

Congress of the United States
House of Representatives
Washington, D.C. 20515

December 18, 2003

Rear Admiral (ret.) David J. Nash
Director
Iraq Program Management Office
1401 Wilson Boulevard, Suite 502
Rosslyn, VA 22209

Dear Admiral Nash:

Recently, you announced that the newly established Program Management Office plans to award 26 cost-plus contracts for the reconstruction of Iraq by February 3, 2004. The source of the \$18.7 billion in funding for these contracts is the latest Iraq supplemental appropriation.

We are writing because the Administration's contracting approach is fundamentally flawed. Rather than creating opportunities for true price competition, the Administration intends to award individual contractors monopolies over different sectors of the Iraqi economy. Moreover, the Administration intends to award these monopolies without full and open competition, effectively limiting the opportunity to submit bids to a few hand-picked companies for each contract. Other problems are the decision to exclude companies from certain countries from the competition, the decision to continue to rely on abuse-prone cost-plus contracts, the decision to contract out the job of overseeing the contracts to yet additional contractors, and the inadequacy of Administration oversight of the contracts.

The end result is to stifle competition. The \$18.7 billion in the supplemental will finance approximately 2,000 discrete reconstruction projects. But under the Administration's approach, there is no opportunity for price competition at the all-important project level. Incredibly, the Administration will not solicit competing bids for even one of these 2,000 projects.

In the absence of price competition to discipline costs, the Administration says it will control costs through contract oversight. Yet the Program Management Office will have just 120 employees on the ground in Iraq to oversee \$18.7 billion in contracts. This is woefully inadequate. The Army Corps of Engineers, in contrast, has 30,000 employees to administer \$14 billion in projects. In effect, the Administration is giving contractors in Iraq a virtual blank check.

We urge you to reassess your contracting plan immediately. The goal should be to protect the American taxpayer and benefit the Iraqi people rather than reward favored government contractors with lucrative monopolies.

Perpetuating Monopolies

Today, the two largest Iraq reconstruction contracts are Halliburton's oil infrastructure contract, currently worth \$2.26 billion, and Bechtel's capital construction contract, valued at over \$1 billion.¹ These contracts essentially have created two massive fiefdoms: Halliburton has a monopoly on all oil work and Bechtel has a monopoly on the remaining construction and restoration work in a variety of sectors, such as electricity and public works. Whenever a new oil project is proposed, it is awarded to Halliburton without any price competition from any other company. And whenever a new public works project comes along, it's handed to Bechtel without any price competition with any other company. This absence of price competition leaves the taxpayer susceptible to vastly inflated costs.

There is no indication that the Administration intends to rethink this flawed approach. To the contrary, the Administration plans to create another 18 giant construction monopolies for different sectors of the Iraqi economy. Two monopolists will be replaced by 18 monopolists, several of whom will have contracts just as large as those of Halliburton and Bechtel. For example, the Administration intends to award four public works contracts — one each for the North, Central, South, and Baghdad regions.² Rather than having four companies compete for specific public works projects, each of the four companies will have a monopoly over all public works projects in their respective zones. Like Bechtel and Halliburton, several large corporations will receive massive contracts worth billions of dollars without ever having to demonstrate an ability to complete specific projects at lower cost than other companies. This may be a good arrangement for the contractors, but it's not a good deal for the taxpayers.

The new contracts will be Indefinite Delivery/Indefinite Quantity (IDIQ) type contracts, in which the total amount of work and specific projects to be completed are unknown at the time of the bid and award. When an IDIQ contract is put out to bid, there is no real opportunity for price competition because the projects under the contract have yet to be defined. For this reason, federal procurement rules say that IDIQ contracts should be awarded to multiple contractors, thereby enabling the federal agency to solicit competing bids from more than one contractor

¹ U.S. Army Corps of Engineers, *Frequently Asked Questions: Engineer Support to Operation Iraqi Freedom* (Dec. 15, 2003) (online at www.hq.usace.army.mil/CEPA/Iraq/March03-table.htm); U.S. Agency for International Development, *Contracts: Capital Construction* (Dec. 3, 2003) (online at www.usaid.gov/iraq/contracts/cc.html).

² Program Management Office, *Executive Summary of Draft Solicitations* (2003) (online at www.rebuilding-iraq.net).

when specific projects are delineated.³ The Administration is not following this sensible approach.

Instead, it is deliberately precluding meaningful price competition. By awarding each IDIQ contract to just a single contractor, it is in effect doling out monopolies. Taxpayers will pay a high price for this imprudent approach.

No Full and Open Competition

The Iraq supplemental appropriation passed Congress on November 3. It provides that the Administration should award contracts funded by the supplemental through full and open competition.⁴ Reflecting this requirement, the Administration has repeatedly promised that the new contracts will be awarded only after full and open competition. For example, you have presented the use of “contracting strategies that employ full and open competition” as a basic tenet of the Program Management Office.⁵ At a December 10 briefing, Deidre Lee, the Coalition Provisional Authority’s Deputy for Operations and manager of the new contracts, stated that among the contractors from eligible countries, “there will be full and open competition.”⁶

In fact, there will not be full and open competition for these new contracts. The Administration is using the term “advisory downselect” to mask the actual result of its contracting process: the limitation of the bidding on each contract to a few hand-picked companies.

