HUD CONTRACTING: VULNERABILITIES AND PROPOSED SOLUTIONS

HEARING

BEFORE THE

SUBCOMMITTEE ON HUMAN RESOURCES

OF THE

COMMITTEE ON GOVERNMENT REFORM AND OVERSIGHT

HOUSE OF REPRESENTATIVES

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HUD CONTRACTING: VULNERABILITIES AND PROPOSED SOLUTIONS

FRIDAY, JUNE 5, 1998

HOUSE OF REPRESENTATIVES,
SUBCOMMITTEE ON HUMAN RESOURCES,
COMMITTEE ON GOVERNMENT REFORM AND OVERSIGHT,
Washington, DC.

The subcommittee met, pursuant to notice, at 10:05 a.m., in room 2203, Rayburn House Office Building, Hon. Christopher Shays (chairman of the subcommittee) presiding.

Present: Representatives Shays, Towns, and Kucinich.

Staff present: Lawrence J. Halloran, staff director and counsel; Samantha Sherman, professional staff member; Jesse S. Bushman, clerk; and Cherri Branson, minority counsel.

Mr. SHAYS. I will call this hearing to order; welcome our witnesses and welcome our guests.

Each year the Department of Housing and Urban Development [HUD], enters into contracts totalling more than half a billion dollars. Through thousands of complex agreements, HUD procures a broad array of goods and services from the state-of-the-art software to old-fashioned locks and hardware. Unquestionably, in pursuing its mission to improve housing opportunity and build communities, HUD believes contracting to be a critical tool.

But others have been very critical of HUD's contracting. The General Accounting Office [GAO], last year said HUD poses a, "high risk," and abuse, in part due to lax contracting practices. The National Academy of Public Administration [NAPA], found significant weakness in procurement practices at the Federal Housing Administration [FHA], a part of HUD. Last September the HUD inspector general [IG], issued a detailed audit report concluding the Department's inattention to contract management had, in many instances, "resulted in effective and extremely costly contracts."

These independent analyses raise serious questions about the Department's capacity to anticipate, negotiate, or monitor such a diverse and costly contract portfolio. We address those questions and HUD's answers today.

Conceding the scope and gravity of the problem, HUD declared contracting a material weakness, under the Federal Managers Financial Integrity Act, and committed to systematic procurement reforms. The Secretary recently appointed HUD's first chief procurement officer.

These and other steps are a good beginning, but today we seek to be sure they are the start of a sustained effort to confront the

bureaucratic culture and cronyism some believe lie at the heart of HUD's longstanding contract woes.

On this, the IG, GAO, and the Department appear to agree: The success of the HUD 2020 Management Reform Plan depends heavily on types and volumes of contracting not now possible at HUD. It will place growing demands on the very elements of contracting capacity the IG found so lacking: accurate needs assessment, strong negotiating positions, cost consciousness, and vigilant contract oversight.

We asked witnesses today to describe the full extent of HUD's contracting vulnerabilities and to help us measure the potential of planned reforms to correct these deficiencies. We appreciate their willingness to be a part of our oversight work, and we welcome their testimony.

At this time I recognize the gentleman from Ohio, Mr. Kucinich.

Mr. KUCINICH. Thank you very much, Mr. Chairman. In my years of experience in government, mainly local government, what I found is that every time government gets involved in contracting-out services, it generally loses control.

It's just a matter of fact. That's the way it works, and the problem is that government in this current climate—there's such great pressure for government to contract out services. It's almost become a religion, privatizing services, contracting out, and as a result the taxpayers aren't really getting the benefit of their tax dollars.

I am glad you're having this hearing, Mr. Chairman, to look at the effects of contracting-out procedures, to see if there's been any improvements, but frankly, I am skeptical about this whole theory that says that the private sector ought to be performing jobs and duties that are more rightly—should be under the control and province of government employments.

And so while we are looking at this and hearing these reports, I want to say I'm skeptical about everything you represent when you're involved in this contracting-out practice, and so—and again, I say this from years of experience at a local level where we found tremendous amounts of waste and inefficiency because government lost the ability to control various functions through contracting them out.

And when I see telephone inquiries being handled by—or being contracted out—the simple responses that people want from government—no wonder people think government doesn't work because they're not dealing with the government half the time. They're dealing with agents of the government who have the mantle of the government but not the accountability.

So this is a good hearing. It's important, Mr. Chairman. Thank you very much for holding it. I am looking forward to it.

Mr. SHAYS. I thank the gentleman, and I look forward to the hearing and considering all aspects of the issue. If I could, I'd like to just deal with two requirements that we have as a committee—to ask unanimous consent that all members of the subcommittee be permitted to place any opening statement in the record and that the record remain open for 3 days for that purpose. Without objection, so ordered.

I ask for unanimous consent that all witnesses be permitted to include their written statements in the record, and without objection, so ordered.

At this time we will hear from our first panel: Susan Gaffney, Inspector General, Department of Housing and Urban Development; accompanied by Edward Momorella, District Inspector General for Audit, Mid-Atlantic District; and also Stanley Czerwinksi, Associate Director, Housing and Community Development Issues, U.S. General Accounting Office, accompanied by Rick Hale, Assistant Director, Housing and Community Development Issues.

We welcome them to come and ask them to remain standing so I can swear them in. Let me just say I think we're having two presentations and then the others who accompanied will be responding to questions. It would be helpful, if there's anyone else that may be responding to questions, if they would stand and be sworn in at that same time.

[Witnesses sworn.]

Mr. SHAYS. For the record, all four of our witnesses have responded in the affirmative, and we appreciate that.

My daughter is going to her senior prom this evening, so I am going to be very punctual. [Laughter.]

Ms. Gaffney.

STATEMENTS OF SUSAN GAFFNEY, INSPECTOR GENERAL, DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT, ACCOMPANIED BY EDWARD F. MOMORELLA, DISTRICT INSPECTOR GENERAL FOR AUDIT, MID-ATLANTIC, 3 AGA; STANLEY J. CZERWINKSI, ASSOCIATE DIRECTOR, HOUSING AND COMMUNITY DEVELOPMENT ISSUES, U.S. GENERAL ACCOUNTING OFFICE; AND RICK HALE, ASSISTANT DIRECTOR, HOUSING AND COMMUNITY DEVELOPMENT ISSUES

Ms. GAFFNEY. Thank you, Mr. Chairman. As you know, last year we did a comprehensive review of HUD contracting. That review was led by Mr. Momorella. So he knows the ins and outs of all of this.

Our first briefing for the HUD senior principal staff on our work was just about a year ago, and HUD is now making plans to correct the weaknesses. HUD is notoriously good at making plans and notoriously bad at implementing corrective action plans.

I am hopeful that this will be a different circumstance for one principal reason, and that is that HUD has hired a chief procurement officer who has 34 years of experience. He knows the business. He believes in doing the business right, and I've been quite concerned about what his authority would be in the agency, and just yesterday—perhaps related to this hearing—that was resolved.

The deputy secretary has said that he will report directly to the secretary and the deputy secretary. The contracting office will report to him. Those are all very good signs, but, Mr. Kucinich, to go to your point, this is not going to be an easy task because HUD has a tradition, has a culture that used contracting as almost an easy thing to do.

HUD often contracts from weakness. If we don't have the expertise, we think, well, we'll just go out and buy it, but if you don't have the expertise, that means you can't define precisely what you

need or want, and it means you can't oversee what you're getting. So the balance of power shifts to the contractor almost inevitably.

So what Mr. Carberry, the new chief procurement officer, is going to have to do is much more than fix individual processes in HUD. He is going to have to change the culture and attitude of HUD employees, and we are going to stay on top of this and make sure that that happens because, as you have indicated, there is an enormous amount of money involved here, and it's getting bigger and bigger and bigger, and I don't see any way that that won't happen.

Just one concern about the plans that HUD has: They're quite good, these plans, except in one area. HUD has also appointed a chief information officer, but her duties and responsibilities have not yet been defined because the biggest of HUD's contracting is in the area of information technology. This is really a critical issue. If she is subordinate to the program assistant secretaries, she will not be able to turn that area of contracting, so that's my one major concern about the plan at this time.

Thank you.

[The prepared statement of Ms. Gaffney follows:]

STATEMENT OF
SUSAN GAFFNEY, INSPECTOR GENERAL
BEFORE THE
SUBCOMMITTEE ON HUMAN RESOURCES
COMMITTEE ON GOVERNMENT REFORM AND OVERSIGHT
HOUSE OF REPRESENTATIVES

JUNE 5, 1998

HUD CONTRACTING: VULNERABILITIES AND PROPOSED SOLUTIONS

Chairman Shays and Members of the Subcommittee, I appreciate the opportunity to testify, along with Edward Momorella, about HUD contracting issues. Mr. Momorella, the OIG's District Inspector General for Audit in Philadelphia, directed the nationwide audit that resulted in the Office of Inspector General's (OIG's) September 30, 1997 report titled "HUD Contracting."

Our testimony today will review i) the principal findings of the OIG's September 30, 1997 audit report; ii) HUD's reactions to the audit report; iii) current efforts to improve HUD contracting, as the OIG understands them; and iv) the importance of efficient and effective contracting to HUD's 2020 Management Reform Plan.

The OIG's September 30, 1997 Audit Report on HUD Contracting

By letter dated November 14, 1996, Senator Bond, Chairman of the Subcommittee on VA/HUD Appropriations, and Senator Faircloth, Chairman of the Subcommittee on HUD Oversight and Structure, asked the OIG to comprehensively review HUD's use of its contracting authority. Their request was based on concern, as HUD downsizes, about the risks associated with HUD's reliance on contracting its responsibilities.

In response to the Senators' request, between February 1997 and June 1997 Mr. Momorella directed a team of 26 auditors in reviewing HUD contract activity from 1992 through 1996. During this period, HUD awarded about 9,600 contracts worth over $3.2 billion. The OIG team examined in detail 63 contracts worth $1.5 billion held by 30 contractors. In the process of the audit, the team interviewed more than 225 persons, including HUD managers, Contract Specialists, Government Technical Representatives and Monitors, contractors and unsuccessful bidders.

Our selection of the contractors and contracts for detailed review was judgmental--we wanted to provide broad coverage of HUD programs and services and to focus on areas of greatest vulnerability. This targeted focus notwithstanding, it is significant that the auditors found problems in virtually every contract they reviewed.

The September 30, 1997 audit report identifies seven major categories of problems in HUD contracting:

1. Need Determination, Planning, and Periodic Assessments. A lack of adequate planning, needs assessment, good initial estimates, monitoring, and control of performance and cost expenditures on several multimillion dollar contracts has made HUD vulnerable to waste and abuse.

   While initial need determinations were documented for most contracts, OIG auditors found little in the way of periodic reevaluations to assure the contract was still beneficial to the Department and worth the cost. Many contracts were extended longer than anticipated and more costly than originally estimated. In some instances, products or studies took so long to complete that the results were no longer useful to HUD because of changing program priorities.

2. Cost Consciousness. HUD often contracted for a desired outcome without specifically knowing what tasks to request to achieve the outcome. While this may be a time saving process to award the contract, it often is the most costly, as HUD was unable to prepare good cost estimates on the tasks needed to accomplish the end product. As a result, the contractors had a clear advantage, as HUD was not in a position to reject costly modifications or time extensions, at the risk of having to start all over again.

   By paying closer attention to negotiating contract terms, contract types, and overhead rates, HUD could save millions of dollars, especially in the area of information technology and consulting contracts. Management's contracting environment needs to change to seek ways to emphasize cost consciousness and assure the best value for dollars spent. Because HUD managers did not have the staff to complete the product or service in house, the question of "What will it cost?" was often not seen as an issue.

   Current contract costs could be significantly reduced by providing better government estimates and allowing more competition. Indefinite Quantity Contracts (IQCs) gave HUD the flexibility of quicker and easier procurement, but often cost more because no competition was required for individual task orders. Without well defined task orders, HUD often had no idea what the final cost would be for these services.

3. Contract Oversight and Monitoring. OIG auditors found contract monitoring very lax throughout HUD programs. In some cases, HUD had contractors monitoring contractors. Many Government Technical Representatives (GTRs) and Monitors (GTMS) had a poor understanding of their respective roles and responsibilities. Indeed, training was not a prerequisite to being assigned as a GTR or GTM.

   In several instances, the current GTRs were not involved in the original award or even knowledgeable about the purpose or usefulness of the contracts. Where top level managers were assigned as GTRs, often they were too busy addressing other organizational and program crises to pay much attention to contract management. Where mid and lower level staff were assigned as GTRs and GTMs, most regarded their contracting roles as ancillary to their positions--something to do only if they had the time. In fact, contract management was not one of the performance elements they were rated on.

4. Contracting for Prohibited Services. OIG auditors found several instances where HUD has contracted for services that appear to be prohibited under the Federal Acquisition Regulations and HUD's Procurement Policies and Procedures. These prohibited services included personal services contracts, advisory and assistance services contracts to aid legislative initiatives, and contracts to perform inherently governmental functions.

5. Data and Financial Systems. Until early 1997, the Office of Procurement and Contracts (OPC) had maintained a data system to keep track of contracts awarded at headquarters; field offices had maintained separate systems to keep track of their contract awards. OIG auditors found numerous data errors and omissions in the OPC system, and concluded that it was not reliable for comprehensive contract management.

   In early 1997, HUD combined the OPC and field office systems into one system, the HUD Procurement System (HPS). While this goes a long way in improving OPC coordination and standardization between Headquarters and the field, HPS still lacked integration with the financial systems in HUD's Office of Finance and Accounting. This integration is essential so that GTRs can readily determine exactly what has been paid or drawn per contract per task order.

6. Contract Close-out Procedures. Approximately 50 percent of the contracts awarded by HUD are cost plus

contracts. Under this type of contract, one of the critical steps for the Department is the final or close-out audit. This is the Department's assurance that the contractor charges only costs directly related to the contract and that applicable overhead rates and other fees are appropriate. OIG auditors found a high number of cost plus contracts that had been completed, for which close-out audits had not been performed or requested.

7. Interagency Agreements. The Department paid other Federal Agencies over $263 million for services provided under numerous interagency agreements. In some instances, these agreements go back many years, and current GTRs could not explain certain provisions of the agreements, or what cost methodology was used to determine reimbursable amounts.

The September 30, 1997 audit report illustrates each of these problems in terms of specific HUD contracts.

While the OIG audit was in process, the Department contracted with the National Academy of Public Administration (NAPA) for a review of contracting by the Federal Housing Administration (FHA). The initial NAPA review, issued in May of 1997, concluded that FHA's contracting system neither responded effectively to Department needs nor adequately ensured accountability. The Congress then directed HUD to contract with NAPA for, among other things, a top-to-bottom redesign of the HUD procurement system.

The first deliverable under the expanded NAPA contract was a February 1998 Interim Report, which focuses on improvements needed in FHA/Office of Housing contracting and makes recommendations on how to bring about those improvements. NAPA's Interim Report reiterates the findings of the OIG's September 30, 1997 Audit Report, as well as the findings of NAPA's initial review of FHA contracting. It concludes that:

- Housing/FHA cannot accomplish its critical work with the current [contracting] system.
- "Fixing" specific steps in [the contracting] process will not be sufficient to address [the] complex, interdependent challenges of: ensuring accountability and integrity; effective risk management; and effective contract administration.
- Housing/FHA is unlikely to implement these [NAPA's] recommendations without a clear mandate and accountability.

HUD's Reactions to the OIG Audit Report

The audit report was issued in draft to HUD's former Deputy Secretary on August 7, 1997. The former Deputy Secretary responded on September 8, 1997 with a two-part message. First, the former Deputy Secretary said that the OIG draft report validated the conclusions reached by NAPA in its initial review of FHA contracting, and the OIG recommendations would be provided to NAPA for consideration as part of the contract system redesign. Second, the former Deputy Secretary said that the OIG draft report was "flawed in its methodology, [contained] factual inaccuracies, and [was] unbalanced in its characterization of specific contract actions," and therefore inconsistent with Generally Accepted Government Auditing Standards. The Deputy Secretary's response is Appendix A of our September 30, 1997 audit report.

When the audit report was issued in final on September 30, 1997, the OIG requested--within 60 days--a status report on each recommendation in the report, indicating i) the corrective action taken; ii) any proposed corrective action and the date to be completed; or iii) why action is not considered necessary.

The Department's response came 160 days later, on March 10, 1998. The response promised immediate institution of the following procurement reforms: establishment of a Chief Procurement Official (CPO); mandatory training and certification for GTRs/GTMs; inclusion of contracting rating elements in the performance plans for GTRs/GTMs; Office of General Counsel participation in certain procurements; and improvements in HPS. The response also reported that the Office of Procurement and Contracting had made substantial progress in requesting overdue close-out audits, and had also taken measures to prevent future backlogs in this area.

Notably, the Department's response disagreed with the OIG's assessment that certain HUD contracts were prohibited under the Federal Acquisition Regulations, but failed to provide any basis for this disagreement. Further, despite the delay in responding to the audit, the Department reported no action on the OIG's recommendation that the Department i) review problems identified by the OIG with regard to specific contracts and interagency agreements; then ii) determine what steps are necessary to protect the Department's interest; and iii) where necessary, either amend or terminate contracts/agreements not providing a necessary service or cost efficient results. The response was simply that the Chief Procurement Officer, when hired, would be tasked with reviewing these matters.

In summary, the Department has committed itself to prospective corrective actions, but has not embraced the opportunity to right past wrongs and exact accountability for them.

Current Efforts to Improve HUD Contracting

Most importantly, HUD has hired Steve Carberry, a highly experienced contracting professional, as Chief Procurement Officer. Today, you will undoubtedly hear about Mr. Carberry's plans for/progress in establishing a Contract Management Review Board; establishing a cadre of full-time GTRs and GTMs; instituting GTR/GTM training; placing procurement rating elements in GTR/GTM performance plans; and establishing meaningful performance measures for a reformed HUD procurement system. This is all good news.

The not-so-good news is that there has been no official definition of Mr. Carberry's authorities, responsibilities, or placement in the organization. This is a critically important matter: reforming HUD contracting is going to require, among other things, a change in the HUD culture, and the CPO is not going to be in a position to force that change if he is understood to be in a subordinate position vis a vis the program Assistant Secretaries.

Similarly, Mr. Carberry briefed the HUD Management Committee this week on his plans and progress, but we have seen no written definition of these efforts. This is not just a matter of being bureaucratic: the OIG would like to see the proposals laid out so that we could offer our advice and counsel up-front, rather than our criticism after the fact.

In the same vein, we applaud the Department for meeting its obligation to appoint a Chief Information Officer (CIO). This position is critically important to the reform of HUD contracting, since information technology contracts represent the highest dollar amount of contracting in HUD. Again, Gloria Parker, the new CIO, has superb credentials for this position. But, as yet, there has been no official definition of Ms. Parker's authorities, responsibilities, or placement in the organization.

The Importance of Efficient and Effective Contracting to HUD's 2020 Management Reform

As noted above, HUD has historically done a substantial amount of contracting: 9,600 contracts worth over $3.2 billion were awarded from 1992 through 1996. Under the Secretary's 2020 Management Reform plan, HUD staff has been downsized while ambitious new performance goals have been set throughout the Department. Attaining the new performance goals will be heavily

dependent on additional procurements for services such as single family property disposition, physical inspections of multifamily and public housing, Section 8 contract administration, and definition of a resource estimation system for HUD. The OIG estimates that these additional contracts could easily involve more than a billion dollars a year.

It is unfortunate that HUD staff was downsized and plans were developed for additional contracting without a cost benefit analysis. At this point, however, that is water under the bridge. The key point is that an efficient and effective procurement and contracting system is absolutely critical to HUD's meeting its HUD 2020 Management Reform goals. To illustrate this point:

- A major objective of HUD 2020 is to integrate HUD's financial systems. In the information technology area, HUD's reliance on contractors is virtually total.
- Another major objective of HUD 2020 is to ensure that the multifamily and public housing programs in fact provide decent, safe, and sanitary housing. This objective is heavily dependent on a new HUD physical inspection program to be carried out by contractors.
- In the single family area, HUD 2020 aims to improve the property disposition function by contracting it out. Single family staffing has already been reduced accordingly.
- HUD has contracted with NAPA to devise a resource estimation system for the Department. This is intended to correct HUD's material weakness in the area of staffing and administrative resource management.
- HUD 2020 further intends to better assure the accuracy of project-based Section 8 payments by using contractors rather than HUD staff to administer this payment function.

Mr. Chairman and Members of the Subcommittee, that concludes our testimony. We thank you for holding this important hearing, and giving us the opportunity to testify.

Mr. SHAYS. Thank you. Should we go to the GAO or does Mr. Momorella have some comments that he would like to make? OK, so we'll just let you jump in on the questions and feel free to elaborate on your answers as well. Thank you for your statement, Ms. Gaffney.

Mr. Czerwinski.

Mr. CZERWINSKI. Mr. Chairman, Mr. Kucinich, first of all, thank you for getting my name right. I mean it's probably the toughest thing we'll get today.

Mr. SHAYS. You have said one of the nicest things to me that anyone has ever said. I always mess up names. If I got your name right, it was a total accident. [Laughter.]

Mr. CZERWINSKI. And Mr. Kucinich, it's a pleasure having you because somebody has a name more difficult than mine.

Mr. SHAYS. Is it "Koocinich" or "Kucinich?" I call him "Kucinich?"

Mr. KUCINICH. Don't call me late for breakfast.

Mr. SHAYS. OK. Thank you. Nice to have you here.

Mr. CZERWINSKI. Thank you. We're pleased to be here to discuss issues related to HUD's contracting, and today I would like to talk about three basic issues. The first one is HUD's overall reliance on contractors. The second is weakness that we, the HUD inspector general and the National Academy of Public Administration have identified in that contracting. And third, I'd like to talk a little bit about HUD's plans to address those weaknesses.

To elaborate further on each of those points, even as HUD downsizes, its contracting obligations continue to grow steadily. According to HUD's own data, annual contract obligations in headquarters have grown from $213 million in 1991 to $376 million in 1996. And 1996 is the most recent year for which HUD has data. This is going to be a theme that I will be addressing later on, and that is the amount of information available to HUD as they try to manage contracts. And this is particularly important, because HUD's plan is to continually rely on contracting in the foreseeable future.

To illustrate the kind of weaknesses that we identified in HUD's contracting, I'd like to highlight a report that we issued earlier this spring. Our report focused on the oversight of real estate asset management contractors or REAMs. HUD has an average inventory of about 30,000 properties, and this makes them the largest real estate manager, with the biggest portfolio in the country. The REAMs are responsible for managing this inventory.

REAMs are supposed to be overseen by HUD's field offices. Now I want to tell you a little bit about what we found about oversight. The first point that we found is that the field offices don't always evaluate how well REAMs are doing.

For example, we found that one field office had only reviewed the REAMs contract one time since 1995, and specifically that office went out in 1996 and evaluated the REAM contractor and found, among other things, that the contractor had failed to remove debris from some properties; but in this case, even though HUD's field office found this problem, they didn't tell the REAM what it found.

So we went back and looked at some of the properties a year after HUD did its review and found, not surprisingly, debris at a lot of properties. And just to illustrate, there's a photo that we took

at one of the properties, and you can see off to your left. That property that was showing there, realtors had been showing that property just like that, and I can't imagine too many people wanting to buy that property. In fact, one of the realtors mentioned that the entrance to the property was blocked with furniture and debris.

So that was the first point that, when evaluations are made, they're not really telling the contractor what's coming out. Also, we found that when they're doing evaluations, HUD field offices often aren't visiting the properties. This photo represents a case where this property they did visit, but in a lot of cases they weren't. For example, 1 field office, we evaluated 42 properties, found that HUD hadn't done onsite inspections of any of them, and as a result of this, the properties were in a certain physical condition, but the REAM contractor was able to tell HUD that things were fine. For example—and we didn't show you this picture just out of sensibility—we went to one property and found animal feces, fur, and personal possessions. However, the contractor had told HUD that that property had been cleaned out. Of course it hadn't.

Furthermore, we visited properties and found health and safety hazards, warranting immediate repair by the contractor. And we have another photo there of a property, 3 months after HUD learned that the front steps were dangerous and needed immediate attention. Yet, as the photo shows, in those 3 months that deficiency had not been corrected.

It gives you a little bit of the flavor of the kinds of deficiencies that we are finding in the REAM's contract. That's just one illustration of the contracting problems. Overall, we, the inspector general, and the National Academy of Public Administration, have identified numerous weaknesses in contract. And I'll just give you a couple for an example: procurement systems that contain inaccurate information, inadequate oversight of contractor performance—I've sort of given you some examples of that today—and staff who have poor understanding of their contract management roles and responsibilities.

To their credit, HUD has recognized the need to improve its contracting process, is beginning to take action to address the problems which we, the IG and NAPA, have identified. I'll just give a few examples. I am sure Mr. Carberry will go into these in more detail during his statement of the kind of things that HUD is talking about.

In its self-assessment under the Financial Integrity Act, HUD itself cited contracting as a material weakness. The 2020 plan that HUD has put together includes efforts to redesign contracting procurement processes. HUD has appointed a chief procurement officer; they've established a Contract Review Board, and finally, addressing REAM's contracts themselves, HUD has modified its requirements so that the field offices will now be required to submit routine reports on the performance of the contractors.

We view HUD's actions as positive steps, but obviously key questions remain, and as I mentioned, information is a key word that we had focused on. Another would be implementation. I think HUD's ideas are good, but I think you really have to focus on the follow-through, and just a couple of thoughts to help guide that: first, the question of whether HUD will have the resources it needs

to effectively carry out some of the plans that it has; and also, just spelling out the specifics of some of its ideas. For example, what would the role of the Contractor Review Board be?

I just wanted to throw a couple of those ideas out. That concludes my statement, Mr. Chairman. We'd be pleased to answer any questions that you may have for us.

[The prepared statement of Mr. Czerwinski follows:]

Mr. Chairman and Members of the Subcommittee:

We are pleased to be here today to discuss issues related to contracting activities at the Department of Housing and Urban Development (HUD). Each year, the Department purchases millions of dollars worth of supplies and services through contracts. However, HUD's downsizing plans and allegations of contracting abuses have raised concerns about the Department's ability to effectively manage its contracting workload. Our statement today will discuss (1) the extent of HUD's reliance on contractors to carry out the Department's responsibilities; (2) the weaknesses in HUD's current contracting practices, particularly with respect to the oversight of property management contractors; and (3) HUD's actions to address its contracting weaknesses. This statement is based on reports that we issued regarding HUD's contracting activities, oversight of property management contracts, and 2020 Management Reform Plan[1] and reports issued by HUD's Office of Inspector General and the National Academy of Public Administration.

