRAINED INVESTIGATORS
82
87
TOTALS
300
250
200
150
100
50
0
60
226
38
135
167
291
110
279
CID
NIS
OSI
DCIS
FISCAL YEAR

Senator METZENBAUM. Without objection, all the statements of all of the witnesses today will be included in the record without further order.

I think I am going to inquire of the witnesses individually as they conclude their testimony. Let me ask you about some disturbing reports about former Pentagon officials convicted or suspected of criminal activity who later became defense contractors or consultants.

Mark C. Saunders, is a former Navy contracting official who was found guilty of making money in the stock market on the basis of insider information about a contract his staff had negotiated.

After his dismissal, Mr. Saunders became a defense industry consultant. According to Federal court papers, he is now being investigated for bribery in the current scandal.

Another case involves Richard D. Ramirez, a former Navy official who has been repeatedly accused in Federal court testimony of accepting bribes in connection with the Wedtech scandal.

After leaving the Navy, Mr. Ramirez acquired a firm that won a $14 million Navy contract. Despite the bribery allegation, he reportedly has been allowed to continue dealing with the Navy, and even had his security status raised from confidential to secret.

Those are only two reported cases of convicted or suspected Pentagon wrongdoers who it seems were free to leave and set up shop as Pentagon business persons. For all we know, there may be many others.

To me, I am frank to say to you, it is incredible that such individuals, rather than being disbarred or suspended, actually could turn around and do business with the Department.

I am not certain how that could be. I am not blaming you, Ms. Brown. But doesn't the Department disciplinary rules bar such employees from doing business with the Department for at least a specific period of time?

Mr. VANDER SCHAAF. I guess maybe it would be more appropriate if I tried to answer that for you, Mr. Chairman. I am the Deputy Inspector General and was on the job while some of the activities took place.

With respect to Mr. Saunders, I am not intimately familiar with the previous prosecution that apparently involved trading in a stock in which he had insider information. I do not want to make any excuses for the Department here, because that case should have resulted in a review of his security status and whether or not he could, in fact, retain a security clearance following a Federal conviction.

I do not know what happened in that particular case, or why it happened. I think it is very unfortunate. You have to remember though, after he left the Department of Defense, as far as I know, he did not have any direct consulting arrangements with the Department or contractual arrangements with the Department. He had a contract with other companies which did business with the Department of Defense.

Regarding Mr. Ramirez situation, I do not believe that he was ever charged with anything while he was an employee of the Department of the Defense, and therefore, there would have been no

reason for the Department of Defense to suspend or debar him prior to the time he left.

Now that is an open case, and I cannot comment any further on it at the present time.

Senator METZENBAUM. You would not think that it would call for some action on your department when he is accused in open Federal court of accepting bribes in connection with the Wedtech scandal, and you would not think that that was a sufficient cause to move in and determine what his relationship is with the department?

Mr. VANDER SCHAAF. We are doing that at the present time, Mr. Chairman. We are involved in investigating the Wedtech scandal. Therefore I cannot comment any further on that at this point with respect to Mr. Ramirez. It is an open investigation.

Senator METZENBAUM. Well, I have to say to you, Mr. Vander Schaaf and Ms. Brown, I think what concerns us is the precision and the dotting of every "i" and crossing of every "t" in aggressively moving in when you find people who have questionable relationships, questionable activities, who have—you make a distinction between being found guilty with respect to insider trading in the SEC and find no relationship to that as far as the Department of Defense is concerned.

Mr. VANDER SCHAAF. Oh, there is clearly a relationship. In Mr. Saunders' case, I do not know what happened. And I would say it has to be looked at again. I do not know why he continued to receive a security clearance under those circumstances.

Senator METZENBAUM. I think what the American people are saying is that you can give us a list of increased numbers of debarments, and yet every time they pick up their paper, they find that programs that they are concerned about are being cut back and defense contractors are ripping off the American Government.

Mr. VANDER SCHAAF. Ms. Brown will tell you, we are here to stop them, and we have been doing so. That is what the 900 suspensions and debarments annually are all about. They are a result of the process. That is what the great increase in the number of indictments and convictions mean. Great progress has been experienced each year since the creation of the Office of Inspector General. This is a matter of record.

The situation is not getting worse. From that aspect, the situation is getting better; if you judge success by convictions and indictments. I sometimes wish we would not have to go through the convictions and indictments phase, and that industry would help to police itself. Unfortunately it does not always happen.

Senator METZENBAUM. Does debarment mean that they are totally barred from further contracts? Or what does it mean? How do you define a debarment?

Ms. BROWN. When an individual or a company is debarred, it is usually for a period of 3 years, but that can vary. It is an evaluation of their present responsibility in doing business with the Government.

Senator METZENBAUM. What was that last thing? An evaluation of what?

Ms. BROWN. Their present responsibility. When the Department looks at a company to determine whether or not it should be de-

barred for a particular offense, we look at the way they operate, whether they had knowledge of an offense, or should have had knowledge, and whether or not they have controls in place and have followed them to identify this type of activity. If it is found that they do not have controls, and they have not made an attempt to put them in place, or that they looked the other way, for instance, when things were happening that should have tipped them off, then they are certainly subject to suspension or debarment.

Senator METZENBAUM. And how long would you say the average debarment is of these 898 in 1987?

Ms. BROWN. Well, the period is 1 to 3 years. I do not know exactly what the average period is. But for the most part——

Senator METZENBAUM. Would you tell me what major companies have been debarred, names that we would recognize as being defense contractors? Because that is a large number, 898, and yet I have not heard of any major companies being debarred. Are there any?

Mr. VANDER SCHAAF. I do not believe any major companies have been debarred for a long period of time. A dozen or so, or a half a dozen to a dozen have been suspended for periods of time. Various divisions have been suspended.

You asked the question, Mr. Chairman, early on, of Representative Hughes, why we do not suspend and debar the big companies. You got into the discussion that they are the sole providers of these resources.

Our office has historically pushed for suspension and debarment of the officials of those companies. I do not think you want to take it out on the workers by putting those companies out of business. Most employees generally have nothing to do with illegal activities and are not responsible. That shipbuilder laborer out there in the shipyard was not responsible for the fraud that took place, and I am not sure it is correct to put him out of business because one of his bosses further up the line defrauded the Government.

We ought to get his boss out of the business and get him out of the business permanently. We have strongly recommended that from time to time to the suspension and debarment officials of the Department of Defense.

Senator METZENBAUM. Mr. Vander Schaaf, you lost me.

You are now saying that we have not debarred any major companies, and you are saying we are not sure we ought to do that because it would result in hurt to the employees, maybe the community as well. And I understand that. Now, then, you also tell me that 898 debarments occurred in 1987, 505 in 1986, and 393 suspension.

Now, my question is: Are you saying that we only take the little guys and debar them and suspend them because not as many people are involved and that that is part of the evaluative decision? I am lost.

Mr. VANDER SCHAAF. Not at all, Mr. Chairman. We suspend and recommend suspension of big guys and little guys. Let's face it. There are 100,000 little companies doing business with the Department of Defense. You take the top 50 companies, and you have got probably 70 percent of the total procurement dollars spent in the Department of Defense. So, obviously, you are going to have far

more suspensions and debarments involving small companies than you will large companies.

Now, you also have to face the realities of the situation. Large companies have, if you will, advantages when it comes to a suspension or debarment situation because the Department of Defense is charged with providing for the defense of the United States. And if we stand to lose critical weapons systems for long periods of time, we have to take that into consideration. There is no way to avoid that problem.

That is why our office has historically said we have to get the corrupters out of the business.

Senator METZENBAUM. Mr. Vander Schaaf, I can understand what you are saying when you are telling me about a Navy yard. I cannot understand it when you are talking about some avionics, when you are talking about some electronic equipment, and I am really getting the message from you that: "Well, we are only picking on the little guys but we are not picking on the big ones because we cannot afford not to do business with them; besides, you put too many people out of work." And it leaves me with a negative feeling.

Mr. VANDER SCHAAF. Let me respond one more time. I will try to get my point across to you, Senator. I can only say, ask the big guys if you do not think we are picking on them. They know they are under investigation.

Senator METZENBAUM. Ask the average American if they think you are picking on the defense contractor. They think that it is a piece of cake to walk in and steal money.

Ms. BROWN. Mr. Chairman, we try very hard to see that these kinds of sanctions are imposed on the people responsible and the units responsible. It is not necessarily proper, aside from the fact that we need the resources of those companies, to debar an entire company if we can identify the elements within that company that have responsibility for the actions. We have not yet identified an entire large contractor, and I do not expect to, that has a general policy that would indicate some kind of improper or illegal activity with the Government.

I think that the American people have to be aware of the kinds of aggressive actions that are being taken. The current case is a good example of the various elements of the law enforcement community working together. The Department of Justice, U.S. Attorney's Office, the various elements of law enforcement, including the FBI, Naval Investigative Service, the DCAA auditors, as well as my own organization, the Defense Criminal Investigative Service—have all supported this investigation, and they are working very hard toward a successful conclusion and successful prosecutions of those people responsible. Although we are all appalled at the kind of activity that sometimes take place, and the offenses that people commit, we still have to recognize that proper actions are being taken. The Department is working to get these people out of the business.

Senator METZENBAUM. Senator Grassley.

Senator GRASSLEY. Mr. Chairman, just to follow up on your line of questioning, I am reminded of what a wise man once said. Laws are like cobwebs: They catch the little flies, but the hornets and

the wasps get through. That might explain the historical problem that I outlined in my opening statement.

What you describe is really a problem, and sometimes I think there is a big public relations game played by the big defense contractors. It is announced in the newspapers that so-and-so is suspended or debarred; and then down the line, 3, 4 months, maybe when there is another contract that has to come up for negotiation, you read about how the suspension or debarment is lifted. We really need to study that when there is a debarment or a suspension, how long-lasting that is.

I would like to ask either Ms. Brown or Mr. Vander Schaaf, am I not right that the DOD, IG agency has regional offices for its DCIS investigators?

Ms. BROWN. Yes, sir.

Senator GRASSLEY. Could you elaborate for me on why you have regional offices instead of centralized direction from the Pentagon?

Ms. BROWN. Well, the offenses take place throughout the United States, and sometimes outside of the United States. The investigative activity is such that it is very important for the people to be very close to the problem under investigation. They have to identify sources; they have to work with this very intensely day to day. Our people work with the local U.S. attorneys as well as the Defense Procurement Fraud Unit, and these successful prosecutions we are talking about are taking place because of that day-to-day relationship and the close coordination that takes place at the site where these crimes and offenses are occurring.

Senator GRASSLEY. Would it be fair to say that the regional concept of investigators and prosecutors is dedicated solely to combating major procurement fraud, and that it is potentially better than the current structure, particularly if more resources are devoted?

Ms. BROWN. Well, I am certainly in favor of more resources being devoted. I have not done any in-depth study of how those might best be applied, and I would like to defer to the Department of Justice.

Certainly, building up those U.S. Attorney Offices would be helpful as well.

Senator GRASSLEY. Would it be fair to say that the age-old problem of cooperation between investigators and prosecutors, particularly between DOD and DOJ, could stand to be improved, and that the regional fraud unit concept might help in that regard?

Ms. BROWN. I think that is always fair to say. We work very hard at improving those relationships, and in very active investigations such as those we are involved in, there is always room for misunderstandings or people hoping that others would do a little bit more. I am sure they feel that way about investigators, as we do about prosecutors.

However, the relationship is greatly improved, and, of course, this would have the potential for improving it even further.

Senator GRASSLEY. Your predecessor, Joe Sherick, in several congressional hearings, spoke of the difficulty he had with prosecutors, and that it was his job to push prosecutors to move his cases. In 1985, when he was before my committee, I quoted him speaking about prosecutors: "We send them letters, we call them up, we talk

to them, we do everything we can but stand on our heads because that is our job to try and get our cases handled."

Have you ever heard complaints from your investigators that cases that they have worked on have languished when they are referred to the Justice Department, and that they cannot learn from Justice whether they have been accepted or declined, and that these delays slow down the momentum of the investigations?

Ms. BROWN. I have heard investigators complain if the priorities are such that their case cannot be considered on the top of the heap. But I have heard much more praise. We have had numerous areas where we have worked together in a partnership. Sometimes we have had ongoing investigative activity that has taken place in conjunction with the U.S. Attorney's Offices, even for a period of years. The *DefCon* investigation in the Los Angeles area is a good example of where not only the U.S. Attorney's Office but my office, NASA, DCAA, and the IRS all participated. This investigation is still going on. Training was jointly given by our offices to U.S. attorneys in other parts of the country, and that same type of activity, which is parallel to the current case, is going on now in three other parts of the country and is under consideration for even more areas.

So I think that the situation that Joe Sherick addressed earlier has been tremendously improved. We have a very good record of successful prosecutions and increases in those prosecutive activities. And that certainly cannot be done by us in isolation.

Senator GRASSLEY. I am not so sure that it is the exception rather the rule, but from what I hear reported to me directly, I guess I would ask you to look a little more dispassionately at the operation. You might come to a different conclusion. But I will leave that for the entire record.

Thank you, Mr. Chairman.

Senator METZENBAUM. Thank you.

Ms. BROWN. Sir, if I could just say, I have been in this job now for 8 months. I have looked at the previous record and looked at the conditions that exist now, and I think there is a contrast to what was being done before. There certainly is room for more improvement, and we will be working on that.

Senator METZENBAUM. Ms. Brown, let me conclude by first complimenting you on the story written about you, first for coming from my own community of Cleveland, and secondly, the excellent article about you in the February 14, 1988, Plain Dealer, which is very complimentary and indicates your strong record of achievement.

Having said that, let me tell you that one quote in there is a little disturbing. That is, " 'I would like to try to increase the comfort level between contractors and the Inspector General and the Department of Defense,' the native Clevelander said in an interview at her office." And I think that we in the Congress are so concerned about what has been taking place at the Department of Defense that we would like to ask you to change that to maybe make it into a discomfort level.

We think the contractors have been too comfortable at the Department of Defense, and the American people, as a consequence, are the uncomfortable ones. Let us reverse that, if we can.

Ms. BROWN. Thank you, sir. I would like to comment on that briefly, if I may.

Senator METZENBAUM. Yes, of course.

Ms. BROWN. It was not an exact quote, but basically, I have taken upon myself the responsibility to increase the communication and the ability of contractors and the Government to work together. The kind of fraudulent activity that has been identified, particularly recently, is something where there is no question about using an aggressive approach. We need to take whatever actions are within our power to see to it that it is permanently ended.

However, there are a vast number of people who are trying to do a good job and need to be able to communicate with the Department of Defense. We need to clearly communicate to them what kind of safeguards we expect them to have, and what they are expected to do, if they identify problems within their own organizations.

One of the statistics given in earlier testimony related to the DII, the Defense Industry Initiatives, to which 46 contractors have signed up. In earlier testimony that Derek and I have given, we were asked how many of the contractors are under investigation. The statement at that time was that we were not sure. It was estimated to be about 39. The correct number is 38. But I would also like to point out that 25 of those 38 contractors have made voluntary disclosures.

Now, in a few cases, there are also independent investigations, but of those 35, 25 contractors have made voluntary disclosures to the Department of Defense. This is not a cure-all; it is a small step in the right direction. We are getting information that was not available to us before, and we are trying to work in conjunction with contractors who are trying to obey the law and do a good job. I think such work has to be done.

Senator METZENBAUM. If they had not made the disclosures, those 25 out of the 35, would the Department of Defense have known enough to proceed against them?

Ms. BROWN. To be in the voluntary disclosure program, it has to be a matter that is unknown to the Government at the time of the disclosure. Now, I do not want to soft-pedal this. At many of those companies, we have ongoing investigations where, even if they disclosed it, the matter was known to us at the time and that is not entered into the program.

In addition, we have investigations going on of contractors who have never made a voluntary disclosure, and we wonder whether or not they are serious about the systems in place. But I do not think we can take the statistic which was given earlier and condemn industry for being under investigation.

Senator METZENBAUM. Thank you very much, Ms. Brown.

Ms. Victoria Toensing, Deputy Assistant Attorney General, Department of Justice, we are happy to have you with us again.

STATEMENT OF VICTORIA TOENSING, DEPUTY ASSISTANT ATTORNEY GENERAL, CRIMINAL DIVISION, U.S. DEPARTMENT OF JUSTICE, ACCOMPANIED BY ANTON R. VALUKAS, U.S. ATTORNEY, NORTHERN DISTRICT OF ILLINOIS

Ms. TOENSING. Good morning, Mr. Chairman, and I would just like to reiterate that it is a pleasure working with the Department of Defense. June Brown and I, when some problem arises, we pick up the phone and we call each other and we meet. And we are working out any glitches that we see. So it has been a very enjoyable relationship. She and Mr. Vander Schaaf have been very responsive to our needs, and I hope we have been to theirs. We will continue to do that.

Thank you for asking the Justice Department views on H.R. 3911. I want to come right out front and say we wholeheartedly support this legislation. We welcome it. We have laws that we are working with that originated about 80 years; and while we have been able to fit most of our prosecutions into these very specific, older statutes, we welcome what we consider a fine new tool for going after a specific fraud.

There are really five significant provisions in this piece of legislation, and I would like to just go over each of the five very briefly to stay within your time limits.

The first is the creation of the general fraud crime in the procurement process. This idea is very similar to what we had in the bank fraud area several years ago when we came here asking for help in that area because we did not have a specific bank fraud crime. We were always having to find some kind of connected act, like a false statement, an 18 U.S.C. 1001. Since that bill was passed, that is now 18 U.S.C. 1344, that has become the statute of choice for our prosecutors in bank fraud cases. So we welcome this new piece of legislation. While we do not need it quite as drastically as we did the bank fraud, we certainly welcome that.

The penalties. You have opted to increase the penalties and the fines, and we certainly welcome that. Some judges have been good in the past years, and they have improved their sentences on white-collar criminals. But some have been very slow to give these kinds of criminals any kind of time whatsoever. But let me provide a caveat to you that the statute might not immediately provide all of us the longer sentences we seek in this area.

Offenses committed on or after November 1, 1987, will be subject to the sentencing guidelines, as we are all aware, unless the Supreme Court does otherwise. At this time, we cannot really predict what kind of outcome these guidelines are going to have. We are going to take a guideline for a first offender, which is usually the case in this kind of crime—you have first offenders most of the time. And if you have a first offender who organizes a group of five or more persons in a procurement fraud, costing the Government more than $5 million, he or she would receive 46 to 57 months under the guidelines. That is short of 5 years, which can very easily be figured out.

But we say go to it. Let us increase those sentences, because the Sentencing Commission will continue to re-evaluate what their guidelines are. And so if they see that we in the executive branch

and you in Congress are pursuing higher sentences for these kinds of crimes, then maybe they will up some of their guidelines. So we have nothing to lose and everything to gain by endorsing this kind of legislation.

On the statute of limitations, again, we wholeheartedly support increasing the statute of limitations to 7 years. These cases are very complicated and require thousands of hours to analyze sometimes literally millions of documents. So we need this increase on the statute of limitations.

In legislation that we had given to this committee in 1987, we had recognized that problem, and we had asked for an increase in the statute of limitations in a more complicated kind of formula, which would have resulted in a maximum of 8 years. But this is a simpler, cleaner approach to it, and we like your approach better than ours. We like the flat 7 years, and we hope that that is included.

The rewards for the whistleblowers. Again, we support this. We think that that is a nice incentive to reward those persons for providing information which leads to a conviction, and it is similar to the drug enforcement legislation which we have also endorsed.

On the whistleblower protection, recently Congress has enacted two whistleblower protection statutes, one in the False Claims Act and the other in the National Defense Authorization Act of 1987. We in no way condone any retaliation against those persons who would cooperate with our efforts to investigate and prosecute procurement fraud. However, what we would like to see is for you to wait until we see how these two statutes work in the present system before we pass any more legislation. And let me point out a very important reason why.

Presently, this provision could conflict with DOD policy, which is that a corporation should punish those persons who are responsible for criminal activity. We have found that many times whistleblowers were also involved in the culpable activity. And so if we pass more and more of this legislation, we put the corporation between a rock and a hard place. We say to them: You have to punish somebody who was involved in criminal activity, and on the other hand, if you do so to this kind of person, there is protection. And we think that we really ought to evaluate how that system works with the present policy that anyone who is involved in criminal activity should be punished in some kind of way.

There are some other technical suggestions that I have made on Pages 10 and 11 of my testimony, and I will just let the record stand on that. We will be delighted to answer any questions if you have them. But I would like to make one more important point, and that is regarding the Anti-Fraud Enforcement Act of 1987 that we had submitted to this committee last year. It was in this legislation that we had made our request for the increased statute of limitations.

We very much need another provision in that proposal, one that would amend Rule 6 of the Federal Rules of Criminal Procedure; that is, the grand jury secrecy rule. Under the present grand jury secrecy requirements, we are severely limited in providing grand jury information to the Civil Division and to our sister agencies. If

I could just finish this one point, because I think you would want to know about this problem that we have, Mr. Chairman.

Therefore, we can be in the middle of a grand jury investigation, know about a contractor's problems, and not be able to tell the Defense Department, for example. That is a ludicrous rule for us to have to continue to comply with. Certainly, we will if it is the law. But if we really want to fight fraud, then we should be able to share with the Defense Department or whatever other agency information that we have during the course of a grand jury investigation. Presently, I am thinking of one that is going on where we see a pattern of problems, but we cannot share this with the agency that is involved.

I will be delighted to answer any questions.

[The prepared statement of Ms. Toensing follows:]

STATEMENT

OF

VICTORIA TOENSING

DEPUTY ASSISTANT ATTORNEY GENERAL
CRIMINAL DIVISION

BEFORE

THE

SENATE JUDICIARY COMMITTEE

CONCERNING

MAJOR FRAUD ACT, H.R. 3911

ON

JULY 12, 1988

Mr. Chairman and Members of the Committee:

I am pleased to have the opportunity to appear before you today to discuss the views of the Department of Justice on H.R. 3911, the "Major Fraud Act of 1988." We strongly support the thrust of this proposal because it would significantly enhance our ability to investigate, prosecute and punish large scale procurement fraud. We believe it would greatly facilitate our efforts in cases arising out of the operations of the Department of Defense, which, as you know, are cases which the Department of Justice has designated as a top priority.

The great majority of government fraud cases today are prosecuted as conspiracies to defraud the United States (18 U.S.C. 371), false statements (18 U.S.C. 1001) or false claims (18 U.S.C. 287). Each of these provisions originated in legislation passed in 1909, and each was recodified in substantially its present form in 1940. While procurement fraud affecting the United States usually falls within the prohibitions of one or more of these statutes, we believe the enactment of a comprehensive prohibition directed at major government fraud, such as that embodied in H.R. 3911, would further our prosecutive efforts very substantially.

Our strong support for the enactment of a comprehensive statute targeting a major species of fraud is based on our analogous experience with fraud affecting the nation's financial

institutions. Prior to 1984, the statutes used to prosecute bank fraud, principally 18 U.S.C. 656, 657, 1005, and 1006, were also dated, having their origins in legislation passed during the depression. No generic bank fraud statute existed. The great majority of cases of bank fraud we encountered were cognizable under these old statutes, but in some cases, prosecution was either very difficult or totally foreclosed.

In 1984, Congress responded to our need by enacting the general bank fraud statute, 18 U.S.C. 1344.The general bank fraud statute makes it an offense to execute or attempt to execute a scheme or artifice to defraud an insured financial institution or to obtain money or property under the custody or control of an insured financial institution. This broad prohibition, following principles well established under the mail and wire fraud statutes, 18 U.S.C. 1341 and 1343, has proven its utility far beyond original expectations. In fact, in less than four years since its passage, section 1344 has become the statute of choice for prosecuting all forms of bank fraud. The presence of the general criminal prohibition has facilitated and simplified the prosecution of hundreds of cases throughout the country. There is every reason to believe that enactment of a general procurement fraud provision such as that embodied in H.R. 3911 would have an equally positive effect. 1/

1/ In the same way, recent legislation, such as the False Claims (Footnote Continued)

H.R. 3911, which follows the language of 18 U.S.C. 1344, would enhance existing law by creating a new section 1031 in title 18, United States Code, to provide that "whoever knowingly executes, or attempts to execute, any scheme or artifice (1) to defraud the United States; or (2) to obtain money or property from the United States by means of false or fraudulent pretenses, representations or promises; in any procurement of property or services for the Government, if the value of the contract for such property or services is $1,000,000 or more" shall be fined up to $10,000,000, imprisoned not more than ten years, or both. A term of two years imprisonment, apparently intended to be mandatory, is required if there is a foreseeable and substantial risk of personal injury. The bill further provides for a statute of limitations of seven years after the commission of such an offense. In addition, upon application by the Attorney General, the proposed legislation would allow payment to an individual who furnished information leading to conviction under this section. The payment would come from funds generated by a criminal fine imposed under the section; the amount of such payment would not exceed $250,000, and officers and employees of the government who furnish information or render service in the performance of official duties would be ineligible for such payment. Finally,

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(Footnote Continued)
Amendment Act of 1986, the Anti-Kickback Enforcement Act of 1986 and the Program Fraud Civil Penalties Act of 1986, reflects recognition by Congress that the civil and criminal penalties provided by earlier legislation were insufficient to address the current problem of fraud perpetrated against the United States.

the bill provides "whistleblower" protection for employees for lawful acts done to assist investigation and prosecution under this section.

In addition to creating a general procurement fraud offense, other significant enhancements to existing law are increased fines and imprisonment provided for major procurement cases, extension of the statute of limitations for such cases to seven years, authority to seek payments for persons who provide information which leads to conviction for procurement fraud violations and "whistleblower" protection. With the exception of the "whistleblower" provision, we support each of these objectives. With your permission, I would like to discuss each of these areas.

PENALTIES

We believe that there is no better deterrent to white collar crime than the imposition of lengthy jail sentences on white collar criminals convicted of serious offenses. When appropriate, we charge multiple counts in prosecutions founded on existing fraud statutes, such as the banking offenses (18 U.S.C. 215, 656, 657, 1005, 1006 and 1344), fraud against the goverrment (18 U.S.C. 287 and 1001) or conspiracy (18 U.S.C. 371). Each of these offenses carries a potential sentence of five years imprisonment. By charging multiple counts, the sentencing court

is given the discretion to impose a sentence in excess of five years.

However, offenses committed on or after November 1, 1987 will be subject to the recently promulgated sentencing guidelines. Until we have acquired a body of experience under the guidelines, it is impossible to predict with any certainty the effect they will have. We note, however, that an initial reading of the guidelines would suggest that a first offender (the typical defendant in procurement cases) who organized a group of more than five persons which conducted a procurement fraud costing the government more than $5 million, would receive a guideline sentence of forty-six to fifty-seven months. This sentence would be within the statutory maximum permitted by existing law. Therefore, we doubt that an increase in the statutory term for procurement fraud would increase the sentences actually received by most defendants.

However, we support this increase because the Sentencing Commission will continue to evaluate the Guidelines. Enactment of H.R. 3911 would reaffirm the serious nature of major procurement fraud, and could cause the Commission to amend the Guidelines to increase the severity of punishment for such offenses.

With respect to fines, and notwithstanding the maximum fine of $10,000 set forth in several of the statutes commonly utilized

in procurement prosecutions, under the Sentencing Reform Act of 1984, now in effect, conviction under the statutes presently utilized in procurement prosecutions exposes the criminal to a maximum fine of $250,000 in the case of an individual defendant and $500,000 in the case of a corporate defendant. Existing law also provides for an alternative fine of double the gain realized by the defendant or double the loss caused by the offense. In many cases, such fine levels will be sufficient. Nevertheless, we recognize that there will be instances where larger fines will be appropriate in cases involving fraud against the United States.

Moreover, the Department of Defense Authorization Act of 1986 provides that "the maximum fine that may be imposed . . . for making or presenting any claim upon or against the United States, related to a contract with the Department of Defense, knowing such claim to be false, fictitious, or fraudulent, is $1,000,000." This provision is applicable to claims made on or after November 8, 1985. It makes penalties proportionate to the potential monetary gain for criminals, and should act as a serious deterrent to procurement fraud in the defense area. This fine provision, taken together with the recently enacted amendments to the False Claims Act which provide for a civil money penalty of three times the amount of the claim, acts as a substantial deterrent.

Thus, while fine levels are adequate in most cases, we suggest the Committee consider extending the defense procurement fine provision to all government procurement cases. In any event, it should be promptly codified to have its maximum deterrent effect.

In light of the foregoing considerations as to both the desirability of a comprehensive procurement fraud statute and the inter-relationships among the various sentencing statutes and guidelines, we believe that the Committee should consider enacting the general fraud provision of H.R. 3911 as a felony carrying a penalty of five years imprisonment or a fine under the provisions of title 18, and to apply the $1,000,000 contract provision as a trigger to invoke the enhanced penalty provisions contained in H.R. 3911.

