Statement of Mr. William H. Reed
Director, Defense Contract Audit Agency
House Committee on Oversight and Government Reform
February 7, 2007

Mr. Chairman, members of the Committee, my statement for this hearing will center on the Defense Contract Audit Agency's (DCAA) oversight of contract costs related to military operations and reconstruction in Iraq.

DoD Contract Performance Oversight Responsibility

DCAA has been an integral part of the oversight and management controls instituted by DoD to ensure integrity and regulatory compliance by contractors performing services in Iraq. DCAA's services include audits and professional advice to acquisition officials on accounting and financial matters to assist them in the negotiation, award, administration, and settlement of contracts. Decision-making authority on DCAA recommendations resides with contracting officers within the procurement organizations who work closely with DCAA throughout the contracting process.

DCAA Staffing and Actions

Since April 2003, DCAA has worked with all U.S. procurement organizations supporting Iraq Reconstruction to establish the resources and planning information needed to carry out required audits of contract costs as they are incurred and billed. These organizations include the Joint Contracting Command – Iraq/Afghanistan, the Army Sustainment Command, the U.S. Army Corps of Engineers, the Defense Contact Management Agency in Iraq and Kuwait, USAID, and the State Department. This coordination has enabled DCAA to maintain an inventory of Iraq-related auditable contracts.

Based on the inventory of auditable contracts as of September 30, 2006, DCAA is responsible for auditing Iraq-related contracts at 93 contractors. These contractors hold more than 175 prime contracts with contract ceiling amounts of $51.8 billion, of which $38.5 billion had been funded at the end of FY 2006. DCAA audits of cost-reimbursable contracts represent a continuous effort from evaluation of proposed prices to final closeout and payment. Initial audits of contractor business system internal controls and preliminary testing of contract costs are carried out to provide a basis for provisional approval of contractor interim payments and early detection of deficiencies. Comprehensive contract cost audits are performed annually throughout the life of the contract and are used by the contracting activity to adjust provisionally approved interim payments and ultimately to negotiate final payment to the contractor.

To carry out these extensive audit requirements, DCAA opened an Iraq Branch Office in May 2003 and implemented planning and coordination procedures to effectively integrate audit work between that office and more than 50 DCAA CONUS Audit Offices with cognizance of companies performing contracts in Iraq.

Results of Audits

Through FY 2006 DCAA has issued more than 1,800 reports on Iraq-related contracts. We estimate issuing another 600 reports in FY 2007. DCAA oversight of contracts in Iraq has found a number of problems. Our resulting action has ranged from recommending changes in business processes – to reduction of proposed or billed costs – to referral of our findings to the Inspector General for investigation and possible legal action against a contractor.

Reliability of business systems affecting contract costs – The most frequent problems disclosed during our audits of business systems involved timekeeping

procedures, cash management procedures, management of subcontracts, or documentation of costs on proposals. The majority of these problems have already been resolved or are actively being worked by contractors and contracting officers. Where appropriate, reductions to billed costs have been taken to avoid potential inaccurate payments until process deficiencies are corrected.

Reductions of proposed and billed costs – Through FY 2006 DCAA has recommended reductions in proposed and billed contract costs of $4.9 billion. Where appropriate, DCAA has taken action to reduce contractor billed costs for disputed amounts pending a contracting officer decision. In addition, DCAA has identified $5.1 billion of estimated costs where the contractor did not provide sufficient information to explain the basis for the estimated amounts. These unsupported costs were usually resolved through contractor submission of additional supporting information at the time of contract price negotiation.

Closing

In closing, I want to underscore that DCAA has worked closely with all acquisition organizations to insure an integrated, well-managed contract audit process in Iraq. We have had a continuous presence in Iraq and the Middle East Theatre of Operations since May 2003, staffing our office entirely with civilian volunteers. To date more than 180 DCAA auditors have served tours and fortunately, none have been injured or killed. The challenges in applying business practices and auditing in Iraq are daunting and have required our auditors to be flexible while insisting that the Department will not tolerate the billing of costs that do not comply with contract terms or are not appropriately documented and supported. DCAA has been and will continue to be vigilant about contract audit oversight and protecting the taxpayers' interests.

I look forward to addressing whatever questions or comments you have on DCAA's important role in Iraq. Thank you.