In summary, we found the following:

- HUD's annual obligations for headquarters contracts have steadily increased in recent years, growing from $213 million in fiscal year 1991 to $376 million in fiscal year 1996 (in constant 1996 dollars), according to HUD's data systems. Furthermore, the Department will continue to rely heavily on contractors to help carry out its responsibilities under its 2020 Management Reform Plan. For instance, the plan calls for HUD to contract with private firms for a number of functions, including physical building inspections of public housing and multifamily insured projects; legal, investigative, audit, and engineering services; and activities to clean up the backlog of troubled assisted multifamily properties.

[1]Procurement: Overview of HUD's Contracting Activities (GAO/RCED-97-132R, May 9, 1997), Single-Family Housing: Improvements Needed in HUD's Oversight of Property Management Contractors (GAO/RCED-98-65, Mar. 27, 1998), and HUD Management: Information on HUD's 2020 Management Reform Plan (GAO/RCED-98-86, Mar. 20, 1998).

- We, HUD's Inspector General, and the National Academy of Public Administration have identified weaknesses in HUD's contract administration and monitoring of contractors' performance. For example, our work on HUD's oversight of real estate asset management contractors, who are responsible for safeguarding foreclosed HUD properties, found that HUD did not have an adequate system in place to assess its field offices' oversight of these contractors. The three HUD field offices we visited varied greatly in their efforts to monitor real estate asset management contractors' performance, and none of the offices adequately performed all of the functions needed to ensure that the contractors meet their contractual obligations to maintain and protect HUD-owned properties.[2] Our physical inspection of the properties for which the contractors in each location were responsible identified problems at the properties, including vandalism, maintenance problems, and safety hazards, which may decrease the marketability of HUD's properties, decrease the value of surrounding homes, increase HUD's holding costs, and in some cases, threaten the health and safety of neighbors and potential buyers.

- HUD has recognized the need to improve its contracting processes and has begun taking actions to address the weaknesses that we and the Inspector General have identified. For instance, HUD has recently appointed a chief procurement officer and is also establishing a contract review board. In addition, HUD is taking steps to revise its property disposition activities which could reduce its reliance on asset management contractors.

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[2]We performed audit work at the Illinois State Office in Chicago, the Massachusetts State Office in Boston, and the Texas State Office in Fort Worth.

BACKGROUND

HUD's procurement offices annually award and administer millions of dollars worth of contracts on behalf of HUD's program offices. This process entails receiving descriptions of need, soliciting and receiving offers, awarding contracts, making necessary contract modifications, resolving disputes, and closing out completed contracts. The Office of Procurement and Contracts performs these functions for headquarters offices, and the three Administrative Service Centers (located in New York, N.Y.; Atlanta, Ga.; and Denver, Colo.) perform them for HUD's field offices. The major types of goods and services procured by headquarters include information technology hardware and software, mortgage-accounting and claims-processing services, advertising for the sale of HUD's properties, and various professional, technical, and administrative management support services. The typical goods and services purchased by the field offices include real estate management services and mortgage insurance-related activities, such as mortgage credit analyses, appraisals, and mortgage insurance endorsement processing.

HUD'S PLANS INCLUDE CONTINUED RELIANCE ON CONTRACTORS

HUD's staffing levels decreased from 12,823 in 1993 to 9,200 in 1998. While HUD has been downsizing, its annual obligations for headquarters contracts have steadily increased. According to HUD's data systems, the annual contract obligations at HUD's headquarters grew from $213 million in fiscal year 1991 to $376 million in fiscal year 1996 (in constant 1996 dollars). No historical data are available for field office contracting activities.[3]

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[3]HUD used to maintain contracting data at each location that performed contracting. We found that the data varied considerably in terms of its completeness and reliability. In 1997, HUD implemented a new procurement system that combined the Department's headquarters and field procurement systems. We have not reviewed the reliability of this consolidated procurement system.

HUD's 2020 Management Reform Plan and supporting documents indicate that the Department's reliance on contractors to help carry out its responsibilities will remain significant. For instance, the plan calls for HUD to contract with private firms for a number of functions, including physical building inspections of public housing and multifamily insured projects; legal, investigative, audit, and engineering services; and activities to clean up the backlog of troubled assisted multifamily properties. Previously, physical inspections of multifamily projects were carried out by HUD personnel, mortgagees, and regional contractors. The plan also encompasses the potential use of contractors to manage construction under the HOPE VI program.[4] Finally, the 2020 reforms call for transferring the Office of Housing's contract administration activities for its rental assistance programs to contract administrators. The new arrangement would be similar to the process under the Office of Public and Indian Housing's rental assistance programs. Currently, approximately 1.1 million assisted rental units are administered by the Office of Housing under contracts with project owners. The Office of Housing performs the role of contract administrator and makes monthly rent payments to owners on behalf of eligible families. Under HUD's proposal, these activities would be carried out directly by contractors (often, housing finance agencies or housing authorities) instead of HUD employees.

WEAKNESSES EXIST IN HUD'S CONTRACTING PRACTICES

We, HUD's Inspector General, and the National Academy of Public Administration have identified weaknesses in HUD's contracting practices. For example, our review of HUD's oversight of real estate asset management (REAM) contractors, who are responsible for safeguarding foreclosed HUD properties, found that HUD did not have an adequate system in place to assess its field offices' oversight of these contractors.

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[4]The HOPE VI program provides funds for, among other things, the demolition, rehabilitation, and construction of public housing.

Weaknesses Exist in HUD's Oversight of REAM Contractors

Our audit work found that HUD does not have a system in place for monitoring its field offices' administration of REAM contracts. To safeguard and maintain the approximately 30,000 properties that HUD has in its inventory at any given time, HUD obtains the services of REAM contractors. These contractors are to secure and inspect the properties, report their condition to HUD, notify interested parties of HUD's ownership, perform exterior maintenance, and ensure that the properties are free of debris and hazardous conditions. REAM contractors are therefore essential to HUD's achieving its goal of returning these properties to private ownership as soon as possible, while obtaining a maximum sale price for HUD. HUD's guidance makes headquarters staff responsible for overseeing the administration of REAM contracts. Specifically, the guidance requires regional offices to ensure that field offices are monitoring REAM contractors and requires headquarters staff to review regional offices' oversight actions through regional reviews. We found, however, that headquarters staff have not been reviewing the field offices since HUD reorganized its field office structure in 1995 and eliminated the regional offices. According to HUD Single-Family Property Disposition officials, the regional offices' oversight function was never absorbed into headquarters after the regional offices were eliminated. Also, after the reorganization, HUD's guidance was not updated to ensure that the administration of REAM contracts was monitored by headquarters.

In addition, HUD's field office staff are not consistently providing adequate oversight of REAM contractors. We believe this lack of oversight contributed to some of the poor property conditions–ranging from graffiti and debris to imminent safety hazards–that we saw when we visited 66 HUD properties. Such conditions can decrease the marketability of HUD's properties, decrease the value of surrounding homes, increase HUD's holding costs and, in some cases, threaten the health and safety of neighbors and potential buyers. Our report made recommendations to HUD for improving its oversight of REAM contractors.

Some Key Oversight Responsibilities Are Not Always Performed

HUD's field office staff are directly responsible for overseeing REAM contractors. We found, however, that some key oversight responsibilities were not always performed by staff at the three HUD field offices we visited. For example, HUD's field staff did not always evaluate REAM contractors as required. Field office staff are supposed to evaluate the REAM contractor's performance every year in the month prior to the contract's anniversary date. This annual evaluation is used to make decisions on contract extensions and, if necessary, to act on inadequate performance. However, at all three field offices we visited, these evaluations were not always conducted or were not always completed in time to provide useful information for contract renewal decisions. For example, one of the field offices we visited has evaluated the REAM contractor's performance only once since the REAM contract was awarded in June 1995, and that evaluation was conducted several weeks after the contract had already been extended beyond the base year. Officials in that field office told us that performance evaluations were not performed because they did not have the staff resources or travel funds to visit the contractor's office. However, it should be noted that the REAM contractor's office is only 37 miles from HUD's field office.

Furthermore, in the one evaluation conducted, field office staff did not convey the results of the evaluation to the REAM contractor, as required. In this evaluation, HUD cited the contractor for failing to remove debris from some properties. Our inspection of properties in this field location revealed that the debris removal problem still existed at the time of our review, more than 1 year later. One property had been shown by realtors eight times while it contained debris. In fact, a realtor noted that the only accessible entrance to the property was blocked with furniture and debris, which was the case when we visited the property. During our August 1997 inspection of 24 properties in this location, we found that most of the properties contained either interior or exterior debris. Consequently, prospective buyers were sometimes viewing properties littered with household trash, personal belongings, and other debris.

In addition, HUD's field office staff did not always inspect the properties managed by REAM contractors, as suggested by HUD's guidance. Because HUD recognizes that physical inspections are the best method for monitoring the contractors' work, HUD's guidance suggests that field office staff conduct monthly physical inspections of a minimum number of properties assigned to each contractor. To help meet this target, the guidance allows the field offices to contract out for property inspection services. Without adequate on-site inspections, HUD cannot be assured that it is receiving the services for which it has paid. In two of the field offices we visited, property files contained evidence that some properties were being inspected. However, of the 42 property files we reviewed in the third field office, HUD's field office staff had not inspected any of those properties. Field office staff told us they did not get out to inspect properties because they did not have the travel funds or staff resources to do so. Subsequent to our visit, in December 1997, this field office started using contractors to make property inspections.

Moreover, HUD's field office staff did not always ensure that the REAM contractors conducted property inspections and submitted appropriate reports for HUD's review. HUD's guidance requires REAM contractors to submit initial inspection reports within 5 working days of being notified that a property has been assigned, but it offers no specific guidance on the submission of routine inspection reports. The REAM contractor's submission of initial and routine inspection reports is essential for HUD to determine its marketing strategy for the properties and to mitigate potential losses to the properties. For example, the initial inspection reports, along with appraisals, are the primary tools for determining the repairs that must be made and whether the property meets certain standards that would allow it to be sold with HUD-insured financing. At the three offices we reviewed, the requirements placed on REAM contractors for submitting inspection reports and the extent to which the reports were actually submitted to the field offices varied considerably. For example, at one location, all of the property files we reviewed contained initial inspections, while in another location, 43 percent of the files contained no initial inspections. Without inspection reports, HUD is unable to readily determine whether the contractors are conducting inspections as required.

REAM's Inadequate Performance and Weaknesses in HUD's Oversight Contribute to Poor Property Conditions

At all three locations that we visited, we found instances where properties were not maintained as required by the REAM contracts. During our inspection of approximately 20 properties in each location, we identified properties that (1) were not properly secured, (2) had physical conditions that did not match those that the REAM contractor had reported to HUD, or (3) had imminent hazards.

For instance, of the 66 properties we visited in all three locations, we found that approximately 39 percent were not sufficiently secured to prevent access to the property. The failure to properly secure properties can lead to trespassing, vandalism, and the property's deterioration. In fact, we visited unsecured properties that had broken windows, graffiti, and exposed walls in the bathrooms where valuable copper piping had been ripped out.

In addition, we found physical conditions that did not match those that the REAM contractors had reported to the three HUD field offices we visited. For example, one property contained animal feces, fur, and personal possessions, while the contractor's inspection report indicated that the house was free of debris. If contractors do not accurately report on the condition of properties, HUD may lack vital information on which to make disposition decisions and to address safety hazards. As a result, the government may sell the property for less than it is worth or incur unnecessary holding and maintenance costs because it is not marketable.

Furthermore, almost 71 percent of the properties we visited in one field office, and about 37 percent in another, contained imminent hazards, such as broken or rotting stairs. Inspection reports submitted to HUD for one property noted that the front steps were dangerous–a condition warranting immediate repair by the contractor. Nonetheless, when we inspected the property about 3 months after the contractor initially reported the

problem, the stairs still had not been repaired. Other imminent hazards that we saw included a refrigerator with the door intact on a back porch and properties containing household waste, food, soiled diapers, paints, and solvents. The failure to address imminent hazards endangers would-be buyers, as well as neighbors, and puts the government at risk of litigation.

On the basis of our review of files and properties in the three locations, we found that the properties were generally in better condition in the locations where staff more actively monitored the contractors' performance. We recognize, however, that the condition of the properties is not totally attributable to HUD's oversight of the contractors. Other factors can contribute to the condition of the properties, including the overall quality of the contractor's work and the susceptibility of the neighborhood to crime and vandalism.

Other Weaknesses Exist in HUD's Contracting

We, the Inspector General, and the National Academy of Public Administration have identified other weaknesses in HUD's contracting with respect to the Department's procurement systems, needs assessment and planning functions, and oversight of contractors' performance.

- Both we and the Inspector General found that HUD's ability to manage contracts has been limited because its procurement systems have not always contained accurate critical information regarding contract awards and modifications and their associated costs. Although HUD recently combined several of its procurement systems, the new system is not yet integrated with HUD's financial systems, thus limiting the data available to manage the Department's contracts.

- The Inspector General reported in September 1997 that (1) inadequate oversight of contractors' performance has led HUD to pay millions of dollars for services without determining the adequacy of the services provided and (2) many HUD staff had a poor

understanding of their contract management roles and have not always maintained adequate documentation of their reviews of contractors. This situation limits assurances that adequate monitoring has occurred.[5]

- In a May 1997 preliminary report on the contracting activities of HUD's Federal Housing Administration (FHA), the National Academy of Public Administration identified a variety of problem areas associated with the procurement process, including the fact that procurements took too long; FHA's oversight of contracted services was inadequate; and FHA sometimes used contracting techniques that limited competition.[6] The Academy is in the process of carrying out a more in-depth review of FHA's contracting activities and is also reviewing procurement practices in other parts of HUD.

In a December 1997 report, HUD's Inspector General noted that a potential reliance on contractors as a means of supplanting HUD staff may not be in the best interests of HUD and the taxpayers.[7] The report noted that HUD relies heavily on contractors to perform studies, design systems, administer functions, and develop plans and strategies but has made little effort to date to formally evaluate the effectiveness and cost/benefits of its contracted work.

HUD HAS TAKEN STEPS TO IMPROVE ITS CONTRACTING OPERATIONS

HUD has recognized the need to improve its contracting processes and has begun taking actions to address weaknesses that we and the Inspector General have identified. In its

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[5]HUD Contracting, HUD, Office of Inspector General, 97-PH-163-0001 (Sept. 1997).

[6]A Preliminary Review of Federal Housing Administration Acquisition Activities, National Academy of Public Administration (May 1997).

[7]Department of Housing and Urban Development, Office of Inspector General Semiannual Report to the Congress as of September 30, 1997 (Washington, D.C.: HUD, Dec. 29, 1997).

latest self-assessment of management controls under the Federal Managers' Financial Integrity Act,[8] HUD added contracting as a new material weakness. The 2020 plan also includes an effort to redesign the contract procurement process.

HUD has recently appointed a chief procurement officer who will be responsible for improving HUD procurement planning and policies, reviewing and approving all contracts of over $5 million, and implementing recommendations that may result from an ongoing study of HUD's procurement practices by the National Academy of Public Administration. HUD is also establishing a contract review board, composed of the chief procurement officer and other senior HUD officials, that will be responsible for reviewing and approving each HUD program office's strategic procurement plan and reviewing the offices' progress in implementing the plans. In addition, HUD is establishing standard training requirements for the HUD staff responsible for monitoring contractors' progress and performance by including standards relating to monitoring contractors in its system for evaluating employees' performance. HUD is also planning actions to integrate its procurement and financial systems.

In addition, HUD officials told us that they are planning to take actions to strengthen the Department's oversight of REAM contractors and to involve headquarters in ensuring that field staff effectively oversee the contractors' performance. Furthermore, with respect to the problems found in property disposition contracting, single-family housing officials have proposed changes that they anticipate would result in only a minimal inventory of properties and therefore only a limited need for REAM contractor services. Specifically, according to HUD Single-Family Housing Division officials, the Department plans to sell the rights to properties before they enter inventory, thus enabling them to be quickly disposed of once they become available. Although the details of these sales, which HUD refers to as "privatization sales," remain to be developed, HUD envisions that properties

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[8]U.S. Department of Housing and Urban Development FY 1997 Accountability Report, Office of Chief Financial Officer.

would be pooled on a regional basis and purchased by entities that could use their existing structures to sell the properties in the same way that the Department currently does, namely, through competitive sales to individuals. In addition, as a part of its budget request for fiscal year 1999, HUD proposed new legislation to allow the Department to take back notes when a claim is paid, rather than requiring lenders to foreclose and convey properties. HUD would then transfer the note to a third party for servicing and/or disposition.

We view the actions that HUD has taken to improve its contracting procedures as positive steps. However, some key issues concerning their implementation are still being finalized, such as the precise role of the contract review board in overseeing HUD's procurement actions, and HUD's ability to have the necessary resources in place to carry out its procurement responsibilities effectively. Perhaps even more important is the extent to which these actions will lead to a change in HUD's culture, so that acquisition planning and effective oversight of contractors will be viewed by both management and staff as being intrinsic to HUD's ability to carry out its mission successfully.

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Mr. Chairman this concludes our statement. We would be pleased to respond to any questions that you or Members of the Subcommittee may have.

Mr. SHAYS. Thank you very much. Let me just welcome our ranking member. I know he's just getting down and not able to sit down. He serves on many committees, and he has been just a tremendous active member of this committee, and I am very grateful for his work. I don't know if you want to make a statement. We've concluded the testimony. Should we just get into questions?

Mr. TOWNS. No, I'll just submit my statement for the record.

[The prepared statement of Hon. Edolphus Towns follows:]

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OPENING STATEMENT OF

REP. EDOLPHUS TOWNS, RANKING MINORITY MEMBER

SUBCOMMITTEE ON HUMAN RESOURCES

JUNE 5, 1998

Mr. Chairman, thank you for holding today's hearing on procurement activities at the Department of Housing and Urban Development. HUD has long had problems with procurement awards. In the 1980's, this subcommittee, under the leadership of Rep. Lantos uncovered major examples of fraud, waste and abuse in HUD contracting practices.

HUD's procurement process entails receiving descriptions of need, soliciting and receiving offers, awarding contracts, making necessary contract modifications, resolving disputes and closing out competed contracts. One must remember that the purpose of procurement is to allow the program offices to perform the mission of the agency. Mr. Chairman, we would make a mistake if we failed to consider the difficult and important mission of this agency. HUD is charged with spurring community development, encouraging private home construction and rehabilitation, providing housing assistance for low and moderate income individuals, the elderly and the handicapped. Additionally, HUD is charged with the responsibility of promoting fair housing laws. In carrying out this diverse mission, this agency has annual contract obligations of approximately $400 million.

HUD's contracting practices have long been an area of concern and were a major factor in GAO's decision to place HUD on its "high risk" list. HUD's IG found that many of HUD's procurement actions resulted in quality, cost efficient products. However, the IG also found that

inadequate planning, needs assessment, monitoring and control, and lack of integrated financial and management data systems, made HUD vulnerable to waste and abuse and made the department overly reliant on the knowledge and expertise of existing private sector contractors.

The IG made several recommendations to fix these problems. In my reading of the HUD's procurement reform plan, it seems that many of those recommendations have been implemented. HUD recently appointed a Chief Procurement Officer who is charged with the responsibility of establishing and enforcing procurement policies and procedures. HUD is in the process of establishing a contract management review board which would be charged with the responsibility of reviewing and approving each program office's strategic plan for new procurement, reviewing interagency agreements, and conducting periodic review of each program office's progress in implementing their strategic plans. The Chief Procurement Officer is in the process of establishing specialized positions for contract award, monitoring and oversight. These positions would require advanced training and on-going recertification. Within the last 30 days, HUD has hired a Chief Information Officer who is charged with the responsibility of implementing the integration of the various information systems at the agency. Mr. Chairman, I am not saying that all is right at HUD. In particular, I am concerned about field office implementation of procurement policies and the use of the private sector to perform traditionally governmental functions. However, I believe that the witnesses today will be able to substantiate that HUD has made significant progress toward the implementation of many of the IG's recommendations and look forward to hearing their testimony.

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Mr. SHAYS. Thank you very much. Mr. Towns hasn't told anybody, but he has learned how to get his seat so it can get up higher. There are four controls on these seats, and we are just trying to figure them out here. [Laughter.]

First off, let me ask both of you. What is anecdotal here? How can we respond to some criticism? Are you just taking these anecdotes and magnifying them as if they are in fact the rule rather than the exception? When you went out to look, when you went out to see sites, did you find that most was done well, but then you have a wonderful picture you can show?

Mr. CZERWINSKI. Mr. Chairman, we would not do that. The types of things we found were pretty widespread. For example, the picture you see about properties needing immediate attention but not being given that attention was fairly typical. Over half the properties at two of the field offices we visited fell into that category.

HUD's requirement is that when an immediate hazard is detected, it should be corrected in 24 hours, but we were going back in many cases months afterwards and finding that over half the cases that that wasn't corrected. So this is not an isolated incident.

Mr. SHAYS. So it's almost the rule rather than the exception?

Mr. CZERWINSKI. In the places we looked it was very frequent.

Mr. SHAYS. OK.

Ms. GAFFNEY. Mr. Shays, we looked at—in our audit—we looked at $1.5 billion worth of contracts. During that period the total amount of HUD contracting was $3.2 billion. So we looked at 50 percent of the contracting, and we found problems in virtually every contract.

Mr. SHAYS. Well, it raises the question of what would be the explanations as to why they weren't dealt with, besides the fact that basically there's a tremendous amount of dishonesty when someone says something has been done and it hasn't been done. What would HUD's response be in the field when you would point out these kind of outrageous circumstances?

Ms. GAFFNEY. I'll let Mr. Momorella answer that, but I am certain we would get the same answer we'd get on virtually every one of our audits, that they don't have enough staff to do their jobs; they don't have enough staff to oversee the contractors; they don't have enough staff to spend carefully planning contracts.

Mr. MOMORELLA. Yes, that's correct. That was the general opinion. Also, there were a number of contracts that were awarded on a nationwide basis, and the Government technical representative would be located in Washington, but the work would be performed all throughout the country. So it was very difficult for someone in Washington to monitor work that's being done in Los Angeles by a contractor, et cetera; and again, the staffing and just the amount of contracts that were out there.

Mr. SHAYS. Explain to me why it's in the District of Columbia and not being monitored outside the District of Columbia in the field.

Mr. MOMORELLA. Well, the general practice was that when a contract was awarded by let's say, for example, the Office of Public Housing, if it was generated by the Assistant Secretary's Office in Washington, someone from that office would be designated as the Government technical representative for the contract. And this was

a weakness in monitoring that they didn't have sufficient Government monitors throughout the area.

Mr. SHAYS. OK, but don't they take advantage of the local housing authorities to help them oversee? These are not public housing projects? These are——

Mr. MOMORELLA. No, this would be contracts, for example, where in public housing HUD would hire a contractor to go out and do specific work at different housing authorities and report back to HUD, not to the housing authority.

Mr. SHAYS. Mr. Czerwinski.

Mr. CZERWINSKI. I think there probably may be three areas, and they are related, and they probably all come under the rubric of management emphasis and priority setting. HUD has not placed as high a priority on contract management as we would like and that's why you're seeing some of the problems. And I think that it signals an intention to start to change that, but, again, I think it's a matter of follow-through.

Second, within that, it would be the information available. If you're not paying as much attention to what's going on with the contract, you just don't know and you don't have the data that you need to manage, and of course related information is the resources needed, as the inspector general mentioned, to go out and get the information to keep an eye on the contractors.

I think the incentives of the Government and the contractor sometimes differ. The contractors want to maximize their profit—do the least to get the most. We, on the other hand, are looking to get the most for the least and to keep that kind of balance you need the resources to oversee them.

Mr. SHAYS. One of the questions Mr. Kucinich raises is, whether should we even be contracting out? It seems to me we have two issues: First, are we contracting out the things that we need to contract out, and the other is, once we are contracting out, are we making sure that those contractors are doing their job?

It's my understanding that sometimes we hire contractors to oversee contractors.

[Witnesses nod in agreement.]

Mr. SHAYS. You all nod your head here. OK.

Mr. HALE. Mr. Chairman, I mean that's something that's done in REAM's contracting and will maybe be done even more in the future, because now some field offices actually do go out, and inspect properties themselves to make sure that the REAMs have been there and have done a good job, but in other cases they hire other contractors to go out and do the inspection.

Then HUD downsizing in the single-family area; I think certainly at least in the short run that's likely to happen more rather than less.

Mr. SHAYS. Any other comment? I think what I am going to do is allow Mr. Kucinich to do his. Yes. I just want to know, do you have anything to add?

Ms. GAFFNEY. Yes. I'd like to say that essentially HUD has downsized to the point where it doesn't have the choice; it has to contract. It doesn't have the staff to do it, and the problem is contracting is seen in HUD as an easy way out. If you don't have staff,

just go get contractors. The trouble with contracting is actually quite a difficult task, not an easy out.

Mr. KUCINICH. Well, I think this is very easy to sum up, Mr. Chairman. It's in my charts. Staffs go down—and this is kind of like Newsweek, you know—staff down, contracts up, controls out. I mean how difficult is this to understand? I thought Mr. Czerwinski's testimony here was right on. He described staff reductions for the 12,823 in 1993 to 9,200 in 1998. It's downsizing. It's contracts increase. Now there's contractors that have contractors.

Mr. Chairman, I am glad you've called this hearing. I am looking forward to hearing more. This is becoming more and more interesting, and by the way, through all of this we should remember there are people who live at these places.

Mr. TOWNS. Will the gentleman yield? So what are you saying, as soon as we finish this hearing we should go to the Budget Committee?

Mr. KUCINICH. No, I think we should go over to HUD's office and talk about why they run the Department this way. But this is a culture. This just didn't happen. That's the problem. This is a culture, and we have a culture which has developed to dismantle government.

Let everyone all over the country know that when you get into a situation where you contract out all these services, you're going to end up losing control and this idea of continuing to cut personnel inevitably produced chaos. It has to.