STATUTE OF LIMITATIONS

We fully concur with the goal embodied in H.R. 3911 of enlarging the statute of limitations for prosecution of procurement fraud cases. These cases often require long and difficult investigations of very complex facts. Indeed, it is common for a defense procurement investigation to require thousands of hours to examine and analyze literally millions of documents. In addition, because concealment and secrecy are the hallmarks of financial crime, there is often a lapse of time before the cases come to our attention in the first instance.

Thus, defense procurement cases frequently are brought to indictment at or near the time the present five year statute of limitations expires.

In one class of cases, those involving defective pricing, the system virtually guarantees that the existing five year statute of limitations will present difficulties. Pursuant to the Truth in Negotiation Act, pricing data in these cases will be supplied to the government prior to the signing of the contract. After the contract is signed, a post-award audit is performed, the contractor is permitted to respond to the audit report, and the entire matter is reviewed again before a determination is made to refer the matter for criminal investigation. This process can take several years to complete. This systemic delay ensures that criminally fraudulent conduct occurring during the negotiation stage will not be discovered until much later. In such cases, an extension of the statute of limitations, such as that embodied in H.R. 3911, is clearly needed.

However, we favor a broader expansion of the statute of limitations than that contained in H.R. 3911. In the proposed "Anti-Fraud Enforcement Act of 1987," which we transmitted to the Congress on September 23, 1987, and which I will discuss further in a moment, there is a provision which would extend the statute of limitations in cases involving fraud (or a breach of a fiduciary obligation) beyond five years to one year after the facts relating to the offense became known, or should have become

known, to the responsible authorities. The maximum extension beyond five years under this provision would be an additional three years. We believe that this provision, which would apply to procurement cases as well as all other forms of fraud, would properly enhance the government's ability to prosecute all well concealed fraud cases, not just the class of cases addressed by H.R. 3911.

REWARD FOR INFORMATION

The provision contained in H.R. 3911 to reward persons providing information leading to conviction in major procurement cases parallels recently enacted legislation in the narcotics area. While such a provision may encourage spurious claims for rewards in many cases, it may also encourage persons who might otherwise file qui tam suits on behalf of the government to communicate directly with law enforcement authorities. This would lessen the burden on the courts and on the Department of Justice. Accordingly, we support the provision.

"WHISTLEBLOWER" PROTECTION

Congress has enacted two "whistleblower" protection statutes in the last two years, one in the False Claims Amendment Act of 1986 (31 U.S.C. 3730(h)) and the other in the National Defense Authorization Act of 1987 (10 U.S.C. 2409). In no way do we condone or defend retaliatory actions directed against those who

cooperate with our efforts to investigate and prosecute procurement fraud. However, until these two recent legislative efforts are proven necessary or, conversely, inadequate, to achieve their stated goals, we do not endorse the enactment of further legislation which is largely cumulative. We do not believe it is timely to create yet another statutory cause of action in federal court.

Moreover, this provision could conflict with remedial administrative action. When procurement fraud is discovered, the appropriate suspension and debarment authority requires culpable individuals be disciplined by dismissal, removal from management or supervisory positions, or financial penalties as part of the contractor's corrective action. However, in our experience, "whistleblowers" frequently have been involved in the fraudulent activity themselves. In these situations, the bill would negate the application of administrative sanctions on the "whistleblower" and could subject the contractor to civil liability arising out a "whistleblower" suit for complying with the remedial administrative action.

OTHER SUGGESTIONS

We believe other language in the bill can be improved. For example, the "value of the contract" language which triggers the prohibitions of the bill presumably is intended to describe the value of the goods provided and/or services rendered to the

government. It should be stated in those terms. This would apply equally if the "value" trigger applied only to enhanced penalties.

As currently drafted, the intended mandatory term of two years imprisonment in cases involving a risk of personal injury might be interpreted to permit the court to sentence the defendant only to a fine or probation. This provision should be redrafted to provide that in such cases, "the court shall impose a term of imprisonment of not less than two years."

I want to emphasize our commitment to investigating and prosecuting major fraud against the United States. In this connection, on September 23, 1987, we submitted three proposed bills to the Congress: (1) the "Anti-Fraud Enforcement Act of 1987" which I mentioned earlier; (2) the "Contract Disputes Act and Federal Courts Improvement Act Amendments of 1987"; and (3) the "Bribes and Gratuities Act of 1988." We would like the Committee to act on these proposals as soon as possible, since each of these bills would substantially assist our efforts to combat procurement fraud.

I would like to discuss in particular the important provisions of the "Anti-Fraud Enforcement Act of 1987." The amendments to the statute of limitations contained in the bill were described earlier. Another provision would amend Rule 6 of the Federal Rules of Criminal Procedure to permit us to

communicate more freely to the Civil Division and our sister agencies the information gathered in the course of a grand jury investigation. We want to be able to share this information for the purpose of imposing civil and administrative sanctions in fraud and other appropriate cases. This provision is particularly important to us. As an example, a current grand jury investigation of one very large government contractor has disclosed systemic weaknesses which should be addressed forthwith by the appropriate administrative authority. However, because the allegations underlying the investigation were received shortly before the expiration of the statute of limitations, we were compelled by time constraints to take the matter directly to the grand jury and could not utilize other non-grand jury investigative techniques. Accordingly, we are unable to communicate the information we have gathered concerning these problems to the affected agency, and the problems persist without being addressed.

The bill also would expand the government's right to audit contractors' books, permit the government to collect the costs of a successful procurement fraud investigation and prosecution, and eliminate the practice of allocating the costs of successful prosecution to future government contracts.

Two other provisions of the bill, the extension of the injunction provision contained in 18 U.S.C. 1345 to government

fraud cases and the creation of an offense for obstructing a federal audit were passed by Senate on June 17, 1988.

Mr. Chairman, that concludes my prepared statement. I would be happy to answer any questions you or the other members of the Committee may have.

Senator METZENBAUM. I think we are going to hear the next witness because I think it will save some time by doing that. Thank you very much for your testimony.

Our next witness is Richard Fogel, Assistant Comptroller General, General Government Division, GAO.

Ms. TOENSING. Excuse me, Mr. Chairman. If I might just say, Mr. Valukas is here to testify for the Department of Justice.

Mr. VALUKAS. Senator, I was invited, or the Department asked me to speak as the U.S. attorney on behalf of all of the U.S. attorneys in connection with Senate Bill 1958. You have my prepared remarks.

Senator METZENBAUM. I would say, Mr. Valukas, we do not have you down as a witness. The Department of Justice does not really tell us who our witness list is, and had they told us, we would try to work you in. Why don't you make it very brief in order to make your point?

Mr. VALUKAS. I will make it very brief, Senator.

The point we would make with regard to Senate Bill 1958 is simply this: We need additional resources in order to combat the problem of defense procurement fraud. Simply put, each of the offices that are involved in actually prosecuting these cases—and those are the U.S. attorney's offices in the various districts—have committed increasing resources, particularly over the last 2 years.

My district, which is one of the largest districts in the Nation and covers the northern 18 counties of Illinois now presently devotes approximately 5 percent of our resources to the investigation and prosecution of these cases alone. That means that other areas which need prosecutive resources—for instance, drugs, corruption, other white-collar crime—are stripped in order to prosecute these particular cases. So we support the additional resources which would be dedicated to the use in defense procurement fraud cases.

We recommend that you not adopt a proposal that will set up regional task forces. What you will be doing is layering by bureaucracy in the various prosecutive offices. You have regional offices right now. They are called the U.S. attorney's offices in the individual district.

I have submitted a brief chart—and I am moving this along—which shows that in the litigation of fraud cases, and we are talking about Government fraud cases from 1983 to 1986, that of the 18,159 fraud cases that were prosecuted were prosecuted by the U.S. attorney's office. The Department of Justice handled 130 of those fraud cases.

So the area of expertise, the people who are actually making the significant fraud cases, be they in securities fraud, commodities fraud, Government contractor fraud, and all of the other areas, are the Assistant U.S. attorneys who are in the field. And what we recommend to you is that in lieu of the regional strike forces or task forces, which would just create another bureaucracy, that you have dedicated assistant U.S. attorneys, much as you do in the OCDEF program who are dedicated solely to defense procurement fraud cases, that you could report separately on those individuals as you do in the OCDEF program. That would be a much more effective way of putting your most experienced prosecutors who are in the field to task with regard to this significant problem.

That is as fast as I can go, Senator.
[The prepared statement of Mr. Valukas follows:]

STATEMENT

OF

ANTON R. VALUKAS

UNITED STATES ATTORNEY
NORTHERN DISTRICT OF ILLINOIS

BEFORE

THE

COMMITTEE ON JUDICIARY
UNITED STATES SENATE

CONCERNING

FRAUD LEGISLATION
S. 1958

ON

JULY 12, 1988

Remarks of Anton R. Valukas,
United States Attorney, Northern District of Illinois
July 12, 1988

I appreciate the opportunity to address the Senate Committee on the Judiciary concerning S. 1958, legislation to establish government fraud law enforcements units to investigate fraud against the government.

By proposing to set up five regional law enforcement units, S. 1958 would impose a bureaucratic structure, with its attendant administrative and travel costs. Such a plan deprives the most difficult government fraud cases of the wealth and depth of experience of Assistant United States Attorneys who have successfully investigated and prosecuted the most sophisticated economic crimes, not only in the defense procurement area, but in the full range of "white collar" crime.

At the same time, the regional task force concept would take from the newer Assistants the more routine and easily prosecuted government contracts and program fraud cases, which are now routinely assigned to assure that every Assistant is trained to prosecute ever more complex government fraud prosecutions, and to assure that even a "routine" defense fraud case is promptly prosecuted. These same smaller cases, so important to our overall obligation to deter all forms and levels of government fraud, if assigned to a regional government fraud unit under the proposed legislation, might take backseat to the high profile case.

It is clearly the premise of Senate Bill 1958 that there is always an advantage in having an attorney assigned to a case who has previously prosecuted a case in the same narrow category of fraud. I reject that assumption and would maintain instead that in our experience such narrow specialization is ultimately counterproductive.

In my opinion, a good Assistant United States Attorney, experienced in the prosecution of economic crime, and drawn from and with access to a pool of other talented Assistants, is the best choice for every case. A good Assistant can develop the narrow expertise necessary for the individual defense procurement case as the need arises. He or she already has the needed familiarity with the strategic uses of the broad range of criminal and criminal tax statutes, and the imagination to use the proper mix of prosecutive tools -- including undercover agents, search warrants, proffers, immunity and plea bargaining -- to carry out a successful investigation focused on the right targets. He or she has the skill in working with agents to follow up the leads and tips which come daily to a United States Attorney's office which is well known to the community. (These same tips and leads are unlikely to come to any regional task force). Such an Assistant has the trial experience to make reasoned decisions or recommendations about witnesses, evidence, plea agreements and immunity, and the credibility with the defense bar and federal district court to assure that the investigation is controlled by

what we need to know, and not what the putative defendants choose to provide to us.

Moreover, it is important to the credibility of the United States Attorney, and to the administration of criminal justice as a whole within a district, that decisions regarding immunity and plea bargaining be closely supervised within the district and not administered from Washington.

An experienced prosecutor familiar with the tough standards of a local district can overcome the expectation of defense contractors that they can get soft deals if they can just find the right ear in Washington. He or she can also press for pleas of guilty which can foreshorten the expenditure of time and resources in complex prosecutions.

In my view, only when defense procurement contractors know that they must deal with the United States Attorney, and cannot turn to other authority in search of a better deal, will they accept a just disposition of their cases which fairly reflects the extent of their criminal or civil violations. If a corporation and its officers accept that responsibility in criminal and civil negotiations, and fully cooperate with the investigation, their demonstrated contribution should be the major factor in decisions regarding application of the sanction of debarment.

My office has demonstrated in its coordinated prosecutions of judicial corruption, other public corruption cases, bank fraud, tax fraud, tax shelter, bankruptcy fraud, securities fraud and,

indeed, large narcotics cases (which we treat as economic crimes), that it can bring together the resources of many investigative agencies and, when appropriate, the regulatory agencies, to improve the quality of complex prosecutions in the Northern District of Illinois. We have successfully prosecuted almost 250 public corruption cases in the past three years, losing only one. We have prosecuted more than 200 bank fraud cases, losing only one defendant in a multi-defendant case. And we have prosecuted more than 250 tax fraud cases with no acquittals. Indeed, we have not lost a tax fraud case in my district since 1981. In the past year, among complex bankruptcy fraud cases, we successfully completed a multi-million dollar fraud prosecution relating to the administration of bankrupt estates and prosecuted a long series of complex fraudulent tax shelters. We have formed a "bank regulator forum" to bring together the financial institution regulatory organizations with the FBI and Postal Inspectors and United States Attorney representatives to enhance training of examiners and the quality of bank fraud referrals, -- a program which has become a model for other districts. It is that broad experience in prosecuting complex economic crime, and not specific experience in the defense fraud area, which has made us able to take on some of the biggest procurement fraud cases in the country.

There is no question in my mind that no attorney brought out from Washington (and placed in a regional task force), could do the job of investigative prosecution and negotiation and respond

as effectively to the day-to-day needs of the cases as have the Criminal and Civil Assistants in my office, working with the designated agencies to prosecute these fraud cases. Moreover, in one great area of fraud against the government -- welfare fraud -- we also have worked closely with the State's Attorneys to increase the resources available -- a tie which could not be exploited by a regional task force approach.

In the past three years my office has successfully prosecuted approximately fifteen defense procurement fraud cases. We presently have approximately twenty active investigations. The increasing number of cases in the past years are a reflection of increased experience and the increasing commitments of the Department of the Army, Criminal Investigative Division, the Naval Investigative Service and the Defense Fraud Investigative Service to provide the auditors, contract experts and inspectors to successfully prosecute these cases. With additional agents and Assistant United States Attorneys no doubt there would be more cases still.

The cases where prosecution has been completed have ranged enormously in complexity. There have been straight-forward schemes to pay kickbacks to obtain government contracts -- not distinguishable from the hundred other procurement contract kickback schemes we have prosecuted this past year. In an insider fraud case, a Department of Defense employee smuggled out an

advance copy of contract specifications for a micro-computer contract to give a competitive advantage to friends. In a particularly outrageous case, officers, employees and the corporation of American Cotton Yarn Co., the defendants illicitly profited from systematically substituting inferior parachute cord, not meeting strength or elasticity requirements, putting American troops in peril of injury or death.

We now have under investigation four extraordinarily complex cases involving hundreds of millions of dollars in contracts involving allegations of defective products, overcharging and mischarging. Each of the Assistants assigned to direct these four largest cases has previously successfully prosecuted complex securities fraud, bank fraud, government program fraud, tax and tax shelter cases. Based on their experience in other investigations, they have turned to other agencies, such as the IRS, to broaden the investigation and provide computer resources. As the demands of the cases have increased, these Assistants are devoting between 50 and 100 percent of their time to the prosecutions. As needed, other Assistants have been made available. In those cases where it has been appropriate, the Civil Division of my office has likewise provided attorneys experienced in complex litigation and tough negotiations to handle the related civil cases.

Such delays have occurred in these large defense procurement cases have not been because we were not prepared to commit the

attorney power of my office when a case required it. Rather the cases demanded personnel not initially available from the Department of Defense because the Defense Department agencies were increasing their skills and expertise in an area which previously fell within the jurisdiction of the FBI. In one case a large squad of auditors was needed; another required experts who could determine with precision the specifications of the contract and measure the performance or product against the contract. And it has become apparent as we have examined the defense contract fraud cases presented to us for prosecutive decision, that contracting procedures and an improved ability to mobilize information of contracts and contract performance will be necessary to increase the probability of successful prosecutions on cases of fraud.

By my words, I do not want to suggest that we are not continually evaluating our resource needs in order to adequately respond to government fraud. In a complex case such as our recently prosecuted case involving Penn Square loans purchased by Continental Bank, three of my ablest Assistants were absorbed full time for most of a year. As we deal with the demands of a major defense procurement fraud case, we are continuously stripping attorney and support resources from other areas of need. I could estimate that five percent of my resources is now engaged in defense contract related cases. If these defense fraud cases result in trials, that percentage will increase to the detriment of other cases.

We work closely with the Department of Justice. Under the present system there is sufficient flexibility and good will for United States Attorney's offices in need of temporary resources to draw on the Criminal Division for additional technical assistance and attorney help without creating a new structure which absorbs scarce funds at a time when Congress has required that spending be cut back.

To reiterate, it is my essential message that it is the United States Attorney's offices and the investigative agencies which are making the most effective use of available resources. If we are serious about a full fledged assault on government fraud resources must continue to be invested in this area.

I thank you for inviting me to present my views and for your attention.

Senator METZENBAUM. Thank you very much. You did very well, and we certainly get your point. Good witness.

Senator Simon, do you have an opening statement?

Senator SIMON. I do not. Thank you very much. We have a U.S. attorney from the northern part of Illinois here.

Mr. VALUKAS. Good to see you, Senator.

Senator METZENBAUM. Happy to have you with us, Senator Simon.

Mr. Richard L. Fogel, I think I introduced you before. Please proceed.

STATEMENT OF RICHARD L. FOGEL, ASSISTANT COMPTROLLER GENERAL, GENERAL GOVERNMENT DIVISION, U.S. GENERAL ACCOUNTING OFFICE, WASHINGTON, DC

Mr. FOGEL. Yes, thank you, Mr. Chairman.

Let me just very briefly summarize the report that we issued last week to Senators Proxmire and Grassley, and then comment very briefly on the Senator's bill.

We said that four things need to be done in the Justice Department if it is to get better information on how it ought to use its current resources most effectively, and to make a better case for saying why it needs more resources in the defense procurement fraud area. Everyone that we talk to in Justice and the U.S. attorney offices said they need more resources. Our concern is: Do they really know what they are doing with what they have got now?

We said they need complete and timely information on the number and status of defense procurement fraud referrals and cases so that management could better track the progress of investigations, and identify problems. They also need data on attorney resources being spent to enable management to monitor the amount of effort being devoted in this area more effectively. We said they could use written plans and periodic updates of those plans that identify the activities of Justice headquarters and U.S. attorney offices that would allow comparison of planned with actual accomplishments. And we asked them to consider a case weighting system to help distinguish the different prosecutive efforts required for the different types of cases.

I would like to note that the management problems we found in this area are no different than those we generally have found over the years when we reviewed other Justice's programs. We issued an overall report in 1986 about the entire management of the Justice Department. One of the problems we found—based on testimony that was given to us by former senior officials at the Department from numerous administrations—was that there has been a general disinclination on the part of Justice for a number of years to really address management issues. This is not just associated with this administration; it goes back over a number of years. These top officials who were, in fact, blaming themselves for part of this, said that this comes in part from their legal backgrounds and the predisposition to focus on legal issues in selected cases, rather than focusing on the management information and systems that you need to develop priority efforts and follow through on those efforts.

I want to emphasize what Senator Proxmire said. In this area, we have seen the Justice Department working very well in the last couple of years with the Department of Defense to begin initiatives, but developing policies is not enough. You have to focus on policy implementation. That means paying attention to such things as management systems, getting information on what is happening, and deciding whether you are having successes or not so you can make changes in mid-course.

What we see is increased concern within the Department to do these types of things, but on the other hand, we have not yet seen the sustained effort over time that, in our mind, has satisfied us that Justice officials have really got a good handle on how they are devoting their resources.

One last comment on the bill that Senators Proxmire and Grassley have introduced. Obviously, the Justice Department headquarter officials we talked to strongly supported that bill. The U.S. attorneys that we interviewed were unanimously against it. That goes, I think, to the historic relationship that has existed for a long-time in this country between U.S. attorneys and Justice headquarters.

There certainly is a willingness to cooperate, but one suggestion we would have in considering your legislation is that you do look, as Mr. Valukas said, at the way the Department organized the Organized Crime Drug Enforcement Task Force program. This was a fairly successful effort by the Department working with the U.S. attorneys, the Customs Service, various other components within Justice, and other agencies to develop a focus on a specific problem, regionally focused to work with the U.S. attorneys and the Department to devote more resources to it, but to try to overcome some of the organizational problems that have existed in the past between the Justice Department and the U.S. attorney's offices when we have had strike forces.

[The prepared statement of Mr. Fogel follows:]

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Defense Procurement Fraud: Justice's Overall Management Can Be Enhanced

Statement of
Richard L. Fogel, Assistant Comptroller General
General Government Division

Before the
Committee on the Judiciary
United States Senate

GAO/T-GGD-88-46

GAO Form 160 (12/87)

JUSTICE'S OVERALL MANAGEMENT OF DEFENSE PROCUREMENT FRAUD CAN BE ENHANCED

SUMMARY OF STATEMENT BY
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U.S. GENERAL ACCOUNTING OFFICE

In response to a congressional request from Senators Proxmire and Grassley, GAO reviewed Justice's overall management of its defense procurement fraud investigations. GAO found that Justice's overall management could be improved if it had basic oversight information on its decentralized operations. Justice needs to acquire the following information to improve its oversight of this high priority area.

-- Complete and timely information on the number and status of defense procurement fraud referrals and cases would enable management to better track the progress of investigations and identify problems.

-- Data on attorney resources being spent would enable management to monitor the amount of effort being devoted to this area.

-- Written plans and periodic updates of those plans that identify the activities of Justice headquarters and the U.S. attorney offices would allow comparison of planned with actual accomplishments.

-- A case weighting system to help distinguish the different prosecutive efforts required for different types of cases could help management assess and identify its resource needs.

GAO made several recommendations to the Attorney General designed to provide Justice with better information so that management can make more informed decisions regarding the allocation and use of scarce resources.

Mr. Chairman and Members of the Committee:

We are pleased to be here today to discuss the findings in our June 29, 1988, report entitled Defense Procurement Fraud: Justice's Overall Management Can Be Enhanced (GAO/GGD-88-96). Our review, which was requested by Senators Proxmire and Grassley, did not focus on specific cases or the current bribery investigation being handled by the U.S. Attorney in Alexandria, Virginia. It involved a broader look at Justice's strategy for coordinating and managing the defense procurement fraud effort among the 93 U.S. Attorneys and the Criminal Division's Defense Procurement Fraud Unit. In doing our work, we interviewed officials from Justice headquarters, seven U.S. attorney offices, and Department of Defense auditing and investigative agencies. We also reviewed work load and other statistical data from the agencies' various management information systems.

BACKGROUND

The Criminal Division at Justice headquarters and the U.S. attorney offices are responsible for the criminal prosecution of defense procurement fraud. The Criminal Division's Defense Procurement Fraud Unit, which was created in 1982 to focus Justice and DOD resources on defense procurement fraud, is supposed to initially receive and review for prosecutive merit all referrals submitted by investigative and auditing agencies involving significant instances of alleged defense procurement

fraud. The Unit has responsibility for some referrals and assists U.S. attorney offices with others. However, the U.S. attorneys, for the district where the alleged criminal acts occurred, handle most of the defense procurement fraud referrals that have prosecutive merit. Some of the larger U.S. attorney offices located in urban centers have specialized sections which handle or monitor the prosecution of white-collar crime cases, including defense procurement fraud, within their district.

The investigation of defense procurement fraud schemes is often a lengthy process taking several years before a decision is made on whether to prosecute or not prosecute a case. According to Justice headquarters and U.S. attorney office officials we interviewed, defense procurement fraud cases such as those involving complex cost/labor mischarging and defective pricing schemes are time consuming and difficult to prosecute criminally for the following reasons:

-- Procurement regulations which govern the defense contracting process are voluminous, complex, and sometimes ambiguous.

-- Auditors, investigators, and attorneys must review and analyze voluminous accounting and performance data to determine if fraudulent acts occurred.

2

-- Defense contractors "out gun" government attorneys with vast legal and accounting resources to defend defense procurement fraud allegations.

-- Investigators and attorneys have difficulty in obtaining information surrounding the alleged fraudulent activity because of the length and complexity of the investigations.

LACK OF COMPLETE AND TIMELY
DATA ON CASE STATUS

Since 1982, Justice headquarters has been attempting to capture some basic information for all of its fraud investigations and prosecutions through its Fraud and Corruption Tracking System. However, this system does not contain information on all defense procurement fraud referrals because Justice officials said the investigative agencies do not always submit the forms needed to enter a referral into the system. The extent of underreporting is not known.

Neither does the system contain current information on the status of a significant portion of the referrals. This is primarily because Justice attorneys do not always report the disposition of the referrals. For example, as of September 1987, Justice attorneys had not reported whether they had accepted or declined

286 (about 42 percent) of the 680 defense procurement fraud and related referrals sent to their offices between October 1, 1983, and May 31, 1987. Most of these referrals had been with Justice for a year or more. U.S. attorney office officials said that the administrative burden associated with completing the required forms, and questionable benefits to their organizations, were the primary reasons that the information was not always submitted.

RESOURCES DEVOTED TO PROSECUTING DEFENSE PROCUREMENT FRAUD NOT KNOWN

Justice officials told us that turnover among attorney and/or support staff has adversely affected their prosecutive efforts. Officials from Justice and the seven U.S. attorney offices also said they need more attorneys and/or support staff to handle defense procurement fraud cases.

Our review showed that Justice does not know how many attorneys are being used for defense procurement fraud investigations and prosecutions because the Criminal Division and U.S. attorney offices are not required to gather this information. Such information would enable Justice to better monitor the amount of effort being devoted to this priority area and compare resources expended to results achieved.

We believe a case weighting system that distinguishes between the amount of prosecutive effort needed for different kinds of cases would be one useful tool for helping assess resource needs.

LACK OF MANAGEMENT PLANS FOR DEFENSE PROCUREMENT FRAUD

One of the Attorney General's management initiatives is the development of strategic/long-range plans to assess the implementation and accomplishment of his priorities. In January 1988, the Attorney General imposed a written planning requirement for Justice's Organized Crime Strike Forces. While defense procurement fraud has been a top white-collar crime priority of Justice, the Criminal Division and the U.S. attorney offices responsible for the prosecution of defense procurement fraud have not prepared written management plans outlining their current and future efforts. We believe that if such plans were developed and updated periodically, Justice could better assess progress and problems in this top priority area. The plans should include, at a minimum, information on (1) the current and anticipated work load and strategies and priorities for handling it, (2) attorney resources being devoted and needed, and (3) objectives to be accomplished and milestones for accomplishing them.

In developing the management plans, each of the components should be asked to address what special problems or issues are affecting their efforts to successfully prosecute the complex defense procurement fraud cases involving cost/labor mischarging and defective pricing and whether different strategies are needed for such cases.

In December 1987, Senate Bill S.1958, the Government Fraud Law Enforcement Act of 1987, was referred to this Committee. The bill would require the Attorney General to establish regional fraud units around the country and authorize additional resources for these units. Under the bill, the units would be under the direction of the Assistant Attorney General for the Criminal Division. The purpose of the proposed legislation is to provide an organizational framework for concentrating investigative/ prosecutive resources and coordinating Justice efforts to combat fraud in government procurement and programs.

Generally, the Justice Criminal Division officials we interviewed as part of our work supported the bill. U.S. attorney office officials in all seven offices where we did our work opposed it because they did not believe dedicated fraud units separate from their offices would work. Regardless of the organizational approach used to investigate and prosecute government fraud, we believe the Department of Justice needs basic information on case

status, resources devoted, and management plans to oversee policy development and implementation in this high priority area.

This concludes my prepared statement. I would be pleased to answer any questions you have.

Senator METZENBAUM. Thank you very much, Mr. Fogel. I might say to you and Mr. Valukas it sounds to me as if your concept along that line has some merit, and maybe has more value. I would be interested if Senator Grassley, when he addresses himself to the subject, as to whether the concept that they have in their bill or your concept might more effectively attack the problem. I do not think anybody is saying the problem should not be attacked. It is a question of what is the best modus operandi.

Let me just ask Ms. Toensing a couple questions. Many critics say that acquiescence in fraud by procurement officials greatly complicates and undermines enforcement. One example is the Pratt and Whitney case where the prosecution was derailed in part by Government acquiescence despite the FBI's conclusion that Pratt and Whitney's overcharges demonstrated "a flagrant abuse to decency and common sense."

As I understand it, while the matter was being handled, the prosecution for $22 million in overcharges was dropped because the Air Force procurement officials had acquiesced in the overcharges. The FBI was much upset about that.

Do you agree that acquiescence is one of the leading problems in procurement fraud? And has the Justice Department prosecuted any Government procurement officials for condoning fraud? And do you have any policy as to whether you intend to do that in the future?

Ms. TOENSING. I think acquiescence is a poor choice of words there. That is not quite what happened in Pratt-Whitney. I happen to have been involved in looking at that case myself, Mr. Chairman.

It was a system that was set up that sounded like a good idea at the time. For example, it was bottom lining, as they call it in defense contracting, and I think that they have eliminated that process now because of the *Pratt-Whitney* case. But what it was, if you want to hear it explained, is: For example, say I go to the grocery store and I have a cart of groceries, and I say to the grocer, "I am going to pay $100 for this cart of groceries," and he says, "No, you are going to pay $140." And we go back and forth, and we finally end up at $110 for the cart of groceries.