³ 48 CFR 16.504(c) (“the contracting officer must, to the maximum extent practicable, give preference to making multiple awards of indefinite-quantity contracts under a single solicitation for the same or similar supplies or services to two or more sources”).

⁴ Section 2202, H.R. 3289, Emergency Supplemental Appropriations Act for Defense and for the Reconstruction of Iraq and Afghanistan, 2004 (“none of the funds appropriated by this Act under the heading ‘Iraq Relief and Reconstruction Fund’... may be used for entering into any Federal contract (including follow-on contract) using other than full and open competition, except in accordance with the Federal Property and Administrative Procedures Act”).

⁵ Adm. David J. Nash, Director of Program Management Office, *Address at Industry Day* (Nov. 19, 2003).

⁶ Deidre Lee, CPA Deputy for Operations in Washington, *Address at Iraq Reconstruction Contracts Briefing* (Dec. 10, 2003).

On November 19, you held an Industry Day in Washington, D.C., at which 1,400 contractor representatives gathered to hear about opportunities in Iraq. At that time, you indicated that contracts would be awarded according to the following process:

- First, potential contractors must submit “expressions of interest” by November 26.⁷
- Second, these potential contractors must submit additional preliminary information in late December describing their financial capability, technical approach, past performance, proposed subcontractors, and organizational structure.⁸
- Third, the Program Management Office will select a few finalists for each contract based on the information from the preliminary submission. This process is called an “advisory downselect.”⁹
- Fourth, the preselected finalists will be invited to submit formal bid proposals for consideration by the Program Management Office.¹⁰
- Fifth, the Program Management Office will award the contract to one of the companies that submits a formal bid proposal.

On December 17, the Coalition Provisional Authority briefed the staffs of the Committee on Government Reform. The CPA explained that any company would be permitted to submit a formal bid proposal, even if the company was not selected as a finalist. In CPA parlance, the “downselect” to finalists would be “advisory” rather than “mandatory.” However, in reality, contractors other than the preselected finalists will not have a viable prospect of obtaining a contract. In other words, although any firm may submit a bid on a contract, only the hand-picked finalists have any real chance of winning the competition.¹¹

This preselection process is not full and open competition. This point is expressly recognized in the draft solicitations, which state: “we anticipate restriction on competition.”¹²

⁷ Adm. David J. Nash, *supra* note 5.

⁸ Program Management Office, *CPA-PMO Amends Iraq Reconstruction, Design-Build Construction Request for Proposals* (2003) (online at www.rebuilding-iraq.net); Program Management Office, *Proposed Timelines for PM and Construction Acquisition Contracts* (2003) (online at www.rebuilding-iraq.net); Program Management Office, *supra* note 2.

⁹ Program Management Office, *supra* note 2; Adm. David J. Nash, *supra* note 5.

¹⁰ Adm. David J. Nash, *supra* note 5.

¹¹ Deidre Lee, CPA Deputy for Operations, Briefing to Committee on Government Reform staffs (Dec. 17, 2003).

¹² Program Management Office, *supra* note 2.

Recognizing this fact, the Administration cites the “public interest” exemption to full and open competition under the federal acquisition regulation to justify its plan to limit the submission of formal bid proposals to preselected contractors.¹³

The Administration is not being candid about its plans in its public statements. While senior officials state that the new contracts will be awarded after full and open competition, the details of the solicitation directly contradict these assertions.

Unsound Nationality Restrictions

Besides limiting competition to hand-picked companies, the Administration is also limiting the firms that can submit bids to contractors from the United States, Coalition countries, and Iraq. Deputy Secretary of Defense Paul Wolfowitz announced this limitation of competition in his December 5 “Determination and Findings,” stating: “It is necessary for the protection of the essential security interests of the United States to limit competition for the prime contracts of these procurements to companies from the United States, Iraq, Coalition partners and force contributing nations.”¹⁴

Beyond its foreign policy implications, the country restriction raises several issues. Many of the countries that are eligible to compete are countries like Ethiopia, Palau, and Mongolia. These countries do not have contractors that are capable of competing effectively for the new contracts. In contrast, many of the countries that are excluded, such as Canada, Germany, and France, do have contractors that could compete effectively for these contracts, with a lower cost to taxpayers.

The Administration’s list of eligible countries is also arbitrary. Turkish firms can compete even though Turkey refused to allow U.S. aircraft to use its airspace during the war and refused to permit the staging of U.S. ground forces on its soil. On the other hand, German companies cannot compete even though the German government permitted the United States to use air bases in Germany during the invasion. Similarly, Canada has pledged almost \$300 million to the humanitarian and reconstruction effort in Iraq and is sending police trainers to Jordan to help train Iraqi police officers, but Canadian companies are excluded. This line drawing just doesn’t make sense.