But people are still paying the same taxes. Mr. Chairman, I have never been a fan of privatization. Back in the days when I was mayor of Cleveland, I stopped a takeover of a municipal light system, and as I get more and more involved in the Federal Government I can see that privatization just ends up setting up a system which doesn't serve anyone except the contractors.

And that might be a broad-based statement that doesn't take into account these many contractors who are toiling on behalf of the people, but I haven't met them yet, but I'll find them somewhere. Maybe you'll find them. I am going to go vote.

Mr. SHAYS. OK. I am going to just say that we will go and vote. We are going to have disagreements because I happen to believe that privatization can be done well. It just depends on how you do it. So this is why we have fun in this committee.

Mr. TOWNS. We definitely have disagreements, but I think that, here again, cutting the budget I mean to the point, you know, what do you do here? That's the point. You're talking about, you need some resources as well. There's a lot of things here that have to be addressed. So I agree with you, Mr. Chairman. I think we're going to have an interesting day.

Mr. SHAYS. My understanding is when HUD was at about 20,000 people they had the same problems. So we'll keep debating this issue, and I got the last word. [Laughter.]

Mr. Kucinich, are you coming back?

Mr. KUCINICH. I wouldn't miss it.

[Recess.]

Mr. TOWNS [presiding]. Let me begin by—I have some concerns that the audit procurement practices will have a chilling effect on

bringing about procurement reform. What is your response to that concern?

Ms. GAFFNEY. I am sorry, Mr. Towns. Could you restate that question?

Mr. TOWNS. Yes. I have some concerns really that the audit or procurement practices—now these are people that are following the rules, doing their jobs—will have a chilling effect on bringing about procurement reform. And I want to know your response to that.

Ms. GAFFNEY. Our audit tends not to deal with the people who are called contracting officers. They are on the whole doing a good job. Our overall concern is with the program people, who have to interface with the contracting officers. What we're trying to say is they need—there needs to be a marriage between the program people and the contracting people.

It's the program people who presumably know the business who need to define the needs for the contracting officer, who need then to monitor the work that's being done after the contract is awarded, and our primary message is: The program people need to take more seriously their role in contracting because the contracting officers cannot do it by themselves.

Does that answer your question?

Mr. TOWNS. Yes, sort of, but I am trying to really sort this out. It is my understanding the HCFA pays for equipment used by contractors in Medicaid and Medicare buildings. This is my understanding. And yet the report questions that practice in a contract with Price Waterhouse. Do you believe that the practice should cease throughout the Federal Government even though it might make it more difficult to obtain qualified contractors? I am trying to sort this out. I mean, what do you really think?

Ms. GAFFNEY. No, I think—Ed, do you want to deal with that?

Mr. MOMORELLA. Yes. I believe that the points that we were trying to raise, the five critical findings where we talk about the overall need determination, the cost consciousness approach to contracting and the periodic assessment is what we were trying to bring up here.

For example, in most instances that we looked at, at the time the contract was executed there appeared to be a good reason as to why HUD should enter into this contract, but, as you know, the organization was constantly changing and things change, and as time went on, some of these contracts, which originally were estimated to only $1 million, now mushroomed through additional task orders up to $9 million.

And what we were saying is there was no information to say that periodically along the way someone would say, "Is this still a good idea? Is this still within our mission? Should we still be spending this?"

We have heard proposals about, well, let's take procurement and give it to another agency; let's take the procurement officials and let's give it all, the responsibility, to program people. I think, as the inspector general indicated, to be very effective it has to be a really good marriage and joint effort. There is an extremely large number of competent and well-qualified, professional procurement people that work for HUD, and they want to do the right job. They are the sworn officials, the procurement officials; and they are in a bal-

ancing act between the pressures of the program people who have a mission and a program goal and expediency; and the trust is placed into the contract officials to see that the dollars are spent properly.

And you often see these battles. And what the inspector general has also indicated, is where the chief procurement officer sits in the organization goes a long way in setting the attitude as to how HUD can contract in the best possible manner for the taxpayers and to accomplish the goals of the program as spelled out by Congress.

In other words, in our review we found that there needs to be a much, much closer agreement. That's why we recommended that someone other than just in a specific cylinder, for example, if you have just housing folks going ahead, saying, "We need to do this, let's contract." We recommended that you bring in the budget people and the chief financial officer, so somewhere along the line someone can say, "Wait a minute. Is this still the best thing for the Department? Is this still the most cost efficient way to get this work done?," and that was, quite frankly, what was lacking.

They were just so over worked, so overwhelmed, they didn't have time to monitor the Government technical representatives as they were required to do, and quite frankly, they couldn't manage and maintain and do the daily housekeeping chores, enter the data into the systems, because they were busy awarding new contracts and constantly being asked to issue new ones.

So, I think it's really important to recognize that from our standpoint there are very good, qualified, knowledgeable people at HUD, and they're trying to do the right thing; but there needs to be more of a coordination effort from the entire Department: the fiscal records, the procurement records, and the program records, and also the general counsel. Some of these contracts didn't have counsel review ahead of time and ended up with loopholes that were very costly for the Government to terminate.

And we tried to say a little bit of prevention in the front of this would go a long way to making sure that it was an efficient effort by everybody involved.

Mr. KUCINICH. I just had a very quick followup question. Do you have a list of the cost overruns on these contracts?

Mr. MOMORELLA. We have——

Mr. KUCINICH. You mentioned that one contract started at $1 million, ended up $9 million.

Mr. MOMORELLA. Right. I guess technically, Congressman, it's not a cost overrun because they extended it. In other words, they modified it——

Mr. KUCINICH. Well, these contracts—have you done a study where you have "contract began at $1 million and now it's $9 million?" Do you have a number of those instances?

Mr. MOMORELLA. We can get you that information.

Mr. KUCINICH. That would be very interesting to have. Thank you, with the permission of the Chair if we could get that information. Thank you.

[The information referred to follows:]

Contractor	Contract Number	Original Contract Amount	Final Contract Amount
ABT Associates	5889	$100,000 - $2,500,000	$3,049,741
	5953	$200,000 - $3,000,000	$3,119,642
Advanced Technology Systems (ATS)	16326	$29,790,334	$51,763,505
American Management Systems, Inc.	16330	$243,604	$16,073,098
Data Prompt, Inc.	12644	$292,000 - $3,761,731	$38,539,294
	14877	$350,000 - $2,907,578	$43,083,678
	14488	$29,117 - $2,271,235	$30,929,554
Golden Feather Realty Services, Inc.	18501	$1,680,257	$3,680,257
Lockheed Martin Information System	14703	$525,908,431	$1,000,000,000+
National Loan Servicenter, Inc.	14753	$38,229,572	$129,044,265
Price Waterhouse	18065	$1,900,000	$9,582,790
Strategic Mortgage Services, Inc.	18150	$13,000,000	$41,846,000

Mr. TOWNS. Let me just——

Mr. SHAYS [presiding]. You're in charge.

Mr. TOWNS. Could you give us some perspective here? What percentage of HUD's procurements do you believe are a problem because you indicated in your report that most of HUD's contracts delivered efficient and cost effective goods and services. What percent would you say that's not?

Ms. GAFFNEY. That are significantly troubled, not just small?

Mr. TOWNS. Yes. What percent of the problem? Well, could you give us—I mean I'm just trying to get some perspective here what we're dealing with.

Mr. MOMORELLA. Well, I think our report tried to do that. What we said was—of course of the 9,000 contracts that we talked about in the universe—these ranged from doing elevator service in the HUD building, to running the cafeteria and in other words, there are a number of contracts.

The 30 contractors that we selected provided various types of services, consulting services, more than just hardware services; and I think that presents a pretty good cross representation from different program areas and types of services. And we weren't focusing on contract by contract as much as looking at the overall systems—the fact that the financial system gave no support. The contract monitors had very poor tools to do their job.

They couldn't go to a system and find out how much this contractor had been paid to date. In some cases, they had to call the contractor to find out because they were newly assigned to that, and the records weren't available from a previous representative.

So, again, what we tried to highlight in our report is not this contract is wrong, that contract is wrong. All together, what those five main areas were that we highlighted in our report: the cost consciousness, the needs planning and the monitoring.

Ms. GAFFNEY. Mr. Towns, could I try it a different way?

Mr. TOWNS. Sure.

Ms. GAFFNEY. I think there's a range of activities, and at one end there are things as straightforward, as Ed said, as elevator maintenance; and we tend not to find problems—or office cleaning—very straightforward, easily measured kinds of activities. And we tend not to find problems in those kinds of contracts.

There is a spectrum though of activities that become increasingly complex, and the vulnerability increases with the complexity and with the knowledge and the expertise of HUD's staff. So let me give me you an example of an extreme, a complex level.

HUD, a couple of years ago, embarked on a program to sell multifamily and single family notes. HUD had never done that. It was a huge undertaking. I mean this involved billions and billions of dollars. HUD had no one on staff with any expertise in that area and was unable for reasons that I cannot explain to you to get anyone on staff.

They contracted out the function, and they were essentially then left in a position of totally relying on—I am not saying the contractors did anything wrong—but HUD was in a position of having to rely on those contractors totally because HUD had no one on staff who knew how to do that or how to manage that kind of a program.

So, it's a big range.

Mr. TOWNS. So, I guess what I am really saying is: Is there any kind of a percent that you can put to this? Eighty percent? Eighty-five percent is good?

Ms. GAFFNEY. In terms of dollars——

Mr. TOWNS. Well, dollars, yes. Actually what percent would you say? Yes, dollars.

Ms. GAFFNEY. I don't think we can give you a percent. I don't think we have a basis for that. Do we?

Mr. TOWNS. Well, can you give me any kind of a percent that is something we might be able to measure? Got any other ideas? I am trying to figure out, you know, I just can't get a handle on this in terms of how big is the problem.

Ms. GAFFNEY. Well, we looked at 50 percent of the dollars.

Mr. MOMORELLA. Well, we looked at the most significant information technology contract—that was Lockheed Martin—and the contractor that was hired, NYMA, to monitor Lockheed Martin. And that area alone represented over $800 million, and there were some significant problems we had with the administration and monitoring, direction, periodic assessment and so forth with that area.

So that's $800 million out of—I mean that was a significant chunk right there. Just to give you some kind of ballpark figure that you're indicating.

Ms. GAFFNEY. That contract alone, during this period, would represent about 25 percent of the total contract expenditures, correct?

Mr. MOMORELLA. Yes.

Mr. TOWNS. It is my understanding that your report set forth several recommendations, and I am going to run through this right fast. I would like to go through a summary of those recommendations and have you tell us whether those recommendations have been implemented or whether there are plans to have them implemented.

First, perform comprehensive planning and assessment of information technology needs.

Mr. MOMORELLA. We—and I will answer your question, sir, as we understand it. Perhaps Mr. Carberry can give you more up-to-date, but what we have been informed to date is that that has been given over to Mr. Carberry to plan to do that. To our knowledge it hasn't been completed. It's been——

Mr. TOWNS. Establish a threshold dollar amount for review of contract proposals by the CFO and others prior to contract award.

Mr. MOMORELLA. HUD has established that board.

Mr. TOWNS. Establish specialized positions for personnel responsible for contract oversight and monitoring to make them full time jobs with performance standards and training requirements.

Ms. GAFFNEY. Yes.

Mr. MOMORELLA. They have a plan established with target dates for improving their Government technical representative and monitor——

Mr. TOWNS. So that's a yes.

Ms. GAFFNEY. Yes.

Mr. TOWNS. Integrate data system and payment system so that contract performance and contract payments will relate and can be systematically monitored.

Ms. GAFFNEY. Plans for doing that.

Mr. MOMORELLA. Plans. It's not implemented.

Ms. GAFFNEY. No, they have plans for doing that.

Mr. TOWNS. Well, that would be a yes.

Ms. GAFFNEY. That's a yes. Right.

Mr. TOWNS. Review current interagency agreements to determine necessity of agreement and suitability of reimbursement rates.

Ms. GAFFNEY. I don't—we do not have a response on that recommendation, to my knowledge.

Mr. MOMORELLA. That's correct. They just said that that would be the responsibility of the chief procurement officer.

Mr. TOWNS. Yes. Let me—the audit process can sometimes lead to controversy. Do you believe that there should be a forum where people with concerns can be heard?

Ms. GAFFNEY. Of course. Mr. Towns, can I just step back for 1 minute and tell you——

Mr. TOWNS. Sure. Go ahead.

Ms. GAFFNEY [continuing]. That to me what is happening at HUD now as the result of our work and NAPA's work is extremely positive. This is good news. As you run through those recommendations, we are answering yes to whether HUD has plans.

I consider it incredibly significant that HUD has moved to name a chief procurement officer who is so well qualified, who is taking steps to make contracting important in HUD. That is a matter of focus. This is good news.

Mr. TOWNS. Let me move, and I'll get out of the way, Mr. Chairman.

Mr. SHAYS. You got a green light, boss.

Mr. TOWNS. As you know, I have a high concentration of public housing units in my congressional district. I think I have the third highest or fourth highest in the Congress. I'm always interested in programs that impact public housing. That is why I was concerned about questions raised by the Senate Banking Committee as to whether the IG's office can both manage and oversee Operations Safe Home.

In light of the Banking Committee's concerns, have you produced an audit report on this program relative to procurement practices and expenditures?

Ms. GAFFNEY. Approximately 1 year ago, Mr. Towns, we had a group of auditors in the OIG who audit HUD's financial statements. When they completed that work on the 1996 financial statements, I asked them to undertake a financial review of OIG operations, and I asked them to do it in the most nitpicking possible way as an internal management review.

They did so. They issued that internal management review in January 1998. In the process of doing that review they looked at $946,000 of Operations Safe Home expenditures. They found support problems for a total of $16,000 of those expenditures, saying that the expenditures either lacked supporting documentation or appeared to be in error.

Mr. TOWNS. How much?

Ms. GAFFNEY. It was $16,000 out of $946,000. That's 1.7 percent. They also found that in another—in 12 percent of the $946,000 there was some aspect of internal control that hadn't held truth;

that is, there was for instance not a supervisory signature on an invoice when there should have been, there wasn't a review by the proper secondary level—that kind of thing.

But that review covered not just Safe Home, it covered all expenditures—travel vouchers, everything in the OIG—and I have a copy of it for you, if you would like. I brought it because it's discussed this morning in the Wall Street Journal, so I brought a copy if you would like to have a copy.

Mr. TOWNS. Mr. Chairman, yes, may I ask that we receive the information and also share it with the Banking Committee?

Mr. SHAYS. Without objection.

Ms. GAFFNEY. Absolutely. Absolutely.

[The information referred to follows:]

U. S. Department of Housing and Urban Development
Washington, D.C. 20410-4500

OFFICE OF INSPECTOR GENERAL

JAN 21 1998

MEMORANDUM TO: Susan Gaffney, Inspector General

Kathryn Kuhl-Inclan

FROM: Kathryn Kuhl-Inclan, Assistant Inspector General for Audit

SUBJECT: Review of the Office of Inspector General Operations

As requested by you in May 1997, the Office of Audit conducted a review of the operations of the HUD Office of Inspector General for the period October 1, 1994 through March 31, 1997, including Operation Safe Home. Attached is our report which presents the results of our review and discusses our findings and other matters we identified. Our report also contains recommendations to assist HUD, OIG in its efforts to correct these problems. We appreciate the courtesies and cooperation extended to the Office of Audit staff by the Headquarters and District staffs.

Within 60 days, please give us, for each recommendation in this report, a status report on: (1) the corrective action taken; (2) the proposed corrective action and the date to be completed; or (3) why action is considered unnecessary. Also, please furnish us copies of any correspondence or directives issued to address our recommendations.

Attachment

REVIEW OF THE OPERATIONS OF THE OFFICE OF INSPECTOR GENERAL DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT

JANUARY 21, 1998

OFFICE OF AUDIT
WASHINGTON, DC

EXECUTIVE SUMMARY

This review was performed of the Department of Housing and Urban Development's (HUD) Office of Inspector General (OIG) operations. The review included operations of the Immediate Office of the Inspector General, Office of Legal Counsel, Office of Management and Policy, Office of Audit, and Office of Investigation in Headquarters. The Offices of Audit and Investigation operations in all district offices were reviewed. We reviewed records and performed tests of transactions that occurred between October 1, 1994 and March 31, 1997 for both the Salaries and Expenses and Operation Safe Home appropriations.

The objective of this review was to determine if OIG Headquarters components and district Offices of Audit and Investigation had controls and procedures in place to provide reasonable assurance that funds expended by the OIG were planned, approved, properly supported and for eligible purposes. In order to accomplish this, we reviewed records from all aspects of OIG operations. These included but were not limited to funds control, payroll, credit card usage, ADP and other equipment, travel, and training.

We performed tests of transactions from the Salaries and Expenses appropriation for all Headquarters operations and the Offices of Audit and Investigation in all district offices. In addition, we performed tests of transactions for the Operation Safe Home appropriation in the Office of Investigation. Our tests covered expenditures from both appropriations by selecting a statistical sample of transactions excluding payroll and travel. Detailed results of our statistical sample are presented in Appendix A. Based on our sample of Salaries and Expenses expenditures, we have concluded with 95 percent confidence that errors in this appropriation did not exceed $7,500. This equates to less than 0.1 percent, based on the population we tested. For our sample of Operation Safe Home expenditures, we concluded with 95 percent confidence that errors in this appropriation do not exceed $16,100. This equates to less than 1.7 percent based on the population we tested.

As part of our statistical sampling we also tested internal controls in the Salaries and Expenses and Operation Safe Home appropriations to assess whether controls to ensure that transactions were properly recorded and assets were adequately safeguarded from loss or misuse were functioning as intended. Based on this testing, we concluded with 95 percent confidence that the exception rate for Salaries and Expenses expenditures was at least 4.2 percent. For Operation Safe Home expenditures, we concluded with 95 percent confidence that the exception rate was at least 12.6 percent (See Appendix A).

We used a judgmental sample to test payroll and travel. Results of this testing are presented in the "Results of Review" section of this report.

We classified findings disclosed by this review as major and minor. Major findings were categorized as such due to their being serious in nature or having occurred in numerous offices. Minor findings were less serious or occurred in only a few offices. This report does not identify specific offices where the findings occurred, but they did not occur in all offices.

Information regarding the number of offices where major findings occurred can be found in Appendix B.

Major Findings

Following are the findings that we classified as Major:

- Offices were not performing periodic reconciliations of amounts charged to their budgets.

- Payroll processing procedures and controls were not consistently followed by offices.

- OIG usage of the International Merchant Purchase Authorization Card (IMPAC) credit card was not always in accordance with established procedures.

- The official system for reporting Operation Safe Home funding shows that funds were being committed and obligated, but were slow in being liquidated and reported as expended.

- Transaction testing of Operation Safe Home funds revealed a number of conditions including lack of or inadequate supporting documentation, advances made for task forces that had cost reimbursable contracts, and expenditures for task forces that did not have agreements.

- Rules for the use of government owned and leased vehicles were not strictly enforced by offices.

- Controls over Operation Safe Home advances to special agents for evidence or information purchases were lax.

- Some offices were not enforcing established procedures for controlling ADP equipment.

Minor Findings

Following are the findings that we classified as Minor:

- Various problems with processing travel vouchers were discovered.

- Office equipment was not maintained as required.

- A few problems with Law Enforcement Availability Pay (LEAP) were discovered.

- Training procedures lacked Individual Development Plans. In addition, one office did not maintain training records for all agents located in that office.

Numerous recommendations have been made to management to correct the findings listed above. Some of the most significant were to perform reconciliations of amounts charged to office budgets, follow established procedures for processing payroll, improve administration of Operation Safe Home funds by more closely monitoring their expenditure, and implement provisions of the recently issued procedures and policies memorandum on Operation Safe Home funds control.

Upon completion of our work in each office, we gave a copy of our findings to the respective supervisors and asked for written comments. We received both written and oral comments to the findings. We took these comments into consideration when determining which findings to include in this report and how to classify them.

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Background

In 1978, Congress created the Office of Inspector General (OIG) for the Department of Housing and Urban Development (HUD) and other Federal Agencies through the Inspector General Act of 1978. The OIG is an independent organization. It's mission is independent and objective reporting to the Secretary and the Congress for the purpose of bringing about positive change in the integrity, efficiency, and effectiveness of HUD operations.

The OIG is comprised of distinct organizational units with different authorities and responsibilities:

- the Office of Audit

- the Office of Investigation

- the Office of Management and Policy

- the Office of Legal Counsel

This review was conducted at the request of the Inspector General. Each of the above offices were reviewed during this examination, as well as the immediate office of the Inspector General. The OIG participates in an external quality control review program with other Federal Offices of Inspectors General and has an internal quality assessment review function in place. To our knowledge this is the initial review of this type of the OIG as a whole.

Objective, Scope and Methodology

Our overall objective was to determine if OIG had controls and procedures in place to provide reasonable assurance that funds expended by the OIG were planned, approved, properly supported and for eligible purposes. To accomplish this objective, we reviewed the operations of Headquarters and all District offices, for the period October 1, 1994 through March 31, 1997.

We reviewed regulations and guidance governing OIG operations to become familiar with systems and procedures. We interviewed key staff at Headquarters and each District Audit and Investigative office. We performed tests of transactions and reviewed records to determine whether procedures and controls were implemented and functioning properly. With respect to our analysis of Operation Safe Home obligations and expenditures, our procedures did not attempt to determine the validity of OIG obligations recorded in the Department's financial system at the end of our review period. We also did not review the effectiveness or qualitative results of any Safe Home task force. The procedures we performed related to the following:

- process for ensuring the accuracy of amounts charged to budgets,

- proper payroll processing to assure accuracy and reliability of payroll records,

- compliance with controls to ensure proper use of the government-wide credit card,

- funds control over Salaries and Expenses and Operation Safe Home,
- control of ADP and other equipment,
- controls over purchased or seized evidence, and
- controls over travel and training.

We performed work at Headquarters and each District level office during the period from June through September 1997. While we structured our review based on the requirements of Government Auditing Standards, this review was not in accordance with those standards. In this regard, the Office of Audit is not organizationally independent of the Office of the Inspector General.

RESULTS OF REVIEW

This report separates the results of our review into two categories, major and minor findings. Major findings were categorized as such due to their being serious in nature or having occurred in numerous offices. Minor findings were less serious or occurred in only a few offices. We also discovered two minor situations which are classified as other items. We feel that all findings need to be addressed in order to stop the occurrence of major findings and to prevent minor findings from becoming major.

MAJOR FINDINGS

Periodic reconciliations of amounts charged to office budgets were not performed.

OIG field and Headquarters components were not periodically reconciling charges to their budgets to ensure their accuracy and validity. The reconciliation becomes more important with revised procedures put into place by the Department in June of 1997. The new procedures state that all invoices below $25 will be paid and not sent to the program office for approval. Invoices between $25 and $2,500 will be paid without program office approval but a random sample of these invoices will be selected for a post-payment review. All invoices $2,500 or over will be sent to the program office for approval prior to payment. This places a greater importance on performing reconciliations of what is charged to an office's budget.

Our review of field office invoices revealed two disbursements in Fiscal Year 1996 totaling $2,456 that were erroneously charged to an OIG office. They should have been charged to other program offices within HUD. This fact was not known until our review questioned them. This would have been discovered sooner if a monthly reconciliation had been performed. Steps are currently underway to charge the appropriate Departmental accounts.

The November 1996 publication on financial management responsibilities and Federal Financial Systems (FFS) states that the OIG has the responsibility of data stewardship for all transactions entered into FFS. Data stewardship addresses the process of managing information to ensure that information entered into FFS is accurate, accessible, timely and usable. Included in the management process is providing for segregation of duties, establishing a structure of approval and data entry authorities, and performing reconciliation and adjustment processes.

OIG officials gave various reasons for not performing periodic reconciliations. Among these were that they did not know of their reconciliation responsibilities and have not been given instruction on how to perform their reconciliations.

Due to the fact that periodic reconciliations were not being performed, OIG field and Headquarters components have not ensured the accuracy and validity of amounts charged to their respective budgets. As stated above, the advent of new procedures implemented by the Department places greater importance on reconciliations.

Recommendation:

We recommend that the Office of Management and Policy establish procedures requiring that offices perfonn reconciliations of amounts charged to their budgets. The policy should require offices to perform reconciliations of amounts charged to budgets at least on a monthly basis. This information should suggest a report from FFS to be used for this purpose and be explicit as to the extent of the reconciliations and resolution of discrepancies.

Payroll processing procedures were not consistently followed.

OIG was not consistently complying with procedures or internal controls established for processing payroll. Various conditions exist which were not in accordance with established procedures. First, timekeepers were preparing and maintaining their own Time and Attendance (T&A) report without proper approval. In addition, supporting documentation was not always attached to the T&A report or the supporting documentation that was attached was not approved or not approved in a timely manner. We also noted that some supervisors were not properly reviewing or documenting their review of TANDARPTs. We also found occasions when leave or credit hours from one pay period were being recorded in another pay period.

The Department's T&A Reporting Procedures require that only under extenuating circumstances can a timekeeper maintain and/or prepare his/her own T&A report. If a supervisor believes these circumstances exist, a request and justification must be submitted to the appropriate Departmental personnel office for approval. This was not done for any of the situations where timekeepers were maintaining and preparing their own T&A report. Reporting procedures also require that T&A reports contain supporting documentation that is approved in a timely manner. The reporting procedures also state that supervisors must compare TANDARPT data (generated by the National Finance Center) to the certified T&A report and document their review by initialing the TANDARPT.

These conditions existed because supervisors were not aware that the requirements existed or were not aware of the extent of the requirement.

Due to the existence of the above conditions, the OIG was not in compliance with procedures or internal controls established for processing payroll. Also, the OIG had insufficient assurance that its payroll records or those of its employees were accurate and reliable.

Recommendation:

We recommend that the Office of Management and Policy inform supervisors of provisions set forth in the Department's T&A Reporting Procedures. Supervisors should ensure that these procedures are followed in order to comply with established payroll processing procedures and ensure accurate and reliable payroll records.

IMPAC credit card usage was not always in accordance with established procedures.