We both consider that a fair deal. We have negotiated, and we have agreed on the bottom line price. The fact that somebody is going to put down a loaf of bread cost $10 and a carton of milk costs one penny in there is irrelevant to the bottom line of what is considered a fair price for the entire cart of groceries.

What happened in Pratt-Whitney is that very similar kind of situation where defense contractors were allowed to put anything they wanted to down to be reimbursed. I exaggerate. It is probably not anything they wanted to, but it was mostly that. And then they would negotiate on a bottom-line price.

So it was not really acquiescence as far as somebody at DOD being culpable; it was a situation where it sounded like a good way to negotiate a contract, and it turned out that it was not, in fact, a good way to negotiate a contract.

So now because of the *Pratt-Whitney* case, and because we worked closely with the Department of Defense, they have changed that process.

Senator METZENBAUM. Wait a minute. I am not quite willing to buy off on this grocery cart, saying I will offer you $100 or $140.

According to the Pentagon auditors, Pratt and Whitney's plant in West Palm Beach, Florida, billed the Government for such expenses as fishing and golfing trips for Air Force officers, lavish banquets, luxury cars for executives, Miami Dolphins football tickets, rodeo outings, 4,000 souvenir baseball caps, and a $4,500 seminar for executives' wives at a yacht club.

The company also charged the Pentagon for a $67,500 donation to the Oklahoma Arts Center, made at the request of an Air Force Major General in Oklahoma City. And the spokesman for Pratt and Whitney, a subsidiary of United Technology, said, "Our position is that the grand jury proceedings in Florida were secret hearings." When the investigation was closed, he said, "As far as we were concerned, that was that."

Now, for you to say to me that that is similar to getting a load of groceries and saying, well, I would like to pay $100, that is not the way we buy things. We do not buy things like that at all. You do not go to grocery store and—you know that the price is something. The price of a piece of Air Force equipment is X or the loaf of bread is Y, and you do not buy things for the Government on that kind of basis.

Here is a company that was really loading up on to the taxpayers of America all of——

Ms. TOENSING. And it stinks. And it looks so lousy, and it was not a process that we thought was a good process as we examined it. But that is the way everyone agreed that it should work. It is a little more complicated than my analogy——

Senator METZENBAUM. Everyone agreed that it should work?

Ms. TOENSING. Let me explain it to you——

Senator METZENBAUM. To pay for fishing trips? To pay for baseball games?

Ms. TOENSING. They could ask for anything. And what they would contract for was the bottom-line price. And if that bottom-line price was considered fair, then that was considered a fair way to negotiate that contract.

As I said, as we looked at it, we kept in communication with the Air Force, and they changed their practices. And so I say even though we could not prosecute that case, we did do something very good from that. They have changed the way they do those contracts. It is a very good success story as far as DOD and DOJ working together.

Senator SIMON. I think Mr. Vander Schaaf wants to add something.

Mr. VANDER SCHAAF. Mr. Chairman, could I interrupt? We are not talking about the negotiation of a specific contract. We are discussing the negotiation of overhead rates which will be applied to all contracts that we have with that facility or contractor over a period of time.

At the point that you are speaking about, Ms. Toensing is absolutely right. There were a number of locations in which all of these "allowable" but questionable overhead charges that were made on defense contracts remained unclear. Each year, the Defense Department negotiators would go to the table with the company nego-

tiators. They would argue over the same old things, many of which our audit offices said we should not pay for at all. Now the Congress has put some tougher laws in effect, and we are not paying for those things. They would sit down, and they would say: Well, we cannot agree on these things, let us split this 60–40. But we did not know what fell out, or what stayed in. So in effect, it looked like—and probably was the case—that the Government did pay for the executives' wives to go to a seminar at a yacht club. We should not have paid for that.

Now, we have a tougher policy in effect, as Ms. Toensing indicated, but we are not talking about a specific negotiation on a specific contract. We are talking about overhead costs to be spread against all of the contracts. That is the point I wanted to make.

Senator METZENBAUM. The thing that is so bothersome is that the FBI stated that the Pratt and Whitney billing practices could not have been successful without the cooperation or indifference shown by the U.S. Air Force plant representative's office.

Mr. VANDER SCHAAF. Sir, I agree completely. The U.S. Air Force Plant Representative's Office and Pratt and Whitney historically have had a close relationship going back into the 1950's. I do not know how many people came out of that office and went to work for Pratt and Whitney. I have testified to this before Congress on numerous occasions. We have to close that revolving door. Now we have some new legislation to get at that problem.

I think there is some temptation on the part of the Government negotiator to think—"Well, I am going to be looking for work down the line, and I do not want to be too tough about these things." That kind of situation has certainly existed. I hope as a result of our office being here we have helped to close some of those doors.

Senator METZENBAUM. Senator Grassley.

Senator GRASSLEY. Mr. Chairman, I will start with Mr. Valukas.

Even though your oral statement might not have given this impression, your written testimony surprises me, frankly. It is not consistent with the comments that you raised in private with me last night, when we met for 45 minutes. So I would like to have you explain why there is a mismatch between your written testimony and your comments to me last night.

Mr. VALUKAS. Well, I am not sure what the mismatch is. My view on it is as I have put it in my oral testimony, as I have put in my written statement, that the place where you are going to successfully prosecute these cases is in the U.S. attorney's offices. That is where the prosecutions are occurring right now. That is why in Chicago we have 5 percent of the resources dedicated to it. That is why virtually every Government fraud case that you make and every complex securities fraud case across the board is prosecuted by an Assistant U.S. Attorney.

My disagreement with the legislation last night and today is the setup of the regional task force. What I do agree with is that we can dedicate assistant United States attorneys to this particular position; that is to say, dedicated in terms of designating them as assistant U.S. attorneys dedicated to Government procurement fraud cases.

Senator GRASSLEY. Well, what we need to know now then: Is that the Justice Department's position?

Mr. VALUKAS. The Justice Department's position is they are against the idea of these regional strike forces, that their first preference would be to have assistant U.S. attorneys out there who are working these cases undedicated. But the second position, a position which they can agree with, is a position that they would have dedicated assistant U.S. attorneys as defense procurement fraud assistants, if you will, and that we could report separately on those individuals within the framework of the U.S. attorney's office.

Senator GRASSLEY. So your principal objection to the bill is in the control of the resources by main Justice, rather than the individual U.S. attorney's offices?

Mr. VALUKAS. Actually, it is more than that, Senator. The problem you have in regional offices is that you do not have the assistants who are out there on a day-to-day basis who are working hand in glove in a given community where they have developed expertise, have developed trial experience, and have developed experience. Let me see if I can be more specific.

Senator GRASSLEY. But answer my question. Is that your principal objection to the bill?

Mr. VALUKAS. Right, it is.

Senator GRASSLEY. Okay.

Mr. VALUKAS. But I am just saying to you it is not simply control of resources. It is the deployment.

Senator GRASSLEY. And the Justice Department would support the bill if control were assigned to the individual U.S. attorney's office; is that correct?

Ms. TOENSING. That is correct. We support more resources for U.S. attorneys. They need them badly.

Senator GRASSLEY. I am glad, Ms. Toensing, that you and I finally agree on the need for more resources for prosecuting defense procurement fraud.

Ms. TOENSING. I knew we could find an agreement.

Senator GRASSLEY. Not only based on your comment now, but based on what you told network television last week. Because you have heard me say over a period of the last several years that I have been trying to get the Justice Department to realize that more resources were needed to fight defense procurement fraud. Quite frankly, you are the first Justice Department official to face that fact, that I have heard of, and I congratulate you for that.

I might add, too, that the Proxmire-Grassley bill has been around for at least a year; that the Justice Department has been aware of it for a year; and that obviously this bill is not a seat-of-the-pants response to the current defense investigation. I appreciate very much your statement of support of S. 1958, and I appreciate the department's suggested changes in the bill.

This morning, Mr. Chairman, I spoke with a Justice Department official who the committee invited to testify. His name is Joseph Fisher. He is an Assistant U.S. Attorney for the Eastern District of Virginia. Mr. Fisher told me that he was ordered not to testify, even though we were inviting him to testify as an individual private citizen, and not in his official capacity.

Do you know anything about that, Ms. Toensing?

Ms. TOENSING. Yes. Mr. Hudson, who is the U.S. attorney—a terrific U.S. attorney, by the way, I am sure you will agree because

you have agreed with that statement—speaks for that office. And I met with Mr. Hudson yesterday, as did Mr. Valukas, and Mr. Hudson agrees with our position on the bill, which is that we support this legislation with the comments that Mr. Valukas made.

We do not speak with mixed voices all over, just as you and your staff do not speak with mixed voices. We cannot send you mixed signals, Senator.

Senator GRASSLEY. Well, I have heard that line before, and I know that would probably come from any administration. But I think for the benefit of this committee as well as the Justice Department, I think you ought to know how I look at this as a member of Congress.

I think it is very insulting to the people of this country to deny a public servant the right to testify on matters related to his or her work on behalf of the taxpayers, or even as a private citizen. I think it is damaging to Congress and to the public interest for Federal departments to dictate to Congress who will or will not show up for a hearing. And even in the worst case that I can recall, that of Ernie Fitzgerald and the Air Force, I think that the Justice Department has decided that public servants working for DOJ cannot exercise their rights. I understand that a U.S. attorney who asked to testify was also ordered not to do so.

Ms. BROWN. I do not know anything about that.

Senator GRASSLEY. Do you, or do you not, understand that to be the case?

Ms. BROWN. No, I do not. That is incorrect unless you know something that I do not know. But from anything I know, that is incorrect.

Senator GRASSLEY. Well, Mr. Chairman, I want to make you aware of that fact, and I am sure that there will be some statement in a letter that he will submit. Now, I want to ask Mr. Fogel a question.

From your testimony, I gather that you are saying more resources alone are not enough, and that better management is also needed?

Mr. FOGEL. That is correct, Senator. We do recognize, if you look at the budget, that the general legal activities of the Department over the last 8 years have taken a much bigger hit than the rest of the appropriation accounts in Justice. We are not opposed to more resources being put into these activities. What we are concerned about, too, is if you get more resources, do you know how they are to be used in a coordinated fashion, tying in from an overall strategy the efforts that the Department wants to undertake, with U.S. attorney offices that are located in those areas where you have got a high concentration of defense contractors.

So it is a two-sided coin. More resources need to go with better management.

Senator GRASSLEY. We need your judgment regarding S. 1958, especially since you mentioned a dispute among U.S. attorneys in the Central Office. From your point of view, would S. 1958 be more effective the way Mr. Valukas sees it or the way that the Justice Department officials prefer it?

Mr. FOGEL. Well, we did not find a lot of disagreement. Some of the officials we talked to in the Department obviously felt that re-

gional units around the country would be beneficial. I think our concern is, over time, given the historic relationship between the U.S. attorneys and the officials in the Department, to the extent you can reduce the amount of organizational bickering over who is going to prosecute the cases and work together better, you have a better law enforcement effort. And like I did say, the work that was done looking at setting up these Organized Crime-Drug Enforcement Task Forces—which did take a lot of planning—seems to have paid off some.

So I think we have to defer, really, to Justice and the U.S. attorneys in the end. Our concern is that over time the strike forces seems to have some successes but then they——

Senator GRASSLEY. Please do not equivocate. Which side does your agency come down on, giving the U.S. attorneys additional resources under their control, or under the control of main Justice? You have studied it, and Senator Proxmire and I asked you to look at it. We appreciate very much your recommendations. We think that your report contributes well to this discussion. But we need a bottom line.

Mr. FOGEL. Well, I think our bottom line is we need resources in both places.

Senator GRASSLEY. You ought to get elected to any office. [Laughter.]

Ms. TOENSING. And Mr. Valukas and I are going to vote for him.

Senator METZENBAUM. Senator Simon.

Senator SIMON. Yes. First, something that is not touched in either bill as I look through them, and I would like to ask Ms. Brown and Mr. Fogel this.

I talked to a reasonably high officer of the Air Force recently, and he said there just is no incentive for people to report things that are going wrong. He says, "What you do is you jeopardize your career if you do it."

How do we move? And, Mr. Vander Schaaf, you may have some observations here, too. My colleague, Senator Grassley, mentioned Mr. Fitzgerald who has had a whole series of unhappy experiences. How do we structure something so that we build an incentive for people who see abuse to report that abuse and get some action on it?

Ms. BROWN. I think the situation is gradually changing. We have been able to recognize publicly and give awards to some people who have turned in information to our office that has proven to be meaningful and very cost effective. Of course, the Major Fraud Act would provide for additional incentives. However, it does exclude Government employees, and that is one of the items in my written comments that I have asked to have reconsidered. Should Government employees who are not part of the oversight community and not directly working on the contract be considered for such awards. The situation is moving but not completely turned around.

Senator SIMON. And when you say including Government employees, that would include someone who is in the Armed Forces?

Mr. VANDER SCHAAF. Yes. The way I understand the bill, it would include someone who is in the Armed Forces, but he would have to be totally separate from any aspect of this problem. I think that language may have gone a little bit too far.

For example, someone who works in a contract administration office within a defense plant, that person may not have anything to do with respect to a particular wrongdoing that he or she identifies, yet I think the way the legislation is written Senator, you would have some difficulty or the Attorney General would down the road have some difficulty in making that award to that particular whistleblower because of the closeness of the relationship to the wrongful act.

I think you ought to be sure that you do not want to put on too many restrictions. I think there are a lot of Government employees who maybe have some knowledge but it is not necessarily directly related to their job. They are willing to come forward, and let us encourage them to come forward.

Senator SIMON. If I may follow through and then I want to get to Mr. Fogel's answer.

I think the feeling on the part of at least one person in the Air Force is not so much that we need that incentive for that one time kind of reporting, but we somehow have to structure things so you do not discourage that overall career development if you blow the whistle.

Mr. VANDER SCHAAF. Absolutely. I do not know the answer, Senator. I think it comes from on high; it comes from our officials in the Department of Defense, including officials for the Inspector General's office and elsewhere to encourage and support whistleblowers with their problems up and down the line.

But it is a difficult area to work in. We get whistleblowers who have personal or private agendas, and it is sometimes difficult to sort them out, as we have to do regularly in our business. I think it is a matter of management.

Senator SIMON. Mr. Fogel.

Mr. FOGEL. I would echo that comment. I think, too, we feel it is also a matter of the attitude and philosophy of the top people running an organization. As the Comptroller General testified yesterday before the Senate Armed Services Committee on this whole situation in DOD now, you had a massive defense buildup. We think the Secretary's office should do a better job than it has managing the Defense Department. And if you are going to turn everything over to the services and not focus enough on internal controls, not be aggressive, and not create an atmosphere when you are concerned about these things, it makes it more difficult for employees to come forward.

Again, I would support what Senator Proxmire said this morning, and the Comptroller General supported yesterday. We believe the Foreign Corrupt Practices Act worked when the Congress passed it. It changed the attitude in the industries. The SEC now is looking at a rule to tighten up the responsibility of corporate officials and boards for assuring that the internal controls in their companies are adequate.

So I think we have supported the IG's whistleblowers award program, but we also think it has to go deeper than that in terms of the philosophy and the attitude people bring to the job.

Senator SIMON. I recognize this is not the subject of this hearing, but if I may follow through on the Foreign Corrupt Practices Act. For us to weaken that Foreign Corrupt Practices Act in a trade bill

would not be in the national interest, I sense you are testifying. Is that correct?

Mr. FOGEL. Well, we viewed that it was successful in the past. We have not done any current studies. I guess this would be my own personal view on this, that we think the Act has had a salutary effect.

Senator SIMON. All right. Then, Mr. Valukas, just some specifics on H.R. 3911. It includes mandatory minimum term of two years imprisonment where you would cause personal injury; for example, the parachute case.

Mr. VALUKAS. Correct.

Senator SIMON. Does that make sense to you?

Mr. VALUKAS. Yes.

Senator SIMON. Number two. An ultimate fine of $10 million may be imposed if the gross loss to the U.S., or the gross gain to the defendant equals $250,000, or more?

Mr. VALUKAS. I would agree with that.

Senator SIMON. Number three. Extend the statute of limitations from 5 years to 7 years.

Mr. VALUKAS. Absolutely. In cases that we have under investigation we are frequently required to go back to the defense attorney and ask him to extend the statute of limitations so that we can complete the investigation. These are complex matters.

Senator SIMON. It seems to me, Mr. Chairman, that we can mesh these bills that are before us, and come up with something that really can send that signal that you are talking about, and I hope we do it. Thank you.

Senator METZENBAUM. I think we intend to do that, and you did say "mesh," not "mash"?

Senator SIMON. Yes.

Senator METZENBAUM. Thank you. Senator Specter.

Senator SPECTER. Thank you, Mr. Chairman.

As I review these materials, it seems to me that these statutes may be, these bills may be helpful, but they really do not go to the core problem of enforcement and of tenacity in the investigative, prosecutorial sense.

There is a super-abundance of legislation on the books at the present time to deal with these problems, and this legislation proposed could be helpful, but it does not go to the core at all.

In the few minutes that I have this morning, I would like to pursue two questions, one for Ms. Toensing and one for Mr. Vander Schaaf, really, on the kinds of pursuit on these factual matters.

The Judiciary Committee will never be able to provide sufficient oversight to prod the prosecutors or the investigators or the inspectors general to do this job. It is just not humanly possible for this committee to do that.

And we do not scratch the surface; we just sort of come down near the surface in these hearings.

A concern that I have, and that I have expressed to Attorney General Meese, is the supervision by the Justice Department. I know Ms. Toensing, and I know of her capabilities, and she is a very able lawyer. But I also know that she is very overworked with a tremendous range of responsibilities in many fields, including international terrorism.

And a concern that I have expressed to the Attorney General is what has happened to the supervision. The Attorney General was out of the loop on these investigations because he was allegedly mentioned in a wiretap.

We have been without an Assistant Attorney General in the Criminal Division since Mr. Weld left. We have Mr. Dennis now as Acting. He has not been confirmed. The responsibility for supervision has come to Ms. Toensing.

You have a U.S. attorney operating in Virginia, and there is a real question—which we will pursue later—as to whether there has been anywhere near the kind of supervision from the Justice Department that is necessary to really give direction here.

When I hear Mr. Vander Schaaf testify about the revolving door, and pursing the questions which Senator Metzenbaum has raised, it is just astounding to me, if the facts which are forth in this "Washington Post" article are correct, about what goes on with Pratt and Whitney, where you have the FBI office, Miami office contending that there should have been a prosecution of Pratt and Whitney.

And you have the recitation of these facts about the kind of billing involved. A $67,500 donation to the Oklahoma Arts Center made at the request of an Air Force Major General in Oklahoma City. It sounds like extortion to me, and I have had a few extortion cases.

And if these facts are correct, it looks to me that the files are rampant with forceful evidence of fraud. And while there is a conclusion that there was no quid pro quo to establish a bribery case, which you have to establish, but you had several Air Force supervisors assigned to the West Palm Beach plant later go to work for Pratt and Whitney, you can establish the elements of bribery without having somebody witness money changing hands.

Bribery cases and a quid pro quo are often based on inferences as to what happens, and the real question in my mind, which we can explore thoroughly in the 10 minutes I have, is, what happened in the pursuit of this evidence?

Mr. Vander Schaaf, I can understand your frustration, but it surprises me to hear you testify that you have seen this cozy arrangement in the past, and you have testified, and nothing has been done.

What are the specifics? What did you observe with Pratt and Whitney?

Mr. VANDER SCHAAF. Senator, I did not say nothing was done, but I have seen, in the past, this revolving door problem. You talked about "this cozy arrangement," if you will, and we have seen problems.

Senator SPECTER. Well, what was done, if you say you did not testify that nothing was done?

Mr. VANDER SCHAAF. Well, we had a major investigation of the situation and the particular contractor to which you are making reference. In the end, the prosecutors, in their discretion chose not to prosecute. That decision is out of our office's hands. We however certainly felt that that case could have gone to trial. But it is a question on which I am not going to try to second-guess them. I am

not saying that. We thought—and I am sure the FBI agents involved thought—the case should have gone to trial.

Senator SPECTER. Well, you have responsibilities besides observing what they do. You go back to the Department of Defense and you recommend changes. There are a number of remedial procedures available.

One is putting people in jail, and another is changing the procedures to stop the conduct in the future.

Let me ask you this, Mr. Vander Schaaf: What is the worst you saw, that was not corrected? The very worst——

Mr. VANDER SCHAAF. What was the worst case?

Senator SPECTER. Well, give me a case which comes to your mind as the worst you saw, where nothing remedial was done.

Mr. VANDER SCHAAF. May I provide some of those for the record.

Senator SPECTER. No.

Mr. VANDER SCHAAF. No? Okay.

Senator SPECTER. Nobody ever reads what you provide for the record, Mr. Vander Schaaf.

Mr. VANDER SCHAAF. I just do not want to jump up and give you one case, and then two or three others will come to mind.

Senator SPECTER. Well, you do not have to give me the very worst. Just give me your recollection.

You have seen a lot of things that are bad. Let's pursue one, in the course of 4 minutes that I have left. What have you seen that is really bad, and let's see what was done about it?

Mr. VANDER SCHAAF. Well, I guess that the case you are talking about; it is as good as any. I do not have to introduce some new information.

Senator SPECTER. What are the facts?

Mr. VANDER SCHAAF. The facts deal with the number of difficulties the Department and its negotiators, at that facility, in my opinion, had in not enforcing the procurement regulations——

Senator SPECTER. Those are conclusary statements. What did you see that was done? What are the facts? Who did what?

Mr. VANDER SCHAAF. The individuals negotiating those overhead rates went to the bottom line—as Ms. Toensing explained—and said, all right, we will split the differences. We will not decide these individual cases.

Now, in addition, to those individuals—in particular, I believe there was a colonel involved at this point who was responsible for those investigations, who later took a job as an employee of the Pratt and Whitney Company.

Senator SPECTER. All right. You are talking about overhead rates?

Mr. VANDER SCHAAF. Yes.

Senator SPECTER. Specifically, what was charged that should not have been charged?

Mr. VANDER SCHAAF. You mentioned one item there. I think in that particular case the funds were disallowed after the fact.

Senator SPECTER. Well, Mr. Vander Schaaf, you must know more than my brief reading of the Washington "Post."

Mr. VANDER SCHAAF. Senator, this is 4-plus years ago, and I do not remember specifically what items were charged. That can certainly be checked.

Many items were charged which, in my personal opinion, I would believe should not have been charged. The question is not what Derek Vander Schaaf thinks should be charged or not. The question is what did the procurement regulations, as imposed, and determined over a period of years, allow to be charged under the allowability conclusions and the conclusions of reasonableness?

Senator SPECTER. Well, I think it is important what Derek Vander Schaaf thinks. I am interested to know what is the worst thing you have seen. So far you have not said anything. You have not been specific at all.

Mr. VANDER SCHAAF. I am not sure what you mean by the "worst thing." The fact that we did not go ahead and do that prosecution?

Senator SPECTER. Well, what is the most egregious piece of evidence you have seen in your work for the Inspector General's Office?

Mr. VANDER SCHAAF. Egregious piece? That was not prosecuted or was not treated? That is what I think you are talking about.

Senator SPECTER. Well, I will take anything you have seen. Something that was prosecuted. I just want to know what is the worst you have seen.

Mr. VANDER SCHAAF. I guess the worst would be some of the product substitution cases, in terms of inpact on safety and performance. I will mention one, although I just hate to bring this up because it brings in new circumstances and new situations.

Senator SPECTER. That is okay.

Mr. VANDER SCHAAF. All right. We had a firm in Minnesota, a firm that I felt had, over a period of years, provided us with a substandard product. The agents worked very, very hard on this case. This particular piece of equipment was part of the Phoenix missile.

Over a period of years we were—if I can say "jerked around" by the Navy with respect to testing that piece of equipment, to find out if it was in fact defective or not defective. We could not get very good answers to the questions that the investigators asked or get the support the investigators needed.

Senator SPECTER. Well, a substandard product is not necessarily fraud. It is probably not fraud.

Mr. VANDER SCHAAF. Well, if you guarantee you are going to use an original casting and you do not use an original casting, or you take a product that has a known defect, you X-ray it and see it is defective and then tell somebody to weld over the defect, cover it up and ship it to the Government, that is fraud, Senator.

Senator SPECTER. Okay. You are getting there; you are getting there. Substandard does not necessarily mean fraud. Could be. You are getting there.

What was done?

Mr. VANDER SCHAAF. In this particular case, we found at least two other items that the manufacturer had failed to provide with the specifications we called for.

There was a plea agreement reached, and the individual was brought into court to plead guilty to the manufacture of a piece of equipment that did not involve risk to human life. That bargain was agreed to and reached. Looking at it, from the outside, I felt that the plea bargain was ill-advised. They should have taken this

company to court for providing us with a piece of equipment that knowingly presented our military personnel with a risk to their lives and their safety; however, they did not pursue the violations related to that item. They pursued a less critical item. I think it was a crank that raised a radio antenna—

Senator SPECTER. The chairman has asked me to cease and desist in the interest of time, and it is a fair request. I am going to accept your offer for supplementing the record. Please send it directly to me as well as to the committee.

I want to know what it is, the worst you have seen, and what was done about it.

Mr. VANDER SCHAAF. All right

[The information of Mr. Vander Schaaf follows:]

INSERT FOR THE RECORD									
	HOUSE / SENATE	APPROPRIATIONS COMMITTEE		HOUSE / SENATE	ARMED SERVICES COMMITTEE		HOUSE / SENATE	OTHER	Committee on Judiciary
HEARING DATE		TRANSCRIPT PAGE NO.	LINE NO.		INSERT NO.				
July 12, 1988		102	23						

Senator Spector: Well, I will take anything you have seen. Something that was prosecuted. I just want to know what is the worst you have seen.

Mr. Vander Schaaf: Examples of the most egregious product substitution cases are attached:

RAUSCH MANUFACTURING COMPANY, INC
St. Paul, MN

Rausch had been contracted by the U.S. Navy to produce aluminum castings for the Phoenix air-to-air missile, and by the U.S. Air Force for mobile radio towers and cockpit display units for the F16.

The investigation determined Rausch deliberately substituted remelted aluminum for virgin ingots. Rausch also cosmetically concealed welding defects and falsified manufacturing and testing reports. False progress payment requests were also submitted under the contract.

The president of Rausch and another company officer were convicted on multiple counts of conspiracy and false claims. The president was sentenced to 2 years imprisonment, and the second officer to 18 months.

Prepared by SA Kevin B. Kuhens, ext 30029

METAL SERVICE CENTER OF GEORGIA, INC.
Marietta, GA

CERTIFIED PRODUCTS, INC.
Marietta, GA

Metal Service had been contracted by the Defense Logistics Agency to provide millions of dollars in different type metals. The metals had a variety of applications, but were primarily used to refurbish naval vessels. The metals were used on refurbishment of the superstructure of the battleship USS New Jersey.

The investigation determined 2 officers of Metal Service engaged in a massive product substitution scheme wherein inferior metals were provided, testing results were fabricated and falsified, and the metals were mismarked to pass contract specifications. When the scheme was exposed by investigators, the 2 officers opened Certified Products, a second company designed to continue the scheme.

The metals were extremely difficult to trace once they entered the DoD supply system. Tracing efforts centered on metals intended for critical applications. These efforts were largely successful and averted safety hazards to personnel and equipment failures.

Both companies and both officers were convicted of multiple fraud charges. The officers were each sentenced to 10 years imprisonment for their offenses. The Federal judge which sentenced the pair likened their crimes to "sabotage and treason" against their country.

Prepared by SA Kevin B. Kuhens, ext 30029

DIVERSIFIED AMERICAN DEFENSE, INC.
Boaz, AL

Diversified had been contracted by the U.S. Army to supply M27 fin assemblies, which are used on 60mm mortar rounds to stabilize the rounds during flight. These fin assemblies caused erratic flight and posed a threat to the safety of personnel.

The investigation determined Diversified falsified testing reports and supplied defective assemblies. The scheme by Diversified included a burglary commited by a company vice president, in which he entered the DoD office and switched parts he believed would pass inspection, for defective ones already provided.

Diversified and its vice president were convicted on multiple fraud charges. The vice president was sentenced to 1 year imprisonment, and the company was fined $750,000 and ordered to provide restitution in the amount of $150,000.

Prepared by SA Kevin B. Kuhens, ext 30029

A & R PRECISION
Southgate, CA

A&R had been contracted by the U.S. Air Force to supply a large number of components for use in F15 and F16 aircraft and related ground support equipment. Thirty four of those items were identified as safety critical components.

The investigation determined A&R deliberately substituted inferior materials, and falsely certified test results. A&R also submitted false progress payment requests.

A&R and four company officers were convicted on multiple fraud charges. The officers were sentenced to terms of imprisonment ranging from 18 months to 2 years, fined a total of $41,000 and ordered to pay restitution in the amount of $160,000.

Prepared by SA Kevin B. Kuhens, ext 0029

ROACH CADILLAC, INC.
Kansas City, MO

Roach had been contracted by the DoD to supply rebuilt engines and transmissions and other automotive parts under contracts, which called for new and unused genuine General Motors parts. The parts were to be utilized in vehicles of the military services of the United States.