¹³ *Id.*

¹⁴ Paul Wolfowitz, Deputy Secretary of Defense, *Determination and Findings* (Dec. 5, 2003).

Reliance on Cost-Plus Contracts

The continued reliance on cost-plus type contracts is another invitation to abuse, especially in the absence of any competition at the project level. Under this type of contract, the government reimburses the contractor for its actual costs and then pays an additional fee. The fee can be fixed at a percentage of costs or at a specific dollar amount, as in the Bechtel contract, or it can vary as a percentage of costs based on the performance of the contractor, as in the Halliburton contract. In either case, there is little incentive for the contractor to keep costs down because costs are completely reimbursed. This is why cost-plus contracts are notoriously prone to abuse.

Halliburton's gasoline importation work under its oil infrastructure contract is a good example of how cost-plus contracts can lead to inflated costs. The cost-plus framework provided little incentive for Halliburton to locate a low-cost subcontractor to purchase gasoline in Kuwait and transport it into Iraq. The result is predictable and distressing. On December 11, the Defense Contract Audit Agency announced that Halliburton "has not demonstrated . . . that they did an adequate subcontract pricing evaluation prior to award of that particular order and as a result . . . potential overpricing could be as high as \$61 million through September 30th."¹⁵

Inadequate Oversight

Compounding these problems, the Administration will not have adequate staff in Iraq to oversee these massive contracts. The Program Management Office will have only between 110 and 120 employees on the ground in Iraq to oversee \$18.7 billion in contracts. By comparison, the Army Corps of Engineers has 30,000 employees to administer just \$14 billion in domestic and international projects.¹⁶

The Administration's response to this staffing shortage is to turn over much of the oversight of these contracts to private contractors. For each construction sector, such as electricity or oil, the Administration plans to select a private contractor to supervise and manage the construction contracts for that sector.¹⁷

This is a major mistake. Hiring yet more contractors is not the best way to protect the taxpayer from overcharging contractors. Instead, this essential oversight function should be performed by government officials, not private contractors.

¹⁵ U.S. Department of Defense, *Transcript of News Briefing* (Dec. 12, 2003).

¹⁶ Deidre Lee, *supra* note 11.

¹⁷ Program Management Office, *supra* note 2; Paul Wolfowitz, *supra* note 14.

Weak oversight would be problematic in the best of circumstances. When cost-plus contracts are awarded in the absence of full and open competition, the risks of waste, fraud, and abuse are magnified enormously.

A Better Approach

There is a straightforward alternative to the Administration's approach. There should be full and open competition without nationality restrictions. To foster competition for specific projects, the Program Management Office should award each of the IDIQ contracts to multiple qualified contractors. Then, for a specific project, the contracting agency should solicit bids and select the company that offers the best value for the specific restoration project. For example, if a power plant needs to be restored, the agency should solicit bids from the multiple companies that have been awarded electricity contracts and choose the best contractor for the power plant work. This approach would create genuine price competition. Instead of relying on a company's "past experience" or general capabilities in determining who should receive a given task, the contracting agency would be able to compare actual bids for the specific work to be done.

There is ample precedent for such an approach. Realizing the benefits of true price competition at the project level, federal agencies frequently have awarded IDIQ contracts to multiple contractors. Indeed, this is recommended in the federal acquisition regulation.¹⁸ As recently as October 24, the U.S. Army Corps of Engineers announced that up to ten contractors would be awarded the IDIQ contract for the design and construction of military facilities for the U.S. Central Command.¹⁹ The goal is to have contractors compete for the various task orders.²⁰

Conclusion

The Administration's approach is irresponsible. Companies will be granted massive monopolies without even having to go through full and open competition to obtain them. Numerous potential contractors will be excluded from what competition there is based on their nationality alone. There will be inadequate government oversight of these abuse-prone, cost-plus contracts. Without the discipline of either price competition or rigorous oversight, there is little to protect the taxpayer from inflated prices or poor performance.

¹⁸ 48 CFR 16.504(c).

¹⁹ U.S. Army Corps of Engineers, *Corps Plans Additional IDIQ Contracts for U.S. Central Command Area of Operations* (Oct. 24, 2003).

²⁰ Telephone conversation between Joan Kibler, U.S. Army Corps of Engineers, and Minority Staff, Government Reform Committee (Oct. 24, 2003).

Rear Admiral (ret.) David J. Nash
December 18, 2003
Page 8

We urge you to reconsider the Administration's approach. As the recent disclosures about the Halliburton contract have revealed, there are serious flaws in the Administration's plans for Iraq reconstruction. The goal should be to foster — not suppress — competition among qualified contractors, especially at the crucial project level. The best way to ensure that U.S. taxpayers get their money's worth is with true price competition.



Henry A. Waxman
Ranking Minority Member
Committee on Government Reform

Sincerely,



John D. Dingell
Ranking Minority Member
Committee on Energy and Commerce