Conditions in this area included copies of credit card statements maintained by offices not containing evidence that they were properly supported or approved, ADP equipment purchased with the credit card, statements not processed in a timely manner and one situation where an office appeared to split purchases to remain below the $2,500 limit. We encountered many instances where copies of credit card statements did not contain evidence of approval or documentation to adequately support the purchases made. Adequate documentation includes items such as the invoice that supports the purchase on the credit card statement. The situation where it appeared purchases were split occurred during October 1996. In that month, an office had five transactions with one vendor which totaled $4,784 for the purchase of furniture. Also, ADP equipment was purchased with the credit card. Regarding approval, some copies of credit card statements maintained by offices did not contain evidence that the approving official reviewed and certified purchases made during the preceding month.

HUD Handbook 2212.1, REV-2 requires that the cardholder certify the credit card statement within five working days of receipt and forward it to the approving official. The approving official must review and certify the appropriateness of all purchases within fifteen working days of receipt. Approving officials are tasked with establishing appropriate internal controls and documentation procedures. This entails maintaining copies of records including statements of transactions and accountability, all supporting invoices, and related documents. The handbook limits an individual purchase transaction to $2,500 and states that purchases may not be split in order to stay within that limit. In addition, the handbook specifically prohibits the purchase of ADP equipment with the credit card.

Some offices stated that they did not maintain copies of supporting invoices or the approved statements because they did not want to bulk up their files. They stated that they can get a copy of the statement or invoice from the Office of Accounting should a discrepancy arise. They also state that the Office of Accounting will not pay the statement unless it is properly certified and approved so there is no need to maintain copies. We did encounter a situation where the approving official was out and the Office of Accounting instructed the cardholder to sign as the approving official in order to pay the monthly statement in a timely manner. This could lead one to conclude that timely payment is more important to the Office of Accounting than ensuring proper approval of statements. For ADP equipment purchases made using the credit card, offices have stated that they were told by the Office of Management and Policy that they could purchase ADP equipment with the credit card. We contacted the Office of Management and Policy who stated that HUD's Office of Administration gave OIG the authority to purchase ADP equipment with the credit card. However, the Office of Management and Policy could not produce a written document supporting this assertion.

Based on the above, OIG is not complying with the procedures and internal controls established to assure that purchases made with the IMPAC credit card are proper and that approval is documented.

Recommendations:

The following recommendations for the Office of Management and Policy should bring OIG into compliance with procedures and internal controls established for IMPAC credit card purchases:

1. Remind offices of procedures established in HUD Handbook 2212.1, REV-2 for approving statements in a timely manner and maintaining copies of supporting documentation. A second or alternate approving official should be assigned to approve the statements in the absence of the approving official.

2. Obtain written authority from the Office of Administration to purchase ADP equipment with the credit card. If this written authority is not received, OIG should comply with the provision not to use the credit card for this purpose.

3. Remind offices of the $2,500 limit placed on purchases and the prohibition on splitting purchases to remain within that limit.

The official system for reporting Operation Safe Home funding showed that funds were being committed and obligated, but these commitments were slow in being liquidated and reported as expended.

The Office of Investigation was allocated $2.5 million in Fiscal Year 1996 and $5 million in Fiscal Year 1997 for Operation Safe Home activities. This is no-year money and as such is not lost at fiscal year end. As of July 10, 1997, the FFS reported the following regarding the total Operation Safe Home allocation of $7.5 million:

- $2.7 million has been committed
- $1.8 million has been obligated
- $0.9 million has been expended
- $2.1 million was uncommitted/unobligated

Only $900,000 or 13 percent of the $7.5 million allocated for Operation Safe Home was reported as expended in FFS as of July 10, 1997. This means that $6.6 million or 87 percent of Operation Safe Home funds were reported as unexpended in FFS on this date. The $4.5 million of commitments and obligations were slow in being liquidated. The Office of Investigation has given several reasons for the slow liquidation of obligations and reporting of Safe Home expenditures. They include:

- Memorandums of understanding with local police departments call for reimbursement of overtime expenditures. Funds cannot be disbursed until police departments submit invoices with supporting documentation requesting reimbursement for services provided.

The police departments have been slow in producing the necessary invoices and documentation.

- It is difficult to estimate the amount of funds a task force will need for evidence buys and information purchases. This amount may be over estimated and result in an obligation that is too large.

- SACs have been delayed in purchasing larger equipment because it is necessary for these purchases to go through proper procurement channels which can be time consuming.

- Investigative assistants have had training on FFS but many still don't know what their responsibilities are when they receive invoices. Because of this, invoices remain in the field office for a long time prior to being paid.

Our review of two task forces in one office illustrates this point. The two task forces began during Fiscal Year 96 and obligated a total of $201,122. As of July 1997, only $6,090 (3 percent of the total obligated) had been reported as expended for these task forces. In another office, $44,000 was obligated for a one year task force that was to expire on August 4, 1997. As of July 24, 1997, the task force reported only $4,775 as expended.

This has resulted in Operation Safe Home funds that were slow in being liquidated and reported as expended. Some task forces may not be operating as originally planned or may not need the total amount of funds originally obligated. As a task force progresses, experience should provide information about whether the total amount obligated will eventually be expended. If the total obligation is not expected to be expended, an amount can be de-obligated. This would more accurately reflect the status of Operation Safe Home funds and provide management with better information when making funding decisions.

Recommendations:

We recommend that the Office of Investigation take the following steps to improve administration of Operation Safe Home funds:

1. By March 31, 1998, the Office of Investigation should perform a review of Operation Safe Home obligations in order to determine if all task force obligations are still valid and likely to be expended. Any obligations not likely to be expended should be de-obligated and made available for use by other Safe Home operations. For task forces with valid obligations that are slow in being expended, a legitimate reason for the slow expenditure should be documented in order to justify not de-obligating the funds. We further recommend that the Office of Investigation perform a similar review of Safe Home obligations at least quarterly to determine their validity.

2. Remind local police departments of their responsibility to promptly provide invoices and supporting documentation for expenditures relating to Safe Home operations. Task force agreements should be for a specified period of time and should include a clause setting a

deadline after which invoices for the task force will not be accepted or reimbursed. This deadline should be no longer than three months after expiration of the task force. If a task force still has funds obligated when the deadline is reached, they should be de-obligated and made available for use by other Safe Home operations.

3. Investigative assistants should be reminded of their FFS responsibilities and should process invoices in a timely manner in accordance with these responsibilities.

4. In formulating future budget requests for Operation Safe Home, the Office of Management and Policy should consider the availability of funds from prior years' appropriations.

Various conditions existed regarding Operation Safe Home expenditures.

Our review of Safe Home expenditures revealed a number of issues. First, supporting documentation for some expenditures was not available for review. Also, we concluded that some of the support that was available was inadequate. In addition, advances were made for task forces whose agreements called for cost reimbursements and expenditures were made for task forces that did not have agreements outlining the responsibilities of the parties. Moreover, offices expended funds for task forces and did not maintain copies of the task force agreements or the agreements were not signed by the other agency.

This occurred because formal written procedures were only recently established to control the expenditure of Operation Safe Home funds. Offices were given procedural guidelines which in many cases were distributed by CCmail. It is not known whether these guidelines were viewed as being authoritative. Based on the variety of methods offices have employed regarding Safe Home expenditures, it appears that offices did not view the guidelines as authoritative.

Guidelines that were set forth state that use of Operation Safe Home funds are limited to combating violent crime in public and assisted housing and cannot be used for normal operations or administrative expenses. This increases the importance of having adequate documentation to support expenditures.

For the situations where there was a lack of or inadequate supporting documentation, offices did not have records to prove that Safe Home expenditures were used for their stated purpose. When task forces did not have valid agreements there was no official written document governing expenditures made by the other agency to ensure that they are in accordance with the stated purpose of Operation Safe Home. Advances made on cost reimbursable agreements were not in accordance with the agreements and unless the other agencies provide an accounting of how advances were expended, OIG has no documentation to prove that expenditures were in accordance with Operation Safe Home rules.

Recommendation:

The Office of Investigation, in an August 27, 1997 memorandum to Special Agents in Charge of investigation offices, issued final procedures and policies relating to Operation Safe Home funds control. These procedures, if implemented as written, will address the condition noted regarding Safe Home expenditures. Paragraph 5 of this memorandum establishes specific procedures for requesting Safe Home funding and setting up task forces. It states the types of expenditures Safe Home funds will cover and requires appropriate documentation to support expenditures. Paragraphs 6 on processing requests for Safe Home funds and 7 on financial controls, establish controls over Safe Home expenditures. Paragraph 8 on using cooperative agreements states that funding for such is typically on a reimbursable relationship. We strongly recommend that the Office of Investigation implement the procedures and policies contained in the August 27, 1997 memo and enforce its provisions.

Rules regarding government owned and leased vehicles were not strictly enforced.

Rules for the use of government owned and leased vehicles were not strictly enforced by offices. OIG employees were using these vehicles for transportation between home and office without proper written justification and approval. Also, not all offices were maintaining an inventory of these vehicles. In addition, a review of vehicle records in one office led us to question the necessity for having two vehicles. The two vehicles were driven a total of 2,054 miles over a period of 16 months.

Offices only recently became aware of restrictions regarding the use of government owned and leased vehicles for transportation between home and office. They state that this usage is necessary for the efficient performance of their law enforcement duties but were unaware of criteria that had to be met for such use. At the time of our review, the Inspector General was in the process of developing a written policy. Offices who were not maintaining an inventory of these vehicles did not have knowledge of the requirement. As far as the necessity for having two vehicles, the office has agreed that two vehicles are not needed and has taken action to return one.

Recommendations:

1. On August 8, 1997 the Inspector General issued procedural requirements for the approval of home to office use of government vehicles for law enforcement duties. This includes quarterly certifications by first-line supervisors and annual certifications by second-line supervisors. The Office of Investigation needs to ensure that this policy is strictly adhered to.

2. The Office of Management and Policy should remind offices of their responsibility to maintain an inventory of government owned and leased vehicles under their control. The continuing need for such vehicles should be assessed on an annual basis.

Controls regulating advances of Safe Home funds to special agents for evidence or information purchases were lax.

Advances of Safe Home funds using the American Express debit cards were not always used for their stated purpose of evidence or information purchases. Offices were using these advances to purchase supplies and equipment. In addition, some advances were given verbal approval and this approval was not documented. In another situation, the supporting documentation for advances was maintained by the field agents who were not documenting expenditures or reporting outstanding balances to the district office on a regular or monthly basis. We also found situations where supporting documentation accompanied the advance but did not contain adequate information such as the related task force or the evidence or information purchased.

A memorandum from the Assistant Inspector General for Investigation dated September 5, 1996 established basic procedures for controlling the use of the debit cards. The memo stated that debit cards should only be used for drug buys or informants on projects or task forces that have been approved by Headquarters. This memo gave primary responsibility for establishing procedures and maintaining adequate documentation and ensuring appropriate use within the approved budget to the Special Agent in Charge of the district office.

Lack of specific policies and procedures governing the use of the American Express debit card has led to the conditions that existed in the field offices. There were no uniform internal controls or documentation requirements established to provide procedures for the use of the American Express debit cards.

This has resulted in some advances not being in accordance with the general guidelines established for their use. Moreover, the lack of uniform procedures and internal controls has led to a variety of methods for administering this program. This includes everything from approving advances to documentation requirements and the return of any unused amounts.

Recommendation:

The Office of Investigation, in its August 27, 1997 procedures and policies relating to Operation Safe Home funds control, if implemented as written, will address the condition noted in this finding. Paragraph 12 sets forth specific purposes for which advances can be used. Paragraphs 13, 14, and 15 establish specific procedures and controls for the requesting, approving, safeguarding, documenting and returning unused advances. We strongly recommend that the Office of Investigation implement the procedures and policies contained in this memo and enforce its provisions.

Procedures established to control ADP equipment were not being enforced.

Internal controls established for maintaining ADP equipment were not being enforced in all offices. Various conditions existed regarding the maintenance of ADP equipment. Some offices were not maintaining an inventory of all ADP equipment or the inventory was not current. Offices did not always maintain custody receipts for notebook computers. One office assigned a notebook computer to a non-OIG employee of HUD and no custody receipt was signed by the employee. Also, field office and headquarters ADP inventory lists did not agree. Another point regarding ADP equipment is that there was no hard plan which states the number and types of equipment to be purchased during the fiscal year. Instead, a minimum standard for equipment was set and purchases were made if they met this standard and funds were available. This has led to many purchases taking place at the end of the fiscal year which gave the appearance of year-end spending.

OIG Manual Chapter 1054 establishes controls over microcomputers, associated hardware, software and documentation. It states that such equipment should be included in a local and central inventory. It also states that employees must sign custody receipts for portable computers assigned to them.

Because all offices were not maintaining a current inventory of all ADP equipment or requiring custody receipts for notebook computers, OIG was not in compliance with procedures established to control ADP equipment. Should equipment be lost or stolen, recovery or replacement of this equipment would be more difficult. This would be especially true in the case of custody receipts, if it is concluded that an employee is to blame for lost equipment.

Recommendations:

1. We recommend that the Office of Management and Policy remind offices of their responsibility to follow the provisions of OIG Manual Chapter 1054 regarding ADP equipment. They should remind offices to pay particular attention to the section on inventory control and maintain a current inventory, keep Headquarters advised of any purchases made and require custody receipts for all portable equipment assigned to employees.

2. As far as purchasing ADP equipment is concerned, the Office of Management and Policy should establish a more detailed plan. This plan should give more detail about the number and type of equipment to be purchased during the fiscal year. Planning for the purchase of this equipment should be spread out over the course of the fiscal year.

MINOR FINDINGS

Problems with processing travel vouchers were discovered.

Some problems in the processing of travel vouchers were discovered during our review. Some offices did not maintain copies of all vouchers. In some cases a copy of the travel order was not maintained. Other vouchers were not supported by necessary invoices. In other offices, the copy of the voucher maintained by the office did not contain evidence of supervisory review and approval. Another office had telephone charges which were not supported by charges on hotel receipts. Offices have given various reasons for the above conditions. They stated that the originals contained all the necessary documentation and approvals, the accounting office would not process the vouchers without all the necessary documentation and signatures, and they did not want to bulk up their files with copies of the supporting documentation for travel vouchers.

OIG Manual Chapter 1031 on records management states that files should be retained by subject, such as travel. It goes on to state that copies of travel vouchers should be maintained. It does not state that the voucher should include all supporting documentation. However, good business practices would require maintaining signed copies of vouchers and supporting documentation in case the original travel voucher is lost. This would facilitate quick replacement of the voucher.

As a result of the above conditions some offices of the OIG were not in compliance with records management requirements of OIG Manual 1031. In addition, they were not following good business practices by not maintaining signed, complete copies of the vouchers and supporting documentation.

Recommendation:

The Office of Management and Policy should remind offices of their records management responsibilities. Offices should be told to maintain signed copies of vouchers and clarification should be given on the extent of records to be maintained with travel vouchers.

Some offices were not complying with requirements for maintaining office equipment.

Some offices we reviewed were not following required procedures for maintaining office equipment. In some cases the offices were not maintaining an inventory control system or the inventory list was not current. One office did not require agents to sign out equipment, such as cameras or VCR's, used by them on a temporary basis.

OIG Manual Chapter 1120 requires that offices establish and maintain a furniture and equipment inventory control system. Good business practices would require custody receipts for equipment assigned to employees on a temporary basis.

Because some offices were not following requirements for maintaining office equipment these offices may have a difficult time establishing responsibility or recovering on lost, stolen or destroyed equipment.

Recommendation:

We recommend that the Office of Management and Policy remind offices of their responsibilities under OIG Manual Chapter 1120 to establish and maintain a furniture and equipment inventory control system. This system should require that custody receipts be maintained for equipment assigned to employees on a temporary basis.

A few instances of problems with procedures regarding Law Enforcement Availability Pay (LEAP) were discovered.

Our review of LEAP records in one office found that there were discrepancies between the Investigative Case Management System (ICMS) monthly report and the agent's monthly LEAP report. Reconciliations of these two reports were not performed and the discrepancies were not discovered until our review. In another office, one of the three months of LEAP reports we attempted to test was not maintained. Also, we found that not all agents were retaining daily time records to substantiate their LEAP.

IG Bulletin 95-IG-01 states that the supervisor will perform a monthly review of each criminal investigator's hours worked. It states that appropriate supporting documentation should be generated using existing ICMS case hour input forms and report summaries. Although not required by regulation, agents should maintain some form of daily time records to substantiate LEAP.

This condition has resulted in these offices not being in complete compliance with LEAP documentation requirements and could lead to questions as to whether all agents performed the hours required for LEAP.

Recommendation:

The Office of Investigation should remind their offices of procedures required to perform monthly reviews of each criminal investigator's monthly LEAP report and appropriate reports from ICMS. Also, the Office of Investigation should require that all agents maintain some form of daily time records to substantiate LEAP. In a revision to the Investigation/Operations Manual dated September 12, 1997 the Office of Investigation requires that criminal investigators track and maintain a record of availability hours. However, it stops short of requiring that the record be maintained on a daily basis. We feel this requirement could be strengthened by requiring daily record maintenance.

Training process was not in complete compliance with established procedures.

The training process in many offices was not in complete compliance with established procedures because Individual Development Plans (IDP) were not complete or not current. In addition, we found that one office was not maintaining training records for all agents located in that office.

OIG Manual Chapter 1092 requires IDPs for all OIG employees.

Offices have stated that they thought IDPs were no longer required. They said it was their understanding that the new OASIS system made IDPs unnecessary.

As a result, employees are receiving training without formal planning. This could lead to employees receiving training which is not job related or will not enhance their performance.

Recommendation:

The Office of Management and Policy should determine if the training module in OASIS will adequately replace IDPs. If so, OIG Manual Chapter 1092 should be revised to reflect this change in policy. If it is determined that OASIS will not adequately cover planning, the Office of Management and Policy should remind offices of their responsibility for maintaining IDPs for all employees. Offices should also be told that they are responsible for maintaining training records for all employees.

OTHER ITEMS

We also encountered two other minor situations. One was that an evidence log maintained by one office did not contain enough information to adequately identify the evidence or its location. To remedy this, the Office of Investigation should remind offices that information contained in evidence logs should adequately identify the evidence and its location.

The other situation involved one office not performing unannounced counts of the cash/imprest fund at the location. This would be remedied by periodic cash counts being performed and documented by someone other than the responsible cashier. The Office of Management and Policy should remind offices that if they hold a cash/imprest fund a periodic (at least quarterly) unannounced cash count should be performed on the fund by someone independent from the responsible cashier.

Appendix A

STATISTICAL SAMPLE RESULTS

We tested transactions for both the Salaries and Expenses and Operation Safe Home appropriations in order to ascertain whether expenses recorded in these two appropriations were accurate. To accomplish this, we determined the maximum amount of errors that could have occurred during the period under audit. We selected a statistical sample of transactions from the audit period of October 1, 1994 through March 31, 1997 for each appropriation. We used stratified random sample methodology to select transactions for testing. Our statistical sample did not include payroll and travel expenditures because they were tested separately using a judgmental sample. Following are the results of our statistical sample for each appropriation.

For the Salaries and Expenses appropriation, our population totaled $22,240,557 in expenditures. Based on our sample, we concluded with 95 percent confidence that errors in these accounts (due to expenditures that were in error, not allowable or not reasonable) did not exceed $7,486. This equates to less than 0.1 percent of the tested population. For the Operation Safe Home appropriation, our population totaled $946,450 in expenditures. Based on our sample, we concluded with 95 percent confidence that errors in these accounts (due to expenditures that were in error, not allowable or not reasonable) did not exceed $16,047. This equates to less than 1.7 percent of the tested population.

As part of our statistical sampling we also tested internal controls in the Salaries and Expenses and Operation Safe Home appropriations to assess whether controls to ensure that transactions were properly recorded and assets were adequately safeguarded from loss or misuse were functioning as intended. For Salaries and Expenses expenditures, we tested sample transactions as to whether they were: (1) properly planned, (2) supported by vendor invoice where appropriate, and (3) approved by an authorizing official. If one or more of these conditions was not met for a given transaction, the transaction was considered an exception for purposes of evaluating our sample results. Based on this testing, we concluded with 95 percent confidence that the exception rate for Salaries and Expenses expenditures was at least 4.2 percent.

For Operation Safe Home expenditures, we tested transactions as to whether they were (1) properly planned, (2) supported by vendor invoice where appropriate, (3) approved by an authorizing official, and (4) covered by a cooperative agreement approved by Headquarters, where appropriate. If one or more of these conditions was not met for a given transaction, the transaction was considered an exception for purposes of evaluating our sample results. Based on this testing, we concluded with 95 percent confidence that the exception rate for Operation Safe Home expenditures was at least 12.6 percent.

To the extent that we considered these internal control deficiencies significant, we discussed them in the body of our report.

Appendix B

NUMBER OF OFFICES WHERE MAJOR FINDINGS OCCURRED

Following are the findings that we classified as Major followed by the number of offices where at least one of the items mentioned in the finding occurred:

- Offices were not performing periodic reconciliations of amounts charged to their budgets. (15 offices)

- Payroll processing procedures and controls were not consistently followed by offices. (22 offices)

- OIG usage of the International Merchant Purchase Authorization Card (IMPAC) credit card was not always in accordance with established procedures. (19 offices)

- The official system for reporting Operation Safe Home funding shows that funds were being committed and obligated, but were slow in being liquidated and reported as expended. (5 offices)

- Transaction testing of Operation Safe Home funds revealed a number of conditions including lack of or inadequate supporting documentation, advances made for task forces that had cost reimbursable contracts, and expenditures for task forces that did not have agreements. (6 offices)

- Rules for the use of government owned and leased vehicles were not strictly enforced by offices. (13 offices)

- Controls over Operation Safe Home advances to special agents for evidence or information purchases were lax. (4 offices)

- Some offices were not enforcing established procedures for controlling ADP equipment. (17 offices)

Appendix C

REPORT DISTRIBUTION

Deputy Inspector General, GD

Counsel to the Inspector General, GC

Assistant Inspector General for Management and Policy, GF

Assistant Inspector General for Investigation, GI

Deputy Assistant Inspector General for Audit, GA

Deputy Assistant Inspector General for Investigation, GI

District Inspectors General for Audit, GA

Special Agents in Charge, GI

Mr. TOWNS. I yield back.

Mr. SHAYS. There are different elements of this hearing that we're not going to get into in depth. I mean one is how much. Should there be any contracting and at what level? I don't care to get into the debate now about that because we have to vote—a lot of time on that policy issue. What I care about is determining what, under present law, is allowed to be contracted out and then how well we oversee it.

What I hear is a pretty devastating report that HUD contracts out and doesn't do very good oversight, doesn't have the people capable to do the oversight, and even if it has the people capable, they seem incapable of following through and making sure that people who are paid for services actually do the job. It's pretty serious, and we're not talking about a few million dollars; we're talking really in terms of billions of dollars.

Just very briefly, I have three urban areas I represent, and our public housing authorities are pretty good, but one was on the troubled list and was taken over by HUD; and we spent literally tens of millions of dollars, if not over $100 million, and we had to redo what was sent to the Bridgeport Housing Authority because it was done so poorly.

We have a new housing director who for the last 10 years—11 years—has taken money, and he spent it so well, and what I see are beautiful facilities, well run and well kept; and I am very proud of what we did with our public money.

So, we are sending lots of money to the housing authorities, and we want to make sure they're overseen well. I'd also say for the record that this committee has not provided the kind of oversight of HUD in the last few years because we feel we've had two very good secretaries, and we have five different departments we look at, but we give a lot of weight to what both of you have done—your agencies have done—and feel our contribution is just making sure that your story hears the light of day because we are seeing HUD start to respond to it.

What I am hearing, though, is that our responsibility in the next year is to make sure that they carry out on their plans, and if they carry out on their plans, rather than our criticizing them for past deeds, we are going to congratulate them for what they found and just move from there.

So, we have capable people managing HUD. They've come into a culture that's difficult, and we are going to just make sure that they do their job, and we are going to obviously speak with Mr. Carberry and find out what he thinks about his challenges.

Let me just ask this question: How do we distinguish between what can be done and what can't be? I guess what we do is we say there are certain prohibitive services. Aside from the service that we do, that we contract out, how well do we over see them, but there are some services we can't get into: personal service contracts, advisory and assistant service contracts, State legislative initiatives, and contracts to perform inherently governmental functions.

This would probably be where Mr. Kucinich and I would probably get in our debate as to what is inherently government service. Is the third area the one where we would tend to have the biggest

dispute; where you might have the biggest disagreement with HUD? I mean the first two, you know what's prohibitive, but what about in this third area of prohibition, contracts to perform inherently government function. Give me an example of where you might draw the line and where HUD might draw the line; where you'd have a disagreement.

Mr. MOMORELLA. Yes, Mr. Chairman, that's correct. That was one area where we do have and still have a disagreement. The Department has agreed that they will reaffirm the policy that's spelled out by the Office of Federal Procurement, the guidelines for this area with all the procurement officials and the programming officials and the Deputy Secretary has done that.

However, we have not yet received and are looking forward to keeping the specific reasons why they disagree. Once we review those, on the specific cases that we brought up, we will then possibly be asking the Office of Management and Budget, whose rules they are, who wrote the rules, to decide if in their opinion——

Mr. SHAYS. Yes, I want to ask——

Mr. MOMORELLA. We have an opinion and HUD Program has an opinion.

Mr. SHAYS. I want to ask Mr. Czerwinski if the GAO has gotten into this issue. I mean, I would gather that my colleague from Cleveland might decide that he would want to err on the side of providing as many prohibitives and giving HUD an inherent responsibility to do a lot more than others may, but is HUD erring on the side of not contracting out too much or contracting out too much in what some might call an inherent government service?

Mr. CZERWINSKI. We haven't gotten into the area of compliance for what is contracted out or not. Back about a year or two ago, House and Senate Banking and Senate Appropriations came to us and asked us to get into issues such as these. However, the time the inspector general was doing it, was just in the process of starting up a very broad-based audit and contracting.

So rather than duplicate their efforts, what we agreed to do is to do two things: One was to focus, in detail, on the specific contract of REAM's and illustration, and two, then later on do the review that we did for you, Mr. Towns, on HUD's 2020 to get a feel for the overall management.

So what I would add is a little bit different perspective, and that is to look at the cost-benefit issues of deciding when or when not to contract out, and I would probably then throw in maybe four or five criteria that you might want to consider when you talk to HUD to oversee how they're doing that, because really it becomes a management decision.