The investigation determined Roach and its officers schemed with 2 other companies to provide the DoD with used, remanufactured and non-GM parts that were disguised to meet contract specifications. In a 2 year period, the DoD was provided 16,000 inferior parts valued at over $2 million.

Roach and the 2 other companies, and 4 company officers pleaded guilty to multiple charges relating to the scheme. The officers were sentenced to terms of imprisonment ranging from 3 months to 3 years. Total fines and restitution exceeded $850,000.

Prepared by SA Kevin B. Kuhens, ext 30029

GENISCO TECHNOLOGY CORPORATION
Simi Valley, CA

Genisco had been contracted to supply pressure transducers to the U.S. Navy. Genisco served as both a prime contractor to DoD and as a subcontractor to prime DoD contractors.

The investigation determined Genisco delivered inferior transducers to the U.S. Navy. Testing results had been fabricated and the transducers falsely certified as meeting contract specifications.

Genisco and 3 officers pleaded guilty to multiple charges relating to the scheme. Genisco was fined $200,000 and ordered to make restitution in the amount of $525,000, and placed on probation for 5 years. Sentencing is still pending for the officers, who face 5 years imprisonment on several counts and millions of dollars in fines.

Prepared by SA Kevin B. Kuhens, ext 30019

GRANTEX INDUSTRIES
Dallas, TX

Grantex had been contracted by the U.S. Army to supply helicopter windows and launching canopies for various Army aircraft and missiles.

The investigation determined Grantex knowingly manufactured helicopter windows and and missile launching canopies from inferior and nonconforming materials, which it falsely certified as meeting contract specifications.

Grantex, and its 2 owners, pleaded guilty to multiple charges related to the scheme. Grantex was fined $25,000 and ordered to make restitution in the amount of $35,000. The 2 owners were sentenced to 2 years imprisonment and fined $45,000. An additional $125,000 in restitution was ordered paid for charges related to a similar contract.

Prepared by SA Kevin B. Kuhens, ext 30019

CONTINENTAL CHEMICAL CORPORATION
Terre Haute, IN

Continental had been contracted by the Defense General Supply Center to supply a highly specialized fluid, for use in purging jet aircraft fuels. The specifications for this fluid are very exact and conformance is imperative. Any deviations could result in loss of life or damage to military equipment.

The investigation determined Continental had provided nonconforming fluids, and had falsified test results. Continental and its chairman pleaded guilty to multiple charges related to the scheme. The chairman was sentenced to 5 years imprisonment, fined $25,000 and and ordered to make restitution in the amount of $100,000. Continental was also fined $100,000.

Prepared by SA Kevin B. Kuhens, ext 30029

Senator SPECTER. Mr. Chairman, I have complimented Ms. Toensing more than I have said anything else, but she may want to respond on the supervision question because I have raised it. If the chair would allow that.

Ms. TOENSING. Let me just say, for the record, that on the *Pratt and Whitney* case, Senator, the FBI main headquarters reviewed the case after the Miami office had expressed concern that we did not indict, and the main FBI headquarters concurred with the prosecutor's decision.

You know, as a prosecutor—as I do—that there are times that it breaks your heart that you cannot indict. But another responsibility that we have as prosecutors, as our agents—the agencies tug at us, and say go after these cases—that at times, we, as lawyers and officers of the court, have to say no, and it is not fun.

Senator SPECTER. Ms. Toensing, when I was a prosecutor I was only a district attorney. I could make the decisions myself. It did not break my heart. I brought the case. There is just a lot of therapy in breaking the cases. You just have to have confidence in your judgment. You do not have to win them all.

Ms. TOENSING. Well, there are certain cases that——

Senator SPECTER. You are a good prosecutor, Ms. Toensing. We just need to give you more help. I am inclined to——

Ms. TOENSING. We will accept that.

Senator SPECTER [continuing]. Join that dynamic team of Grassley and Toensing.

Ms. TOENSING. It is a great duo, now a trio.

Senator SPECTER. Thank you.

Senator METZENBAUM. We have learned what the Senator from Pennsylvania used as therapy when he was a prosecuting attorney. What does he use around the Senate? Would he care to share that with us?

Senator SPECTER. Yes. I just listen to my seniors, like you, Senator Metzenbaum. [Laughter.]

Senator GRASSLEY. Mr. Chairman, I asked Ms. Toensing if she would answer some questions in writing because of time.

Mr. Chairman, you might be interested in knowing the line of questioning. It deals with the fact that the taxpayers pay twice; we pay for DOJ's prosecution of Defense procurement fraud cases, and then, we pay the defense attorneys, because the defense contractors are the only group I know of in this country that have the privilege of getting reimbursed for their legal fees.

Senator METZENBAUM. How about all these people out there in that audience that the taxpayers are paying for today? Does that bother you, too? You know, these people out there, many of them are here for defense contractors.

Senator GRASSLEY. Well, we did pass legislation addressing this issue on the Defense Department authorization bill, which the Justice Department backed.

However, it was gutted in Conference Committee. I am determined to pursue this, and my questions are an attempt to determine the Justice Department's approach. Again, I will submit these for answers in writing from DOJ.

Senator METZENBAUM. If you would be good enough to. I might say that all responses should actually be addressed to the chairman

of the committee, Joseph Biden, with copies to each member of the committee. That is, yours, Mr. Vander Schaaf. I have a got a lot of trouble with your name.

Mr. VANDER SCHAAF. It is a good Dutch name, Senator.

Senator METZENBAUM. You should see what they do to Metzenbaum. All right. Thank you very much. I appreciate the cooperation of the panel.

Our next panel is Mr. Alan Brown of Miller and Chevalier on behalf of the U.S. Chamber of Commerce; Mr. King Culp, vice president and general counsel, Magnavox Corporation, on behalf of the Electronic Industries Association; and Don Fuqua, president of the Aerospace Industries Association, Washington, DC. We are happy to have you with us, gentlemen.

The staff tells me that they advised you that your statements should be confined to 5-minute presentations, and we appreciate you doing that. Mr. Brown, I have you listed as the first witness, on behalf of the U.S. Chamber of Commerce.

STATEMENT OF A PANEL CONSISTING OF ALAN C. BROWN, MILLER AND CHEVALIER, ON BEHALF OF THE U.S. CHAMBER OF COMMERCE, WASHINGTON, DC; KING K. CULP, VICE PRESIDENT AND GENERAL COUNSEL, MAGNAVOX CORP., ON BEHALF OF THE ELECTRONIC INDUSTRIES ASSOCIATION, FORT WAYNE, IN; AND DON FUQUA, PRESIDENT, AEROSPACE INDUSTRIES ASSOCIATION OF AMERICA, INC., WASHINGTON, DC

Mr. BROWN. Well, good morning, Mr. Chairman, and members of the committee. My name is Alan Brown, and I am happy to be here this morning to testify on behalf of the U.S. Chamber of Commerce regarding H.R. 3911, the proposed Major Fraud Act of 1988.

The impetus behind this legislation appears to be a concern regarding defense procurement fraud, but I wish to emphasize to the committee that this legislation is not so limited in scope.

The chamber of commerce represents thousands of companies, small businesses, and other organizations. Many of these do no business whatsoever with the Department of Defense, but nonetheless, they would be covered by H.R. 3911, and are very concerned about the impact of this bill.

Though the chamber supports efforts to prevent fraud and punish fraud, we cannot support H.R. 3911 in its present form for several reasons.

First, the legislation is redundant and unnecessary. The simple fact is that there is not one act prohibited by H.R. 3911 which could not just as easily be prosecuted under various existing statutes.

Second, the bill would create fines which are excessive and disproportionate to the offenses charged. Third, by extending the statute of limitations, the bill would prejudice the right of individuals and corporations to have these serious allegations investigated and concluded as promptly as possible.

Fourth, the proposed cash-award system would undermine any remaining ability of corporations to build workable self-governance systems.

Over the long haul, the best protection against fraud is a viable internal ethics and oversight program. Congress should encourage, not hinder, efforts by industry to build such systems.

Finally, the bill, while creating vastly increased penalties, excludes the requirement that intent to defraud be proven. If we are to create such enhanced penalties as those proposed by H.R. 3911, those penalties should be saved only for the truly culpable and should not be imposed for mistakes or negligent behavior.

These points are set out in the written testimony which has been provided to the committee but I would like to address two of these points more fully.

First, the penalties imposed under H.R. 3911 are excessive. Just 4 years ago, the maximum fine for submitting false claims and false statements to the United States was only $10,000.

In 1984, Congress increased the fines for all felonies, including fraud, to $250,000 per count for individuals, and $500,000 per count for corporations.

In 1985, the fine for false claims under defense contracts was increased to $1 million per count.

Thus, we have only recently seen a 100-fold increase in the available fine. But because those fines only apply to acts committed after the effective date of the legislation, in most cases prosecuted to date, the applicable fines have still been limited to $10,000.

Consequently, we have no record at all on which to judge that these recently increased fines are not more than adequate to punish and deter fraud.

The chamber of commerce believes that they are and recommends that the committee extend the $1 million fine which currently reaches only false claims on defense contracts to all fraud on all contracts with the United States.

This amount would be more proportionate to the penalties applicable to other equally serious Federal crimes, and would be in excess of fines available under State laws covering similar offenses.

In considering appropriate fines, this committee should also consider the availability of other sanctions. Under Section 3571 of Title 18, as amended just last December, a court is entitled to impose an alternative fine of twice the pecuniary gain to the defendant or twice the pecuniary loss to the United States.

This provision solves any problem with the unusually large case in which the size of the fraud may demand a fine greater than the fixed $1 million amount.

It should also be recognized that H.R. 3911 would allow multiple fines pursuant to multi-count indictments and convictions. Although the bill defines the offense as a scheme or artifice to defraud, the ninth circuit has held in *United States* v. *Poliak* that the identical language in the bank fraud statute permits a separate conviction for each false document prepared as part of a fraudulent scheme.

This holding would permit multiple one million-dollar fines in appropriate cases, but also underscores the excessiveness of the proposed $10 million fine. Using multi-count indictments, a prosecutor could, under H.R. 3911 as written, seek hundred or multi-hundred-million-dollar fines or could use the very threat of those enormous fines as a lever to coerce a guilty plea.

The committee should also keep in mind the availability of treble damages and civil penalties under the Civil False Claims Act as an additional punishment and deterrent, as well as the possibility of suspension and debarment from receiving further government contracts.

The chamber of commerce believes that when all of these elements are considered together, it is apparent that a $1 million fine would be a more appropriate sanction for violation of H.R. 3911, and urges the committee to make this change in the bill.

Lastly, I would like to address briefly the statute of limitations. Both the Constitution and the longstanding practice in the United States demand that criminal prosecutions be pursued vigorously and promptly.

The 5-year statute of limitations for non-capital offenses has been on the books for many decades and there is no evidence that it has hindered the enforcement of the law. It does, however, protect the important right of the accused to be able to defend himself effectively.

There is no record that prosecutions of procurement fraud have been lost because offenses have not been discovered or could not be investigated within 5 years. These cases are not more complicated than bank and securities frauds cases, which also need to be prosecuted within 5 years. We therefore urge that you amend the bill to maintain the 5-year statute of limitations applicable to other statutes.

I would be happy to answer any questions the committee may have.

[The statement of Mr. Brown follows:]

STATEMENT
on
THE MAJOR FRAUD ACT OF 1988 (H.R. 3911)
before the
SENATE COMMITTEE ON THE JUDICIARY
for the
U.S. CHAMBER OF COMMERCE
by
Alan C. Brown
July 12, 1988

Mr. Chairman and members of the Committee, my name is Alan Brown. I am a member of the law firm of Miller & Chevalier, Chartered. I am testifying today as a member and representative of the U.S. Chamber of Commerce.

The Chamber is the world's largest federation of business companies, chambers of commerce, and trade and professional associations. More than 92 percent of the Chamber's members are small firms with fewer than 100 employees, 59 percent with fewer than 10 employees. Moreover, virtually all of the nation's largest companies are active members. The Chamber is cognizant of the problems facing small businesses, as well as the problems facing the business community-at-large.

The Chamber is thoroughly supportive of the government's efforts to deter and punish any type of fraudulent action. However, we are unable to support H.R. 3911 in its present form. Generally, we believe that the bill substantially duplicates the coverage and purpose of existing laws.

Specifically, particular elements of the bill are contrary to basic fairness and sound public policy. Our major objections to the legislation are the following:

1. The bill would establish excessive penalties which are not related in any rational sense to the severity of the underlying crime or the penalties imposed for other serious crimes.

2. An extension of the statute of limitations from five to seven years would be contrary to the government's obligation to investigate and act expeditiously on suspected criminal activity.

3. The cash reward system would create questionable incentives without the adequate safeguards to discourage frivolous allegations.

4. Proof of specific intent to defraud the government should be required for conviction under this bill.

EXISTING LAWS ARE SUFFICIENT TO PROSECUTE AND PUNISH PROCUREMENT FRAUD

Congress, the Executive Branch, industry, and the public are all vitally interested in preventing and punishing fraud in government contracting. The Chamber understands that the motivation behind H.R. 3911 is to strengthen the legal prohibitions of such conduct. While we agree with the motives behind H.R. 3911, we are compelled to point out that the bill is redundant to many laws on the books. There is no activity prohibited by H.R. 3911 which is not already a crime under existing statutes.

The current investigation of procurement fraud illustrates the many laws which are being used to investigate and prosecute fraud. Among these are:

From Title 18, U.S. Code:

Section 201 - Prohibits offering, giving, or promising any bribe or gratuity to a federal employee, and prohibits federal employees from soliciting or accepting bribes and gratutities. Bribes and gratuities include anything of value provided with an intent to influence any official act, or provided for or because of any official act.

Section 218 - Permits the President or any agency to declare void and rescind any contract in relation to which there has been a final conviction for bribery or conflict of interest. This provision is implemented by Federal Acquisition Regulations Part 3.7.

Section 286 - Prohibits agreements and conspiracies to defraud the United States through the submission of false, fraudulent or fictitious claims.

Section 287 - Prohibits the submission of false, fictitious, or fraudulent claims against the United States.

Section 371 - Prohibits conspiracies to defraud the United States or to commit any other offense against the United States.

Section 793 - Prohibits providing, receiving, transferring, or communicating, without authorization, any document or information relating to the national defense, if such information or document could be used to the injury of the United States.

Section 1001 - Prohibits the making of false statements to the United States.

Section 1341 - Prohibits the use of the mails in connection with any scheme or artifice to defraud. (Mail Fraud)

Section 1343 - Prohibits the use of the telephone, telegraph, or radio in connection with any scheme or artifice to defraud. (Wire Fraud)

Section 1905 - Prohibits federal employees from disclosing any trade secrets or confidential financial information learned in the course of official duties. (Trade Secrets Act)

Sections 1961-1968 - Prohibits operation of an enterprise through a pattern of racketeering activity. (Racketeer Influenced and Corrupt Organizations Act)

Further, over the past few years, Congress has enacted many statutes which greatly have increased the scope and severity of fines and penalties for the purpose of deterring and punishing fraud. For example:

-- There are increased fines for false claims, false statements and other felonies from $10,000 per count to $500,000 for corporations and $250,000 for individuals, effective December 31, 1984. (18 U.S.C. Sections 3571 and 3623)

-- The Fiscal Year 1986 Department of Defense Authorization Act further increased the maximum fines for false claims relating to a contract with DOD to $1 million.

-- The Criminal Fines Improvements Act of 1987 (P. L. 100-185) permits a fine of up to twice the gross pecuniary gain to the defendant or twice the gross pecuniary loss to the United States for crimes, including false claims against the government.

-- 18 U.S.C. Sec. 3663 permits a court to order restitution to the United States for losses suffered as a result of false claims and other crimes. Restitution can be ordered as part of the sentence for crimes committed after January 1, 1983.

-- The False Claims Amendments Act of 1986 permits the government to recover treble damages plus up to $10,000 per false claim in a civil action. Recovery is virtually automatic after a criminal conviction.

— On false claims of up to $150,000, the government may recover double damages plus up to $5,000 per false claim in an administrative proceeding under the Program Fraud Civil Remedies Act of 1986. The government may also recover administratively a penalty of $5,000 for any false statement not related to a claim.

— The Anti-Kickback Enforcement Act of 1986 provides a fine of $500,000 for corporations and $250,000 plus 10 years' imprisonment for individuals who offer or solicit kickbacks in connection with government contracts.

There has been no compelling suggestion or evidence that existing criminal and civil statutes are inadequate to investigate, prosecute, and punish procurement fraud. It would be premature to define new crimes and create penalties before it is shown the current statutes are insufficient.

THE CRIMINAL FINES IN H.R. 3911 ARE EXCESSIVE

The criminal fines proposed in H.R. 3911, up to $10 million per violation, are excessive. Such fines, in our view, could well violate the Eighth Amendment, which "bars not only those punishments that are 'barbaric' but also those that are 'excessive' in relation to the crime committed. . . .[A] punishment is 'excessive' and unconstitutional if it . . . is grossly out of proportion to the severity of the crime." Coker v. Georgia, 433 U.S. 584, 592 (1977) (White, J.) (plurality opinion).

It is important to recognize that by reducing the fine in H.R. 3911 from $10 million to a $1 million figure as exists in current law, it is not creating a $1 million ceiling on the total penalty which can be imposed for fraud. In almost every case of procurement fraud, there are numerous counts. This can and does result in multi-million dollar fines.

The courts have upheld the application of penalties to each count in an indictment. The language of H.R. 3911 is modeled on the bank fraud statute, 18 U.S.C. 1344. In the recent case of U.S. v. Poliak, 823 F.2d 371 (9th Cir., 1987), the Court of Appeals held that, under the bank fraud statute, each fraudulent check prepared in connection with a single plan to defraud a bank constitutes a separate "execution" of a scheme to defraud and can be separately punished. By this interpretation, every false time card or invoice executed as part of a single plan to defraud the government could be construed as a separate violation of H.R. 3911.

Moreover, the unfairness and destructiveness of these large fines are not limited to their actual imposition. The threat of such fines alone can force a company to abandon valid defenses. The return of an indictment carrying the possibility of such massive fines can create a threat of bankruptcy, destroy a company's credit, foreclose access to capital markets, and critically injure a company's ability to carry on its business -- all before it has ever had a chance to defend itself. Confronted with such a threat, a company may have no option other than to negotiate a plea bargain.

The inappropriateness of the proposed fines can be demonstrated by reference to the chart attached to this testimony. This chart shows the maximum fines that can presently be assessed with regard to a number of kinds of federal and state laws. It can readily be seen that there are many serious activities for which the fines are much less than the $10 million level being proposed in this legislation. We believe that the Committee should gauge the appropriate fines for procurement fraud based upon existing fines for other types of criminal acts.

The Chamber recommends that the provision on fines be changed to assess a maximum fine of $1 million or twice the pecuniary gain or loss, whichever is greater. This would have the effect of increasing the fines for corporations for all government contract fraud from $500,000 to $1 million per count; today, the higher amount applies only to violations of the criminal False Claims Act on defense contracts. In addition, the civil False Claims Act would still permit treble damages to be imposed. Together, these would provide a substantial penalty, with substantial deterrent effect.

EXTENDING THE STATUTE OF LIMITATIONS DENIES SPEEDY JUSTICE

After a company or individual learns that it is the subject of a criminal prosecution, enormous amounts of time and attention are focused on that single activity. Tremendous uncertainty is created in the lives of all individuals who are implicated. Basic fairness dictates that neither individuals nor corporations should be subjected to this stress and expense any longer than is absolutely necessary. Extending the statute of limitations to seven years would deny companies and individuals their right to have the government act expeditiously on suspected criminal activity.

The policies underlying statutes of limitations have been summarized by the United States Supreme Court in Toussie v. United States, 397 U.S. 112 (1970):

> The purpose of a statute of limitations is to limit exposure to criminal prosecution to a certain fixed period of time following the occurrence of those acts the legislature has decided to punish by criminal sanctions. Such a limitation is designed to protect individuals from having to defend themselves against charges when the basic facts may have become obscured by the passage of time and to minimize the danger of official punishment because of acts in the far-distant past. Such a time limit may also have the salutary effect of encouraging law enforcement officials promptly to investigate suspected criminal activity. (emphasis added)

Increasing the statute of limitations is a poor substitute for dealing with the real problem -- inadequate enforcement resources in the Department of Justice. The Department of Justice admits that it lacks the necessary resources in this area. There is no evidence that prosecutions are being lost because frauds are not discovered within five years. If any problem with the limitations period exists, it is that the Department of Justice lacks sufficient prosecutors to pursue the cases in a timely manner. If the goal is to eliminate procurement fraud, Congress should demand prompt resolutions of fraud allegations and not permit prosecutions to be prolonged.

THE PROPOSED CASH REWARD SYSTEM LACKS SUFFICIENT SAFEGUARDS

The cash reward system in H.R. 3911 would create questionable inducements to informants without the appropriate safeguards to separate valid allegations from frivolous claims. We continue to maintain that the best protection

against fraud is sound and effective internal control systems, and Congress should encourage such self-governance efforts. The cash reward system in H.R. 3911 would undermine these efforts. We recognize that this view has been rejected by the House Committee on the Judiciary. Nevertheless, we urge this committee to strike the cash reward provision from H.R. 3911.

At the very least, any cash reward system should be limited in a manner similar to that of the qui tam provisions of the False Claims Act. We recommend the following language:

> No person shall receive payment if the furnished information is based upon public disclosure of allegations or transactions in a criminal, civil, or administrative hearing, in a congressional, administrative, or GAO report, hearing, audit or investigation, or from the news media unless the person is the original source of the information. For the purposes of this paragraph, "original source" means an individual has direct and independent knowledge of the information on which the allegations are based and has voluntarily provided the information to the government.

CONVICTION SHOULD REQUIRE PROOF OF SPECIFIC INTENT

Section 1301(a) should require the defendant to be found to have acted ". . . knowingly and willfully." The "knowing and willful" standard is included in over 30 criminal statutes, including the "False Statements" statute, 18 U.S.C. 1001, the government's most frequently used statute in procurement fraud cases. In an environment where corporate officials must deal with an enormous number of complicated federal acquisition regulations, procedures, and accounting methods, specific intent to commit fraud should be proven. If Congress is going to create substantially increased fines and penalties, it should ensure that those enhanced penalties are only imposed on the truly culpable. Where the conduct is not willful, it is more

appropriately dealt with under the Civil False Claims Act and other civil penalty statutes. This "willful" standard has not hindered prosecutions of fraud under 18 U.S.C. 1001 but will prevent innocent mistakes from being treated as criminal offenses.

CONCLUSION

Over the past six years, there has been great attention in Congress, the executive agencies, and industry to prevent fraud in government contracts. This attention has led to several initiatives, including large increases in the number of auditors and investigators; dramatically increased criminal penalties for fraud; new and enhanced civil penalties for fraud, false claims, and kickbacks; and efforts by industry to ensure strict contract compliance by all of its employees.

This hearing provides a useful review of existing statutes to determine whether new laws are needed. We believe that a careful, dispassionate look at the content of H.R. 3911 will yield the conclusion that current law is sufficient and that H.R. 3911 is seriously flawed.

We share your goal of ensuring that the procurement system is free of fraudulent activities, and we appreciate this opportunity to present our concerns and recommendations. Thank you, Mr. Chairman, for this opportunity to testify. I would be pleased to answer any questions.

EXAMPLES OF CRIMINAL AND CIVIL PENALTIES — FEDERAL & STATE

Crime	Jurisdiction	Classification	Imprisonment	Fine/Count
Major Fraud, H.R. 3911	Federal	Criminal	10 Years	$10,000,000
False Claims - Pre 1986	Federal	Civil	0	$2,000, plus double damages
False Claims - Current	Federal	Civil	0	$5,000 - $10,000, plus treble damages
False Claims - Pre 1986	Federal	Criminal	5 Years	$10,000
False Claims - Current	Federal	Criminal	5 Years	$250,000 - Individual $500,000 - Corporation
False Claims - Current	Federal	Criminal Defense Contracts	5 Years	$1,000,000
General - Felonies, Class A-E	Federal	Criminal	3 Years to Life	$250,000 - Individual $500,000 - Corporation or double damages
Theft of Property or Services Valued at $100,000 or More	Ohio	Criminal	3-15 Years	$7,500
Corrupting Another With Drugs	Ohio	Criminal	7-12 Years	$10,000
Trafficking in Drugs	Ohio	Criminal	1-10 Years	$7,500
General - Felony 1	Ohio	Criminal	4-25 Years	$10,000
General - Felony 4	Ohio	Criminal	1/2-5 Years	$2,500

Continued...

Crime	Jurisdiction	Classification	Imprisonment	Fine/Count
Making False Entries, etc. on Books of Corporations	Florida	Criminal	5 Years	$5,000 or double damages
Bribery	Florida	Criminal	15 Years	$5,000
Selling Drugs	Florida	Criminal	30 Years to Life	$10,000
Bribery	Wisconsin	Criminal	5 Years	$10,000
False Statement to Obtain Property or Credit	Texas	Criminal	1 Year	$2,000
Bribery	Texas	Criminal	2-20 Years	$10,000

Senator METZENBAUM. Just a couple brief ones. Do you find anything good in the bills?

Mr. BROWN. Mr. Chairman, we support the view that steps should be taken to stop procurement fraud. Unfortunately, this bill duplicates what has been done in the past few years.

It is too early for this legislation. We have enacted an enormous number of new statutes in the past 2 to 4 years to combat this problem and they are not in place yet. In the same period of time, over the past 2 years, industry has taken enormous steps to police itself. Those efforts also take a while to develop and we have not given those a chance either.

Senator METZENBAUM. Do I understand your answer to be no?

Mr. BROWN. We think that this bill is unnecessary and should not be passed.

Senator METZENBAUM. Mr. Brown, I am not going to ask you any questions, but I would say to you that I think the American people think that the U.S. Chamber of Commerce is just totally out of step with the American people generally.

I can understand some difference with respect to whether it ought to be $1 million or $10 million, or whether the $250,000 for the whistleblower ought to be an automatic amount or whether there ought to be some judgment on the part of the court, or whether certain aspects of the bill are good or need tightening, need to be restricting.

But I guess I have to say that it is almost a knee-jerk reaction on the part of the chamber; anything that touches business is bad. And when I say that I think the American people think the U.S. Chamber is out of step with the Nation, I only have to look at the vote by which Mr. Hughes' bill passed the House, 419 to zero.

Notwithstanding your strong lobbying efforts, your strong distribution of PAC funds, the other things that you do to garner support for candidates, nobody voted with you, and yet you come here and you say there is nothing in the bill that you think is good.

Mr. BROWN. Mr. Chairman, I think the indictment of the chamber in this area is unfair. Two years ago, this Congress passed the False Claims Act amendments and the Program Fraud Civil Penalties Act.

I worked with the chamber of commerce in relation to those bills as well. The chamber of commerce was instrumental in working out the compromises, and worked with Mr. Grassley's staff and Mr. Hatch's staff in working out those compromises, that enabled that legislation to be enacted.

That legislation is new; it only applied to acts committed after 2 years ago. Those acts have not been investigated; causes of actions have not yet been brought under those bills.

What we are pointing out with respect to this statute is that it seems to be a reaction to publicity that has been generated over the last few months, but it adds nothing too new to the government's arsenal in fighting procurement fraud.

The provisions of this bill simply will not result in one additional prosecution being brought for procurement fraud. If there is any problem at all—we have taken this position before the House in connection with H.R. 3911 and we have stated this in our testimo-

ny to this committee today—it is that there are simply not enough prosecutors in the Justice Department.

In the past few years, we have created thousands of investigators within the inspector general's office. It is difficult for companies to carry on their business today without stumbling over auditors and investigators at every step of the way, but at the same time we have not added any prosecutors to the Justice Department.

We have created a bottleneck at the top which not only prevents valid cases from being brought, but it also prejudices the defendant, since there is no one to review these cases and to determine that there is no merit to the allegations and to close them. So cases drag on and stay open forever.

If you extend the statute of limitations 2 more years through this bill, the only result is going to be that those cases will stay open for two more years. They will still be pushed to the end of the statute of limitations period. People will be under investigation, under a cloud of an investigation, for two more years. The fact is that most of those investigations result in no prosecution because they had no merit in the first place.

Senator METZENBAUM. Thank you, Mr. Brown.

Mr. Culp, we will be very happy to hear from you, sir.

STATEMENT OF KING K. CULP, VICE PRESIDENT AND GENERAL COUNSEL, MAGNAVOX CORP., ON BEHALF OF THE ELECTRONIC INDUSTRIES ASSOCIATION, FORT WAYNE, IN

Mr. CULP. Thank you, Mr. Chairman. I am here on behalf of the Electronic Industries Association. Our written testimony was provided to you. I will not review all of that in here. I would like to concentrate on one aspect of the bill and share the view of the chamber that, in essence, the bill at this time seems to be misplaced and not necessary.

Our written material contains a list of current and existing statutes which are quite adequate and apparently are being used to cover the current investigations that have been making the press lately.

I would like to address the statute of limitations position as well as anything else because I agree with Mr. Brown. The statute of limitations is quite adequate at 5 years right now.

The bottleneck at the top that could be solved, in addition to the alternate legislation calling for extra prosecutors, is if the Congress would emphasize to the executive branch the necessity for using the administrative tools that are now at their disposal.

It is very easy for them under current rules and legislation to take care of most of the major problems that seem to concern everybody in this country—product substitution, defective pricing, false claims, and mis-charging.

If we could somehow figure out a way to give back the discretion to the DCAA, to the contracting officers, and to the IGs and the procurement fraud units, there are methods administratively available now which will work faster at less money for the taxpayer and everybody's benefit to solve the problems that exist.

They range from withholding or suspending progress payments, rejection of those supplies that do not work, rejection of those serv-

ice that are bad, terminating contracts if they have defaulted on some performance. Suspension of contracts and debarment, I must say, are the strongest penalties that currently exist. For many companies large and small, the threat of suspension and debarment, the use of suspension and debarment will literally put these people out of business.

Also, the statutes and regulations already exist for getting money in mis-charging cases. Mr. Vander Schaaf mentioned the *Pratt and Whitney* case. In those cases where the costs are determined to be unallowable, there is an administrative way to get those monies back in the hands of the government without going to a Federal court, without using a Federal prosecutor, and without taking everybody's time.

My suggestion is if the product does not work, we should not buy it. There is no one company in this country that would subscribe to any kind of a situation where product substitution was tolerated. It is not tolerated by anybody who is a responsible contractor.

If you want to talk about bribery, bribery is an easy case. Everybody knows what bribery is; it has been illegal for a long time. There are statutes on the books which prohibit it, and all those cases ought to be prosecuted.

We have to change the focus, however. We have to change the focus of determining that everything a government contractor does is automatically fraud. If the specifications are not followed, the product should not be bought. If the testing was not performed, the contracting officer ought to reject that product.

If there was defective pricing, the government ought to get its money back. If there is default, they ought to be terminated, and if there is a serious question, contractors ought to be suspended or debarred. All of those actions are currently available to the Defense Department without even talking to the first prosecutor or spending any more of the government's money.

Thank you.

[The statement of Mr. Culp follows:]

TESTIMONY OF THE
ELECTRONIC INDUSTRIES ASSOCIATION

PRESENTED TO

COMMITTEE ON THE JUDICIARY

UNITED STATES SENATE

BY

KING K. CULP

VICE PRESIDENT AND GENERAL COUNSEL

MAGNAVOX

JULY 12, 1988

Mr. Chairman and Members of the Committee: My name is King Culp. I am the Vice President and General Counsel of Magnavox, and I am appearing today on behalf of the Electronic Industries Association (EIA). EIA appreciates the opportunity to present their views on H.R. 3911, the Major Fraud Act of 1988. EIA represents the entire spectrum of electronic manufacturers in the United States, ranging from manufacturers of the smallest electronic part to corporations that design and produce the most complex systems used in defense, space and industry.

EIA member companies pursue business on a daily basis in both the highly competitive government market and commercial markets throughout the world. They continue to compete based on the high quality of their products and services.

Recently published reports of alleged misconduct by contractors, consultants, and DoD officials once again focuses the public spotlight on the government contracting system. The allegations, in so far as we understand them from press reports, involve improper release of information valuable to companies competing for defense business and possible bribes. We, as much as anyone, condemn these abuses of the system and hope that the guilty are punished to the fullest extent of the law.

Congress, however, should recognize that the extent of the law now available to punish these abuses is considerable. In fact, a long list of criminal as well as civil statutes is apparently applicable to this situation, as recognized by a recent article in the publication "Defense News". (Excerpted in the attachment)

Because this extensive body of law is currently available and apparently sufficient to enable investigators and prosecutors to proceed in the current case, Congress should not create further legislative "solutions" to these problems until the success or failure of these laws can be measured in the context of the current cases.

We recognize Congress's concern that current and future expenditures of the taxpayers' money should not benefit those who engage in this type of misconduct. For that reason, Congress and the public will naturally desire some assurance that this situation will not arise again.

While we in EIA agree with this reasonable concern, we are equally troubled that Congress may attempt to label H.R. 3911 as a solution to this problem. In fact, it only indirectly addresses the alleged misconduct, while the laws listed below deal with it directly. We hope Congress will not react precipitously to the current investigation by passing legislation such as H.R. 3911.

EIA continues to oppose the enactment of H.R. 3911 for a number of reasons.

- First, H.R. 3911 substantially duplicates the intent and purpose of existing laws.

- Second, the increased penalties incorporated in H.R. 3911 represent a departure from the constitutionally based tradition in American law which directly relates the amount of a fine to the amount of damage suffered by the government.

- Third, there is no demonstratable need for a unique extension of the statute of limitations in cases involving the government contracting system.

- Fourth, particularly in cases where imprisonment for up to 10 years can be imposed, a finding of specific intent, under a "knowing and willful" standard of intent, is only appropriate.

- Fifth, the "bounty hunter" provision will, because of the complexity of government contracting, enable disgruntled former employees of defense contractors to recharacterize any dispute with management in terms of violations of the government procurement regulations in the hope of receiving a financial windfall. This increased informant activity will only generate large investigatory demands both for the government and contractors, most of which will not result in findings of improper action.

We are aware of no public policy purpose that would be achieved by the passage of H.R. 3911. In just the past five years, Congress has enacted laws which substantially strengthen the deterrents to fraud and the tools available to investigators and prosecutors. The current investigation shows that these tools are working as Congress intended. We believe that Congress should not pass measures such as H.R. 3911 until these new remedies and tools have been shown to be inadequate.

Existing Deterrents

As an intended deterrent, H.R. 3911 ignores what is, and what will remain, as the largest deterrent against fraudulent activity by government contractors -- the possibility of being suspended and debarred from receiving further government contracts. For businesses, suspension and debarment, the total prohibition against doing business with the government, is equivalent to capital punishment. For those small companies whose marketplace is primarily the government, suspension and debarment simply puts them out of business, permanently. For larger companies doing significant business with the government, suspension and debarment results in an enormous financial penalty as entire production lines are shut down and a significant source of revenue is eliminated. The intended deterrent effect of H.R.

3911 is simply unnecessary as long as the government continues to pursue actively suspension and debarment procedures against companies which are found to engage in illegal conduct.

There is another deterrent in the present system: The fact that many government contractors also have substantial amounts of commercial business. Those companies know that there is nothing worse for business than having your name on the front page of the newspaper for being prosecuted for procurement fraud. This is viewed by some as having the effect of being proven guilty before the matter has been heard. Much like suspension and debarment, the resulting financial penalties, including the need to shut down production and lost markets, are significant considerations for any business and encourages those businesses to maintain proper internal controls to try and prevent fraudulent activity. H.R. 3911 becomes yet another unnecessary deterrent in an area where the functioning of our marketplace actually provides the best of deterrents.

Government contracting is subject today to numerous technical disputes. Many of the companies involved in this market employ tens of thousands of individuals. The aggregate number of total employees and former employees is a number in the tens of millions. In an acquisition system as complex as this, it is obviously that honest mistakes will be made. This does not automatically demonstrate, however, that the entire system is flawed, or that any company operating within the system has intended to defraud the government.

Specific Provisions

In addition to the concerns about H.R. 3911 outlined above, EIA is concerned about several specific provisions of the proposed legislation. In particular, we are concerned that H.R. 3911 establishes a "knowingly" standard for fraud in cases where the punishment can be as much as ten years' imprisonment. The standard of culpability with respect to criminal activity of the magnitude addressed in this bill should be knowing and willful action. Someone ought to have specific intent to violate the law in order to be subject to such severe criminal penalties.

We are also concerned about the increase in the statute of limitations. Once a company or individual is subject to criminal prosecution, their careers, their businesses, and their futures are placed in grave doubt. There is no evidence whatsoever to suggest that cases are not being brought or evidence is being lost because of the current five year statute of limitations.

The government ought to be under an obligation to investigate and act expeditiously on suspected criminal activity. To permit the government to leave such matters open for a period as long as seven years creates a disincentive to appropriately expedite prosecutions. Such a lengthy period of time also destroys a primary value of a reasonably expeditious statute of limitations, which is to guard against evidence becoming lost or unreliable.

Finally, the size of the financial penalty incorporated in H.R. 3911, up to $10 million per count, is totally inappropriate. Existing statutes already provide for penalties of up to $1,000,000 for DoD contract fraud. In almost every case of procurement fraud, there are numerous counts, because the submission of a single false time card could represent a false statement and the submission represents a false claim. There is seldom any procurement fraud matter that arises where the government is limited in the number of counts that it can bring against the contractor. Thus, the prosecutors have almost unlimited discretion to accumulate counts and magnify companies' financial exposure. Loosely-worded statutes like the one proposed in H.R. 3911, create tremendous potential for bureaucratic abuse in leveraging unreasonable settlements with companies that can not afford to lose their government business eligibility. The specter of a multi-billion dollar penalty also creates the opportunity for bureaucratic abuse.

No company can risk a fine which equals the value of a substantial portion of the company's assets. Under H.R. 3911 thousands of businesses, both large and small, could have their very existence threatened by mere allegations of fraud in contracts valued at millions, or even hundreds of millions, of dollars. Many government contractors perform a function unique and essential to national defense. The guilty must be punished with a severity proportional to their crime. But public policy is not well served by disproportionate fines which can drive companies out of business or out of the marketplace.

The government investigators who could bring allegations of fraud under H.R. 3911 could easily threaten a company with bankruptcy simply to blackmail the management into a settlement which would not be supported by the facts of the case if decided by a court. The threat of such immense fines itself acts to deprive the defendant of the ability to mount a defense. For corporations, the risk is simply too great.

Existing Internal Controls

The two provisions in H.R. 3911 that are intended to provide for whistleblower protection and payment for information leading to a fraud conviction are of particular concern.

Why are these bounty and qui tam provisions as a matter of public policy a bad idea? In part, because there is so much judgement involved in the application of complex government regulations, that any two people can reasonably disagree on numerous actions that any company could elect to take. There are requirements that contractors must submit the data which underlies their pricing of proposals, and that it be current, accurate and complete. However, data which is judgmental or of an estimating nature need not be submitted. There has always been disagreement about what constitutes cost and pricing data, and what needs to be submitted. Reasonable people may have honest disagreements.

There are categories of unallowable costs where certain costs may have several purposes and thus fall into multiple categories. The categorization of the costs as allowable or unallowable is not necessarily a black or white matter. There are 19 cost accounting standards, most of which are highly technical from an accounting standpoint, covering the allocation of indirect costs to various contracts. There is endless litigation about the interpretation of these various standards and their proper application. There will continue to be legitimate differences of opinion, which alone should not give rise to allegations of criminal conduct.

I am concerned about the pernicious influence of these two provisions. Some individuals who become aware of these disagreements could try to use them as allegations of fraud in the hope that the government one day will recover some money and that they will share in a recovery.

The Electronic Industries Association remains opposed to H.R. 3911. We believe that there are already ample legislative and regulatory controls and penalties in place to protect the government, and the taxpayer against fraud. The imposition of additional layers of rules and laws would be superfluous and only contribute further to the complexities of administering justice.

ATTACHMENT TO THE STATEMENT BY KING K. CULP ON BEHALF OF THE ELECTRONIC INDUSTRIES ASSOCIATION

Many of the current laws and executive orders that could apply to the information release and trading alleged in the Pentagon fraud investigation are listed below. All the statutes have criminal or civil penalties attached, and debarment for government contracting is a possible sanction.

From Title 18, U.S. Code:

Section 201-The bribery statute makes it a crime to offer to a federal employee, or for a federal employee to accept a bribe or illegal gratuity.

Section 218-Authorizes the President or an agency under certain regulations to declare void any contract where a final conviction has been obtained for any bribery or conflict in connection with its award.

Section 286-Conspiracy to defraud the United States with respect to claims, attempting to obtain payment for allowance of any false, fictitious, or fraudulent claim.

Section 287-False claims statute, filing false or fictitious claims against the United States.

Section 371-Conspiracy statute, often used where a group of people attempt to defraud the United States.

Section 793-Prohibits anyone from disclosing to unauthorized people classified information in a way that is prejudicial to the safety or interest of the United States or to help a foreign government.

Section 798-Prohibits anyone from disclosing to unauthorized people classified information in a way that is prejudicial to the safety or interest of the United States or to help a foreign government.

Section 1001-False statements statute, prohibits lying to the federal government and includes falsifying business records, time sheets and other documents.

Section 1905-The trade secrets statute, prohibits federal employees from divulging proprietary information of a private firm that comes to them in the course of their employment.

Program Fraud Civil Remedies Act, 31 U.S.C. section 3801 creates an administrative remedy for government agencies which believe they have suffered a fraud.

Executive Order 11222, Section 205-Ethical standards of conduct for federal employees. Specifically prohibits anyone from using

or allowing others to use for financial gain official information not available to the general public (no criminal penalty).

Federal Acquisition Regulations, Part 9, debarment procedures.

Title 10 section 2207-This section provides that any contract, awarded because of a bribe or gratuity offered or given to any Federal employee, may be terminated as if the contractor had breached the contract. In addition to remedies for breach, the United States is entitled to damages in an amount at least 3 but not greater than 10 times the cost incurred by the contractor in giving the bribe or gratuity.

A brief review of these new laws is essential to an evaluation of H.R. 3911.

Anti-Kickback

As part of the Anti-Kickback Enforcement Act of 1986, Congress extended and expanded the coverage of the Anti-Kickback Act of 1946, 41 U.S.C. sect. 51-54, applicable to kickbacks made in connection with contracts of the federal government. The legislation prohibits attempts as well as completed kickbacks and now applies to all federal contracts, not just negotiated contracts. In addition, the Act requires government contractors to use internal procedures to detect and prevent kickbacks.

Criminal penalties were increased from a maximum two year prison term and a $10,000 fine to a maximum two year prison term and a $250,000 fine with a maximum fine of $500,000 for business entities. Civil penalties were increased, in cases of knowing violations, from the amount of the kickback to twice that amount plus up to $10,000. A six year statute of limitations provision was also established.

Criminal False Claims

In addition to the significant changes outlined above, Congress, as part of the False Claims Act of 1986 raised criminal penalties for criminal violations involving false claims. The penalty for conviction of making a false claim to the government was raised from $10,000 to $250,000 for individuals and to $500,000 for corporations. It should be noted that as part of the Defense Procurement Improvement Act of 1985, Congress raised the penalty for making a false claim to the government related to a Department of Defense contract to $1,000,000.

Again, there has been no demonstrable need to increase once again these penalties or any evidence that these existing penalties are inadequate.

Criminal Fines

As part of the Criminal Fines Improvements Act of 1987, Public Law 100-185, Congress enacted legislation that permits the imposition of a fine after conviction of a crime, including false claims against the government, of up to twice the gross gain to the defendant or twice the gross loss to the United States.

The totality of these new and revised statutes means that where evidence surfaces that a contractor may have engaged in any type of fraudulent activity, the federal government is well-equipped both to investigate and prosecute such fraud. The breadth and scope of this most recent legislation is a clear indication that Congress has, in just the past 5 years, dealt forcefully with the perceived procurement fraud problems.

The Program Fraud Civil Remedies Act

After many years of reconsideration Congress passed the Program Fraud Civil Remedies Act in 1986 (31 U.S.C. sect. 3801, P.L. 99-509). For the first time, this Act creates an administrative remedy for federal agencies which believe they have suffered a fraud. In cases valued at under $150,000, the agency may proceed before an administrative tribunal which can impose fines of up to $5,000 per offense and assess damages of up to twice the amount of the fraud.

The purpose of this Act is to ease agencies' access to fraud remedies and provide an additional deterrent.

Civil False Claims

In 1986, Congress also enacted the False Claims Act Amendments Act of 1986, Public Law 99-562. This major piece of legislation, enacted after many days of hearings and intense debate between Congress, the Executive Branch, and industry, substantially rewrote the 120 years old False Claims Act. This comprehensive statute now provides the government a major prosecutorial tool in fighting procurement fraud. The False Claims Act amendments:

- increased the statutory penalty for submitting a false claim from $2,000 to $10,000;

- increased recoverable damages from double to treble the amount;

- permits the Government to obtain consequential damages from the submission of a false claim;

- establishes liability for those persons who have actual knowledge, or act in deliberate ignorance or in reckless disregard of the truth or falsity of the information;

- substantially strengthened the provisions relating to "bounty hunter" qui tam suits and permits suits and permits up to 30 percent of the recovery to be provided to the qui tam party;

- tolls the statute of limitations until 6 years after the date on which the violation occurred or 3 years after the date when facts material to the right of action are known or reasonably should have been known by the official of the United States charged with responsibility to act in the circumstances;

- provides for "whistleblower" protection for anyone who is discharged, demoted, suspended, threatened, harassed, or in any other manner discriminated against by his employer due to his involvement with a false claim disclosure.

We note that many of the provisions in H.R. 3911 merely attempt to duplicate the provisions for the False Claims Act Amendments enacted by Congress less than two years ago, including whistleblower protection, encouragement of private party involvement in fraud cases, establishment of statute of limitations, and clear responsibility for improper conduct. At the present time there is simply no evidence that these provisions and standards need to be altered once again.

Unallowable Costs

As part of the Defense Procurement Improvement Act of 1985, Congress enacted Section 2324 to Title 10 of the U.S. Code, "Allowable costs under defense contracts" which provides that for any contract, other than a fixed-price contract without cost incentives, valued at more than $100,000, a cost that is submitted and determined by clear and convincing evidence to be unallowable will result in a penalty of up to twice the amount of such unallowable cost plus $10,000 per proposal. In addition, the statute specifically provides for certification by a corporate official concerning the allowability of all submitted costs. A false certification subjects the corporate official to prosecution under the False Statements Act, 18 U.S.C. Sect. 1001. Any cost submitted with knowledge that such cost is unallowable is also subject to the penalties of both the criminal and civil false claims statute, 18 U.S.C. Sect. 287 and 31 U.S.C. Sect. 3729. The penalty for the second submission of an unallowable cost is now three times the amount of the cost submitted.

Senator METZENBAUM. Mr. Culp, how many different companies are members of your organization?

Mr. CULP. I do not have the total here, but it numbers in the hundreds. They are large and they are small; they are in the defense business and they are in commercial business as well. They make televisions to electronic equipment.

Senator METZENBAUM. Would you be good enough to advise this committee as to how many of your members are in the defense contract business?

Mr. CULP. Certainly.

Senator METZENBAUM. And at the same time, advise us how many are presently or have been within the last 5 years under investigation, indicted or prosecuted in connection with a defense contract either fraud or overcharging or any other alleged illegalities concerning their defense contracts.

Mr. CULP. To the extent that information is available, we will be glad to provide it.

Senator METZENBAUM. I appreciate it. Thank you. I have no special questions.

Mr. Don Fuqua, President of the Aerospace Industries Association, we are happy to have you with us, sir.

STATEMENT OF DON FUQUA, PRESIDENT AEROSPACE INDUSTRIES ASSOCIATION OF AMERICA, INC., WASHINGTON, DC

Mr. FUQUA. Thank you, Senator, and Senator Grassley. I am President of the Aerospace Industries Association, the trade association representing the major manufacturers of aircraft, aircraft engines, helicopters, spacecraft, missiles, space launch vehicles, and their related components and equipment.

We very much appreciate the opportunity to——

Senator METZENBAUM. You used to sit on this side of the table, did you not, Congressman?

Mr. FUQUA. Yes I did, sir.

We very much appreciate the opportunity to appear here at this hearing on the Major Fraud Act, H.R. 3911, and the Government Fraud Enforcement Act of 1987, H.R. 1958. However, let me first offer some thoughts on the current DOD investigation, Mr. Chairman.

Annually, DOD initiates approximately 15 million transactions. And virtually none of the large-dollar transactions for major defense systems are automated. Both the government and industry must rely on people to get the job done and to meet our national security needs.

We believe that the vast majority of these people are conscientious and dedicated. However, given the volume of transactions and the millions of government and industry employees involved on a day-to-day basis in establishing requirements, awarding and performing contracts, errors will occur under the best of circumstances.

Unfortunately, in any population of this size, there are bound to be a few bad apples. I have confidence in our industry's overall recruitment and hiring procedures, but none of us can guarantee that they will never have a problem.

We also must rely on the integrity and fairness of the system, and I believe that it is generally reflective of those qualities. By the same token, we must insist on the vigorous identification and prosecution of those individuals who violate the rules.

Contractors, through their own voluntary disclosure programs and their adherence to the mandatory disclosure programs, have joined the government in an effort to bring abuses to light.

From what we have learned in recent media reports, the current Department of Defense procurement investigation appears to be based principally on allegations of bribery and unauthorized disclosure of government information. Both of these types of unlawful behavior appear to be extensively covered by current statutes, thus enabling the government to go forward with their criminal prosecutions and administrative remedies.

We do not believe that H.R. 3911 would provide the government with any additional tools to investigate or prosecute these allegations, and we urge the committee not to rush toward enactment of H.R. 3911 as even a partial solution to the current investigation.

I think the committee should analyze the substantive provisions of the bill to determine the need for and the application of this criminal statute to address cases of fraud in the Federal contracting process.

However, I do not want to leave you with the impression, Mr. Chairman, that we in the defense industry are unconcerned about the implications of the current investigations, and I have personally offered to Defense Secretary Carlucci, Chairman Nunn, and Chairman Aspin, the expertise and the assistance of our association in any way that they deem appropriate in trying to address this situation, and I offer that same assistance to this committee, as well.

I might add that our association has asked the Ethics Resource Center located here in Washington, a group which has long worked with business concerning business ethics to assist our association in formulating some recommendations to our members as relates to the use of consultants. We are also assessing the revolving door policies, and certain types of cost information which are exchanged between industry and the government.

Our member companies fully support efforts to deter and detect procurement fraud. To that end, over the past several months we have worked closely with the House sponsors of H.R. 3911, Crime Subcommittee Chairman Hughes, who appeared before you earlier this morning, and the subcommittee's ranking minority member, Rep. Bill McCollum.

While we are disappointed that a number of our major concerns remain unresolved in the House-passed bill, we look forward to continuing to work in this important area with your committee.

With respect to the Government Fraud Enforcement Act, we fully support the purpose of this legislation to establish an effective and efficient structure for combatting fraud. Our industry is committed to the full and vigorous detection, prevention, and prosecution of fraud, regardless of where it might occur.

We also support making adequate investigative and prosecutorial resources available to ferret out fraud. However, the government structure necessary to carry out this critical function is a decision

that is best left to the collective judgment of Congress and the law enforcement agencies.

In conclusion, Mr. Chairman, we do not believe that either of the bills before the committee today can be viewed as necessitated by the allegations resulting from the current investigation regarding defense procurement.

Fundamental fairness dictates that we await the outcome of the ongoing investigation before trying to craft legislative remedies to address the allegations raised by the early disclosures of the investigation.

Secondly, as a freestanding bill, H.R. 3911 has a meritorious purpose, but we do have some serious reservations about several of its substantive provisions, and we believe that the Senate Judiciary Committee should thoroughly analyze the premises on which this measure has been offered and the deleterious effects that it could have on government contracting.

Finally, the Congress, the executive branch, and the industry, individually and collectively, have a responsibility to prevent fraud. Aerospace Industries Association is committed to undertaking our responsibility.

That concludes my statement, Mr. Chairman. I will be glad to answer any questions you might have.

[The statement of Mr. Fuqua follows:]

TESTIMONY OF DON FUQUA
AEROSPACE INDUSTRIES ASSOCIATION OF AMERICA, INC.
CONCERNING THE
MAJOR FRAUD ACT OF 1988
BEFORE THE
COMMITTEE ON THE JUDICIARY
UNITED STATES SENATE

July 12, 1988

Mr. Chairman and Members of the Committee:

I am Don Fuqua, President of the Aerospace Industries Association of America, Inc. (AIA), the trade association representing the nation's major manufacturers of aircraft, aircraft engines, helicopters, spacecraft, missiles, space launch vehicles, and their related components and equipment.

We very much appreciate the opportunity to appear at this hearing on the Major Fraud Act of 1988 (H. R. 3911) and the Government Fraud Law Enforcement Act of 1987 (S. 1958). Before turning to the specifics of the subject legislation, let me offer some thoughts on the current investigation of DoD procurement.

CURRENT INVESTIGATION

Annually, DoD initiates 15 million transactions. Virtually none of the larger dollar transactions for major defense systems are automated. Thus, both the government and the industry must rely on people to get the

job done and meet our national security needs. We believe that the vast majority of these people are conscientious and dedicated. However, given the volume of transactions and the millions of government and industry employees involved in the day-to-day business of establishing requirements, and awarding and performing contracts, errors will occur under the best of circumstances. Unfortunately, in any population of this size there are bound to be a few bad apples. I have confidence in our industry's overall recruitment and hiring procedures, but none of us can guarantee that we will never have a problem.

Ethical behavior cannot be legislated. As Quartermaster General M.C. Meigs stated in 1861:

> "As a protection against fraud, he who will steal will not hesitate to shield himself from detection by violating an oath made as common as a custom-house oath. Some confidence must be reposed in human agents. The officers of the Government endeavor to do their duty. If a dishonest man finds a place among the number, mere forms and certificates of record will not prevent his stealing. The greater the fraud, the more perfect the papers."

We must also rely on the integrity and fairness of the system, and I believe that it is generally reflective of those qualities. By the same token, we must insist on vigorous identification and prosecution of those individuals who violate the rules. Contractors, through their own voluntary disclosure programs and their adherence to the mandatory disclosure programs, have joined the government in an effort to bring abuses to light.

From what we have learned from recent media reports, the current Department of Defense procurement investigation appears to be based

principally on allegations of bribery and unauthorized disclosure of government information. Both of these types of unlawful behavior appear to be extensively covered by current statutes, thus enabling the government to go forward with their criminal prosecutions and administrative remedies. We do not believe that H. R. 3911 would provide the government with any additional tools to investigate or prosecute these allegations. We urge the Committee not to rush towards enactment of H. R. 3911 as even a partial solution to the current investigation. Your Committee should thoroughly analyze the substantive provisions of H. R. 3911 to determine the need for, and application of, this criminal statute to address cases of fraud in the federal contracting process.

However, I do not want to leave you with the impression that we in the defense industry are unconcerned about the implications of the current investigation. We recognize that DoD has established a task force to review its options and to coordinate with the law enforcement agencies. In the Congress, both the House and Senate Armed Services Committees have initiated their own internal reviews; other committees, such as yours, are conducting hearings as well. We welcome this oversight. I have personally offered to Defense Secretary Carlucci, Dr. Costello, and Chairmen Nunn and Aspin, the expertise and assistance of the Aerospace Industries Association in any way they deem appropriate. I offer the same assistance to your Committee, as well.

MAJOR FRAUD ACT OF 1988

Our member companies fully support efforts to deter and detect procurement fraud. To that end, over the past several months we have

worked closely with the sponsor of H. R. 3911, Judiciary Crime Subcommittee Chairman Bill Hughes, and the Subcommittee's Ranking Minority Member, Representative Bill McCollum. While we are disappointed that a number of our major concerns remain unresolved in the House-passed bill, we look forward to continuing our work in this important area with your Committee.

The following provides an outline of some of our concerns with particular provisions contained in H. R. 3911, as passed by the House.

EXISTING FEDERAL STATUTES

Any legislation dealing with government contract fraud must recognize the controls, restrictions, and penalties enacted by Congress in just the last two years. This Committee has initiated many of the laws now available to deter and punish these abuses. There have already been numerous prosecutions and convictions for this type of behavior when it has occurred in the federal contracts arena and there is no evidence to suggest that these existing criminal and civil statutes are inadequate to prosecute, punish, and deter procurement fraud. The litany of investigations being undertaken by DoD alone is graphic evidence of the viability of these laws.

Among the new penalties are:

- Fines for false claims, false statements, and other felonies were increased from $10,000 per count to $500,000 for corporations and $250,000 for individuals, effective December 31, 1984.

- The FY '86 DoD Authorization Act further increased the maximum fines for false claims relating to DOD contracts to $1 million.

- The Criminal Fines Improvement Act of 1987 (P. L. 100-185) permits a fine of up to twice the gross pecuniary gain to the defendant or twice the gross pecuniary loss to the U. S. for crimes including false claims against the government.

- 18 U.S.C. 3663 permits a court to order restitution to the U. S. for losses suffered as a result of false claims or other crimes. Restitution may be ordered as part of the sentence for crimes committed after January 1, 1983.

- The False Claims Amendments of 1986 permits the government to recover treble damages plus up to $10,000 per false claim in a civil action. This recovery is virtually automatic after a criminal conviction.

- On false claims of up to $150,000, the government may recover double damages plus up to $5,000 per false claim in an administrative proceeding under the Program Fraud Civil Remedies Act of 1986. The government may also recover administratively a penalty of $5,000 for any false statement not related to a claim.