So the first criterion that I would throw out would be the overall vision that HUD has for contracting as well as the commitment from the Secretary because for Mr. Carberry to do his job, he really needs that commitment, because you really have to reconcile the interests of the contracting office versus the program office, as Ms. Gaffney talked about, and that's essential. So that's the first one.

The second one is: What plans are in place to carry out this vision?

The third is: Well, once you are carrying it out, you have to monitor contracts, but you can't monitor every single one. So you have to choose. So what priority setting does HUD have?

The fourth is: Even if you set your priorities, you need the resources. So I would ask: What kind of resource commitment the Secretary is giving Mr. Carberry to do his job.

And the final one is, even if you have the resources, you must have the information. How good are HUD's data? How much do they have and how reliable are those data and what are they doing to ensure that reliability?

So that's sort of the management perspective that we have versus the compliance view.

Mr. SHAYS. OK.

Ms. GAFFNEY. Maybe I could help you.

Mr. SHAYS. Then I'll get to my colleagues, and we'll get to the next panel. Yes.

Ms. GAFFNEY. I think you are right, that there is ambiguity in this area. I don't think it's a huge problem in terms of inherently governmental functions and contracts for them, but the kind of thing that we question is using a contractor to prepare congressional testimony. We consider congressional testimony essentially——

Mr. SHAYS. Does that happen?

Ms. GAFFNEY. That has happened. Now HUD's answer to that would be, "We just had the contractor doing drafts, you know. We really had final approvals so there's nothing wrong with a contractor working on congressional testimony." I don't think that kind of issue is a huge issue. I think it happens in isolated——

Mr. SHAYS. Yes, it's not a huge issue and I am happy it is not happening often, but the bottom line is I would think that almost anyone reading the law would say that was improper.

Ms. GAFFNEY. I think that's right.

Mr. SHAYS. We have two other panels——

Mr. KUCINICH. I'll try to be brief, if I may, Mr. Chairman. I looked at Ms. Gaffney's testimony, and there are a few things that strike me, and I'd just like to share this with the members of the committee. It seems that when—Ms. Gaffney writes—the Department has committed itself to prospective corrective actions but has not embraced the opportunity to right past wrongs and extract an exact accountability for them, and then you go on to talk about the current efforts to improve HUD contracting.

What I see here, Mr. Chairman, is the offer by HUD in their efforts to improve contracting is the form of a solution but not necessarily the substance. We have a form of a solution through a chief procurement officer being appointed; yet, as Ms. Gaffney points out, there has been no official definition of Carberry's authorities, responsibilities or placement in the organization, no effort to get advice from the IG's office and counsel up front——

Ms. GAFFNEY. Mr. Kucinich, could I just interrupt for 1 second? The definition of his roles and responsibilities happened yesterday, just the day before this hearing, and it wasn't an appropriate definition.

Mr. KUCINICH. Well, we are making progress.

Ms. GAFFNEY. That's good news. That's good news.

Mr. KUCINICH. So your testimony then would be corrected to indicate that——

Ms. GAFFNEY. It happened after my testimony, yes.

Mr. SHAYS. But the record should state that, and you did state that you were pleased, but the statement here does not reflect what you said.

Ms. GAFFNEY. No, that's correct, but the second part of what you are reading, which is we have yet to see a definition of the Contract Review Board's charter, all those other things. That remains correct.

Mr. KUCINICH. OK, then let me continue. We have the form of a solution with a chief information officer, and yet we see no official definition of those authority's responsibilities are placed in an organization. Is that still correct?

Ms. GAFFNEY. That's correct.

Mr. KUCINICH. And we have the form of a solution with a contract management review board. See, I have to tell you, I am not as optimistic about what I am seeing here. I don't see a—this is a problem with some kind of bureaucratic schematic. I see it as a virus that infects every decision that's made at every level because you start with the logic of a system which is set up guaranteeing—where contractors are contracting out the contractors, lack of control by HUD, and it's good news that they have defined some responsibilities for Mr. Carberry. We will be looking forward to hearing him, but I don't know if HUD's learned anything.

Frankly, Mr. Chairman, it's going to be—it'll remain to be seen whether HUD has learned anything at all from any of this, instead of just coming up with cosmetics, and this is, you know, I too represent an urban area where there's a lot of people who live in public housing and in Government-subsidized housing, and people depend on us to be able to see government work.

And I am a supporter of the administration, generally speaking. I am very concerned when I see these pictures, but it's not just the pictures. I've seen it in my own district, and I see it in lack of control over Government programs which impact on people's lives. I want the administration to know, cosmetics are not going to work here.

There needs to be some—apparently, in my view, there need to be some structural changes in the way that HUD is doing business, and simply doing the same old thing a different way isn't going to cut it. I want Mr. Cuomo to understand that. Cosmetics are not going to work here, and if you think you can come—if HUD thinks it can enter into this by just appointing some committees and giving someone a title and no responsibilities will not work.

I just want to say that, on behalf of the people I represent, who live in subsidized housing and who are not getting the services they ought to be getting or who are not being taken care of in the way they ought to, where the Government is passing off its responsibility, I happen to think Government can work. I really believe it can, but I also believe that we have a process here that is out of control. So that's my homily for the day.

Mr. SHAYS. If Mr. Towns is not objecting, I think what we'll do is get to the next panel. You've introduced this issue nicely, and I know you've been in contact with our staff on a lot of these issues.

So we've gone into it in greater depth in our committee with our staff work.

I'll just end by saying, is there anything that any of the four of you would like to say before we go to the next panel? OK, thank you very much.

Our next panelist is Stephen Carberry, the Chief Procurement Officer, Department of Housing and Urban Development; accompanied by Howard B. Glaser. And I'd invite both of you to come forward and remain standing and I'll swear you in.

Mr. KUCINICH. Mr. Chairman, I don't know Mr. Carberry, but I know HUD.

Mr. SHAYS. I know that. [Laughter.]

If you would stand, please.

[Witnesses sworn.]

Mr. SHAYS. Mr. Carberry, just before you start your testimony, I just want to make sure we have the proper perspective. You are hired as of when? How long have you been working at HUD?

Mr. CARBERRY. About 2½ months. I came on March 17.

Mr. SHAYS. We all recognize that you've been in for 2½ months, and we know that you have tremendous expertise in this area because of your past employment, but we know that you are just getting your feet wet in a sense. The bottom line is we recognize you've been in 2½ months.

Mr. CARBERRY. Thank you, Mr. Chairman.

Mr. SHAYS. And we welcome your testimony and we look forward to having a dialog with you.

STATEMENT OF V. STEPHEN CARBERRY, CHIEF PROCUREMENT OFFICER, DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT, ACCOMPANIED BY HOWARD B. GLASER, DEPUTY GENERAL FOR PROGRAMS AND REGULATIONS

Mr. CARBERRY. All right, thank you.

Secretary Cuomo had taken a personal, intense interest in procurement reform at HUD. That's why he generated the system of the Chief Procurement Officer. That's why I am at HUD. I came here because I am convinced that HUD really wants to do it well, they are going to do it well, and they have the resources to do it well.

I'll go through some of the elements of what we plan to do. What we don't have a problem with is whether or not this agreement on the definition of the procurement problem at HUD. There is no disagreement on that. IG, GAO, NAPA, everybody has looked at it. We all agree. And I have come for 2½ months. We all see the same things and agree that, yes, they have their serious problems and they need to be taken care of.

What we are having a disagreement on? What are the processes needed to improve the process? Mr. Czerwinksi had said it earlier; it depends on what we do now and we'll be doing that. We have not done a good job of needs assessment. We have not done a good job in procurement planning. Contracting oversight and monitoring has not been what needs to be done.

What we have not followed is fundamentally sound business practices. That's been changed. First the Department indicated that—or declared that—procurement was a major weakness, and

this makes it clear to everybody at HUD that that has to be improved on.

I've been named as the chief procurement officer. I have both the authority and the accountability for fixing the problem. I don't have any reservations whatsoever with regard to the authority that Secretary Cuomo has given me and given to the whole Department to get this fixed. And I am going to be here a year from now, and longer, and I'll be able to come back and tell you, "This is what we've done instead of talking about it." This is to some extent the easy stage.

Mr. SHAYS. Well, the thing you need to remember is that I may not be chairman. It may be Mr. Towns or Mr. Kucinich, but we'll all be here. We just may be moved over.

Mr. CARBERRY. All right.

Mr. TOWNS. Thank you very much, Mr. Chairman, for that comment. Thank you very much. [Laughter.]

Mr. CARBERRY. But there won't be any change on this side of the table.

Mr. SHAYS. No, but what Mr. Towns doesn't know is maybe Mr. Kucinich might be the chairman instead of him. [Laughter.]

Mr. KUCINICH. I want Mr. Shays to know that I am comfortable if it's Mr. Shays or Mr. Towns.

Mr. CARBERRY. One of the things we've established is the contract management review board, and what we're doing is designing end quality management and business functions at the very beginning of processes.

No programs are going to be approved unless they have come forward and gotten approved in terms of what their proposed cost schedule performance parameters are going to be, and that's simply: how long is it going to take, how much is it going to cost, and what are we going to get for it. They are all measurable.

We are going to use those measurements to approve a program. We are going to make sure that the programs are properly staffed. We are going to make sure that the team that's supporting that program is properly trained, and we are going to use those measures on an annual basis to go back and review this to see what extent those parameters are being met, and we are going to use them ultimately to see whether or not we've had a successful program.

These are the kinds of things that DOD has been using for many, many years. They are effective in working on these. Private industry uses the same things, and we'll be doing that at HUD.

A big change again that's occurring—this is the first time it's going to in HUD—in the program offices we're going to going to have full-time GTRs, full-time people responsible for program and contract management. In the past that's been an ancillary function, and it's been given marginal support.

And to a great extent I think people do exactly what they are told to do and what they are managed to do, and what we are telling and managing people to do is that this is critical, once we award those contracts we have to make sure we got what we've contracted for.

There's no way in the world we can award a contract so well and so perfectly, and if it's not properly managed after contract award,

we can't lose all the things that we got for the good contract award. So we have to finish off what we start.

Also for the first time in history we are going to have mandatory training of the people both in contracts, which we've had in the past, and also of the people in the program offices. We're going to train them separately. We are also going to train them individually—excuse me, as a team. We're going to do just-in-time training.

We expect a lot of these people to work as a team. We are going to make sure they have the individual skills that they bring to the team, and we're going to make sure they have the team skills to make sure they can work together as a team, with the team headed up by the project manager.

We're also adding an integrated financial system. It's been mentioned before—certainly this morning by GAO—but good management is dependent upon good data. We have a system that's going to provide that data. We are also going to train people to learn how to use it.

And last, and this is a critical one, we're trying to change the culture at HUD so that the problems we've seen in the past, which may well have been systemic, aren't. And I think we've got a good beginning for making those changes.

The IG reports—and even before I got hired I went through and reviewed those—they involve about $1.1 billion that were contracted for before 1983, and some of them even go back as early as 1984, but I also believe that some of the same problems that caused those still apply.

We have not done well in the management of our programs and our contracts, and one of the reasons I'm at HUD personally is to make sure that changes. Secretary Cuomo has said that the contracting function at HUD has been a poster child on how not to do it, and for my 2½ months I think he's right. We don't need to turn everything around, but there's a lot of awfully smart, capable people at HUD who want to do the right thing.

The timing is right at HUD. HUD is changing in so many different ways, and the concept that HUD needs to change significantly and radically is complete throughout the whole organization, that when you raise a problem as has been raised by the IG that these are problems that need to be fixed, we lose our credibility entirely as a department unless we get them fixed.

Now if a program needs to be contracted out, therefore it's important to the Department we need to put the resources on it to make sure we get what we contract for. Those things are now being understood, and changes are occurring relatively rapidly. I am optimistic.

I really came to HUD to make this all work, and I plan to see that that's the case. Now with me is Howard Glaser, who is the deputy general counsel for HUD, and he's also on the Contract Management Review Board that will be reviewing all the programs, both in their initiation and throughout their life.

If you have any questions, I'd be glad to answer them.

[The prepared statement of Mr. Carberry follows:]

Statement For V. Stephen Carberry
Oversight Hearing

HUD Contracting

Good Morning, Mr. Chairman and members of House Subcommittee on Government Reform and Oversight. I am V. Stephen Carberry, Chief Procurement Officer (CPO), of the Department of Housing and Urban Development (HUD).

On behalf of Secretary Cuomo and the Department, I appreciate the opportunity to come before you on HUD's procurement reform initiatives.

I recently came to HUD from the Navy where I worked for 34 years in contracts. I have been assigned to all three of the Navy's major systems acquisition commands, and for the last ten years, I was the Executive Director for Contracts with the Naval Air Systems Command and responsible for annual obligations from $9 to $12 billion. The position of HUD Chief Procurement Officer, for which I have been selected, was recently created by Secretary Cuomo to lead the efforts on HUD procurement reform.

Secretary Cuomo has taken an intense and personal interest in procurement reform at HUD. In the HUD 2020 Management Reform Plan, he directed that the Department engage in a top to bottom redesign of the HUD procurement system with an emphasis on safeguarding taxpayer dollars with a system that ensures quality and value. In addition, Congress gave its support to HUD by authorizing the agency to retain

National Academy of Public Administration (NAPA) to assist with the procurement redesign.

Our review of the HUD procurement system indicates two fundamental weaknesses. First, the Department has done a poor job of needs assessment and procurement planning. Second, contract oversight and monitoring do not receive sufficient allocation of resources or attention. The GAO and IG reviews confirm these findings. To address these weaknesses, the Secretary directed that the Department take a number of concrete steps to improve accountability and performance. A more detailed conclusion of our Action Plan has been included with my written testimony. I'd like to briefly describe the main points of the plan.

First, the Department identified procurement as a material weakness of Departmental management. This step tells Department managers that procurement reform is a top priority and deserves the highest level of attention.

Second, the establishment of a Chief Procurement Officer, responsible directly to the Deputy Secretary and the Secretary, is a strong signal of the importance of procurement management and creates accountability for procurement activities at the highest levels of the agency.

Third, the Department has established a Contract Management Review Board (CMRB) to improve needs determination, planning and monitoring. The CMRB

examines program offices' strategic procurement and staffing plans to assure that they encompass the critical needs of the Department and are not duplicative of other proposed, ongoing or completed work. The CMRB reviews all plans for contracts that will exceed $5 million, including legal review. New programs will be approved only after detailed cost, schedule and performance parameters have been reviewed and justified. For capital asset acquisition, HUD will follow the capital programming principles in OMB's capital programming guide. For service contracting, we will use performance-based service contracting, as appropriate, to reduce costs (including contract administration costs) and increase satisfaction with contractor performance. These same parameters will then be used to evaluate annual performance of the programs and for measuring the success of programs when completed. As the chair of this committee I am currently leading the Board in the review of planned FY 98 procurements. This summer, we will review planned procurements for FY 99.

Fourth, for the first time in HUD's history, contract management will be a full time job. Until now, contract management was minor ancillary duty for staff already overburdened with too many conflicting responsibilities. By creating a core group of full time contract managers in each program area whose only responsibility is contract management, the critical function of contract oversight and management will finally get the attention and resources it deserves. Full-time personnel will manage the cost, schedule and performance parameters of critical HUD programs using earned value management system reporting for capital assets and formal quality assurance plans for

our large service contracts. For critical, complex HUD programs, Integrated Project Teams (IPT) are being established. The IPT is comprised of personnel from the program office, Office of General Counsel and contract specialists, along with other functional specialists, as appropriate. This concept has been used in private industry and other government agencies with great success.

Fifth, the Department is establishing --again for the first time in its history-- mandatory training and certification for these contract managers. This includes both program managers and contracting officers. Our goal is to create the best trained and most professional contract management workforce in the federal government.

Sixth, the Department is well on its way to establishing an integrated financial payments data system to provide contract managers with the information they need through the enhancement of our information systems.

Finally, and perhaps most important, there is a culture change taking place across the board at HUD in which protecting the public trust is seen as a key mission for all employees; with zero tolerance for waste, fraud or abuse of HUD programs.

As the IG audit report indicates, contract problems at HUD are long-standing. In fact, of the $1.5 billion in contracts identified in the audit, $1.1 billion involve contractors with whom the Department contracted prior to 1993. In spite of the fact that these contracts stretch as far back as 1984, the Department is committed to taking aggressive

action now to fundamentally restructure its procurement system.

Mr. Chairman, Ranking Member Towns, I have been a contracting professional for over 30 years. I am confident that the changes the Department is making in its procurement systems will transform HUD from what Secretary Cuomo has called the "poster child" for how not to contract, into a model for federal government procurement activities. Independent objective reviewers including the General Accounting Office, the National Academy of Public Administration, and Booz-Allen all agree that these are the right steps. And implementation is well underway. I am excited about being a part of HUD's management team and I plan to ensure that we succeed.

Thank you.

ATTACHMENT A

ACTION PLAN
Management Improvements in the Contracting Process

- **Needs Determination, Planning and Periodic Assessments.**

The Department will establish a Contract Management Review Board (CMRB) chaired by the Chief Procurement Officer and comprised of senior officials from the Office of the Secretary, the Chief Financial Officer, the Office of General Counsel and the Assistant Secretary for Administration the Office of Policy Development and Research. The CMRB will perform the following functions:

⇒ Review and approve each program office's procurement strategic plan for all new procurements and interagency agreements estimated to exceed $5 Million.

⇒ Conduct periodic reviews of each program office's progress in implementing their approved strategic plans.

Proposed Implementation Schedule:

Appoint CMRB members	Completed.
Hold initial CMRB meeting to adopt rules	Completed.
Hold first business meeting	Completed.
Complete review of procurement components of FY 1999 Business Operating Plans	By September 1, 1998

- **Contract Oversight and Monitoring.**

The Department will improve contract oversight and monitoring by:

⇒ Appointing a Chief Procurement Officer (CPO) who will chair the CMRB, review new contracts and interagency agreements over $5 Million and supervise an ongoing program to improve GTR monitoring performance.

⇒ Implementing a Government Technical Representative (GTR) Certification Program which would:

- Assure that all GTRs have received basic training (the current GTR course or equivalent) in their responsibilities **prior to** their assignment;

- Require advanced GTR training for individuals charged with monitoring large and/or complex contracts; and,

- Require annual contracting-related training to maintain active certification.

⇒ Placing the GTR course on HUDWEB to make it more accessible.

⇒ Developing a performance element to be included in the EPPES of all GTRs.

Proposed Implementation Schedule:

Hire Chief Procurement Officer	Completed
Develop proposals for GTR training, certification and EPPES element.	Completed
Place GTR training course on HUDWEB.	Completed
Issue memorandum to Principal Staff establishing GTR training and certification requirements.	Completed
Major program offices establish full-time monitoring staffs	By September 1, 1998
Provide basic classroom training to full-time monitoring staff.	By September 30, 1998

- **Prohibited Services**

To sensitize staff to concerns related to "personal services" and "governmental functions," the Department will take the following steps:

⇒ Program and contracting staff will be reminded of the prohibitions related to "personal services" and "governmental functions."

⇒ The GTR training course will be revised to incorporate a module with appropriate case studies concerning these areas.

⇒ All new contracting requirements for services will be reviewed by OGC staff to assure their legality.

Implementation Schedule:

Issue memorandum to program and contracting staff concerning these areas.	Completed
Revise GTR training to incorporate a module concerning "personal services" and "governmental functions."	Completed

- **Timely closeout of contracts.**

To simplify the method by which the procurement office initiates audit requests which are subsequently transmitted to the Defense Contract Audit Agency (DCAA). By consolidating audit requests on a ***contractor*** basis (this includes contracts which are under the $500,000 audit threshold) we have requested 104 audits representing $379,463,933.

To assure that backlogs do not develop in the future, we will take the following steps:

⇒ OPC's Policy and Evaluation Division will generate a monthly list of cost-reimbursement contracts which have been completed and follow-up with the operating divisions to assure that audit requests are generated.

⇒ Closeout of cost-reimbursement contracts requiring audits will be reassigned to the Administrative Service Centers after submission of the request.

Implementation Schedule:

OPC's Policy and Evaluation Division generates monthly list of completed cost-reimbursement contracts and follows-up with operating divisions regarding audit requests.	By June 30, 1998
Procedures are established for assigning contracts with requested audits to the Field.	Completed.

- **Improve and Integrate Procurement and Financial Systems**

We will continue to work with FSI team to create interfaces between the HUD Procurement System (HPS) and the accounting system. In addition, we will modify HPS to produce reports which will assist GTRs and contract specialists in their contract monitoring and administration responsibilities.

Implementation Schedule:

Complete new release of HPS which includes improved edits for data integrity.	Completed.
Complete coding for HPS/HUDCAPS interfaces for reservation and obligation.	By July 17, 1998
Interface operational	By October 1, 1998
Modify HPS to incorporate improved monitoring reports.	By December 15, 1998

ATTACHMENT B

GTR CERTIFICATION PROGRAM

Purpose

As the Contracting Officer's authorized technical representatives, the Government Technical Representative (GTR)[1] and Government Technical Monitor (GTM)[2] play critical roles in the success of Departmental contracting.

In the pre-award phase of a procurement, the GTR helps the Contracting Officer ensure that HUD accurately portrays its needs to potential contractors and accurately estimates the cost of the ensuing contract to the Department. The GTR may also assist in the selection of the contractor and in negotiating the final terms of the contract.

Once a contract has been awarded, the GTR is the Contracting Officer's technical "eyes and ears." The GTR monitors contractor progress and the quality of work performed, and guides contractors in using the most efficient, cost-effective methods of performing the contract. When contractor performance is deficient or when problems associated with the technical requirements of the contract arise, the GTR is expected to be the first to know and to quickly alert the Contracting Officer. The GTR is also expected to help the Contracting Officer determine the best remedial action for deficient contracts and contractors. (See Handbook 2210.3, Procurement Policies and Procedures, Chapters 4, 5, 11 and 12.)

Given the critical nature of the GTR's role in the procurement process, HUD staff serving as GTRs must: (1) be thoroughly knowledgeable of the technical areas covered by the contract; **and,** (2) possess a solid fundamental understanding of the Federal contracting process as implemented by HUD.

Therefore, this certification program is designed to ensure that all otherwise technically qualified GTRs receive appropriate procurement instruction sufficient to prepare them to perform their duties.

Training Requirements

Basic Curriculum. *Prior to their assignment*, all GTRs must complete the following courses of instruction, or an acceptable substitution (see below):

Government Technical Representative[3]

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[1]The term "GTR" is a HUD creation. Most Federal agencies use the terms "Contracting Officer's Representative (COR) or Contracting Officer's Technical Representative (COTR). As those names reflect, the GTR is truly the Contracting Officer's representative.

[2]Except as specifically noted, the term GTR shall include GTM.

1 course (40 hours) covering the GTR's role in the entire contracting process, including: contract planning and request; proposal solicitation and evaluation; contractor selection and award; contractor performance monitoring, (including record keeping and technical guidance) and contract administration (including modifications, disputes and terminations); *or*

1 course (20 hours) covering the GTR's role from planning through contract award; *and*,

1 course (20 hours) covering all aspects of contract administration.

Advanced curriculum. GTRs who monitor large (exceeding $5 million) and/or highly complex contracts (or significant portions of such contracts, e.g., task orders over $5 million) are required to complete training in advanced topics such as:

Writing Performance Work Statements, (24 hours) (*Note*: Courses in writing work statement other than performance work statements will be considered on a case by case basis.)

Cost Estimating for Technical Personnel (24 hours)

Evaluating Contractor Performance (24 hours)

GTRs assigned to monitor multiple contracts may also be required to meet the advanced training requirements.

Substitution of other training. The Chief Procurement Officer (CPO) may on a case by case basis, approve the substitution of substantially similar instruction for the requirements listed above. The following are provided as examples of potentially acceptable substitutions for the basic courses. The CPO may approve other courses based upon an individual's expertise and experience.

Introductory course in Federal Procurement with an emphasis on types of contracting most frequently used in HUD (e.g., services vs. supply)

Basic Federal contract administration with an emphasis on services contracts (vs. supply)

Completion of HUD's intranet (HUDweb)-based self-instructional GTR course

[3]Normally, these courses will be offered in-house.

Provisional certification. The CPO may provisionally certify a GTR nominee who has not completed the basic training requirements prior to appointment. The provisional certification will specify the period in which the nominee must meet the requirements. All provisionally certified GTRs shall complete intranet-based self-instructional GTR course. GTRs with provisional certification shall be given priority for placement in the next available formal GTR course.

Experience in lieu of training. As approved by the CPO, relevant experience may be substituted for formal training requirements (either basic or advanced) on a case by case basis.

Management Training. Departmental management personnel with programmatic oversight for contracts are advised to complete a course providing a basic overview of the contracting process and the role of the program office, e.g.,

Procurement for Executives and Managers (1 day)

Re-certification Requirements

To maintain an active status, GTRs must renew their certification every two years. Re-certification requirements include:

Continuing education. This may be met by completing ** hours of procurement and contract-monitoring related training. Such training may include:

GTR refresher courses (HUD-sponsored or external)

HUD's intranet-based self-instructional GTR course (*Note*: the HCA may deny the repeated use of this course if it used as the sole means of meeting this requirement.)

Other procurement-related courses as approved by the HCA; *and,*

Satisfactory performance of GTR or GTM duties assigned during the two-year period.

Lapsed certifications. GTRs whose certification have expired (i.e., not been renewed), will have to complete the requirements for new certification.

Responsibilities:

Certifying GTRs. The CPO shall certify GTRs who have completed all requirements for certification. The cognizant Primary Organizational Head in Headquarters or the cognizant field

program office head shall be responsible for the accuracy of information reported to the cognizant HCA concerning training and past performance of GTRs and GTR nominees.

Maintenance of GTR training records. The CPO will maintain a list of all certified GTRs. The list will be available on the Department's HUDweb Contracting homepages. It shall be the responsibility of personnel appointed as GTRs to provide the CPO with information needed to update and maintain their status (e.g., evidence of courses completed).

U. S. Department of Housing and Urban Development
Washington, D.C 20410-3000

March 10, 1998

OFFICE OF THE ASSISTANT SECRETARY
FOR ADMINISTRATION

MEMORANDUM FOR: Susan M. Gaffney, Inspector General, G

FROM: Willie H. Gilmore, Deputy Assistant Secretary for Administration, A

SUBJECT: Response to Final Audit Report on Procurement

Thank you for the opportunity to respond to the final audit report on HUD Contracting.