- The Anti-Kickback Enforcement Act of 1986 substantially strengthened the original Kickback Act, providing a fine of $500,000 for corporations and $250,000 plus 10 years imprisonment for individuals who offer or solicit kickbacks in connection with government contracts.

Individually and in combination, these statutes provide dramatic new penalties, more than sufficient to enable the U. S. to punish offenders and recoup any losses suffered by reason of fraud in government contracts. However, they were not applicable to the cases studied by the Crime Subcommittee of the House Judiciary Committee. For example, in 1983, one contractor pled guilty to 100 counts of false statements and false claims in connection with the failure to properly test electronic components. The contractor paid what, at that time, was the maximum fine of $10,000 per count for a total of $1 million.

Under current law, a conviction on those same 100 counts would subject that contractor to a maximum fine of up to $100 million if the fraud was committed on a DoD contract, or $50 million if on a civilian contract, or up to double the government's loss or the defendant's gain if that amount is greater. Additionally, the court could order restitution of any damages suffered by the government, and in a civil suit under the False Claims Act the government could recover civil penalties of up to $1 million for the 100 false claims, plus three times any damages suffered as a result of the fraud. Finally, the contractor may be debarred from doing business with the U. S. for up to three years. If H. R. 3911 were enacted in its present form, the monetary

penalty for the same violations could escalate to $1 billion. Potential penalties of this magnitude are not warranted or realistic.

Suspension and debarment from government contracting is not just an empty threat, and the government frequently and increasingly relies on this administrative remedy. Press reports from July 1, 1988 indicate that DoD has already commenced these administrative actions against four contractors, based solely on an affidavit used to support a wiretap. Parenthetically, a recent decision by a Federal judge in Missouri held that the information in an affidavit supporting a request for a search warrant could contain significant errors of fact and yet not be quashed by subsequent challenge.

DEFINITION OF THE CRIME

H. R. 3911 is modeled after the Bank Fraud Act (18 U.S.C. 1344) for establishing the elements of the crime of procurement fraud. It is our understanding that the House chose a "knowing" standard specifically to circumvent the need for the government to prove specific intent for a violation. As the Committee is well aware, there are a variety of intent standards contained in the many fraud provisions of Title 18. Other statutes, such as False Statements (18 U.S.C. 1001), provide for a "knowing and willful" standard for prosecution. Given the substantialpenalties provided for in H. R. 3911, we believe a specific intent standard should be a basic element of any crime.

Furthermore, we have concerns regarding the interpretation of the "scheme or artifice" language used in H. R. 3911, particularly in the context of day-to-day activities in government procurement. For example,

in U.S. v. Poliak, 823 F. 2d. 371 (9th Cir., 1987), the court, in interpreting the Bank Fraud statute, allowed charging each execution under a scheme as a separate act so that the defendant who wrote ten separate checks was properly charged with ten counts of bank fraud. Therefore, based upon this case of first impression in construing the Bank Fraud Act, it is frightening to consider the implications of separate counts being alleged for each time card or purchase order issued in conjunction with the performance of a major government contract. We hope the Committee will reform the definition such that individual acts which are part of a scheme are consolidated as a single count of procurement fraud.

PENALTIES

As the Committee is well aware, H. R. 3911 authorizes a court to impose a monetary penalty of up to $10 million where the amount of the fraud is "substantial in relation to the value of such contract and the gross loss to the government or the gross gain to a defendant" is at least $250,000. This same penalty and a mandatory minimum prison sentence may also be imposed if the offense involves a "foreseeable and substantial risk of personal injury", without regard to financial gain or loss. To our knowledge, the magnitude of this penalty is unmatched in other areas of criminal law, and raises questions in our mind about violations of the Eighth Amendment concerning the imposition of excessive fines.

As we have stated previously, the House viewed this $10 million amount as a means of deterring the prohibited behavior, not as a

restitution for loss. Furthermore, as currently written, the subjective standard contained in H. R. 3911 does not offer sufficient guidance as to what dollar amount ascribed to the fraud would be considered "substantial".

Traditionally, the courts have insisted on a clear standard of proportionality in looking at the relationship between the crime committed and the penalties imposed. In Solem v. Helm, 463 U.S. 277 (1983), the court noted that the prohibition against disproportionate punishment is firmly rooted in both our common law and constitutional history, stating: "When the framers of the Eighth Amendment adopted the language of the English Bill of Rights, they also adopted the English principle of proportionality." In U.S. v. Busher, 817 F. 2d. 1409 (9th Cir., 1987), the court questioned whether forfeiture required by the RICO statute violated the Eighth Amendment. It held that courts were required to consider factors such as the harshness of a penalty in light of the gravity of the offense, sentences imposed for other offenses, and similar factors, to ensure that the penalties imposed are not so grossly disproportionate to the offense so as to violate the Eighth Amendment (See Solem v. Helm; Enmund v. Florida, 458 U.S. 782 (1982).) We strongly believe that the severity of the fine must be tied directly to the severity of the crime committed. We are concerned that the penalties provision of H. R. 3911 could impose fines which are disproportionate to the value of the fraud.

STATUTE OF LIMITATIONS

H. R. 3911 would, without justification, designate a special class of fraud covered by federal statute and would establish a seven year statute of limitations for prosecutions of covered contract fraud. The statute of limitations for other federal fraud felonies, including bank and securities fraud, remains at five years. We believe the additional two years to be an unnecessary and unjustified extension.

The basic five year federal statute of limitations (18 U.S.C. 3282) has been in its present form since 1954. No deviation from the basic statute of limitations should be made unless it is accompanied by a thorough review of the effect of such a deviation on law enforcement and the administration of justice. To our knowledge, there has been no showing that procurement fraud cases have not been brought because of the present five year statute, though these cases may be complex and paper burdened.

A seven year statute of limitations will promote sluggish law enforcement as the government will have less incentive to expeditiously pursue allegations of wrongdoing. As stated by the Supreme Court:

> "The purpose of a statute of limitation is to limit exposure to criminal prosecution to a certain fixed period of time following the occurrence of these acts the legislature has decided to punish by criminal sanctions. Such a limitation is designed to protect individuals from having to defend themselves against charges when the basic facts may have been obscured by the passage of time and to minimize the danger of official punishment because of acts in the far distant past. Such a time limit may also have the salutary effect of encouraging law enforcement officials promptly to investigate suspected criminal activity."
>
> Toussie v. U.S., 397 U. S. 112, 114-115 (1971) (emphasis added)

And the Third Circuit:

> "By encouraging speedy prosecutions, they (statutes of limitations) also afford society protection from unincarcerated offenders, and insure against a diminution of the deterrent value of immediate conviction as well as reduced capacity of the government to prove its case."
>
> U.S. v. Levine, 658 F.2d 113, 119 (3rd Cir. 1981)

Furthermore, the Sixth Amendment provides defendants with the right to a speedy trial. (See U.S. v. Marion, 404 U.S. 307 (1971)). An extended statute of limitations will burden the courts with claims of violations of this right when old cases are brought under the new law. For the defendants, lengthening the statute of limitations would create serious problems in providing for their own defense.

Moreover, there has been no case made that supports the contention that extending the statute of limitations would result in more or better prosecutions. Executive Branch witnesses at the December 1987 House Crime Subcommittee hearing spoke of a need for additional investigative and prosecutorial officials in the Executive Branch. The Department of Justice's limited resources will be further strained with the responsibility of pursuing stale allegations that will inevitably surface with this new law. In fact, one principal reason for the Congressional enactment of the Program Fraud Civil Remedies Act was to provide an alternative administrative mechanism for easing the Justice Department's prosecutorial burdens while still holding violators accountable for their acts. Additionally, the Department of Defense has promulgated regulations regarding a limited contractor voluntary disclosure program as an additional mechanism for the deterrence of fraud. According to

DoD, 101 disclosures from contractors have already been received, 96 of which were "accepted" by DOD under the voluntary disclosure program.

One of the basic arguments raised by the House in support of the Major Fraud Act is that it will increase the number of prosecutions brought by the government for procurement fraud. However, the premise that there are few prosecutions for fraud is flawed. Indeed, current headlines and evidence presented at a variety of Congressional hearings demonstrate that DOD and civilian agency investigations and referrals for fraud are on the increase. No factual evidence has been presented which would indicate that the investigative agencies lack the authority to support their responsibilities.

BOUNTY HUNTER PROVISION

The so-called "bounty hunter" provision, authorizing the court, at its discretion, to order a payment of up to $250,000 to an individual furnishing information leading to a conviction, raises a number of concerns.

As currently written, this provision does not provide any limitations or guidance as to who may furnish information and from what source(s). This language may encourage persons to disclose information acquired through parasitic means rather than from the "original source". This could include public disclosures of allegations, transactions in a criminal, civil or administrative hearing, a Congressional or GAO report, an audit or investigation, or from the news media.

Any system which provides a reward for information diminishes efficiency and employee/management teamwork -- both key ingredients to a highly productive working environment. Furthermore, it entices employees to circumvent internal corporate review mechanisms that might prevent or mitigate deterrence and detection of fraudulent actions. This portion of H. R. 3911 is counterproductive to these goals.

VICARIOUS CORPORATE LIABILITY

While we believe that individuals who violate the law should be fully and vigorously prosecuted, we do not believe that employers should be held generally liable for unauthorized actions taken by their employees. The Major Fraud Act raises a number of serious concerns for businesses in the context of respondeat superior liability. Corporations have been held criminally liable for the unauthorized criminal acts of their employees, even if the misconduct violated express orders and was without the knowledge of corporate officers. In the recent case of U.S. v. Bank of New England, N.A., 821 F.2d 844 (1st Cir.), cert. den., 108 S. Ct. 291 (1987), criminal liability was imputed to a corporation when the collective acts and knowledge of a defendant's employees amounted to a criminal offense, even though no particular individuals of the company had committed acts or had the requisite intent sufficient to constitute a criminal offense. With the staggering fines and sentences contemplated under the Major Fraud Act, corporations would be literally "betting the company" with every major federal contract they accept, regardless of the precautions they take to prevent wrongdoing.

We urge the Committee to carefully consider imposing the liabilities of the Major Fraud Act on those individuals knowingly and willfully committing the fraudulent acts. Corporate liability should only occur where responsible officers or directors of a company have actual knowledge of, and approve of, the fraud.

GOVERNMENT FRAUD LAW ENFORCEMENT ACT (S. 1958)

In your letter of invitation to testify, it was requested that we address the Government Fraud Law Enforcement Act of 1987 (S. 1958), introduced by Senators Proxmire and Grassley. We fully support the purpose of this legislation -- to establish an effective and efficient structure for combatting fraud. As we have said repeatedly, our industry is committed to the full and vigorous detection, prevention and prosecution of fraud, regardless of where it may occur. We also support making adequate, well-trained, and knowledgeable investigative and prosecutorial resources available to ferret out fraud. Whether the government's ability to carry out this critical function is best enhanced by establishing regional fraud units, augmenting the existing centralized Procurement Fraud Unit at the Justice Department, assigning dedicated resources to the U. S. attorneys, or some other alternative, is a decision best left to the collective judgment of the Congress and the law enforcement agencies.

CONCLUSION

In conclusion, Mr. Chairman, we do not believe that either of the bills before the Committee today can be viewed as necessitated by the

allegations resulting from the current investigation regarding defense procurement. Fundamental fairness dictates that we await the outcome of the ongoing investigation before trying to craft a legislative remedy to address the allegations raised by the early disclosures of the investigation.

Secondly, as a free-standing bill, H. R. 3911 has a meritorious purpose but we have serious reservations about several of its substantive provisions. We believe the Senate Judiciary Committee should thoroughly analyze the premises on which this measure has been offered and the deleterious effect it could have on government contracting.

Finally, the Congress, Executive Branch, and the industry, individually and collectively, have a responsibility to prevent fraud. AIA is committed to undertake our responsibility.

That concludes my statement. I would be glad to answer any questions.

Senator METZENBAUM. Mr. Fuqua, you were a distinguished member of the Congress for a number of years, I know, and I think you were involved in the Science and Technology Committee, if my colleague to my left's information to me is correct.

Do I understand you to say that the aerospace industry might be willing to work with the Congress in dealing with each of these measures in a constructive way, and that you would be willing to participate in discussions as to whether or not you might—towards the end, that you might then come on board as supporters of the legislation?

Mr. FUQUA. Mr. Chairman, we would gladly participate in such discussions. We have worked with Chairman Hughes and Chairman McCollum. As I stated, we do have some serious reservations in three particular areas. I have outlined those concerns in a more elaborate written statement, but one deals with the definition of the crime and another with the statute of limitations.

We do not think that defense procurement should be singled out as different from other types of procurement and other types of fraud that may be perpetrated.

Senator METZENBAUM. Well, I would say to you that if you are inclined to work with us, the general posture of this Senator has been to try to work with people to the end that they might come on board as supporters of the legislation. I have never really thought it made a lot of sense to work with somebody who was going to oppose you on the legislation regardless of how you might draft it.

We would like to have the aerospace industry on board, and that is the reason I tender the offer for you to work with our staff.

Mr. FUQUA. We offer that assistance.

Senator METZENBAUM. With respect to the other two, I gather that you are unalterably opposed to the legislation, but if there is some basis on which you might be willing to look at some specific modifications, some specific terms, we open the door to you, with the understanding that if we can find a resolution of some of the differences that you would be inclined to be supportive of the legislation. The door is open on that basis.

For those who come forward only to criticize and then say we are opposed to the bill under any and all circumstances, there is not a lot of reason for us to waste our time with them.

Mr. BROWN. Mr. Chairman, if I could, the chamber of commerce has taken a position that this bill is unnecessary, but we did work with the committee in the House, and would continue to like to work with this committee.

If the committee makes the determination that legislation is required and is to be enacted, we have identified certain specific problems. We did work with the House on working out several of the provisions that are in this bill as it currently stands. We would like to continue to work with this committee on this legislation.

Senator METZENBAUM. Well, we will be happy to have you do that, but I must tell you that this Chairman normally takes the position that part of the reason to spend the time and the effort to work with somebody is to try to get them on board as supporters.

Your original statement was not very encouraging along that line, but with that understanding, we certainly would welcome you, and the same for you, Mr. Culp.

Mr. CULP. Thank you, sir.

Senator METZENBAUM. With that——

Senator GRASSLEY. Mr. Chairman, I would like to say just one thing.

The fact that you oppose specific legislation or do not work with us on these bills does not really bother me. However, obviously, you are not for fraudulent use of the taxpayers' money, and obviously you would like to see something done about the present situation.

The best possible way for this problem to be solved once and for all would be for associations like yours, if you are really against government fraud, waste, and abuse and are really willing to do something about it, to police your members to see that they live within the law. That will be much more effective than anything we can do here.

I guess what I am asking you to do is do not just wait until there is a problem, because the present situation is just the symptom of a more pervasive disease.

We have got to change the whole thought process of contractors, and politicians are not necessarily the best ones to bring that about because *our* ethics are sometimes in question.

Politicians have to do better and have to have higher standards in order to improve our political institutions. Each one of us individually has that responsibility.

So too, must business people, both individually and within your associations, take the lead and go out and help solve this problem; do not wait for our initiatives, and you will do much more good than we can do or much more good than the Justice Department can do. But until we can achieve that attitude within the business community, I do not think we are going to solve the problem.

Senator METZENBAUM. Thank you very much, gentlemen. Thank you, Senator Grassley.

Our next and last panel is Danielle Brian-Bland, research associate, Project on Military Procurement, Washington; Brian Bruh, associate commissioner, Criminal Division, Internal Revenue Service; Joseph Fisher, Norfolk, Virginia; and Frank Dunham, Cohen, Gettings, Alper and Dunham, of Arlington, Virginia.

The Senator from Ohio wishes to apologize to these four witnesses for not being able to stay, but Senator Grassley will be able to stay. It is not an indication of my lack of interest, but it is matter of a conflict of a previously-made commitment.

So I want to welcome you to the hearings this morning. I only see three of you.

Senator GRASSLEY. Mr. Fisher was the one who was not allowed to appear.

Senator METZENBAUM. Well, I am sorry that the Justice Department saw fit to preclude our opportunity to hear from Mr. Fisher, and perhaps the Senator from Iowa will be heard from further on that subject.

Thank you all for being here, and my staff will remain and I certainly will be kept apprised of your testimony. Thank you.

Senator GRASSLEY [presiding]. I think I would like to start with Mr. Bruh first, then Mr. Dunham, and then Ms. Brian-Bland. Would you go ahead, Mr. Bruh, please?

STATEMENT OF A PANEL CONSISTING OF BRIAN BRUH, ASSOCIATE COMMISSIONER, CRIMINAL DIVISION, INTERNAL REVENUE SERVICE, WASHINGTON, DC; FRANK W. DUNHAM, JR., COHEN, GETTINGS, ALPER AND DUNHAM, ARLINGTON, VA; AND DANIELLE BRIAN-BLAND, RESEARCH ASSOCIATE, PROJECT ON MILITARY PROCUREMENT, WASHINGTON, DC

Mr. BRUH. Yes, sir. Senator, I appear this morning in response to your request that I testify concerning H.R. 3911, the Major Fraud Act, and S. 1958, the Government Fraud Law Enforcement Act of 1987.

The subject matter of the bills is not directly focused on my current responsibilities as Deputy Assistant Commissioner of Criminal Investigation at the Internal Revenue Service, and thus I am not presenting the views of IRS or Treasury with respect to these matters.

From December 1981 through December 1984, I was the Director of the Defense Criminal Investigative Service. The organization was established by Joe Sherick while he served as Assistant to the Secretary of Defense, Review and Oversight.

When Congress created the Office of Inspector General for the Department of Defense in 1982, the Review and Oversight Unit became the nucleus for the Office of Inspector General and, as you know, Mr. Sherick became the first Inspector General of DOD. I was the first Assistant Inspector General for Investigations and retained duties as head of the DCIS organization.

The mission of DCIS, both under the Assistant to the Secretary of Defense for Review and Oversight and the Inspector General, was to conduct investigations relating to the programs and operations of the department.

Following Congress' intent that we concentrate on fraud matters, we worked to develop cases that related to the DOD procurement process.

During my tenure, the organization grew to some 200 agents and has grown significantly beyond that number in recent years. We recruited experienced Federal investigators from a number of agencies such as Secret Service, Drug Enforcement Agency, the military investigative agencies, other inspector general offices, as well as special agents from the Criminal Investigation Division of the Internal Revenue Service.

Working sometimes independently, and at times with other law enforcement agencies, we focused on matters affecting the Department of Defense procurement process. We obtained convictions for offenses relating to shoddy materials, like rotten parachutes, defective computer chips, and for offenses like bribery, conflict of interest and, in the *GTE* case, for illicitly trafficking in classified government information, the latter case being of particular interest in light of recent developments.

At the same time that the Defense Criminal Investigative Service was gearing up, the Secretary of Defense and the Attorney General agreed that a special unit should be established within the Fraud Section of Justice's Criminal Division to ensure that there was a cadre of prosecutors skilled in defense contracting.

This organization, the Defense Procurement Fraud Unit, contained lawyers from the Department of Defense and several attorneys from the Department of Justice. The four Defense investigative agencies, plus the FBI, maintained liaison with the unit.

As an aside, I believe I was the first person in the Department of Defense contacted by the Department of Justice to ask what I thought of a special unit of prosecutors to be set up to handle defense fraud cases. The then Deputy Assistant Attorney General for the Criminal Division, Roger Olsen, contacted me. I could have not supported the idea more.

Before concluding my introductory remarks, I think it important to state that I found the DOD people involved in fraud enforcement to be as dedicated, honest, and hard-working as any group I have seen in 22 years in Federal law enforcement, just as I have a great deal of respect for the vast majority of prosecutors in Washington, DC, and across the country. I also have a great deal of respect for the present IG and her staff trying to do a tough job.

Sir, I have one recommendation with regard to H.R. 3911 and I have three recommendations with regard to S. 1958, should the legislation pass as it is now, proposed with regional units to be set up for prosecutors.

My final sentence sir: Much legislation exists to combat fraud and corruption in government. Those bills have much merit, the bills being proposed today as well. What is certainly needed, though, is leadership to do the job that has to be done.

[The statement of Mr. Bruh follows:]

Mr. Chairman and Members of the Committee:

I appear this morning in response to your request that I testify concerning HR 3911, the Major Fraud Act and S 1958, the Government Fraud Law Enforcement Act of 1987. The subject matter of the Bills is not directly focused on my current responsibilities as Deputy Assistant Commissioner (Criminal Investigation) at Internal Revenue Service and thus I am not presenting the views of IRS or Treasury with respect to these matters.

From December 1981 thru December 1984, I was the Director of the Defense Criminal Investigative Service (DCIS). The organization was established by Joe Sherick while he served as Assistant to the Secretary of Defense (Review & Oversight). When Congress created the Office of the Inspector General (OIG) for Department of Defense (DoD) in 1982, the Review and Oversight unit became the nucleus for the OIG and, as you know, Mr. Sherick became the first Inspector General at DoD. I was the first Assistant Inspector General for Investigations and retained duties as head of the DCIS organization.

The mission of DCIS both under the Assistant to the Secretary of Defense (R&O) and the Inspector General was to conduct investigations relating to the programs and operations of the Department. Following Congress' intent that we concentrate on fraud matters, we worked to develop cases that related to the DoD procurement process.

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Working sometimes independently and some times with other law enforcement agencies, we focused on matters affecting the DoD procurement process. We obtained convictions for offenses relating to shoddy materials, like rotten parachutes, defective computer chips, and for offenses like bribery, conflict of interest and in the GTE case, for elicitly trafficking in classified Government information. The latter case being of particular interest in light of recent developments.

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Mr Chairman, I intend to be fully cooperative, candid and responsive to your questions. Of course, in this setting, I am not able to discuss classified information or information that is protected by grand jury secrecy provisions.

Before concluding my introductory remarks, I think it important to state that I found the DoD people involved in fraud enforcement to be as dedicated, honest and hardworking as any group I have seen in my 22 years in Federal law enforcement.

Senator GRASSLEY. Thank you, Mr. Bruh.

Now, Mr. Dunham, and then we will ask questions at the end of the panel.

STATEMENT OF FRANK W. DUNHAM, JR., COHEN, GETTINGS, ALPER AND DUNHAM, ARLINGTON, VA

Mr. DUNHAM. I was requested by this committee and by the Joint Economic Committee to assist in the preparation of a report last year which involved an analysis of a particular case that went through the Justice Department to try to determine how a case that had resulted in a declination of prosecution was handled, particularly focusing on case management and the assignment of attorneys to the case.

It is my belief that the two measures, particularly S. 1958, that are before the committee today, would have improved the situation in the handling of that particular case.

I share the belief of the previous speaker that the vast majority of Federal prosecutors are skilled and dedicated people, but some of these procurement fraud matters can tax even the most skilled and the most dedicated if they are not organized and provided the leadership that makes it attractive, rewarding, and provides a work environment in which they can pursue these things, these complicated cases, without being reassigned to other cases or finding other career alternatives more attractive. That is why the geographically-located regional fraud units, to me, would be a great boon to the Department of Justice in combatting major defense procurement fraud.

The individual who is the Assistant Chief of the Fraud Section in the Department of Justice, in charge of procurement fraud, Ted Greenberg. I cannot speak highly enough of him, but he needs, I believe, more resources to do the job. I believe the matter that is being exposed by the U.S. Attorney's Office in the Eastern District of Virginia, at the present time, is not really the problem that needs to be addressed.

It is a longstanding problem. Those cases seem to me to be run-of-the-mill cases that we are reading about in the paper today. We are talking about the complicated defense procurement case that is going to take 2 or 3 years on a particular contract, on a particular contractor, on a particular matter, to even come close to bringing the case into the court.

That is where we need to concentrate some resources, and I would hope that you all would see fit to pass this bill.

Senator GRASSLEY. Thank you. Ms. Brian-Bland. Or is it Brian?

Ms. BRIAN. Brian.

Senator GRASSLEY. Ms. Brian-Bland.

STATEMENT OF DANIELLE BRIAN-BLAND, RESEARCH ASSOCIATE, PROJECT ON MILITARY PROCUREMENT, WASHINGTON, DC

Ms. BRIAN. Good afternoon, Senator Grassley. My name is Danielle Brian-Bland, and I am a research associate at the Project on Military Procurement.

For 8 years, the project has investigated cases of mismanagement, fraud, and abuse brought to us by whistleblowers inside the

procurement system. Unfortunately, the term "whistleblower" has taken on negative connotations in some circles, so from now on I will refer to these people as "closet patriots."

Our experience at the project has taught us that there are fundamental elements to the military procurement system that not only allows such abuses as we are seeing in the news today, but ensure that they will happen.

Without substantial reforms to this system, abuse of power and conflict of interest will certainly continue to occur. The activities that are being alleged in the current scandal—bribery and bid-rigging were already illegal—but clearly, these people did not fear either the current penalties or the current enforcement efforts.

The committee is considering two bills that apply to each part of this equation, and perhaps they will help change those attitudes.

The Major Fraud Act would help deter illegal acts by substantially stiffening the penalties for committing fraud. Particularly important is the provision in the Act that mandates a prison sentence for a fraudulent act that leads to personal injury.

Sometimes people forget that this type of white-collar crime does more than waste the taxpayers' money; it also threatens the safety of our own soldiers, because contracts are awarded for reasons other than the superiority, reliability, and safety of a weapon.

The second bill before the committee, the Government Fraud Law Enforcement Act, establishes regional fraud units to investigate and prosecute defense fraud cases.

This bill strengthens the second part of the criminal justice equation by improving the enforcement system. It would provide critical additional investigators and attorneys at the prosecution level.

This help has become necessary because of the void created by the Justice Department in its prosecution of major fraud cases. Their track record does not reflect their rhetoric.

In my written testimony I have enclosed a few examples of cases against major defense contractors that were dropped by Justice. In Justice's defense, frequently their efforts are undermined by Government officials who acquiesce to the fraud in the first place, as Senator Metzenbaum was mentioning earlier, and all of these people will remain in the system after those involved in this particular scandal are gone.

Instead of dropping these cases, the Justice Department should begin to prosecute Government officials who acquiesce to fraud. The Major Fraud Act and the Government Fraud Law Enforcement Act could be the tools with which to do this.

Since the Pentagon scandal story broke, the debate that has emerged is whether the problem stems from bad people or a bad system.

It is both. A failure to address either of these elements would only serve to perpetuate these problems. These two bills only address the back-end of the procurement system, once the fraud has already been committed.

Because neither bill affects the underlying incentives of the current system, they will only be successful if they are applied in concert to other changes.

Many people in Congress and the Pentagon argue that we just need to get rid of a few unethical people. Clearly, the people found

guilty through the FBI probe should be put in prison, but closing the case there is not enough. The real people problem will continue unscathed.

As long as individuals who are concerned about profit-padding, unrealistic testing, or time-card fraud are invariably squelched and usually fired, our people problem will go unanswered.

How often is someone promoted and held in high regard, inside the establishment, for recommending to cancel a weapons system because it does not work, or for cutting a budget of its waste and fat? Never.

And this message rings clearly through all the halls of the Pentagon, out to all the commands, and into the contractors' plants. That is our people problem.

The highest levels of the DOD bureaucracy need to seek out these people so that they can be promoted and put in charge of bigger projects and more people.

Instead, closet patriots are only sought out for retaliation. They are then left to fight losing battles to keep their jobs, having been given very weak remedies from basically antagonistic whistleblower protection offices.

Another improvement would be to augment existing revolving-door law. As of now the top echelon of Department of Defense officials are not restricted by revolving-door law because they did not work for a majority of their time on a particular contract.

In fact they have supervisory roles over many contracts at a time, making them even more likely to have influence over, or knowledge about a contract than most mid-level people.

Revolving-door law should place a 2-year moratorium on anyone who had personal and substantial responsibility affecting the interests of the contractors from going to work for that contractor.

Any time that an individual can affect the interests of the future employer, that should be considered a conflict of interest. This is the only way to close, firmly, the revolving door.

Over the past few years, Congress has passed laws, and the Pentagon has implemented regulations aimed at preventing the problems we are now facing. That just is not enough.

Once the press moves on to the next scandal and public outrage has ebbed, Congress must maintain rigorous oversight over the implementation of these laws and force the Pentagon to adopt an entirely new view of the type of person they want for protecting our national defense.

[The prepared statement of Ms. Brian-Bland follows:]

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Statement of

DANIELLE BRIAN-BLAND

The Project on Military Procurement

Committee on the Judiciary

U.S. Senate

July 12, 1988

Good morning Mr. Chairman and members of the Committee,

My name is Danielle Brian-Bland, and I am a research associate at the Project on Military Procurement. For eight years, the Project has investigated cases of mismanagement, fraud and abuse brought to us by whistleblowers inside the procurement system. Unfortunately, the term whistleblower has taken on negative connotations in some circles, so from now on, I'll refer to these people as closet patriots.

Perhaps the most surprising thing about the FBI probe of the Pentagon is the fact that people are surprised to discover that the military procurement system is mired in conflict of interest and disregard for the taxpayer and the soldier. Our experience at the Project has taught us that there are fundamental elements to the military procurement system that not only allow such abuses as we're seeing in the news today, but ensure that they will happen. Without substantial reforms to this system, abuse of power and conflict of interest will certainly continue to occur.

This Committee is currently considering two bills that will help to address these problems. For the criminal justice system to be effective, would-be criminals must (1) fear the penalties and (2) believe that criminal acts are likely to incur these penalties. The activities that are being alleged in the current scandal, bribery and bid-rigging, were already illegal, but clearly these people did not fear either the current penalties or the current enforcement efforts. The two bills apply to each part of this equation, and perhaps they will help change those attitudes.

The Major Fraud Act, H.R. 3911, would help deter illegal acts by substantially stiffening the penalties for committing fraud. Particularly important is the provision in the Act that mandates a prison sentence for a fraudulent act that leads to personal injury. Sometimes people forget that this type of white collar crime does more than waste the taxpayer's money -- it also threatens the safety of our own soldiers, because contracts are awarded for reasons other than the superiority, reliability and safety of a weapon.

The second bill before the Committee, S. 1958, the Government Fraud Law Enforcement Act, establishes Regional Fraud Units to investigate and prosecute defense fraud cases. This bill strengthens the second part of the criminal justice equation by improving the enforcement system. It would provide critical additional investigators and attorneys at the investigation and prosecution level. The Regional Fraud Units would be a first step towards ending the perception that defense procurement fraud is a protected racket.

This help has become necessary because of the void created by the Justice Department in its prosecution of major fraud cases. Their track record does not reflect their rhetoric.

In 1982, for example, the Justice Department chose to ignore further allegations of fraud in its investigation of mischarging at Rockwell International Corp. on the B-1 bomber and other contracts. It levied only a $500,000 civil penalty on what investigators in the case believed was $4 million to $6 million in fraud in one year alone.

In 1986, the FBI wrote that the Justice Department's refusal to prosecute Pratt & Whitney Aircraft Group for $22 million in overcharges "defies logic", because they found that Pratt & Whitney's behavior demonstrated "a flagrant abuse to decency and common sense."

This year, the Justice Department settled with Bell Helicopter for only half the size of the government's estimated loss due to Bell's improper bookkeeping practices. They also agreed not to bar the company from future military contracts or to subject any company officials to criminal prosecution.

In Justice's defense, frequently their efforts are undermined by government officials who acquiesced to the fraud in the first place. A week ago the GAO stated that "management officials and attorneys at Justice cited complications in defense procurement fraud cases" due to the "acquiescence of some government officials in tolerating potential fraud to obtain their equipment and weapons systems." A letter from the Inspector General's office explains that "in general, it is very difficult for the Government to sustain default termination in supply contracts due to the actions and inactions by the acquisition teams that waive the Government's right to pursue default terminations..." The people we entrust with the responsibility of providing our national defense tend to look the other way or sign -off on questionable procedures, or even worse, engage in such activities themselves. And all of these people will remain in the system after those involved in this particular scandal are gone. The fraud that is being uncovered in the news is blatant and easy to understand, but there has been

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and will continue to exist, a far more elusive and intangible climate of corruption. Instead of dropping these cases, the Justice Department should begin to prosecute government officials who acquiesce to fraud. The Major Fraud Act and The Government Fraud Law Enforcement Act could be the tools with which to do this.

Since the Pentagon scandal story broke, the debate that has emerged is whether the problem stems from bad people or a bad system. It's both. A failure to address either of these elements would only serve to perpetuate these problems. These two bills only address the back-end of the procurement system -- once the fraud has already been committed. Because neither bill affects the underlying incentives of the current system, they will only be successful if they are applied in concert with other changes.

Many people in Congress and the Pentagon argue that we just need to get rid of a few unethical people. Clearly, the people found guilty through the FBI probe should be put in prison. But closing the case there is not enough. The real people problem will continue unscathed. As long as individuals who are concerned about profit-padding, unrealistic testing or time-card fraud are invariably squelched and usually fired, our people problem will go unanswered. How often is someone promoted and held in high regard inside the establishment for recommending to cancel a weapons system because it doesn't work, or for cutting a budget of its waste and fat? Never.

And this message rings clearly through all the halls of the Pentagon, out to all the commands, and into the contractor's plants. That is our people problem. The highest levels of the Department of Defense bureaucracy need to seek out these people so that they can be promoted and put in charge of bigger projects and more people. Instead, closet patriots are only sought out for retaliation. They are then left to fight losing battles to keep their jobs, having been given very weak remedies from basically antagonistic whistleblower protection offices. A genuine change of heart with regard to rewarding closet patriots is the best way to encourage government officials who go along with or facilitate fraud to remember that their ultimate bosses are all U.S. citizens.

Another improvement would be to augment existing revolving door law. This would correct some of the flaws in the system that allow the fraud to be committed in the first place. As of now, the top echelon of Department of Defense officials are not restricted by revolving door law because they did not work for a majority of their time on a particular contract. In fact, they have supervisory roles over many contracts at a time — making them even more likely to have influence over or knowledge about a contract than most mid-level people. Revolving door law should place a two year moratorium on anyone who had personal and substantial responsibility affecting the interests of the contractor from going to work for that contractor. Any time that an individual can affect the interests of a future employer, that should be considered a conflict of interest. This is the only way to close firmly the revolving door.

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There are several other ways to change the procurement system so that it would produce more bang for its buck. The Project has additional information on all of these suggestions.

— The defense budget must be cut. Until the DoD gets a signal that there is an exhaustible amount to which they will have to adjust their demands, there will always be padding and gross amounts of waste in defense spending.

— Make it illegal for defense contractors to contribute through PACs or honoraria to Members of Congress.

— We must remove the military from the procurement process, perhaps using the example of several NATO countries as a model. The military should determine our defense needs, but they should then turn over the contractual process to career civil servants. The military can then test the weapons themselves. Military officers are subjected to an "up or out" promotion policy that creates job instability during a time in their lives when they are likely to have many financial pressures. It is only natural for them to view the contractor that they are overseeing as a potential future employer. This is also true for short-term Presidential appointees. They are only in for a few years and are very likely to join the defense industry after leaving the government.

— Congress must have access to all Black Program budgets, and members of the appropriate committees must be kept apprised of the program requirements and progress in meeting these goals.

— The work measurement basis for pricing must be <u>required</u> as a cost-cutting measure to determine how much a program should cost. This method eliminates the practice of accepting a contractor's assertion of what a weapon costs, and determines the price of what the system should cost.

— We must require realistic testing of weapons systems <u>before</u> they into into full production. A GAO study concluded that "all too often, there is an overwhelming tendency to build now and fix problems later."

— We must increase the percentage of competitively bid contracts. Ironically, increased competition is being used as an excuse for the current Pentagon scandal. Current definitions of competition now include "negotiated procurement", where the DoD and selected contractors work out how to divide up the contract together. It is in this type of environment that bid-rigging is most likely. We must open competition to anyone who is willing to submit a bid.

— Non-disclosure forms required of all DoD and contractor employees with clearances stifle the flow of information to Congress, and foster the belief that problems in the system must be kept from the public. They should be abolished by Congress.

— The officer corps should be reduced because their total has increased far beyond that of enlisted personnel. By including officers in civilian business and public affairs functions, we take them away from learning how to fight wars.

Over the past few years Congress has passed laws, and the Pentagon has implemented regulations aimed at preventing the problems we're now facing. That just isn't enough. Once the press moves on to the next scandal and public outrage has ebbed, Congress must maintain rigorous oversight over the implementation of these laws and force the Pentagon to adopt an entirely new view of the type of person they want for protecting our national defense.

Senator GRASSLEY. Thank you very much.

I want to commend each of you, as I know the chairman did before he left, for your outstanding work.

Now, while I and other people in Government know what you contribute to the debate, and how you have been effective in helping to improve Government and law enforcement, I think it is important that the public know it too.

I will start with Mr. Bruh. Would you please give us a brief background of your work as an investigative agent?

Mr. BRUH. Yes, sir. I started out approximately 22 years ago in New York City as a special agent with the then-intelligence division of the Internal Revenue Service.

I worked on a variety of white-collar fraud cases as well as organized crime and narcotics trafficking. I was the first Federal agent, to my knowledge, ever loaned to a local agency to investigate police corruption in New York, the Knapp Commission.

I was then promoted a number of times, with the top position being the chief of the Criminal Investigation Division in Boston for IRS.

In 1980, July of 1980, I became the Assistant Inspector General for Investigations at GSA, having at the time a corruption problem. About a year and a half later, after having also acted for about 6 months as Inspector General at GSA, I became the Assistant Inspector General and Director of the Defense Criminal Investigative Service in the Department of Defense.

From the time I left the Department of Defense in April of 1985, to May, 1988 I was the Director, Office of Investigations, for the Criminal Investigation Division of the Internal Revenue Service, and now I am the Deputy Assistant Commissioner for Criminal Investigations, Internal Revenue Service, sir. I also was detailed to serve as the Chief Investigator for the President's Special Review Board for the Iran/Contra matter, commonly called the Tower Commission.

Senator GRASSLEY. When you went to the DCIS, how well qualified were the agents under you?

Mr. BRUH. Well, sir, at that time there was only about 20 agents in the organization across the whole country. Some of them did not have significant criminal investigative experience. Most of them had spent their careers in doing background type of investigations.

We then started to recruit, as we were given resources, experienced criminal investigators.

Senator GRASSLEY. You said you supported the concept of the Defense Procurement Fraud Unit early on. Was there a difference between the concept and the practice at the unit?

Mr. BRUH. Yes, sir.

Senator GRASSLEY. There was? Could you elaborate just a little bit on that?

Mr. BRUH. I felt that the Defense Procurement Fraud Unit had three main purposes—four main purposes, I should say. One was to prosecute those cases that a particular U.S. Attorney did not have either the resources or expertise to do.

A second reason was to prosecute those cases that, for some reason, a U.S. attorney would not prosecute, but was still impor-

tant to do so to the Department of Defense because it had a deterrent effect in a particular program.

Another reason was to coordinate multi-jurisdictional investigations. Sometimes these investigations, cross U.S. attorneys' geographic lines, and it needs therefore, that kind of coordination.

And finally, Senator, it was to unglue investigations that may be sitting in a U.S. attorney's office for a long period of time without action.

Unfortunately, the unit did not always live up to those expectations, at least to our expectations.

Senator GRASSLEY. What kind of relationship should there be between the DOD investigators and Justice Department prosecutors, and has the working relationship been the way it ought to be from your experience?

Mr. BRUH. Well, again, I must qualify that. I do not know how it has been the last 3 years. I have been out of the Department. With regard to the period of time when I was there, in my opinion, and in my whole experience, both before and after the Department of Defense, the system works best when the investigators have a pretty sizeable say in the way investigations are conducted. Additionally when companies get prosecuted, individuals also need to be prosecuted.

And there has to be the capability of the investigators, as well as the Department itself—and I am talking about the Department of Defense here—to tell the Department of Justice what cases are important to it.

That, at times, was difficult.

Senator GRASSLEY. Did it work the way you suggested—meaning, that it worked best when the investigators were closely involved with what was to be prosecuted, or not prosecuted? Did it work that way?

Mr. BRUH. Well, it would work that way on certain cases. It would work that way in certain locations around the country, in many locations around the country.

It did not always work that way, however, with the fraud unit, if that is what you are getting at, sir.

Senator GRASSLEY. You have worked as an agent in both defense and civilian agencies.

Is there any difference in the relationship between prosecutors and investigators in the defense agencies versus the civilian agencies?

Mr. BRUH. I do not think there should be a difference.

Senator GRASSLEY. No, but is there? That is my question.

Mr. BRUH. Well, again, speaking back some 3 years ago, sir, I think there is a difference when you compare military investigative organizations with civilian investigative organizations to include the Defense Criminal Investigative Service, in that the military generally works with military attorneys within the services; while the civilian investigators generally work with attorneys in the Department of Justice throughout the country and in Washington, DC.

I think there is somewhat of a difference in the way they react toward each other, although I think it is presumptuous of me to

say what all the differences would be. I have never been a military investigator.

Senator GRASSLEY. Well, if I could get you to give us some sort of general feeling that you have about the cooperation displayed between investigators and prosecutors. You know, that is the bottom line of what we are trying to get at here.

Mr. BRUH. I think in general, from what I saw, civilian investigators, to include those people in the Defense Criminal Investigative Service—and I do not mean this as a slant against military investigative organizations at all are generally more aggressive with the prosecutors in trying to get cases prosecuted, or to expand investigations.

Senator GRASSLEY. Do you have any recollection of the DCIS's investigation that led to the *GTE* case?

Mr. BRUH. Yes, I do, Senator.

Senator GRASSLEY. Then I'd, like to have you explain the problems you and others encountered in attempting to develop that case.

Mr. BRUH. Obviously for two reasons—I will tell you, sir. I just want to put a caveat on it for classified information reasons, as well as grand jury reasons, I will have to be careful as to what I say.

Senator GRASSLEY. I can understand that, yes.

Mr. BRUH. Somewhere around, either early 1983, or the end of 1982—I do not recall the exact date and I have kept no memoranda since leaving the Department—we received information that corporations and individuals, both in and out of the Department, were trafficking, so to speak, in classified documents, which—much like we read about in the papers today. I have no personal information at all about the current investigation which alleges that defense consultants and defense contractors, have advantages over other corporations in getting Government contracts, in this case, Department of Defense contracts by illegally trafficking in classified documents.

We tried hard, in our early days, to expand that investigation. We felt it was a very important investigation, and, unfortunately, for several reasons it was a struggle for a long period of time.

The investigation, I am told, closed out with the prosecution of GTE and an indictment of another individual after I left the Department.

However, we had leads to a number of corporations and a number of individuals and a fair amount of evidence that others were doing it.

Senator GRASSLEY. Do you feel that the apparent reluctance with which DOJ and DOD pursued the GTE investigation is indicative of the way procurement fraud is approached by the Government?

Mr. BRUH. To a certain extent, yes, sir.

Senator GRASSLEY. Had the GTE case been aggressively pursued, would the problems that have surfaced in the current defense probe come out a long time ago?

Mr. BRUH. Obviously I cannot speak with certainty on that. All I can tell you is that I believe that our investigation if supported to the extent many of us felt the need for it would have gone on for a couple years or more. It needed that kind of effort. I believe it

would have exposed something just like we are talking about, and could have very likely gone into the same investigation the government is doing now.

I guess what I am saying is that I do think that the illegal trafficking of classified information could have been stopped earlier.

Senator GRASSLEY. Would you repeat that?

Mr. BRUH. I think this kind of practice, this widespread practice—I do not say that every individual now involved——

Senator GRASSLEY. Yes?

Mr. BRUH [continuing]. Could have probably been stopped earlier.

Senator GRASSLEY. Well, I think that is a very significant statement. I am sorry that is the situation. But, would it be fair to say, then, that there was a problem in the Defense Procurement Fraud Unit sitting on cases referred to it?

Mr. BRUH. That was a part of the problem. There was also a difference in philosophy. The philosophy of what is important. We felt that the illegal sale or distribution of classified documents was very important. We felt that the Defense Procurement Fraud Unit did not show great concern at the time.

We felt it was not only important because it helped to defeat the procurement procedures and controls in the Department of Defense, but that individuals were taking these documents, which were required to be fully protected, they were making unauthorized copies of it with no controls and were discussing classified information over unsecure lines.

Other individuals were making notes of that, in effect creating additional classified documents. Frankly, there is no reason to believe that if foreign hostile sources are able to get at some of our information that we try to protect, that they cannot get that information that we are not protecting at all.

And it was always strange to us that everyone seemed to be concerned about spy-type cases where classified information was going overseas, and yet, there was not the same sense of urgency when the stealing of classified documents was done by the contracting community who did not properly service the documents.

One of the problems was that you could not show a dollar amount. That was an explanation given to us by the Defense Procurement Fraud Unit. Show us the dollar amount of the fraud.

Well, it is very difficult to show the dollar amount of the fraud. How do you know what the bids on the contracts really would have been? How much money the Government would have had to truly spend or save for something like a weapons system unless it was honestly bid.

What you had was individuals getting their hands on illegally obtained classified documents through the use of these involving huge Defense contracts. Undoubtedly, by having classified documents, and information, being able to get at this inside information it cost the Government huge amounts of money. But we could not prove that in dollar terms.

It was just sort of in common-sense terms, that you know that something was wrong and the government and the public was being badly beat.

Senator GRASSLEY. During all this time, did you ever suggest to the Justice Department, or the Defense Department, that they might need more resources?

Mr. BRUH. Yes. I did, sir.

Senator GRASSLEY. What was their response?

Mr. BRUH. Well, with respect to the Justice Department, the Chief of the then-Fraud Unit which supervised the Defense Procurement Fraud Unit, responded on a few occasions to me when I made that recommendation, was that the Defense Procurement Fraud Unit is merely just a group of attorneys sitting in Alexandria. They're part of a bigger section and if they need more attorneys I'll give it to them. It almost never happened.

Senator GRASSLEY. Is it fair to say, then, that the Defense Procurement Fraud Unit poorly handled the investigation of the *GTE* case?

Mr. BRUH. In my opinion, yes sir

Senator GRASSLEY. The Proxmire-Grassley bill, combines the efforts of prosecutors and investigative experts.

What is your reaction to that approach?

Mr. BRUH. I like the intent of the bill. I do not have particularly strong feelings whether or not additional prosecutors should be given to U. S. attorney's, who are truly dedicated to prosecuting defense fraud cases, which are different than other kinds of fraud cases, rather then having a Defense Procurement Fraud Unit. Fraud in Defense contracts affects our national security. When people try to defraud the Department of Defense, the monies that could be used for better weapons system so as to protect the troops, are wasted. It is a lot different than when the government is defrauded in buying pencils.

Having a special unit like the Defense Procurement Unit has certain advantages as well because it emphasizes the problem to the public. I have three recommendations with respect to your proposed legislation.

Senator GRASSLEY. I would like to have those recommendations.

Mr. BRUH. I turned them in, sir.

Senator GRASSLEY. Also, you said you had one recommendation for the major fraud act?

Mr. BRUH. Yes, sir.

Senator GRASSLEY. That has been submitted. I happen to think the major fraud act is a good bill. My comment involves the provision that states that "an offense involves a foreseeable and substantial risk of personal injury. The term of imprisonment imposed shall not be less than 2 years."

My only recommendation is that I think that that minimum sentence is too small. Unfortunately, substituted products or defective pieces of equipment that could affect military machinery and threaten the lives of our soldiers may be sold to the Defense Department. We may not find out about the defective merchandise until years after, when things start happening.

And so, that is why I support the longer, 7 year statute of limitation period for procurement fraud prosecutions, and I also believe that a 2-year minimum sentence, sir, is not enough.

When a soldier goes into the military, both he and his family believe that he's being provided with the best equipment that the United States can get for him.

Senator GRASSLEY. Thank you very much for your testimony.

I would like to go now to Mr. Dunham, and I would like to ask you the question I asked Mr. Bruh; please give us just a little bit about your background as a DOD employee and as a Federal prosecutor, and your experience with defense procurement fraud cases.

Mr. DUNHAM. Yes. It is been almost 10 years, now, since I worked for the Federal Government. I am in private practice over in Arlington. But before I went into private practice, I worked for 6 years in the Navy Department in the acquisition of new ships, as a project engineer, and then I worked for 7 years in the Department of Justice, U.S. Attorney's Office, Eastern District of Virginia, where I spent most of my time working in procurement fraud-type cases.

Since I have been out of the Justice Department, and in private practice, I have gone back once as a special prosecutor to handle one case, and I have worked as a consultant for this committee.

I have also been a defense attorney on a number of procurement fraud cases.

Senator GRASSLEY. Mr. Bruh, I'd like to return to you for one minute.

Mr. Bruh, do you know of any IRS colleagues of yours, or Treasury Department employees, that were up here to hear your testimony before this committee?

Do you know of any?

Mr. BRUH. I believe there was one person coming over, Senator.

Senator GRASSLEY. Did you know he was coming?

Mr. BRUH. Yes. I did. I had no problem with that.

Senator GRASSLEY. Okay. Mr. Dunham, thank you for that statement of background.

Based on your experience as a Federal prosecutor, I would like to have you discuss the adequacy or inadequacy of resources in the U.S. attorney's offices and in the main Justice Department, to deal with defense procurement fraud.

Mr. DUNHAM. Well, one of the questions that we were asked when we were conducting the case study I referred to in my opening remarks—one of the questions we were asked by the people in the Department of Justice that we were interviewing—which included the then-chief of the Fraud Section and the head of the Defense Procurement Fraud Unit—was, why are you looking over our shoulders regarding the manner in which a particular case was handled?

And we tried to explain to Mr. Silverstein and Mr. Ogrin that we were not second-guessing their prosecutive decision as much as looking at their methodology for reaching it, and to determine whether they had adequately done their job, and adequately been able to staff it to do the job.

And the response we got was stunning to me, because I have never known a Federal agency not to want to increase its size and its budget, and its positions for people within it to advance. And we were told that they had plenty of prosecutors, they did not have

any resource problems, and that there had been no resource problems on the case that we were looking at.

I was surprised by it because, given the facts of the case I was looking at, it looked to me like if they had had some more bodies they could have reached a more intelligent decision than the one they had reached.

It might not have been a different decision; it may well have been the same decision. And the decision they reached may well have been a correct decision on the particular case we were looking at.

But it was clear to, I think all of us that looked at that case, that it had not been adequately staffed, it had not been staffed in a continuous fashion, and that many of the problems that S. 1958 attempts to address would have cured these problems, had S. 1958 been in place, and the case had been handled under the regional fraud units that you propose to create.

Senator GRASSLEY. We have had testimony that suggests a serious lack of cooperation between prosecutors and investigators in defense procurement fraud cases. Has this been a problem in your experience?

And if so, what steps do you think need to be taken to correct that?

Mr. DUNHAM. I have not been a prosecutor for some time. When I was a prosecutor, I always found that the investigators and prosecutors for the most part got along fine.

And I have heard stories recently that that is not always the case. I think that's a shame if that's true. But I cannot verify it one way or the other.

Senator GRASSLEY. There is evidence of inadequate cooperation between Federal prosecutors and investigators of fraud cases. Do you see this as a problem? And if so, what would you do to correct it?

Mr. DUNHAM. Well, I think there needs to be—frequently the problem arises because the person in the Defense Department can see an abuse of the system. He lives in that world, and he understands the abuses of the system, and he understands the potential for fraud, and he can see fraud in their complicated procurement system that a line assistant U.S. attorney, in a U.S. attorney's office, might not appreciate.

So there may be a little bit of resistance that the Defense Department gets when they walk over to present or to try to interest the U.S. attorney's office in a particular matter.

I think that is how the problem can be relieved, if you have prosecutors who are well tuned and well trained in the fine points of the procurement process, and dedicate their prosecution efforts to those kinds of cases.

Senator GRASSLEY. Do you see the Proxmire-Grassley bill as helping that situation in any way?

Mr. DUNHAM. Definitely. It provides a career channel for the prosecutor, the man who wants to go to court to try a case, rather than become a supervisor or a manager in the Department of Justice, to move ahead in his chosen field, which is as a litigator, but yet specialize in a particular kind of case.

And the more experience he gets, the better he is going to become; the better he's going to be able to stand up against the big law firms that the Defense industry will bring in to defend themselves, and I think the government will have better overall results in court and will have more cases will go forward.

Senator GRASSLEY. You acted as a consultant to the Joint Economic Committee and to me in the investigation of the *Newport News Shipbuilding* case.

Based on your work on that case, and your interviews with various Justice Department officials, was there an awareness on the part of those officials of the shortage of prosecutors in defense procurement fraud cases?

Mr. DUNHAM. There was an awareness on the part of some of them. Some people were saying that they were shorthanded. Other people were saying that they were not shorthanded. It was not a consensus.

What was distressing to me was that the people at the top, the people at the top of the fraud section in the Department of Justice didn't appreciate the fact that they could really use more people; that really they needed more help.

That fact didn't seem to be in their lexicon. Yet down at the working level, it was quite apparent that a man would get familiar with the case, he would start to move the case, and then he would get pulled off to work on some other matter, and the case would sit to the point where the statute of limitations ran and began to control the prosecutor's decision in the case, not the evidence as to whether there was or was not a crime. What began to control the prosecutive decision was, well, can we get everything we need to get done before the statute of limitations runs on this whole business?

I don't think a procurement fraud matter should ever be controlled by the prosecutor's concern that he hasn't done his job by the time the statute is about to run. We in the private bar frequently will come into contact with a matter that is brought into us by a client, and I've heard many a lawyer tell his client, sometimes we're representing two or three different clients that are involved in the same situation, you know, don't wake up that sleeping dog. Let that sleeping dog down there in the U.S. attorney's office, just let it keep on sleeping.

Because if you poke it with a stick, and it wakes up, it might do something. But if you're just quiet, that 5 years is going to run and you're home free. Because frequently the client wants you to go do something. And you say, hey, you are just going to just call their attention to it. There are a lot of cases, gathering dust, that could be moving forward if we had more people to work on it.

Senator GRASSLEY. Give me what you would consider the most serious problems confronted by the government in defense procurement fraud cases.

Mr. DUNHAM. I think one of the most significant problems is that your witnesses for the most part depend for their livelihood on a network, whether they're government employees or whether they're private employees, a network in which their promotions, their acceptance among their fellow workers, depends on being part of the team.

And I think that what Ms. Bland talked about, the negative connotation that is put on a whistle blower, is a major problem in any of these investigations; any one I've ever been in, it was simply agony for a guy who knew something to talk about his coworkers. I think that is one problem.

I think another problem that the regional fraud units, I think, would help counteract is the parochial nature of many of these particular contractors. They become powerhouses in the political jurisdiction in which they sit.

Frequently, the person that appoints the U.S. attorney is a member of your club, Senator Grassley. And that U.S. attorney has to be aware of the political implications and the financial implications, the economic ramifications, of a possible debarment or fines, a loss of contract to a major contractor within that particular political jurisdiction.

One of the good things about the regional fraud unit is that it might give the prosecutors a choice of U.S. attorneys to go to. Most U.S. attorneys are very honest. I can't think of any who aren't. But you really put a guy in a difficult position when you ask him to take on a major economic factor in his State. And you could take the burden off him if there was an alternative that could make the prosecutive decision.

Senator GRASSLEY. The view was expressed earlier that the best way to investigate and prosecute defense procurement fraud on a regional basis is through the existing U.S. attorney's offices, rather than with regional task forces.

Which side do you come down on?

Mr. DUNHAM. I come down on the regional fraud unit. And the reason I come down on that side is, if I can just tax you for a couple of minutes, the reason people go to U.S. attorney's offices.

People go to U.S. attorneys offices because they want to become trial lawyers. They don't go to U.S. attorney's offices because they want to become career government lawyers. They want to move on.

They want to become a litigator. They want to get litigative skills, and then they want to move on to something else.

And there are some guys that have made careers out of it. But for the most part, U.S. attorney offices around the country are a good starting point for a bright young lawyer to get some trial experience under his belt and to move on to private practice.

Most of them want to get a wide variety of things. They don't want to be stuck in a pigeon hole. Those that are willing to be placed in a pigeon hole and become a specialist, sometimes they're not the best attorney.

I think that if you create this specialty area, and you create a pay system for it that makes it attractive, you will attract the kind of attorneys that want to do that kind of work.

Senator GRASSLEY. I have a question for both you and Mr. Bruh.

Are you aware of the statement that pertains to prosecutors and prosecutions and goes something like this:

"Big cases, big problems; little cases, little problems; no case, no problems, and big promotions"?

Is that generally the attitude you hear out there?

Mr. BRUH. Not to me, sir.

Senator GRASSLEY. How about you, Mr. Dunham.

Mr. DUNHAM. I think it's a natural fact of life. I think that when a guy gets involved in a big case, he disappears if he's doing it right. And he's not available to lobby for a promotion. He's not available to help out on some other matter. Because he is completely involved and enmeshed in something that is important. And he tends to be forgotten. He can have his office taken from him. They can even forget he's part of the staff.

Yet because he's willing to tackle that complicated matter and submerge himself in it, he should be being rewarded and promoted instead of just, almost put out to pasture, because he's not available. You know the old saying, out of sight, out of mind, is the way it goes.

Mr. BRUH. Senator, may I add something?

Senator GRASSLEY. Yes.

Mr. BRUH. The reason why I say, not in my opinion, is that I think where there's problems is not in that way. Virtually every prosecutor that I've ever known wants to make a big case. And that isn't usually the problem, at least not in my experience.

What the problem is is sometimes getting them to tackle tough cases, cases that are important to a particular department or agency.

For example, you could have a long drawn out investigation against one of the major defense contractors. With some of these cases, there is no way to know even the first year whether or not it's going to ultimately result in a successful prosecution.

It is tough to get those kind of resources committed to it even when it is important to the Department, because the Department in an area needs that prosecution as a deterrent; for example, with shoddy materials.

Everyone always refers back, not at this hearing, but they always refer back to American Cotton on the power chute court case that we made when I first got there. That was a case that bounced around for years. We never even did any investigative work on that.