The report is the latest in a series of recent undertakings by the Department to review its contracting and procurement systems. At the Secretary's direction, a review of the Federal Housing Administration (FHA) procurement system was conducted by the National Academy of Public Administration (NAPA). The study found that the current system neither responds effectively to Department needs nor adequately ensures accountability. As a result of the NAPA review, the Secretary incorporated contract reform as a priority in the HUD 2020 Management Reform Plan. The plan calls for NAPA to engage in a top-to-bottom redesign of the HUD procurement system, with an emphasis on safeguarding taxpayer dollars with a system that ensures quality and value(Management Reform Plan, page 16).

The Office of the Inspector General's final report is consistent with the conclusions reached by NAPA and the Secretary and provides further support for HUD's contract reform efforts. The OIG's recommendations have been provided to NAPA for consideration as part of the contract system redesign. I also repeat an earlier invitation to you and your staff to join the NAPA team in the redesign effort. I am sure that you will agree that there is no better way to ensure that the expertise and experience of the OIG is fully utilized in resolving the issues identified by NAPA and your office. We look forward to your participation in this crucial effort.

As your report indicates, contract problems at HUD are longstanding. In fact, of the $1.5 billion in contracts identified in the audit, $1.1 billion involve contractors with whom the Department contracted prior to 1993. Nonetheless, the Department does not believe that the fact that these contracts stretch as far back as 1984 should prevent the Department from taking aggressive action now to ensure integrity and efficiency in the HUD procurement system.

Although the final results of the NAPA effort are not expected until late this year, we believe that there are some immediate steps which can be taken to improve contract oversight. We briefed you and your staff concerning our proposals and invited your comments. You indicated that you would have none. We also discussed our approach with NAPA and have adjusted it based upon some of the concerns they expressed. Accordingly, the Secretary has directed me to immediately institute the following procurement reforms:

- Establishment of a Chief Procurement Officer (CPO)

We are hiring a Chief Procurement Officer who will report directly to the Secretary and Deputy Secretary and be responsible for procurement planning and improving the Department's contract oversight capabilities. Priorities include emphasis on cost estimates and cost consciousness, needs determination, and periodic assessments. The CPO must review and approve all contracts over $5 million, and will be charged with review of all interagency agreements.

- Mandatory Training and Certification for GTR/GTMs

The Office of Administration is implementing mandatory training for all new GTR/GTMs prior to assuming these duties; all current GTR/GTMs will be required to complete mandatory training by the end of FY 1998. Certification must be renewed every two years, and requires continuing advanced training in procurement and contract oversight. Mandatory training will also be instituted for senior program managers to emphasize the importance of contract oversight.

- Rating GTR Responsibilities

The Department is adding performance standards for all GTR/GTMs. All GTR/GTMs will be evaluated on the performance of these responsibilities. Ratings for GTR/GTM elements will be reviewed by the Chief Procurement Officer.

- Legal Review of Procurements

The Office of General Counsel will establish a team of contract specialists to review contract terms and assist in negotiations. OGC review and input will be required on all contracts over $5 million.

- Systems Enhancement

The Chief Procurement Officer will be charged with standardizing GTR/GTM record-keeping, and making integrated financial payments data systems accessible to GTR/GTMs.

- Broader Use of GSA Schedules and GSA Contract Vehicles

To avoid overreliance on contractor and industry influence in the award or cost proposals of HUD contracts, the Department will utilize a GSA schedule contractor for major contracts where a GSA schedule meets the Department's needs. If there is an available GSA schedule contractor, the program office must seek consent of the Chief Procurement Officer before conducting a new procurement.

Finally, the report profiles 30 procurements undertaken by the Department since 1984. With regard to these specific procurements, the Chief Procurement Officer will be asked to undertake appropriate action on each of these contracts.

Attached is an action plan for responding to the major concerns raised in your report.

Once again, we look forward to continuing to work with you and your staff to improve the Department's contract systems.

Attachment

cc: S. Ramirez
H. Glaser
R. Keevey

Mr. SHAYS. Thank you, Mr. Carberry. It's nice to have you here Mr.—is it Glaser?

Mr. GLASER. Glaser, yes.

Mr. SHAYS. Thank you, Mr. Glaser. I don't think we need to spend a lot of time now, but I do think that we're establishing a relationship, and you know that our staff will be in contact with you, and you know that there will be continual review and oversight.

So, as far as I am concerned, you start with a clean slate with us, and you've won my heart in the sense that you're willing to accept accountability and that you feel you have the authority as well as the resources to do the job. If you find that that's not the case, then you need to get back to us. We are going to hold you accountable, and then we need to be held accountable, if we don't give you the resources if you need them.

One thing that I want to say for the record: The initial response of HUD to the IG was one that was seemingly resistant, and whoever at HUD who counseled HUD to be more willing to accept the fact that the system was flawed and that we need to move forward deserves congratulations, and if anything that person has done a lot to protect HUD from our getting in the dialog of proving how bad it is, and we don't have to do that. I am convinced that you know it's bad and that we need to make changes, and I am convinced the Secretary does as well.

So whoever at HUD was able to get that across deserves a pat on the back. He or she has protected the Secretary, not hurt him.

Mr. CARBERRY. Mr. Chairman, when I was interviewed by—one of the interviews was with the gentleman on my left. He's the one that told me before I got hired by HUD that was the case.

Mr. SHAYS. OK, well, it's nice, Mr. Glaser, that you did that. I want to know these questions, and they're general, but what's the biggest challenge so far that you're having to face. Then I want to know how do you change a culture not just a process that a culture could corrupt. In other words, how do you change the culture? That's a big thing, but first tell me what's the biggest challenge? Or maybe changing the culture is the biggest challenge.

Mr. CARBERRY. I don't want to minimize that at all. The first one for me was just learning HUD. My experience in contracting—I think I know contracting pretty well, but what I didn't know was HUD and how to put the two together, and I've gotten a lot of help, and on the other hand, I needed a lot of help, but I think it's worked well.

I've been learning HUD—I've still got a lot to learn. I don't even know at this point how much I don't know about HUD, but that's the critical part, is the most difficult thing that I've got to do. I think it's true of anybody coming into a new job.

On changing the culture, I think——

Mr. SHAYS. Let me just ask you this: You've been there 2½ months. So what do you think is going to be the most difficult area of change in procurement? What area will be the most difficult—the training, getting a handle on what all the contracts are? What will be the biggest?

Mr. CARBERRY. I don't think the training is. I think we're well on our way to solving the training problem, and that's going to be

well on the way to solving I guess what I'd say is the most critical one is establishing fundamentally sound business practices in HUD. We're in a business. All of the things that apply to business apply to us. It's kind of like the laws of gravity. You don't have to believe in them for them to apply.

Cost and supply and demand. Cost schedule performance in all our contracts, all of our programs. And we'll be doing that, and there's a lot of enthusiasm for doing it, but that's the tough one.

Mr. SHAYS. Let me do this—let me yield to my colleagues and maybe they'll get at the culture, but I'd like you to come back to that if it's not answered. Mr. Towns.

Mr. TOWNS [presiding]. Yes, thank you very much, Mr. Chairman. Let me just begin by saying I am not as pessimistic as some of my colleagues. I am optimistic. First of all, I know of Mr. Carberry's work and his background, and of course he comes with the reputation of a man that says something and he goes about doing it. It's really the follow through.

Also I know the Secretary. I've known him for many, many years, and I know in terms of his ability to make things happen. So, I am optimistic. I want you to know that, and I feel very good about some of the things that are going on. I think that, sure, we can look at HUD down through the years, but I think that we have somewhere at this point begun to focus on the new leadership, and I think that that's important.

Let me just ask: Can you tell us what role the Contract Review Board will play in overseeing HUD's procurement actions?

Mr. CARBERRY. We are going to be reviewing the strategic plans and the procurement plans of every program that HUD has. We are going to be reviewing in detail all of the contracts that are proposed over $5 million. We are going to do that from a needs assessment. We are going to do that from the point of view of cost schedule and performance. We're going to do it from the point of view of inherently governmental functions, personal services, all the basic things that need to be looked at.

And once we get that information we are going to be—we'll be filing it, and we'll go back and review programs as they go along to make sure that's the case. We need to make sure we don't have duplication in our efforts. We need to make sure that what we are buying is consistent with the strategic plan of HUD, and, you know, when we give our managers programs, we give them three things: We give them time and money and people. And we need to make sure the priorities of HUD are being met and the time and the money and the people that they are being given are being managed well.

So that's the function of that Contract Management Review Board. It's brand-new. It hasn't occurred before, but that's probably the single most effective way we are going to instill an institutionalized, fundamentally sound business practices into HUD.

Mr. TOWNS. Right. When the chairman asked the question, I thought you might say that integration of information technology might be the toughest thing for you. Can you tell us about the challenge you face in accomplishing this goal, what actions have been taken so far by you?

Mr. CARBERRY. We've established the Contract Management Review Board. It's up. It's running. It's met. I have been meeting with all the program managers and assistant secretaries, telling them exactly what we're going to be doing, what's going to be required. We've got a detailed plan for training of the people and the program offices.

The Secretary has announced that the people who are managing contracts are going to be full time in all of the programs. They are not going to part time. They were all part time before, and it didn't work well, and it's one of those things—if you design it poorly, it's going to work poorly. It was a poor design. The Secretary has turned that around.

Those things are going to have payoffs and benefits in the next month or two because that's when they're going to be occurring. The need to track and monitor our contracts more closely is already getting through. The message is there. The Secretary has said it repeatedly.

I don't know if that's responsive to your question.

Mr. TOWNS. That's basically—yes. On that note, let me just ask you, can you tell us about your contract closeout procedure which has been a problem?

Mr. CARBERRY. You know, it really is a problem. It's such a small problem at HUD compared to the one I left with the Navy. I was kind of glad to see it. We've got about 91 contracts we need to close out. That was an issue raised by the IG. What we've done is combined all of those and had them—we need to have the Defense Contract Audit Agency go through and do a final audit. We've requested those. We're getting the audits in. We've got a process we've set up to send a lot of those contracts to the field and have them closed out.

We have some really big problems at HUD in procurement that I've discussed. I don't consider contractor closeout to be a major one, and it's also getting resolved.

Mr. TOWNS. Thank you very much, and let me just say that this Member is prepared to work with you in every way to try and make certain that the problems that we've had down through the years—I want you to feel free to work with us in terms of—I think that this committee—you know the chairman is not here, but I get the feeling that he too feels very strongly about working with you to try to fix the things that are broken, rather than just point the finger and criticize.

At this point I yield to my colleague.

Mr. CARBERRY. Thank you very much, Mr. Towns.

Mr. KUCINICH. Thank you very much, Mr. Towns, and I wanted to also tell Mr. Carberry that I've worked with every single department in this administration, and I'll be glad to work with HUD because I've worked with them before. When it comes to procurement, though I am a Member from Ohio, I am also going to adopt the views of my friends from Missouri when they say, "show me."

Now it's our understanding that HUD has not used the OMB circular A–76 process to conduct a public-private competition in over 10 years. Is that correct?

Mr. CARBERRY. No, I don't think it is. When I first came to HUD, I kept hearing repeatedly that we had problems with A–76, and I

haven't found any yet. All of the requirements that are placed on us by A–76 I think we've accomplished. We have not done the specific—we've done a few but no specific A–76 studies. That's because they weren't required.

Mr. KUCINICH. So, but I want to know—how is it that HUD has managed to spend millions and millions of the Federal dollars to procure commercial services and never fully followed the Federal policy on performance of commercial activities. I know you just got here, but are you aware of that?

Mr. CARBERRY. No. I do believe that all the requirements of A–76 have been complied with.

Mr. KUCINICH. OK, that's fine. And HUD is planning to depend more and more on contractors to perform work either currently done by HUD employees or that was previously done by HUD employees. Now, do you plan to use the OMB circular A–76 in the upcoming conversions from HUD employees performing work to private contractors performing work? Are you going to use that?

Mr. CARBERRY. If we did contract out things that formerly had been done by HUD employees, we'd have to be—be required to use A–76. We don't plan to contract out any work that's formerly been done by HUD employees.

The amount of contract we are going to be doing this year is about the same as what we did last year. That contracting may well go down. With the kind of detailed review with the Contract Management Review Board, it's really unusual where reviews increase the amount of contracting out that you do.

So I don't think we're going to have an A–76 issue.

Mr. KUCINICH. Well, let me ask you this. For example, it's my understanding—if this is incorrect, tell me—that HUD has already held preproposal meetings with contractors about its managing and marketing services contracts for home ownership centers in Philadelphia and Atlanta, and under these contracts the role of the contractor is to do everything HUD staff does to manage HUD's portfolio property and everything the real estate assets management contractors currently do. Is anyone here familiar with that?

Mr. GLASER. Yes, if I may, Congressman. What that refers to is actually what GAO was talking about earlier today. I missed the beginning of their testimony, but I understand that they spoke about the real estate asset management problem at HUD which has—is actually much worse than they described it to you.

That is a situation where HUD has an inventory of 30,000 properties that——

Mr. KUCINICH. I heard that and actually read her testimony—read the testimony.

Mr. GLASER. OK, I won't detail with that. What HUD has to do in those situations is take care of the property. That's mowing the lawns, fixing the windows, making sure the lights stay on and taking care of the thousand little things that a landlord does.

That is not something the Federal Government does or has ever done itself. We don't employ lawn mowers or gardeners or any of the other things that deal with property management.

Mr. KUCINICH. Well, if I may, Mr. Glaser, reclaiming my time, did HUD conduct an A–76 study for these contracts specifically, these contracts? Was there an A–76 study?

Mr. GLASER. No, there was not.

Mr. KUCINICH. OK, and then why not?

Mr. GLASER. Because it's already contracted out with 400 contracts, the results of which the GAO discussed this morning.

Mr. KUCINICH. Was there a waiver in the process?

Mr. CARBERRY. Excuse me, Congressman, it wasn't done because under the A–76 requirements it wasn't required.

Mr. KUCINICH. So it's your position it was not required?

Mr. CARBERRY. Yes.

Mr. KUCINICH. So, therefore, a waiver wasn't necessary?

Mr. CARBERRY. Right.

Mr. GLASER. If it's already been contracted out, if it's currently contracted out, the agency continues to contract it with no A–76 because it's not performed by HUD employees presently.

Mr. KUCINICH. Well, let me ask you something. If you have a situation where—isn't it true that under your rules for performance on commercial activities that it's within the agency's authority to contract work back in-house if the performance of a contractor is poor? We heard a lot about poor contractor performance. Has HUD ever used that option?

Mr. GLASER. This is an option. I am not aware that HUD has used it, has migrated work back into the agency.

Mr. KUCINICH. It is an option, though? It is an option?

Mr. GLASER. It is an option, yes.

Mr. KUCINICH. But you haven't used it?

Mr. GLASER. No.

Mr. KUCINICH. Why not?

Mr. GLASER. Well, as an example, for the REAM contractor, those are tasks that are done by maintenance operations across the country. Again, we are talking about maintaining individual properties. It's not something that HUD is generally in the business of doing. The only reason we have the properties is so that they can be sold and put back into the private market so people can buy the homes. It's a short-term, intermittent process. We don't have the capacity to have individuals in each of our field offices—we would have not the geographic coverage. The agency went to these so-called REAM contracts in the past to do the job. There are way too many of these contractors. The contracting system doesn't work. We intend not to contract that out anymore.

Mr. KUCINICH. Well, let's think about this. Mr. Carberry just testified you are going to review all the contracts over $5 million. I am sure you have contracts that are in the millions, not five, where there may be performance respecting the tax dollars of the people of the United States of America.

So in theory contracting out is supposed to be of benefit, resulting in savings, efficiency. I am just wondering what post contract provisions will HUD put in place to determine whether or not projected outsourcing costs and efficiencies are being realized.

Mr. CARBERRY. When we do the Contract Management Review Board work, we are going to be getting the data from the program offices as to what they plan to accomplish, what the outcome is.

Mr. KUCINICH. Are you going to put some measures in place?

Mr. CARBERRY. Yes, we are.

Mr. KUCINICH. For managers to revisit or reverse that outsourcing decision, such as if there's contractor default, overruns and nonperformance?

Mr. CARBERRY. Yes, we are going to review those contracts on an annual basis to see what extent the parameters are given to us to get the program approved are actually being met. Those are the kinds of reviews that are done on a regular basis in private industry, and we are going to be doing the same thing.

Mr. KUCINICH. And so at a minimum you're going to—will you have annual audits of the post contract award performance of outsourced activities?

Mr. CARBERRY. We'll be reviewing the performance. I would not call it an audit.

Mr. KUCINICH. Will you recompete commercial activities if they don't realize their savings in performance protection?

Mr. CARBERRY. It depends on what the circumstances are. I mean we could cancel programs, too. I mean if it's not accomplishing what it was intended to accomplish, if it's going to take too long, we can decide we are not using the resources like that anymore and cancel it entirely.

Mr. KUCINICH. You know, as we all know, Mr. Cuomo is a major proponent of labor-management partnership and the process of government reinvention, and I just wonder how that principle could be applied to the new Contract Review Board.

Mr. GLASER. We should note that as part of the overall reorganization of HUD which is called the HUD 2020 Management Plan. That plan was developed in consultation with AFGE and NAFE, our two major unions, and in something which is unprecedented as far as we understand in the Federal Government, we actually signed an agreement, several agreements, with both unions last summer, accepting the components of the plan.

The union agreed to do certain things. HUD agreed to do certain things. Last week our AFGE local president addressed HUD employees to say he was very satisfied with the progress of what HUD has done. It truly has been a model of labor partnership.

Mr. KUCINICH. I applaud you for that, and I wonder if you'll take the next step and put a member of the union on your board.

Mr. GLASER. It's certainly something we will consider thinking about.

Mr. KUCINICH. I think that would take an important step toward coordinating because, as you know, the people who are doing the work out there at the front line, they get the information and could probably make things work a little bit more effectively. I just thought that I would offer that for——

Mr. GLASER. It's a very interesting idea.

Mr. KUCINICH. I wish you well in your work, Mr. Carberry. It's a task that I think, given the amount of evidence that is available for your review, must at times appear to be daunting. But I will support you in your efforts to try to straighten out the contract procurement process and to try to make sure that the people of the United States are getting full value for their tax dollar and to make sure the people that HUD serve will find that the agency will be more responsive. I wish you, and the people working with you, well.

Mr. CARBERRY. Thank you very much.

Mr. GLASER. Thank you.

Mr. TOWNS. Thank you very much, Mr. Carberry, and thank you very much, Mr. Glaser. Thank you very much. Now our third panel: Terry Carlson; Bobby Harnage Sr., national president of the American Federation of Government Employees.

Mr. KUCINICH. Mr. Chairman, before you swear in the witnesses, I have two other committee meetings that I am having simultaneously that I have to move on to, but I certainly will have my staff here to get the information, and I appreciate your indulgence.

Mr. TOWNS. Thank you very much. I understand that we have these conflicts. They do come about.

[Witnesses sworn.]

Mr. TOWNS. Mr. Carlson, you may proceed first.

STATEMENTS OF TERRY A. CARLSON, PRESIDENT, T.A. CARLSON AND CO.; AND BOBBY L. HARNAGE SR., NATIONAL PRESIDENT, AMERICAN FEDERATION OF GOVERNMENT EMPLOYEES

Mr. CARLSON. Thank you. I guess I have a little different perspective on some of these things than others. The first thing I did to take a look at this, was to take a look at it from the perspective of the relationship between the contracting officers and the inspector general's office, and the contracting officers and the contractors.

My perspective has been generated as a result of working with companies that do business with the Federal Government for over 23 years as a consultant and advisor to them, and I was asked if I wanted to do this kind of testimony, if I had anything meaningful to contribute, and was given the inspector general audit to take a look at.

And it raised several questions in my mind about the basis upon which everybody is moving forward to reform the procurement process at HUD. There were many, many examples in the audit report where it did nothing but put the contracting officers in kind of an impossible position.

For example, in three instances the audit talked about the government estimate of what the cost would be for a particular program. In two of those instances, the contractor's estimate was significantly higher than the government's estimate, which wouldn't be unusual. I mean that would not be an unusual event. And the contracting staff were criticized for that phenomena having occurred.

In the third instance, the auditor pointed out that the government estimate was $500,000; although I think he or she was a little confused about what the $500,000 was. HUD had no problem in awarding contracts greater than the Government estimate. In this particular case, however, HUD got the contractor to reduce the scope of their work so that HUD could get it for $500,000, which indicates to me it really was a funding number and not a government estimate. And HUD was criticized for that, too.

So if you were a contracting officer trying to figure out what you are supposed to do, we have two instances where we had a contract awarded for greater than the Government estimate and we were criticized, and we had one where we made the contractor meet the

budget number, which they represented as a government estimate, and we were criticized for that as well.

The inspector general was talking about the Lockheed contract for $800 million or whatever, kind of leaving the impression that there was a 50 percent problem in the dollar amount of the contracts reviewed, but if you look at what the IG wrote, there was nothing in the audit report that said that anything was improper or contrary to the regulation on the Lockheed contract.

So I think when you take a look at trying to empower contractors and contracting officers to be innovative and creative in solutions to problems that HUD and other agencies for that matter are facing, you have to be sensitive to what audit reports like this do.

The audit demonstrates a lack of understanding in contracts. I think it's important for people to know that when you have an indefinite quantity contract, normally the Government will say, "We're going to give you $10 million worth of awards," or whatever—it's a huge number, usually, the value of the contract, but it's not a contract. It's merely an opportunity to go after additional task orders.

Well, contractors use that information to develop overhead rates and other sorts of factors. I don't want to bore you with all the mechanics, but what happens is if the contractors don't get that volume of work, then they could potentially, and likely will, experience a financial loss on the contract.

So when you do the original IQC there's tremendous competition because, if you don't get into the initial cut as a contractor, you have no opportunity to get any task orders. So you want to ensure that your price is as competitive as possible. The problem comes in when you have an IQC and the contracting officer doesn't award you any task orders. That can be devastating to a contractor.

I am sorry your colleague from Ohio left because contractors aren't motivated solely by profit. There are contractors that I know of that work with HUD who every day face decisions in taking marginal contracts because they have 700 employees who have families to feed. They take contracts that a normal business person wouldn't take.

But be that all as it may, we talk about the regulations. I mean in the audit report there are even instances where it says that the contracting officer complied with all the regulations, and they still didn't like it. And so my concern is that as long as we keep doing these inspector general kinds of audit reports by people who don't understand how cost plus contracts work, who don't understand how overhead rates are truly applied, and give the impression that this is a process run amok where contractors just walk in with shovels and take out bags full of money, there is a problem.

The other problem is we end up with contracting officers putting together strategies that are designed to solve audit recommendations, not the regulations, and I don't think that's what anybody intends. But a person's not crazy. If you're a government contracting officer—and I run into this every day—if you're a government contracting officer, you are not going to do anything, even though it may make business sense, to facilitate a contractor because 4 years later some auditor might do a review and decide that they didn't like what you did and will penalize you for it.

[The prepared statement of Mr. Carlson follows:]

Mr. Chairman and Members of the Subcommittee:

Thank you for inviting me to testify today about issues raised by recent audits and reviews of HUD's procurement and contracting capacity and to discuss the potential for contract reforms to correct any identified deficiencies or weaknesses.

The primary basis for my statement today is a review of the Office of Inspector General's *Audit Report on HUD Contracting* (97-PH-163-0001, Dated September 30, 1997). However, my statement also reflects my personal observations made over the last twenty years while consulting with companies performing on Government contracts, including HUD contracts, and teaching procurement-related courses to both Government and contractor program and contracting officials.

Executive Summary

1. The audit report issued by the HUD Inspector General is manifestly unsuitable for determining if HUD's procurement challenges require legislative reforms. In fact, this audit report makes it clear that the Office of Inspector General, rather than HUD's contracting organization, needs some legislative reform. To protect the integrity of the procurement process it is imperative that the Inspector General be required to assign auditors possessing substantial procurement knowledge to these types of reviews. Otherwise, the Inspector General will undoubtedly issue similarly misleading audit reports.

2. The potential damage of this audit report is incalculable. Most importantly, it will have a chilling effect on the willingness of HUD contracting officers to apply innovative contracting techniques. The audit report criticizes HUD contracting officers for complying with all of the applicable rules, regulations and standards as well as contract terms and conditions. It also criticizes HUD procurement officials for taking actions that were clearly HUD's best interest.

   In many of these cases, the report inappropriately characterized the contract actions taken, and criticized when it should have been congratulating. In such an environment is it reasonable to expect HUD contracting officials to commit professional suicide by applying innovative contracting techniques in an attempt to streamline the procurement process. I think not despite Congresses attempts to encourage such action. How can anyone expect procurement reform to make any real headway if audit reports such as this one affect the procurement process? And, while the taxpayer is always the ultimate loser when reforms fail, companies doing business with HUD will feel adverse effects almost immediately.

3. The preceding statements are not to imply that the HUD contracting organization has no problems. Abundant anecdotal evidence exists to clearly demonstrate to HUD's management that action needs to be taken to improve procurement workforce training in contracting skills, human relations, team building and other fundamental business skills. However, HUD's management can adequately address these challenges. If HUD's managers are not up to the task, the Secretary can change managers. But passing additional legislative reforms to address these procurement problems is not the answer particularly if the basis for the reforms are the conclusions reached in the Inspector General's report.

4. There seems to be structural impediments in Government that often prevent a manager from building a well-trained, highly motivated staff. One such impediment is being the subject of a misguided audit. While oversight is a necessary function, in the end the overseer has to be able to provide constructive recommendations. Perhaps it is time to hold the Inspector General accountable for the ready foreseeable fall-out from such a far reaching but unsupported audit report. It is not as though HUD's contracting personnel have to remain at HUD to be subjected to this type of innuendo.

Discussion

General Observations

It is not my intention to critique the Inspector General's audit report. Rather, I intend to point out areas where the conclusions reached by the auditor are inconsistent with the factual descriptions provided by the auditor in the audit report. This is imperative since actions taken based on an improper interpretation of the facts is far worse than doing nothing at all.