But we could not get anyone to prosecute the case. All we simply did was, I assigned a couple of special agents to pull the materials from a couple of file cabinets and put in an order that the prosecutors were willing to bite off on it.

So I do not necessarily believe for a moment that the prosecutors don't want to prosecute the big cases. It is the tough cases that is the difficulty.

Senator GRASSLEY. Ms. Brian-Bland, have whistle blowers brought to your organization cases involving allegations, evidence, and knowledge of criminal activities relating to defense procurement fraud?

And if so, how frequently do they come forward with such cases?

Ms. BRIAN-BLAND. How often do they come forward?

Senator GRASSLEY. Yes, generally, do whistle-blowers come to your organization with these kinds of cases?

Ms. BRIAN-BLAND. Absolutely, yes, very often. I imagine these days, especially now with the publicity that has come out, our office is probably getting maybe ten whistle blowers every couple of weeks.

So we are getting enormous numbers of them. And a lot of them involve criminal fraud.

Senator GRASSLEY. And, were these whistle blowers reluctant to go to their superiors because they didn't have confidence in a successful prosecution of their cases by the law enforcement system?

Ms. BRIAN-BLAND. Well, I think the first reason they are reluctant to go to their supervisors is for the obvious reason that they are likely to be retaliated against if they do.

But in addition, they see the experience of their colleagues, and have no reason to believe that their case is going to have a serious investigation taken on by one of those agencies.

What we have found is that the only way to get an agency that investigates these cases, to really take something on, is for it to receive wide publicity. And it's after that, usually, that things start rolling.

Senator GRASSLEY. Given your organization's experience with whistle blowers and your testimony today, to what extent do you think that whistle blowers would welcome the approach taken by the regional fraud unit concept in the Proxmire-Grassley bill?

Ms. BRIAN-BLAND. I think that they would certainly welcome the added efforts in investigation. I think though on the other hand that there is still going to remain the concern that as long as they make allegations of problems within the system, that there is still going to be the fear of retaliation.

Senator GRASSLEY. You will agree that the absence of an effective deterrent to defense procurement fraud acts as an incentive for improper and illegal actions, and among the ways to improve our deterrent is to strengthen law enforcement and to protect government employees who want to testify before Congress?

Ms. BRIAN-BLAND. Oh, absolutely, yes.

Senator GRASSLEY. And you know, earlier, we learned that the Justice Department had ordered an assistant U.S. attorney not to testify before this committee, after he was invited to do so.

Does this disturb you? And if so, what should the committee do about it?

Ms. BRIAN-BLAND. It disturbs me greatly. I would hope that someone on the committee would order a subpoena and have him come in and testify so that he cannot be blamed by his supervisors for doing so.

But obviously, he has got something interesting to say that you want to hear, and I think it is very inappropriate for the agency not to allow that. And I hope Congress does not allow it either.

Senator GRASSLEY. I trust you were here when Ms. Toensing was testifying. DOJ does not support the whistle-blower protections in the Major Fraud Act.

Ms. BRIAN-BLAND. Yes.

Senator GRASSLEY. How do you feel about that?

Ms. BRIAN-BLAND. I was concerned with her reason for being opposed, which was that many whistle-blowers are themselves committing a fraud.

Our experience has been that that's very rare. And when it is true, the whistle-blower does it because his supervisor told him to do so.

There is no incentive for someone who initiated fraud to then become the whistle-blower. So I think what she's saying is really more revealing of the problem that whistle-blowers face with people that are inside the Justice Department. That's really the way they see whistle-blowers.

Senator GRASSLEY. Before I close, let me say that the record will stay open for a short period of time for questions that the witnesses might receive in writing from committee members who could not be here. So, I would hope our witnesses would be appreciative of that, and get those questions answered and back to the committee as quickly as possible.

I thank you for your testimony, and the meeting is adjourned.

[Whereupon, at 1:15 p.m. the committee was adjourned.]

APPENDIX

Public Law 100-700
100th Congress

An Act

To amend title 18, United States Code, to provide increased penalties for certain major frauds against the United States.

Nov. 19, 1988
[H.R. 3911]

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled,

Major Fraud Act of 1988.
Contracts.
18 USC 1001 note.

SECTION 1. SHORT TITLE.

This Act may be cited as the "Major Fraud Act of 1988".

SEC. 2. CHAPTER 47 AMENDMENT.

(a) IN GENERAL.—Chapter 47 of title 18, United States Code, is amended by adding at the end the following:

"§ 1031. Major fraud against the United States

"(a) Whoever knowingly executes, or attempts to execute, any scheme or artifice with the intent—

"(1) to defraud the United States; or

"(2) to obtain money or property by means of false or fraudulent pretenses, representations, or promises,

in any procurement of property or services as a prime contractor with the United States or as a subcontractor or supplier on a contract in which there is a prime contract with the United States, if the value of the contract, subcontract, or any constituent part thereof, for such property or services is $1,000,000 or more shall, subject to the applicability of subsection (c) of this section, be fined not more than $1,000,000, or imprisoned not more than 10 years, or both.

"(b) The fine imposed for an offense under this section may exceed the maximum otherwise provided by law, if such fine does not exceed $5,000,000 and—

"(1) the gross loss to the Government or the gross gain to a defendant is $500,000 or greater; or

"(2) the offense involves a conscious or reckless risk of serious personal injury.

"(c) The maximum fine imposed upon a defendant for a prosecution including a prosecution with multiple counts under this section shall not exceed $10,000,000.

"(d) Nothing in this section shall preclude a court from imposing any other sentences available under this title, including without limitation a fine up to twice the amount of the gross loss or gross gain involved in the offense pursuant to 18 U.S.C. section 3571(d).

"(e) In determining the amount of the fine, the court shall consider the factors set forth in 18 U.S.C. sections 3553 and 3572, and the factors set forth in the guidelines and policy statements of the United States Sentencing Commission, including—

Courts, U.S.

"(1) the need to reflect the seriousness of the offense, including the harm or loss to the victim and the gain to the defendant;

"(2) whether the defendant previously has been fined for a similar offense; and

"(3) any other pertinent equitable considerations.

"(f) A prosecution of an offense under this section may be commenced any time not later than 7 years after the offense is committed, plus any additional time otherwise allowed by law.

"(g) Any individual who—

Discrimination, prohibition.

"(1) is discharged, demoted, suspended, threatened, harassed, or in any other manner discriminated against in the terms and conditions of employment by an employer because of lawful acts done by the employee on behalf of the employee or others in furtherance of a prosecution under this section (including investigation for, initiation of, testimony for, or assistance in such prosecution), and

"(2) was not a participant in the unlawful activity that is the subject of said prosecution, may, in a civil action, obtain all relief necessary to make such individual whole. Such relief shall include reinstatement with the same seniority status such individual would have had but for the discrimination, 2 times the amount of back pay, interest on the back pay, and compensation for any special damages sustained as a result of the discrimination, including litigation costs and reasonable attorney's fees."

18 USC 1031 note.

(b) SENTENCING GUIDELINES.—Pursuant to its authority under section 994(p) of title 28, United States Code and section 21 of the Sentencing Act of 1987, the United States Sentencing Commission shall promulgate guidelines, or shall amend existing guidelines, to provide for appropriate penalty enhancements, where conscious or reckless risk of serious personal injury resulting from the fraud has occurred. The Commission shall consider the appropriateness of assigning to such a defendant an offense level under Chapter Two of the sentencing guidelines that is at least two levels greater than the level that would have been assigned had conscious or reckless risk of serious personal injury not resulted from the fraud.

(c) CLERICAL AMENDMENT.—The table of sections at the beginning of chapter 47 of title 18, United States Code, is amended by adding at the end the following new item:

"1031 Major fraud against the United States.".

SEC. 3. LIMITATION ON ALLOWABILITY OF COSTS OF CONTRACTORS INCURRED IN CERTAIN PROCEEDINGS.

(a) IN GENERAL.—Chapter 15 of title 18, United States Code, is amended by adding at the end thereof the following new section:

"§ 293. Limitation on Government contract costs

"(a) Any proceeding costs incurred in connection with any proceeding brought by the United States or a State government that relates to a violation of, or failure to comply with, any Federal or State law or regulation on the part of the contractor are not allowable costs in a covered contract if the proceeding results in any of the following:

"(1) an indictment by a Federal grand jury, or a conviction (including a conviction pursuant to a plea of nolo contendere) by reason of such violation or failure to comply;

"(2) the assessment of a monetary penalty by reason of a civil or administrative finding of such violation or failure to comply;

"(3) a civil judgment containing a finding of liability, or an administrative finding of liability, by reason of such violation or

failure to comply, if the charges which are the subject of the proceeding involve fraud or similar offenses;

"(4) a decision to debar or suspend the contractor or rescind, void, or terminate a contract for default, by reason of such violation or failure to comply; or

"(5) the resolution of the proceeding by consent or compromise, where the penalty or relief sought by the government included the actions described in paragraphs (1) through (5).

"(b) In any proceeding brought by the United States or a State government that does not result in any of the actions described in paragraphs (1) through (5) of subsection (a), costs for legal services incurred by a contractor in connection with such proceeding shall not be allowed in excess of the rate specified in the Equal Access to Justice Act (28 U.S.C. 2412(d)(2)(A); 5 U.S.C. 504(a)) unless the responsible contracting officer finds that a special factor (such as the limited availability of qualified attorneys or agents) justifies an award of higher rates.

"(c) For purposes of this section—

"(1) the term 'covered contract' means a contract for an amount more than $100,000 entered into by a department or agency of the United States other than a fixed-price contract without cost incentives;

"(2) the term 'proceeding' means a civil, criminal, or an administrative investigation, prosecution, or proceeding; and

"(3) the term 'proceeding costs' means all costs relating to a proceeding incurred before, during, or after the commencement of the proceeding, and such term includes—

"(A) administrative and clerical expenses;

"(B) the cost of legal services (whether performed by an employee of the contractor or otherwise);

"(C) the cost of the services of accountants and consultants retained by a contractor; and

"(D) the salaries and wages of employees, including officers and directors.".

(b) AMENDMENT TO CHAPTER ANALYSIS.—The chapter analysis for chapter 15 of title 18, United States Code, is amended by adding at the end thereof the following:

"293. Limitation on Government contract costs.".

(c) APPLICABILITY.—The amendments made by this section shall apply to contracts entered into after the date of the enactment of this Act. 18 USC 293 note.

SEC. 4. ESTABLISHMENT OF ADDITIONAL ASSISTANT UNITED STATES ATTORNEY AND SUPPORT PROVISIONS.

(a) ESTABLISHMENT OF POSITIONS.—Subject to the funding authorization limitations in section 5(a), there are hereby established within the Department of Justice additional Assistant United States Attorney positions and additional support staff positions for prosecuting cases under both the criminal and civil statutes.

(b) FUNCTION OF PERSONNEL.—The primary function of individuals selected for the positions specified in subsection (a) shall be dedicated to the investigation and prosecution of fraud against the Government.

(c) LOCATIONS.—The Attorney General shall determine the locations for assignment of such personnel. In making such determination the Attorney General shall consider concentrations of

Government programs and procurements and concentrations of pending Government fraud investigations and allegations.

SEC. 5. AUTHORIZATION OF APPROPRIATIONS.

(a) AUTHORIZATION.—Subject to the provisions of subsection (b), for the purpose of carrying out the purposes of this Act there are authorized to be appropriated $8,000,000 for fiscal year 1989, and such sums as may be necessary for each of the four succeeding fiscal years, to be available until expended.

(b) LIMITATION.—Before expending funds appropriated pursuant to subsection (a) to carry out the purposes of this section, the Attorney General shall utilize available existing resources within the Department of Justice for such purposes.

28 USC 522 note.

SEC. 6. CONGRESSIONAL OVERSIGHT.

Reports.

Commencing with the first year after the date of enactment of this section, the Attorney General shall annually report to the Congress with respect to—

(1) the number of referrals of fraud cases by the Department of Defense of defense contractors (with specific statistics with respect to the one hundred largest contractors), the number of open investigation of such contractors, and a breakdown of to which United States Attorney's Office or other component of the Department of Justice each such case was referred;

(2) the number of referrals of fraud cases from other agencies or sources;

(3) the number of attorneys and support staff assigned pursuant to this Act;

(4) the number of investigative agents assigned to each investigation and the period of time each investigation has been opened;

(5) the number of convictions and acquittals achieved by individuals assigned to positions established by the Act; and

(6) the sentences, recoveries, and penalties achieved by individuals assigned to positions established by this Act.

Courts, U.S. District of Columiba.

SEC. 7. RELIEF OF PAULETTE MENDES-SILVA.

(a) Notwithstanding section 2675 of title 28, United States Code, and section 2401(b) of such title, or any other limitation on actions at law or in equity, the United States District Court for the District of Columbia shall have jurisdiction to hear, determine, and render judgment on any claim of Paulette Mendes-Silva against the United States for personal injuries which she allegedly incurred after an innoculation on March 12, 1963, by an employee of the Public Health Service of the United States Department of Health, Education, and Welfare. Any such claim of Paulette Mendes-Silva shall be brought within six months after the date of the enactment of this Act. The court shall apply the laws of the District of Columbia in such case.

(b) Nothing in this section shall be construed as an inference of liability on the part of the United States.

SEC. 8. LIMITATIONS ON ALLOWABILITY OF COSTS INCURRED BY FEDERAL GOVERNMENT CONTRACTORS IN CERTAIN PROCEEDINGS.

(a) AMENDMENT TO THE FEDERAL PROPERTY AND ADMINISTRATIVE SERVICES ACT OF 1949.—(1) Title III of the Federal Property and Administrative Services Act of 1949 (41 U.S.C. 251 et seq.) is

amended by inserting after section 305 the following new section 306:

"LIMITATIONS ON ALLOWABILITY OF COSTS INCURRED BY CONTRACTORS IN CERTAIN PROCEEDINGS

"SEC. 306. (a) Except as otherwise provided in this section, costs incurred by a contractor in connection with any criminal, civil, or administrative proceeding commenced by the United States or a State are not allowable as reimbursable costs under a covered contract if the proceeding (1) relates to a violation of, or a failure to comply with, a Federal or State statute or regulation, and (2) results in a disposition described in subsection (b). 41 USC 256.

"(b) A disposition referred to in subsection (a)(2) is any of the following:

"(1) In the case of a criminal proceeding, a conviction (including a conviction pursuant to a plea of nolo contendere) by reason of the violation or failure referred to in subsection (a).

"(2) In the case of a civil or administrative proceeding involving an allegation of fraud or similar misconduct, a determination of contractor liability on the basis of the violation or failure referred to in subsection (a).

"(3) In the case of any civil or administrative proceeding, the imposition of a monetary penalty by reason of the violation or failure referred to in subsection (a).

"(4) A final decision by an appropriate official of an executive agency—

"(A) to debar or suspend the contractor;

"(B) to rescind or void the contract; or

"(C) to terminate the contract for default,

by reason of the violation or failure referred to in subsection (a).

"(5) A disposition of the proceeding by consent or compromise if such action could have resulted in a disposition described in paragraph (1), (2), (3), or (4).

"(c) In the case of a proceeding referred to in subsection (a) that is commenced by the United States and is resolved by consent or compromise pursuant to an agreement entered into by a contractor and the United States, the costs incurred by the contractor in connection with such proceeding that are otherwise not allowable as reimbursable costs under such subsection may be allowed to the extent specifically provided in such agreement.

"(d) In the case of a proceeding referred to in subsection (a) that is commenced by a State, the head of the executive agency that awarded the covered contract involved in the proceeding may allow the costs incurred by the contractor in connection with such proceeding as reimbursable costs if the agency head determines, under regulations prescribed by such agency head, that the costs were incurred as a result of (1) a specific term or condition of the contract, or (2) specific written instructions of the agency. Regulations.

"(e)(1) Except as provided in paragraph (3), costs incurred by a contractor in connection with a criminal, civil, or administrative proceeding commenced by the United States or a State in connection with a covered contract may be allowed as reimbursable costs under the contract if such costs are not disallowable under subsection (a), but only to the extent provided in paragraph (2).

"(2)(A) The amount of the costs allowable under paragraph (1) in any case may not exceed the amount equal to 80 percent of the

amount of the costs incurred, to the extent that such costs are determined to be otherwise allowable and allocable under the single Government-wide procurement regulation issued pursuant to section 4(4)(A) of the Office of Federal Procurement Policy Act (41 U.S.C. 403(4)(A)).

"(B) Regulations issued for the purpose of subparagraph (A) shall provide for appropriate consideration of the complexity of procurement litigation, generally accepted principles governing the award of legal fees in civil actions involving the United States as a party, and such other factors as may be appropriate.

"(3) In the case of a proceeding referred to in paragraph (1), contractor costs otherwise allowable as reimbursable costs under this subsection are not allowable if (A) such proceeding involves the same contractor misconduct alleged as the basis of another criminal, civil, or administrative proceeding, and (B) the costs of such other proceeding are not allowable under subsection (a).

"(f) As used in this section:

"(1) The term 'covered contract' means a contract for an amount more than $100,000 entered into by an executive agency other than a fixed-price contract without cost incentives.

"(2) The term 'proceeding' includes an investigation.

"(3) The term 'costs', with respect to a proceeding—

"(A) means all costs incurred by a contractor, whether before or after the commencement of such proceeding; and

"(B) includes—

"(i) administrative and clerical expenses;

"(ii) the cost of legal services, including legal services performed by an employee of the contractor;

"(iii) the cost of the services of accountants and consultants retained by the contractor; and

"(iv) the pay of directors, officers, and employees of the contractor for time devoted by such directors, officers, and employees to such proceeding.

"(4) The term 'penalty' does not include restitution, reimbursement, or compensatory damages.".

(2) The table of contents in the first section of such Act is amended by inserting after the item relating to section 305 the following new item:

"306. Limitation on allowability of costs incurred by contractors in certain proceedings.".

(b) AMENDMENTS TO TITLE 10.—Section 2324 of title 10, United States Code, is amended—

(1) in subsection (e)—

(A) by striking out subparagraph (N) and inserting in lieu thereof the following:

"(N) Costs incurred by a contractor in connection with any criminal, civil, or administrative proceeding commenced by the United States or a State, to the extent provided in subsection (k).";

(B) by striking out paragraph (2); and

(C) by redesignating paragraph (3) as paragraph (2); and

(2) by striking out subsection (k) and inserting in lieu thereof the following:

"(k)(1) Except as otherwise provided in this subsection, costs incurred by a contractor in connection with any criminal, civil, or administrative proceeding commenced by the United States or a

State are not allowable as reimbursable costs under a covered contract if the proceeding (A) relates to a violation of, or failure to comply with, a Federal or State statute or regulation, and (B) results in a disposition described in paragraph (2).

"(2) A disposition referred to in paragraph (1)(B) is any of the following:

"(A) In the case of a criminal proceeding, a conviction (including a conviction pursuant to a plea of nolo contendere) by reason of the violation or failure referred to in paragraph (1).

"(B) In the case of a civil or administrative proceeding involving an allegation of fraud or similar misconduct, a determination of contractor liability on the basis of the violation or failure referred to in paragraph (1).

"(C) In the case of any civil or administrative proceeding, the imposition of a monetary penalty by reason of the violation or failure referred to in paragraph (1).

"(D) A final decision by the Department of Defense—

"(i) to debar or suspend the contractor;

"(ii) to rescind or void the contract; or

"(iii) to terminate the contract for default;

by reason of the violation or failure referred to in paragraph (1).

"(E) A disposition of the proceeding by consent or compromise if such action could have resulted in a disposition described in subparagraph (A), (B), (C), or (D).

"(3) In the case of a proceeding referred to in paragraph (1) that is commenced by the United States and is resolved by consent or compromise pursuant to an agreement entered into by a contractor and the United States, the costs incurred by the contractor in connection with such proceeding that are otherwise not allowable as reimbursable costs under such paragraph may be allowed to the extent specifically provided in such agreement.

"(4) In the case of a proceeding referred to in paragraph (1) that is commenced by a State, the head of the agency that awarded the covered contract involved in the proceeding may allow the costs incurred by the contractor in connection with such proceeding as reimbursable costs if the agency head determines, under regulations prescribed by such agency head, that the costs were incurred as a result of (A) a specific term or condition of the contract, or (B) specific written instructions of the agency.

"(5)(A) Except as provided in subparagraph (C), costs incurred by a contractor in connection with a criminal, civil, or administrative proceeding commenced by the United States or a State in connection with a covered contract may be allowed as reimbursable costs under the contract if such costs are not disallowable under paragraph (1), but only to the extent provided in subparagraph (B).

"(B)(i) The amount of the costs allowable under subparagraph (A) in any case may not exceed the amount equal to 80 percent of the amount of the costs incurred, to the extent that such costs are determined to be otherwise allowable and allocable under the single Government-wide procurement regulation issued pursuant to section 4(4)(A) of the Office of Federal Procurement Policy Act (41 U.S.C. 403(4)(A)).

"(ii) Regulations issued for the purpose of clause (i) shall provide for appropriate consideration of the complexity of procurement litigation, generally accepted principles governing the award of legal fees in civil actions involving the United States as a party, and such other factors as may be appropriate.

"(C) In the case of a proceeding referred to in subparagraph (A), contractor costs otherwise allowable as reimbursable costs under this paragraph are not allowable if (i) such proceeding involves the same contractor misconduct alleged as the basis of another criminal, civil, or administrative proceeding, and (ii) the costs of such other proceeding are not allowable under paragraph (1).

"(l)(1) In this section, the term 'covered contract' means a contract for an amount more than $100,000 entered into by the Department of Defense other than a fixed-price contract without cost incentives.

"(2) In subsection (k):

"(A) The term 'proceeding' includes an investigation.

"(B) The term 'costs', with respect to a proceeding—

"(i) means all costs incurred by a contractor, whether before or after the commencement of any such proceeding; and

"(ii) includes—

"(I) administrative and clerical expenses;

"(II) the cost of legal services, including legal services performed by an employee of the contractor;

"(III) the cost of the services of accountants and consultants retained by the contractor; and

"(IV) the pay of directors, officers, and employees of the contractor for time devoted by such directors, officers, and employees to such proceeding.

"(C) The term 'penalty' does not include restitution, reimbursement, or compensatory damages.".

(c) TECHNICAL AMENDMENT.—Section 832(b) of the National Defense Authorization Act, Fiscal Year 1989 is repealed.

10 USC 2324 note.

(d) REGULATIONS.—The regulations necessary for the implementation of section 306(e) of the Federal Property and Administrative Services Act of 1949 (as added by subsection (a)) and section 2324(k)(5) of title 10, United States Code (as added by subsection (b))—

10 USC 2324 note.

(1) shall be prescribed not later than 120 days after the date of the enactment of this Act; and

(2) shall apply to contracts entered into more than 30 days after the date on which such regulations are issued.

10 USC 2324 note.

(e) EFFECTIVE DATE.—The amendments made by subsections (a) and (b) shall take effect with respect to contracts awarded after the date of the enactment of this Act.

SEC. 9. QUI TAM ACTIONS.

(a) AWARDS OF DAMAGES.—Section 3730(d) of title 31, United States Code, is amended—

(1) by redesignating paragraph (3) as paragraph (4); and

(2) by inserting after paragraph (2) the following new paragraph:

"(3) Whether or not the Government proceeds with the action, if the court finds that the action was brought by a person who planned and initiated the violation of section 3729 upon which the action was brought, then the court may, to the extent the court considers appropriate, reduce the share of the proceeds of the action which the person would otherwise receive under paragraph (1) or (2) of this subsection, taking into account the role of that person in advancing the case to litigation and any relevant circumstances pertaining to the violation. If the person bringing the action is convicted of criminal conduct arising from his or her role in the violation of

section 3729, that person shall be dismissed from the civil action and shall not receive any share of the proceeds of the action. Such dismissal shall not prejudice the right of the United States to continue the action, represented by the Department of Justice.".

(b) TECHNICAL AMENDMENTS.—Section 3730 of title 28, United States Code, is amended— 31 USC 3730.

(1) in subsection (c)(4) by inserting "the" after "Government proceeds with"; and

(2) in subsection (d)(4), as redesignated by subsection (a)(1) of this section, by striking out "actions" and inserting in lieu thereof "action".

Approved November 19, 1988.

LEGISLATIVE HISTORY—H.R. 3911:

HOUSE REPORTS: No. 100-610 (Comm. on the Judiciary).
SENATE REPORTS: No. 100-503 (Comm. on the Judiciary).
CONGRESSIONAL RECORD, Vol. 134 (1988):
May 10, considered and passed House.
Oct. 18, considered and passed Senate, amended.
Oct. 20, House concurred in Senate amendment.

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II

100TH CONGRESS
1ST SESSION

S. 1958

To establish regional government fraud law enforcement units for effective investigation and prosecution of fraud against the government.

IN THE SENATE OF THE UNITED STATES

DECEMBER 17 (legislative day, DECEMBER 15), 1987

Mr. PROXMIRE (for himself and Mr. GRASSLEY) introduced the following bill; which was read twice and referred to the Committee on the Judiciary

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A BILL

To establish regional government fraud law enforcement units for effective investigation and prosecution of fraud against the government.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled,

SECTION 1. SHORT TITLE.

This Act may be cited as the "Government Fraud Law Enforcement Act of 1987".

SEC. 2. FINDINGS AND PURPOSE.

(a) FINDINGS.—The congress finds that—

(1) fraud in government programs and procurements is a major and growing problem;

(2) false and fraudulent use of taxpayer funds generally permeates all government programs ranging from Medicare benefits to multibillion dollar defense procurements according to the United States Comptroller General;

(3) the Department of Justice has estimated fraud as draining up to 10 percent of the entire Federal budget;

(4) in addition to monetary loss, fraud erodes public confidence in the government's ability to efficiently and effectively manage its programs;

(5) with current annual Federal spending at approximately $1,000,000,000,000 and a national debt of 2½ times that amount, it is critical that the integrity of taxpayer dollars is ensured;

(6) prosecuting fraud against the Federal government is a core Federal function to be handled solely by the Department of Justice;

(7) with referrals of fraud and false claims allegations on the rise, it is necessary that the Department of Justice have an effective framework and adequate resources for investigation and prosecution of such cases;

(8) prosecuting fraud in government programs and procurement involves a specialized and complex area of law;

(9) because of its unique and complex nature, effective law enforcement against government fraud requires stable and identifiable resources;

(10) to provide maximum protection of taxpayer dollars, it is necessary that investigative and prosecutive resources be maximized across the country in regional units devoted solely to government fraud law enforcement; and

(11) effective government fraud law enforcement units must include coordinated teams of both criminal and civil attorneys.

(b) PURPOSE.—It is the purpose of this Act to ensure—

(1) the establishment of an effective and efficient structure for combatting fraudulent use of taxpayer dollars; and

(2) adequate resources to implement this effort.

SEC. 3. ESTABLISHMENT OF UNITS.

(a) ESTABLISHMENT OF UNITS.—There are hereby established within the Department of Justice no fewer than five government fraud investigative and prosecutive units to be located in regions around the country. These units shall be under the direction of the Assistant Attorney General for the

Criminal Division. The units shall be responsible for prosecuting cases under both the criminal and civil statutes. When necessary the Assistant Attorney General for the Criminal Division shall work in coordination with the Assistant Attorney General for the Civil Division.

(b) FUNCTION OF UNITS.—The primary function of the units shall be to investigate and prosecute fraud against the government.

(c) LOCATIONS.—The Attorney General shall determine the location of the five fraud investigative and prosecutive units not located in the Fraud Section. In making such determinations the Attorney General shall consider concentrations of government programs and procurements and concentrations of pending government fraud investigations and allegations.

SEC. 4. AUTHORIZATION OF APPROPRIATIONS.

(a) AUTHORIZATION.—Subject to the provisions of subsection (b), for the purpose of carrying out the purposes of this Act there are authorized to be appropriated $8,000,000 for fiscal year 1988, and such sums as may be necessary for each of the 4 succeeding fiscal years, to be available until expended.

(b) LIMITATION.—Before expending funds appropriated pursuant to subsection (a) to carry out the purposes of this

Act, the Attorney General shall utilize available existing resources within the Department of Justice for such purposes.

SEC. 5. CONGRESSIONAL OVERSIGHT.

Commencing with the first year after the date of enactment of this Act, the Attorney General shall annually report to the Congress with respect to—

(1) the number of referrals of fraud cases by the Department of Defense of Department of Defense contractors (with specific statistics with respect to the 100 largest contractors), the number of open investigations of such contractors, and a breakdown of to which United States Attorney's Office or other component of the Department of Justice each such case was referred;

(2) the number of referrals of fraud cases from other agencies or sources;

(3) the number of attorneys assigned to each unit established by this Act;

(4) the number of investigative agents assigned to each investigation in each unit and the period of time each investigation has been opened;

(5) the number of convictions and acquittals achieved by the units established by this Act; and

(6) the sentences, recoveries, and penalties achieved by the units established by this Act.

SEC. 6. EFFECTIVE DATE.

This Act shall take effect 90 days after the date of enactment of this Act.

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