Fundamental Sampling and Interviewing Flaws in the Audit Report

The Inspector General's basis for the conclusions in the audit report came from a judgmental sampling of what the auditors termed HUD's problem contracts. A judgmental sampling, by itself, is not problematic. However, any inferences about an entire population drawn from results obtained by testing a judgmental sample are invalid. Thus, any generalizing of procurement shortcomings at HUD using this audit as a basis would be invalid.

Second, the auditors relied on opinions solicited from the Government Technical Representatives (GTR's) and Government Technical Monitors, (GTM's). Since the audit report did not address the procurement training or experience these technical representatives possess, it is unlikely these technical representatives are aware of when the Federal Acquisition Regulations require competition. Nor, for that matter, is there any indication in the audit report that the GTR's or GTM's have any concept of what constitutes a fair and reasonable price. Nor is there any indication that the GTR's or GTM's have any indications of whether or not a contractor is complying with contract terms and conditions, except for required reports that are submitted directly to them.

On the other hand, in the body of the audit report, the Inspector General concludes that the GTR's and GTM's do not know their jobs or view their GTM or GTR tasks as ancillary tasks. Yet, comments from these same individuals form the basis for several audit conclusions.

Fundamental Contract Interpretation Flaws

The audit report examples repeatedly mischaracterize what the various contract types allow HUD to do. For example, the Inspector General cites an example where "HUD is paying a higher price than needed for the $71.6 million of computer hardware and peripheral equipment purchased by Lockheed Martin for HUD." However, the contract between Lockheed and the Government set firm fixed prices, subject to adjustment. This contract type normally has an adjustment clause that specifies the time periods affected by the adjustment and the parameters within which the price adjustments can roam.

The auditor is saying that HUD should pay lower prices to Lockheed Martin because the contractor is making a profit. However, that profit is the result of the contractor accepting a cost risk (increasing costs for computer hardware and peripherals) that did not materialize.

With absolute knowledge of decreasing prices in the computer hardware and peripherals market, the Inspector General is criticizing a contract that actually sounds fairly well thought out. The fact that the audit conclusion would have been different had prices increased serves to cut the heart out of the audit conclusion that the Government is overpaying for hardware and peripherals. The Government is paying for the hardware and peripherals as well as avoiding having to pay increased prices if computer hardware and peripheral costs increase.

The Inspector General uses the same approach on the J.W. Thompson contract. Again with perfect knowledge the auditor concludes that HUD could have saved $790,000, if HUD had done a better job of upfront cost analysis or HUD had selected a different contract type. There is no basis for such a conclusion.

The auditor demonstrates a lack of understanding as to how Indefinite Quantity Contracts (IQC) work. Indefinite Quantity Contracts normally have very competitive beginnings. The initial competition for the award of the opportunity to receive an award helps ensure that the technically qualified contractor offering the best price receives the award - an award based on competition. This ensures that the Government has a supplier, offering a fair and reasonable price, capable of satisfying the Government's requirements without having to go through the competitive process again.

The auditor is critical of HUD contracting for a "... desired outcome without specifically knowing what tasks to request to achieve the outcome. While this may be a time saving process to award the contract, it often is the most costly, as HUD is unable to prepare good cost estimate on the tasks needed to accomplish the end product." (Emphasis in original.)

This criticism is inconsistent with contracting theories. The procurement community is beginning to recognize that contracting for the desired outcome without specifying how to achieve that outcome actually results in a less costly solution. Furthermore, the Government's estimate does not establish the contract value. The contractor's cost estimate sets the contract value.

Another broad area challenged by the Inspector General is contracting for prohibited services. The Inspector General cites as an example of prohibited services contracts with outside accounting firms to:

1. review the contractor's accounting records to determine whether GNMA's fees were appropriately accounted for;

2. determine whether billings submitted to GNMA were for services actually rendered by the contractor or subcontractor; and

3. determine whether billings submitted to GNMA were in accordance with the terms of the relevant contract.

The Inspector General says in the audit report that only HUD staff can perform these activities. The basis for this conclusion is OMB Circular A-76 which states that "..determining if contract costs are reasonable, allocable and allowable..." are inherently governmental functions. Of course, the audit firms performing on these contracts cannot disallow the costs of any contract, other than their own. Only the contracting officer can disallow costs. The accounting firms only recommend an action to their customer -- the accounting firms do not direct their customer to act.

The position taken by the Inspector General is particularly curious since one of the recommendations in the audit report is that HUD expedite contract close-outs by contracting out audits to determine if contract costs are reasonable, allocable and allowable.

Contract Specific Observations

This statement might already be too long but I would be remiss in not identifying a couple of other areas that cause concern.

1. The Inspector General identified as a problem a contract with ABT. The audit criticized HUD for reducing the scope of a contract in order to stay within the budget amount available to do the work. Unfortunately, the auditor is somewhat confused. The auditor states that the HUD cost estimate for the job was $500,000. The only proposal received by HUD for this effort contained a cost estimate of $900,000.

   HUD then worked with the contractor to reduce the scope of work to the point where the agreed upon tasks could be done for $500,000. Rather than being a government cost estimate, the $500,000 appears to be the amount available to do the work. (HUD has no problem in exceeding its own cost estimates, nor should it).

   HUD's actions in this case were prudent. A cost reimbursement contract requires the contractor to execute the statement of work up to the point where funding is no longer available. At that point, HUD receives the contractor's product. Before completion, work notes gathered in a box might represent the contractor's work product. By ensuring the available funding fit the statement of work, HUD maximized the probability of receiving a useful product.

2. The Inspector General also noted as a deficiency a contract with Price Waterhouse. The Inspector General was critical of the fact that HUD is paying for Price Waterhouse employees' equipment. HUD paid a total of $45,583 for 17 laptop computers for Price Waterhouse's employees to use. The $45,583 includes $39,814 for the cost of laptops and $5,769, which is a 14 percent add-on fee by Price Waterhouse.

   If this 14 percent represents the recovery of Price Waterhouse's General and Administrative expenses, which appears likely, the auditor is creating another straw issue. A cost input base allocates G&A expenses to all final cost objectives. If Price Waterhouse uses a total cost input base for allocating general and administrative costs to final cost objectives it must recover the general and administrative costs on all elements of cost. There is no relationship between any benefit received by the contract and the general and administrative expenses allocated to the contract. It is strictly for cost recovery.

Conclusion

I repeat that I do not mean to critique the Inspector General's audit report although that is how it probably appears. For far too long various audit agencies in the Government were able to present allegations of abuse by contractors without being accountable for their errors or assigning auditors lacking the skills and knowledge necessary to conduct a responsible audit. These auditors have also been able to raise allegations of abuse by Government procurement personnel. Again, without fear of being accountable for the

actions. Certainly there are abuses in the procurement process. That is why oversight of the procurement process is necessary.

However, the focus of these oversight activities must change when oversight becomes the source of problems instead of a source for identifying and recommending solutions to problems. The system has to change if managers find they cannot perform their day-to-day duties because they are responding to audits containing unfounded allegations of wrongdoing or incompetence. The system has to change if the public thinks all of the contracting officers at HUD are largely inept because of improper audit allegations that HUD has foolishly squandered taxpayer money.

These changes require a rethinking of what we want the Inspector General's office to accomplish. If they are to review contracting issues, they must be required to have knowledgeable staff perform the audits. Otherwise, we will make no progress toward more efficient and effective procurement operations.

Affidavit Regarding Contracts With The US Government

T.A. Carlson & Company does not now have nor has it ever had any contracts or subcontracts with the US Government. I personally have no contracts or subcontracts with the US Government. I am not representing any organization.

Terry A. Carlson

Terry A. Carlson
June 3, 1998

Curriculum Vitae of Terry A. Carlson

Mr. Terry A. Carlson has experience in applying and interpreting the rules, regulations, standards and guidelines applicable to companies doing business with the US Government. He concentrates primarily in helping contractors use the procurement regulations to their advantage when preparing proposals, evaluating business structures, selecting information technology solutions, preparing requests for equitable adjustments, defending claims made against them by the Government.

Some of Mr. Carlson's recent engagements include:

- Developing policy and procedures manuals covering cost estimating, purchasing, project management and contract administration;
- Providing expert testimony on cost and pricing issues before the GSBCA and the GAO;
- Assisting in the selection and implementation of an enterprise wide resource planning system;
- Assisting in the resolution of audit issues raised during final indirect cost rate audits;
- Assisting contractors in preparing claims stemming from contract termination and delays; and
- Assisting contractors in resolving defective pricing issues.

Before establishing T.A. Carlson & Company, Mr. Carlson was a Professor of Financial Management at the Defense Systems Management College. He also served time as a consultant in the government contractor advisory services department of a "Big 6" accounting firm.

As an assistant professor of accounting at Villanova University, Mr. Carlson taught courses in financial accounting and management information systems. Mr. Carlson has also developed and presented courses on contracting and the procurement process for the George Washington University School of Continuing Education and the George Washington University Law School.

Mr. Carlson also served as an auditor with the Defense Contract Audit Agency, where he was responsible for evaluating contractor submissions to ensure that they were prepared in accordance with applicable regulations and standards.

Mr. Carlson earned the Bachelor of Science degree in Accounting from Virginia Commonwealth University and the Master of Business Administration degree from George Mason University. Mr. Carlson is a certified public accountant in the Commonwealth of Virginia and is a member of the American Institute of Certified Public Accountants, the Virginia Society of Certified Public Accountants, and the National Contract Management Association.

Mr. SHAYS [presiding]. Thank you, Mr. Carlson.

Mr. Harnage.

Mr. HARNAGE. Yes, thank you, Chairman Shays, and ranking member, Mr. Towns, and other members of the committee. I want to thank you for the opportunity for appearing today and give you some of the concerns of AFGE. I have submitted my statement and asked that it be entered into the record.

Now, Mr. Chairman, you've heard much today about how vulnerable HUD is to contractor waste, fraud and abuse; and basically it's because HUD doesn't properly manage or monitor its contracts for commercial service. So I am not going to spend a lot of my time talking about that except to urge Congress to get a handle on this and protect the American taxpayers from such obvious mismanagement of its resources.

I want to focus my remarks on the problems of HUD which are self-inflicted, premeditated mismanagement, if you like, of the resources with which Congress and the taxpayers have entrusted it. HUD's management is not about saving money or being efficient. It's about downsizing for the sake of downsizing. It's downsizing but it's not rightsizing, and much of the testimony you've heard today clearly supports that fact.

It looks to me as if someone out there wants to brag about how small HUD has become or will become. But, in fact, in the future HUD will be much larger, much more expensive and much more wasteful if something isn't done now. They're playing a shell game with the numbers of full time equivalents [FTE's], while underneath those shells are the hard-earned dollars of the taxpayers.

In the end HUD will be larger because of Federal contractor employees instead of Federal civilian employees. It will be more costly. HUD does have a choice, although some of the indications of today would lead you to believe they don't have a choice. As I said, this is a self-inflicted circumstance of downsizing.

I can tell you that it's not the OMB A–76 process that they're using for contracting decisions. They've said today that they don't use it, but the reason is that they don't have to. They didn't say it was a bad process, that they shouldn't have to use. They simply said they don't have to.

And contrary to what you hear, my information is that an A–76 study has not been done at HUD in the past 10 years. In 1995 there was a request that went over to the administration requesting for a waiver from the A–76 and although they didn't receive the waiver they did receive a way around it by telling them that they should classify it as a joint venture. Then they didn't have to come under the A–76 study.

But sound business practices and Federal Government policy dictates that any initial decision to make or to buy should be based on sound cost comparisons, and A–76 requires that comparison. The policy is in the best interests of the taxpayer, and HUD should be following those rules.

Contracting out is a business decision. It's an option to be considered, but HUD is making it a necessity. HUD has taken away the options, ignoring sound business practices and ignoring the rules, and HUD is doing so at your expense. A–76 is not the panacea. Everyone has a disagreement with some parts of it, but it's the rules

with the best we could come up between the Government and private sector and union officials, and it's one that we all try to live by. It works, and it is in the best interests of the taxpayer.

I want to talk briefly about one aspect of A–76, and that's the MEO, the most efficient organization. The provision is to prevent exactly what HUD is doing. If you determine what the most efficient organization is and then compete the jobs with the public-private competition, the taxpayer wins every time.

If you contract out inefficiency, you still have inefficiency. If the contractor eliminates the inefficiency, it has not reduced the cost to the taxpayer. It's merely increased the contractor's profit margin. The taxpayer loses every time. Should HUD be required to manage by budget, not arbitrarily self-inflicted staff ceilings is a question that we ask you to ask yourselves.

I urge you to secure HUD's commitment to start playing by the rules and using the A–76 public-private competition in determining whether to contract out or not. I urge you to require HUD to start conducting cost comparisons before it makes contracting out decisions, and I urge you to require HUD to demonstrate that it is making contracting out decisions for reasons of cost and efficiency, not simply because it has downsized and is half-staffed and created its own inability, incapability to carry out its mission.

The fact that HUD does not know if they are doing the job the least expensive way. If they say so, they cannot prove it. Downsizing at HUD should be stopped until they comply with the rules and prove that they are doing it in the best interest of the taxpayers.

And I urge you to investigate even deeper into HUD's contracting out policies to ensure that the taxpayers of this country are not getting taken to the cleaners. Taxpayers deserve it and the Federal employees have requested it and Congress should want it. Thank you very much for this opportunity to appear before you, and I'll answer any questions you might have.

[The prepared statement of Mr. Harnage follows:]

Mr. Chairman and Subcommittee members, my name is Bobby L. Harnage, Sr., and I am the National President of the American Federation of Government Employees, AFL-CIO (AFGE). The AFGE is the largest union for government workers, representing 600,000 federal employees serving worldwide, as well as employees in the District of Columbia. I appreciate the opportunity to present our views here today.

The General Accounting Office (GAO) and HUD's Inspector General have focused on HUD's failure to follow federal policy and sound practices with regard to contract management. AFGE too believes that HUD's contract management failings place HUD at greater risk for waste, fraud and abuse. Much of HUD's contract management problems stem from self-inflicted in-house staffing shortages and failure to replace needed in-house staffing expertise.

My testimony, however, is focused on how HUD's decides whether or not to contract out work. It is at this initial stage in the procurement process that HUD's contracting problems begin, primarily because HUD routinely fails to comply with existing federal procurement policy and practices, particularly with regard to public-private competitions.

AFGE is deeply dismayed that HUD fails to comply with basic federal procurement policy. AFGE members are determined to see that the federal government's dollars are spent wisely; we are conscientious employees and patriotic Americans, as well as hard-working taxpayers. Contrary to sound business practices and federal policy, HUD does not ask, let alone study, whether it would make more sense economically for in-house staff or private contractors to complete a service.

HUD is trying to get its own house in order by reforming its contracting practices but, thus far, we have seen no indication that HUD plans to comply with existing basic federal procurement policy that requires public-private competitions. HUD seems to be reinventing itself to further circumvent sound federal contracting policy and practices.

For years HUD has eschewed following the Office of Management and Budget's Circular A-76, which is supposed to guide agencies on determining who should perform commercial activities, and encourage competition and choices in management. Under the OMB Circular A-76 process, agencies utilize a public-private cost-comparison to make sound and justifiable contracting decisions.

The Basics of the OMB A-76 process.

At the heart of a public-private cost competition are three core components -- a statement of the performance of work, an in-house cost estimate, and a comparison of the in-house bid against a proposed contract.

The statement of performance of work defines what services are being requested, the performance standards and measures, and time frames required. It is a performance oriented document, specifying what outputs or measures are desired and directions as to how the results are achieved. Without a good performance of work statement, an agency cannot get reliable bids. Failure to prepare a thorough, well-thought out performance of work statement will leave agencies practically unable to monitor contract performance.

Under OMB Circular A-76, HUD's in-house cost estimates must reflect the scope of the performance of work statement. The in-house cost estimate is based upon a

competitive organizational structure and the staffing necessary to ensure that the service is performed in an efficient and cost effective manner. This is usually referred to as the Most Efficient Organization, or MEO. Under the OMB Circular A-76 guidelines, HUD could consider existing management reinvention, consolidation, re-engineering, personnel classification, market and other analyses to identify and develop the MEO. In short, public-private competition under current federal policy encourages HUD management to retool its operations as needed. During the development of the MEO the agency must plan for real workload and real staffing levels to achieve a competitive bid.

In addition, the in-house cost estimate, including the MEO, is to be prepared with the participation of employees and their unions.

OMB Circular A-76 is the rule book for contract competition. **Yet, HUD has not used the OMB Circular A-76 cost comparison process in over ten years.** In essence, HUD has played the game but gotten around the rules for more than a decade.

HUD should be following the federal policy and practice under OMB Circular A-76, not avoiding it. HUD does not need to reinvent basic procurement policy; HUD needs to stop circumventing existing sound federal contracting policy and practice.

Current federal policy under OMB Circular A-76 is already designed to safeguard against wasteful contracting out by using a full and fair competition for federal work that is not inherently governmental (i.e., not so integrally related to the exercise of the public interest as to mandate that it must be done by federal employees) **before** an agency contracts out work.

Not surprisingly, previous GAO studies show that when an agency decides to consider the option of contracting out, A-76 public-private competitions can generate savings.[1] AFGE believes that HUD too could safeguard taxpayer dollars and give federal employees a fair chance to defend their jobs if HUD utilized the OMB Circular A-76 process for public-private competitions prior to contracting out work.

Given HUD's more than ten-year history of ignoring the OMB Circular A-76 competitions and HUD's current plans to depend more and more on contracting out activities, it is imperative to ask key questions regarding HUD's reform efforts in contracting decisions and practices.

Mr. Chairman, will HUD's reformed contracting procedures ensure that HUD will follow federal policy prescribed in OMB Circular A-76, rather than continue to side-step the process? Does HUD plan to do any cost-comparison analyses to make sound and justifiable business decisions that outsourcing HUD work will result in a more efficient and economic performance of that work than if HUD used current employees and/or hired additional staff? Before HUD is allowed to continue to deviate from federal procurement policy, HUD should show why its new way of doing business is sufficiently comparable to current federal policy under OMB Circular A-76.

Absent a public-private competition, what steps is HUD taking to ensure that it has done an adequate cost-benefit analysis and has demonstrated that the performance of

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[1] General Accounting Office, BASE OPERATIONS: Challenges Confronting DoD as It Renews Emphasis on Outsourcing (March 1997), p. 8. Although this report discusses the Department of Defense, the agency responsible for most contracting out, its conclusion applies to HUD.

specified work by a private contractor would result in a cost savings to the Department over the life of the contract? Such a cost benefit analysis should be available to the public.

I would like to direct you to the attached letter from OMB to Emelda Johnson, HUD's Deputy Assistant Secretary for Single Family Housing. The undated letter is in response to HUD's August 10, 1995 request for a waiver from OMB Circular A-76 requirements for a cost-benefit study before contracting out extensive work in Single Family housing disposition. In the letter OMB explains to the Deputy Assistant Secretary for Single Family Housing that an A-76 study is not required if the proposal is a "joint venture" with the private sector. Not surprisingly, HUD's did not conduct a OMB A-76 study before considering the option to contract out its single family property disposition program.

OMB also advised HUD that it could achieve economies of scale for the then current staffing level, "even without additional contracting beyond the current level." Indeed OMB told HUD that "if the FHA employees did 'win' the cost comparison" HUD would not be precluded from fully staffing the most efficient organization as proposed in an in-house cost estimate bid. HUD did not give its employees a fair and full opportunity to defend their jobs because HUD preferred to use a clever tactic to avoid OMB Circular A-76.

AFGE urges HUD to commit to following the A-76 process when it chooses to consider the option of contracting out. HUD does not need to invent new contracting

practices. It simply needs to follow, rather than use clever tactics to avoid, existing federal policy and best practices under OMB Circular A-76.

HUD has a history of eschewing full and fair public-private cost comparisons and directly resorting to contracting out work because of self-inflicted in-house staffing shortages.

OMB reported three years ago, that several agencies--including HUD -- each could have saved several million dollars by performing functions directly rather than having them performed by contractors. They did not do so because either their requests to OMB for the necessary full time employee equivalents (FTEs) were refused or the agencies were so sure such requests would be refused that they were not even submitted.[2]

Independent experts from the National Academy of Public Administration (NAPA) performed an extensive review of HUD's ability to carry out its mission efficiently and effectively. "Because of staff shortages, HUD has relied on contractor assistance in instances where considerations of efficiency and economy would favor performance in house." (*Renewing HUD: A Long-Term Agenda for Effective Performance*, page 140.)

The NAPA report was published in 1994, years before HUD embarked on its plan to cut its federal work force to an arbitrary number of 7,500 by 2002, a 28 percent cut in staff. Even with HUD's updated forecast that it needs approximately 9,000 FTEs, the problem of contracting out solely because of lack of staff, not cost savings, is increasing.

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[2] Office of Management and Budget, Summary Report of Agencies' Service Contracting Practices (January 1994), p. v.

The NAPA study confirms that HUD's contracting decisions were *not* based on cost considerations or based upon improving HUD's ability to carry out its mission and key functions but on arbitrary and inaccurate personnel ceilings.

Unfortunately, the September 1997 HUD Inspector General audit report on HUD's contracting activities from 1992 through 1996, which has been discussed in more detail at today's hearing, indicates that HUD continues to pay higher costs to contract out work due to a self-destructive course of needless downsizing.

> "Management's contracting environment needs to change to seek ways to emphasize cost consciousness and assure the best value for dollars spent. Because HUD managers did not have the staff to complete the product or service in house, the question of 'What will it cost?' was often not seen as an issue."
>
> (Audit Report #97-PH-163-0001, Executive Summary, page iv.)

I direct you to the IG audit of HUD's contract with KAJAX Engineering, Inc. HUD has paid nearly $12 million from September 1993 through February 1997, for the private company to handle written and telephone inquiries from mortgage companies, HUD Field offices, homeowners and other interested parties. The KAJAX employees sit in the HUD building in Washington, DC, represent themselves as HUD employees and process roughly $13 million of HUD proceeds received in the mail each year. The decision to contract out this work rather than perform the work in-house was not made based on a cost comparison.

> "HUD's Deputy Director for Financial Services stated that HUD lacks available staff to handle the volume of calls received and the department was not allowed to hire additional employees. Further, he noted that it was easier to obtain funding for contract services rather than for hiring additional staff."
>
> (*Id.* at Section V, page lxx.)

Last September at a pre-proposal conference for the contract solicitation for the financial advisory services, HUD's Director of the Single Family Property Disposition Division, Ms. Kitty Woodley, conceded that even though HUD already knew how to make its operation more cost-effective it wouldn't. It would contract out its work because it just won't have the staff.

> "We [HUD] know that we could improve our current operation. We know right now how we could cut costs. We know how we could cut holding costs. I mean, if it is a matter of re-engineering our current operation to get there, that is not the answer. . . .The issue is that even with such an operation that takes a sizable number of HUD staff, those staff are not going to be available to us in the future to oversee contractor activities even, and to make decisions about how, you know, we should go about selling our properties, you know, should we lower the price, should we do an auction, etc., etc. We know how to re-engineer our business. We know how to re-engineer this program. So, if that is what you are getting at, that is not the answer. We know how to do that. The answers [sic] that we are not going to, the issue is, **we are not going to have the staff out there to maintain such an operation even if we were to re-engineer it.**" (Emphasis added.)

See attached Transcript of September 22, 1997, HUD Pre-Proposal Conference, at page 41, lines 4-21.

The driving force for contracting out work was not cost-savings or efficiency but staff reductions.

Mr. Chairman, in HUD's efforts to reform its contracting practices, the agency needs to commit to managing its work by its budget, not through self-inflicted staffing shortages.

Self-inflicted staffing shortages, which appear to be the reason HUD has ignored full and fair public-private cost comparisons, is also undermining HUD's capacity to manage and assure adequate contract oversight. Staffing shortages leave HUD even more vulnerable to contractor fraud, waste and abuse. As you know well, GAO has

questioned whether HUD will have the capacity to carry out its responsibilities once the downsizing target is reached.

HUD's targeted personnel ceiling of 9,000 FTE's chokes the agency's capacity to perform work in-house and tethers the agency to contractors, even when efficiency and economy would dictate that public employees are the better way to do the job. The policy of managing by ironclad personnel ceilings rather than the agency's budget is unsound. Forced contracting out means HUD will have no option but to depend on contractors and to pay whatever they demand. HUD should not be held hostage to contractors because of a rigid ceiling on in-house staff.

Mr. Chairman, it is imperative that at the starting point in HUD's procurement -- the decision whether or not to contract out -- HUD make sound and justifiable decisions, not simply outsource work because HUD has mandated that no staff can be replaced or new staff hired. Contracting out as a reflex to self-inflicted in-house staffing shortages is unwise, and costly to the taxpayer. What steps is HUD taking to ensure that when it contracts out work it does so for the right reasons and not because of self-destructive staffing reductions?

CONCLUSION

Again, Mr. Chairman, thank you for inviting me to testify at today's hearing. AFGE is ready to work with you to ensure that HUD uses OMB Circular A-76 public-private competitions when it chooses the option to contract out work. I urge you to require that HUD, when it chooses to consider the option of contracting out, comply with federal policy under OMB Circular A-76 of public-private competitions before any work is to be

contracted out. I urge you to secure HUD's commitment to demonstrate that its contracting decisions are not being driven by self-inflicted staffing shortages. I also urge you to insist that HUD maintain the human resources adequate to monitor contractors' performance and to maintain the in-house capacity to perform such work, in the event that contractors perform inadequately or perpetrate waste, fraud, and abuse.

That completes my statement. I will be happy to answer any questions.

BOBBY L. HARNAGE, SR.
NATIONAL PRESIDENT
AMERICAN FEDERATION OF GOVERNMENT EMPLOYEES, AFL-CIO

As national president of the American Federation of Government Employees (AFGE), AFL-CIO, Bobby L. Harnage, Sr. leads the nation's largest union for government workers representing 600,000 federal employees in the United States and overseas, as well as employees of the District of Columbia.

Mr. Harnage, an activist with AFGE for over 30 years, was AFGE's national-secretary treasurer for six years, from 1991 to 1997, before filling the vacant position of national president. While secretary-treasurer, Harnage also served as chair of the union's privatization committee -- a watchdog for defense workers and the vital role they serve. Harnage's distinguished military career, which includes stints as an Air Police Investigator at Clark Air Force Base in the Philippines and the Strategic Air Command at Warner Robins Air Force Base in Georgia, makes him a vigilant defender of America's national security.

Subsequent to his election as national secretary-treasurer, Harnage's reputation as a trusted leader earned him a 13-year term as 5th District national vice president, from 1978 to 1991. The 5th District represents federal government employees in Alabama, Florida, Georgia, South Carolina. Tennessee, Puerto Rico and the Virgin Islands. He was a member of the Labor Advisory Board, Center for Labor Education and Research at the University of Alabama and served on the Board of Directors of the Atlanta Metropolitan Area Red Cross.

Harnage is married to the former Sharon G. Turner of Jacksonville, Florida, who was president of her AFGE local for 12 years and also served as a vice president and president of the AFGE National Housing and Urban Development Council.

House Rule XI, Clause 2(g)

AFGE has no grants or contracts to declare.

ATTACHMENTS

EXECUTIVE OFFICE OF THE PRESIDENT
OFFICE OF MANAGEMENT AND BUDGET
WASHINGTON, D.C. 20503

MEMORANDUM TO EMELDA JOHNSON

FROM: Steve Redburn *Steve*

SUBJECT: A-76 Waiver

Your August 10, 1995, memorandum requests a waiver from the OMB Circular A-76 requirements for a cost-benefit study before contracting for certain Single Family Servicing and Single Family Property Disposition activities. I am confirming the results of your conversations with OMB and National Performance Review staff concerning the request.

The decision to consolidate Single Family Servicing and Single Family Property Disposition from 70+ locations to five Service Centers, subject to union consultation and Congressional notification, is consistent with the Department's reinvention blueprint. The decision, in turn, to contract for certain activities at the consolidated sites (or any individual site) is subject to the requirements of both Section 5.g. of the Federal Workforce Restructuring Act and Circular A-76.

As discussed with staff, the requirements of Section 5.g. of the Restructuring Act take precedence. The Act requires, <u>under certain circumstances</u>, a cost-benefit study before an agency contracts out activities. Unlike A-76, there is no provision for waiving this requirement. If the Department determines that the Act does not apply, then the requirements of A-76 must be met.

Circular A-76 sets out several conditions which must be met before a waiver for a cost-benefit study can be granted. This determination and waiver can be made by the Department. If the Department is not willing to waive the requirement, then the cost-benefit study should be conducted, or another approach to carrying out the activities found. I understand that Bob Dodge of the NPR discussed with you the possibility of "joint ventures" with the private sector for asset sales. Asset sale joint ventures are not considered contracting out, and are not generally subject to the requirements of the Restructuring Act or Circular A-76.

Other technical comments concerning the requirements of the Restructuring Act and the Circular are provided in the attachment. I would specifically draw your attention the

comments concerning the Most Efficient Organization (MEO) used in pricing the employee bid under the cost benefit comparison. The MEO would be based on staffing requirements in the five proposed centralized service centers. The OMB staff believe that you will achieve economies of scale for FTE with the centralized centers, even without additional contracting beyond the current level. Therefore, if the FHA employees did "win" the cost comparison, we do not believe that FTE ceilings would prevent you from fully staffing the MEO.

I hope this information is helpful. Please let me know if we can be of any further assistance.

Attachment

ADDITIONAL COMMENTS ON A-76 WAIVER REQUEST

1. In the short term, existing staffing shortfalls are causing performance problems in the areas identified. HUD proposes to contract these activities. Short term, emergency, contracts may be authorized to meet these exingencies, without cost comparison. OMB does not interpret Section 5.g., of the Federal Workforce Restructuring Act or the requirements of OMB Circular A-76 to preclude the award of emergency service support contracts.

2. Subject to Section 5.g., OMB Circular A-76 permits agencies to convert functions of 10 FTE or less directly to contract without a cost comparison and to waive larger A-76 cost comparisons. Certain conditions, however, must exist in order to waive an A-76 cost comparison. These include; (1) a determination that effective price competition is available; and (2) an in-house operation, operating under its Most Efficient Organization (MEO), could not win a competition with the private sector.

   The attachments to the August 10 memorandum should be clarified with regard to "price" competition rather than general competition with the private sector. This can be done by comparing private sector prices plus contract administration with an in-house labor and material cost estimate. The attachments do not address the MEO competition question and would need to do so in order to justify a waiver. If cost comparisons are to be conducted, the less than 10 FTE rule is defined by the scope of work in the contract solicitation.

ATTACHMENT 2

DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT

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In the Matter of:        *
                         *
PROPOSED CONFERENCE      *
                         *
FINANCIAL ADVISORY       *
SERVICES                 *
*************************
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Monday,
September 22, 1997

451 7th Street, S.W.
Washington, D.C.

The above-entitled hearing came on for aring, pursuant to notice at 9:32 a.m.

PRESENT:

PATRICIA FIELDS

KITTY WOODLEY

WANDA RITTER

PHIL SCHULTE

DANILLA WEATHERLY

RUSS GREATA

MAUDE WILLIAMS

A G E N D A

PRESENTATION BY:	PAGE:
Patricia Fields	3
Kitty Woodley	3
Danialla Weatherly Russ Greata	12
Wanda Ritter Kitty Woodley	17
Phil Schulte	

1 P R O C E D I N G S
2 (9:32 A.M.)
3 MS. FIELDS: Good morning. My name is Patricia Fields. And I am
4 from the Office of Procurement Contracts. And we would like to welcom
5 you this morning to the pre proposal conference for the Financial
6 Advisory Procurement.
7 We are going to tell you about the program, answer your question
8 that were faxed into us or mailed and questions that we don't have th
9 answers to, yet, will be mailed out in the amendment to this
10 solicitation. And you will be getting them. And that will be all of
11 the questions and answers. We will send you a copy of the transcript,
12 and any other changes that are going to be made to the solicitation.
13 Now, I will turn this over to Ms. Woodley.
14 MS. WOODLEY: Good morning. Good morning. I am Kitty Woodley,
15 the Director of the Single Family Property Disposition Division. I am
16 so glad to see so many of you today. We are interested in getting as
17 many proposals as possible to our request.
18 Let me go over, not in a lot of detail, but at least to give you
19 perhaps a better idea of what we are looking for in this solicitation
20 or what we expect to receive from a financial advisor.
21 As you are aware, the Department is undergoing downsizing and re-
22 engineering. And so our current property disposition program will be
23 downsized and re-engineered as a result of the changes.
24 In reading the solicitation, I am sure that you see that what we
25 are interested in and attempting to do is to sell our single family
26 properties via another method. And that method is what we are calling
27 "privatization sales". Sometimes these have been referred to as bulk
28 sales, but we don't want to use that terminology. Bulk sales, by our
29 current definition, refers to properties that have been in our
30 inventory for some extended period of time and we are now trying to
31 get rid of them. The idea here is to sell our properties in a
32 different manner, other than on a direct sales basis or competitive
33 sales basis to individuals, but we are still interested in maximizing
34 our profits.
35 We have sketched out some ideas as to how we want to go about

1 MS. WOODLEY: We, what we are interested in is selling properties in
2 pools, in large quantities at one time. Now, if they are coming up
3 with an arrangement outside of this, for this particular solicitation,
4 I think you will have gone too far, because the idea, we are very much
5 interested in seeing how we can sell large groups of properties at one
6 time, in somewhat of a pool arrangement. You know, the pools can be
7 broken down into groupings of 4,000, 5,000, whatever, as long as they,
8 all the properties in the inventory are covered, or the projected
9 inventory are covered. If you go outside of that, if you go outside
10 of these options, you are not limited to these two options. This just
11 gives you some range of what we are looking for. But, if you go
12 outside of these two options, I think you may have gone too far.
13 Because we are definitely looking at the sale of properties via some
14 type of a pool arrangement.
15 Yes?
16 AUDIENCE MEMBER: In our limited experience, dealing with HUD is often
17 a significant factor in the evaluation of the proposals, often is
18 prior HUD knowledge and experience. So, if you have never had prior
19 HUD knowledge and experience, of course, you will get a contract with
20 HUD because it is 25 instead 100. I noticed the absence of that
21 criteria here. Is that really, really true? I am sorry, but, I mean,
22 you know -- MS. WOODLEY: No, that is really, really true. Simply
23 because we are going to such a different, we are proposing such a
24 different mode of operation. What we currently do we did not see as
25 being as important as coming up with some new or innovative ideas.
26 The idea is to move away from what we currently do. And so, yes, that
27 is really true.
28 AUDIENCE MEMBER: Thank you.
29 MS. WOODLEY: Okay.
30 AUDIENCE MEMBER: If you pool them, you are going to move them off the
31 books a lot quicker, but if you pool them, you are going to move the
32 book a lot quicker, but what if you come up with a disposition way
33 that reduces your expenses from that, from that 120 days or 160 days
34 that you have there?
35 MS. WOODLEY: What can you give me, you can elaborate some more? Can

1 you give me some other details?
2 AUDIENCE MEMBER: Too many people here for that.
3 MS. WOODLEY: Oh, okay. Okay.
4 Let me just say this, if I can help you somewhat, okay. We know that
5 we could improve our current operation. We know right now how we could
6 cut costs. We know how we could cut holding costs. I mean, if it is
7 a matter of re-engineering our current operation to get there, that is
8 not the answer. We know how to do that. The issue here is that while
9 60 percent of our current operation is privatized right now. We use
10 contractors and national contractors and brokers, etc. The issue is
11 that even with such an operation that takes a sizeable number of HUD
12 staff, those staff are not going to be available to us in the future
13 to oversee contractor activities even, and to make decisions about
14 how, you know, we should go about selling our properties, you know,
15 should we lower the price, should we do an auction, etc., etc. We
16 know how to re-engineer our business. We know how to re-engineer this
17 program. So, if that is what you are getting at, that is not the
18 answer. We know how to do that. The answers that we are not going
19 to, the issue is, we are not going to have the staff out there to
20 maintain such an operation even if we were to re-engineer it. We are
21 just not going to have the staff available to use to do that. So,
22 what we have to do is to come up with an entirely different way of
23 doing business. And that is the real issue here.
24 So, I don't know if that answered your question, but I hope that it
25 did.
26 AUDIENCE MEMBER: Thanks.
27 MS. WOODLEY: Okay.
28 AUDIENCE MEMBER: The solicitation, if I remember correctly, talked
29 about the pipeline concept and the possibility even of the deal that,
30 in effect, conveys the defaulted loans before foreclosure is complete.
31 MS. WOODLEY: No, no, he said loans, but I am sure he meant properties.
32 I mean, he may have referred to loans, if that is what you are leading
33 to. No, we are not talking about loans at this point. We are
34 strictly dealing with properties.
35 AUDIENCE MEMBER: I understand, but I want to talk about loans, that

1 business, and those that are, we do recognize do not retail as many
2 properties on an annual basis as we do. So how can we make this
3 workable for those entities out there that are selling foreclosed
4 properties? Or maybe even interest some new entities out there in
5 such a venture. How can we make this a joint money making effort?
6 That is the bottom line. We are not, don't look at this as a way of
7 HUD moving its properties. Again, that is only half of the objective.
8 How can we make this enticing? How can we make this a profit making
9 venture for both HUD and some entities that may not even be players in
10 this game at this point in time? And that is why, you know, we have
11 included the marketing aspect.
12 So, we need you to think more so than anything. I mean, we can give
13 you all kind of data, but we know what the tried and true answers are.
14 If we had other ways of doing this, we could do it. We could, under
15 the current, under our current operation, with a few tweaks here and
16 there, we could improve this program 150 percent without a doubt. And
17 be even better than we are today and we know that. But, we can't do
18 that. We are limited because of staffing. We can't deed you to help
19 us think about doing it in a different way.
20 Yes?
21 AUDIENCE MEMBER: Going back to the previous question on firms that
22 assisted you in coming to the preliminary work coming on this
23 solicitation, if you determine that consultant firms that assisted you
24 are eligible to bid on this financial advisor contract, will you
25 disclose to the rest of us which firms had been helping you in the
26 preliminary work on this?
27 MS. WOODLEY: I think we have said yes to that already.
28 AUDIENCE MEMBER: No, you said that you would make a determination as
29 to whether they would be eligible to bid on this or not. But, if you
30 determine if they are eligible to bid, would you tell us who they are,
31 so we know that --
32 MS. WOODLEY: Okay. Yes. Yes.
33 AUDIENCE MEMBER: My mind just went blank. I think of it and raise my
34 hand again.
35 MS. WOODLEY: Okay.

1 expense for your staff and so forth, as to what your net return is on
2 the property?
3 MS. WOODLEY: Do we --
4 AUDIENCE MEMBER: Could we know that number?
5 MS. WOODLEY: You know, the real issue is, I am not sure that we can
6 fine tune it, but we have some idea. I would think the, the answer to
7 that is, when we get a financial advisor onboard, we will certainly
8 work with that financial advisor to fine tune those kinds of expenses
9 and costs. I don't think that that is something necessarily important
10 at this stage, for you to know. What we are really interested in, we
11 are looking for some innovative ideas, some creative ideas as to what
12 you think the marketplace will bear based on your experiences as
13 perhaps being realtors or in the retail business, for REO. We don't
14 have experience with the marketplace in this arena. And so, what we
15 are looking for is, through your experiences and your contacts, for
16 you to tell us via a proposal that you submit what you think the
17 market will go for. We don't know. So, that is what we are really
18 looking for. What kind of an arrangement could be used for HUD to
19 accomplish its objective, with reduced staff, taking into
20 consideration that we don't want to give properties away, but would
21 consider deferred payments, create financial arrangements, etc. Based
22 on what we have discussed here today, again, keeping in mind, that
23 there is, if you look at this as a spectrum from pipeline to bulk,
24 what could we do in-between. I mean, what is available? Maybe
25 pipeline is too extreme. I don't know. How would you pool these
26 properties? You know, we certainly don't necessarily think that we
27 are going to have some company come in and buy up our whole inventory,
28 considering the fact that we are largest retailer of REO properties.
29 We are selling approximately 55 to 60,000 properties a year, so, we
30 don't expect anybody to come in and buy up all of these properties for
31 some given period of time. So, what will the market bear? You know,
32 what kind of pool arrangement should we consider, regional, national?
33 What kind of investors, or purchasers do we need to gear this up
34 toward? We don't know. We know that this is a new industry. I mean,
35 we know that there are not a lot of companies out there in the REO

Mr. SHAYS. Mr. Harnage, I think your requests are urging something our committee is very comfortable with. So we will certainly include that as part of our oversight effort. Mr. Towns, why don't you start off and then I'll join you.

Mr. TOWNS. Thank you very much, Mr. Chairman. Mr. Carlson, the IG recommends that HUD conduct a cost-benefit of all major contracts. I am concerned that this will add to the costs of the contracts. Can you tell me whether that concern is justified on my part?

Mr. CARLSON. I can try. I think one of the things that happens, and we talked a lot about review boards and those sorts of things—as long as you have a process that requires a lot of review, that takes time. Time costs money for both the contractor and the Government.

I think a cost-benefit analysis makes a great deal of sense at the outset. Obviously, it's an integral part of the procurement planning process. But you may be referring to some of the recommendations that, for example, in the Lockheed contract we've spent $500 million on a certain aspect of it, and the audit criticism was that HUD didn't do periodic cost-benefit analyses rather than renewing options.

In part 17 of the FAR it does talk about making sure that before an option is renewed it makes sense, but it also says, before you give options, there is a reasonable "surety" that you'll exercise them. So the question becomes: Does it make sense to do a cost-benefit analysis if there's nothing you can do about it anyway except perhaps to terminate the contract?

I mean it's really kind of a shadow exercise. The audit says, "Oh, we're getting really shafted," but so what? It's a firm fixed-price contract. HUD spent a lot of money on it, and at the outset, when it was awarded in accordance with the regulations and a comprehensive cost-benefit, it was the right thing to do.

I think that being able to sit back after the contract has closed, and the IG has done this in several instances—they said, "Boy, the contractor made a lot of money. We shouldn't have done it that way." But at the time that HUD made the award it made a great deal of sense for Lockheed to provide computers, for example.

And I am not picking on the inspector general. I don't mean to do that, but when you say that having a firm fixed-price contract to buy services or goods in a decreasing market, when the prices are going down, is not good—I would agree with that, but a firm fixed-price contract is a firm fixed-price contract. And you just don't decide, "OK, we're paying our contractor a lot of money. We're going to terminate it," because that's an option.

Mr. SHAYS. Will the gentleman yield?

Mr. TOWNS. I'll be glad to yield.

Mr. SHAYS. Isn't the issue though that we made a mistake in the first place, and we need to need to understand why we made a mistake and make sure that we don't do that kind of mistake again? I think that's how I read the inspector general's report.

Mr. CARLSON. Well, I was afraid you'd do that because one of the things that happens is, after the cards have been dealt and the hands are all up, it's easy to say that you made a mistake. I think

the real decision point, where you want to analyze the events, is prior to the award of the contract.

Mr. SHAYS. No. No. But what we want to do is to make sure in the next contract we don't make that same kind of mistake. That's——

Mr. CARLSON. Yes, but Mr. Chairman, that's not a mistake. You see, that's the gross flaw in the inspector general's—I don't mean to pick on the inspector general—many——

Mr. SHAYS. Let me just say something. That's disingenuous to say you don't mean to pick on her. You have a disagreement. We want to know the disagreement. I, frankly, don't agree with you, so I'd like to hash it out a bit.

Mr. CARLSON. I would, too.

Mr. SHAYS. Let me just say I am going to come back to this because we'll pursue it a little bit more. I kind of injected myself.

Mr. TOWNS. That's OK. Sometimes the flow is very good, so I don't want to break the flow that you have there.

Mr. SHAYS. OK, if you didn't mind then, just pursue it. I don't understand your logic.

Mr. CARLSON. Well, when you look at a firm fixed-price contract, what happens——

Mr. SHAYS. I understand a firm fixed-price contract. The contractor may win or it may lose, and the public may win or they may lose, but if it's so out of line, then I want to know what is the culture and the process that allowed it to happen and are we doing that consistently?

Mr. CARLSON. Well, let me—you're two steps ahead of me. If I may just take two steps back. In the firm fixed-price contracting rules, the fact finding and the decisionmaking and all of those processes occur prior to the contract being awarded.

What I am suggesting is that what's evident in the audit report doesn't support the conclusion that it was an improper award. If, in fact, it made sense—let's just say that at that point when the contract was awarded in 1984, whatever it was, computer prices were rising. The costs of PC's were rising. For HUD to enter into a firm fixed-price contract would have made a great deal of sense because they would then have protected themselves against further price increases.

The fact that the prices decreased, and HUD theoretically paid more than they should have, is irrelevant.

Mr. SHAYS. No, it isn't irrelevant. No, it's not irrelevant, and I'll tell you why—at least I don't think it's irrelevant. It may be that we didn't have the proper level grade person with the education and expertise to know that it was 9 out of 10 that prices would drop. And that's all I am saying.

I am not going to over read, but it may be that's the—we don't have people that have the expertise to really understand when they should have one kind of contract versus another. And I am not going to make a determination on that other than to say it's something we need to look into.

Mr. CARLSON. Oh, absolutely, and I think in my testimony I indicated that. I am not in any way implying that HUD doesn't need to take a look at its contracting practices.

Mr. SHAYS. Well, that's the way I read it though. I am going to take the HUD IG report and say, "Are there lessons to be learned?" and we are going to work our new procurement officer to just have him give us some feedback on that.

HUD accepts the criticism of this, and I think rightfully so and is taking action. So, let me just tell you where I get a little suspicious. Mr. Towns and I had a hearing on procurement of health care services and equipment, and we have in our statute that we can only re-bid and lower the price on these products if it was grossly excessive.

So we were paying excessive prices, but as long as they weren't grossly excessive, it was OK. I mean it was this kind of inane process. So I am just suspicious of——

Mr. CARLSON. Well, I don't blame you for being suspicious. I think that you should be suspicious, but the answer is not to go and take action based on subsequent events. I mean I think it's absolutely a legitimate exercise to go back and say, "What were the facts that were available to the contracting officer before he or she made the award in the firm fixed-price contract?"

Mr. SHAYS. Yes, that would be fair. That's what I would—and that's what I am suggesting.

On that we agree. And then we can come to conclusion, but then I also want to know the person at HUD that they had the expertise to really evaluate it.

Mr. CARLSON. Well, that's another whole issue that I have given a lot of thought to, because training—you know, I have been doing this for a long, long time—training is very important to me. I do a lot of lecturing and teaching, and I've had an opportunity to talk to a lot of contracting officers in the Government and on the industry side.

And for the most part, when you get the two of them together it's amazing the things that they learn from each other. Maybe, when I get a chance to talk to Mr. Carberry I have some ideas as to how he might want to approach it.

Because that is the critical thing. To give someone a CD–ROM and say, "Here, go work through this," is not training. Training needs to be something that's interactive and all those sorts of things.

Mr. SHAYS. Thank you. Mr. Towns.

Mr. TOWNS. Right. Thank you very much, Mr. Chairman. You know, I am concerned about privatization and accountability. I am concerned about accountability and privatization. Can you tell me what steps should be taken to assure accountability?

Mr. CARLSON. To assure accountability of the Government representatives and then holding contractors accountable as well?

Mr. TOWNS. Right.

Mr. CARLSON. Well, I think there are several steps that can be taken. First, as Mr. Carberry and others have said, is the procurement planning process. You know, within all organizations there are two groups of people. There are—sometimes we jokingly say, "They're the program people who are trying to get things done. On the other side are the contracting people trying to prove to the programming people that they can't do that."

In reality you need to have a leader that brings the two together. The program manager, the technical person that's buying the services has to have the skills, the interpersonal skills, and those sorts of things to build a team out of the people that are going to be supporting his or her program. Making those people accountable, and I don't know how you do that in the Government. It's been a long time since I worked for the Government, but it's a matter of making them accountable and giving them the tools to do the job.

You don't need millions of pieces of data. What you need is information, and there's a big difference between having access to every little bit of minutiae that a contractor may have available as opposed to useful information such as how much effort has been expended, how much physical progress has been made. Those are two or three numbers. You don't need reams and reams of data to track and monitor a contract.

But a lot of times we get seduced by the fact that we can have access to everything. We had HUD technical people say they want to know by the hour what a person on a services contract charges. That's wild. There's nothing you can do about it because it's been spent.

You can argue about whether you want to reimburse the cost on a cost reimbursement contract, but it's not going to change the fact that the individual charged that. So the metrics have to be re-evaluated to see if we're really measuring the things that make a difference.

Most successful managers pick four or five things that they want to track. That tells them whether their program is in trouble or not. I don't think that HUD has the skills necessarily available to them to do that, identify what makes a successful program.

And those are the things that need to be done. It's not putting in a $600 million computer system. It's allowing people to work in little groups responsible for certain areas, making them accountable for it; letting them have some respite from oversight that draws inferences that are incorrect or that say you complied with the regulations but you still made a mistake.

Protect them from those sorts of things. Tell them, "You have the responsibility for this area." Set up the five or six things you want to do. Set up your data base, but we need these 10 key elements sent up to headquarters. I mean it's all very easy to do. It's not rocket science. It's just a matter of somebody having the will to do it and realize that a whole bunch of little solutions is better than one big one that will never work.

I mean procurement's been in reform since 1776. There were problems with contractors in the French and Indian War who contracted to provide rations to troops up in Michigan, and they only got some of the rations there.

We have words that were created out of government contracting. For example shoddy. Shoddy was generated as a result of the Civil War where contractors took old material and chopped it up into little pieces called shod and rewove it. The troops would wear it, and it would melt off their backs, and so they called it shoddy. It has come to mean shoddy workmanship.

We've had the Grace Commission. We've had the Packard Commission. They all say exactly the same thing. So you've been doing

this for 222 years. You look around and say, "What's happening here? We know the problem. We know the solutions," but we can't seem to put the two together.

And if someone is sitting on the outside, trying to work between the contractors and the Government, it's incredibly frustrating.

I taught at DSM Center—I don't mean to get on a soapbox; I apologize—but when I taught at the Defense Systems Management College, I would explain to the Government program managers there about what happens if they affect a contractor's cash flow, what that meant to a contractor. They had no idea. They said, "Oh, my God, that's kind of serious, isn't it?" Yes, it is.

And so that is the kind of education people need. You need to do training with contractor and Government employees there, with an inspector general representative there too. We need to give them a couple of days training, let them go back to work for 2 months, bring them back for 2 more days and say, "OK, this is what we suggested you do. Did you try it?" "Yes. It didn't work." "Why?" And you work though the problems together.

It's all not like this and it's not working.

Mr. TOWNS. Mr. Harnage, do you want to add anything to that? He brought us from 1776 up. [Laughter.]

Mr. HARNAGE. Well, in his examples I point out a whole lot hasn't changed. No, I'd just say the reference to why do a study if the end result is going to be the same, there's a way with the A–76 under those circumstances. If you know the outcome is going to be what the current is, then you are not required to do an A–76 study.

One of the questions that was asked by Mr. Kucinich was answered, but it wasn't really answered to the full extent, and that had to do with a particular contract that is being considered now with three contractors and they were told, "Well, A–76 was not used because Federal employees didn't do this." Yet the very statement by the official of HUD was telling these three contractors, "You're to do the work currently done by HUD employees plus that work done by REAM's."

Now he's signaled in on the latter part of it and omitting the first part of it. Under the first part of it where you're doing work presently performed by HUD employees, A–76 is required. But, more importantly, I think the question needs to be asked, "Why not use it?"

If it works and it makes sure that the taxpayer gets the best deal, why not use it? Why aren't we making these cost comparisons? Why aren't we doing these performance statements? What aren't we getting the most efficient organization before we do these studies? And where A–76 is being able to be circumvented in HUD is they are reducing the number of employees so that they are not there to do the job and then that justifies the contracting out.

If they looked at it now and came up with the most efficient organization and then made the decision how many HUD employees are to be there, you wouldn't be in this dilemma, but they have the cart before the horse. They downsize the employees and then decide what the job needs to be done. Oops, we don't have any employees. Let's contract it out.

What HUD is doing under its 2020 program is designed to contract out. It is not designed to get the most efficient job done.

Mr. TOWNS. Let me thank you, Mr. Carlson and Mr. Harnage. Mr. Chairman, I yield back.

Mr. SHAYS. Thank you, one of the companies in my district is Pitney-Bowes, and I am not bringing it up as it relates to the fact that they do services down in here for the Postal Services.

I just want to briefly say that when I went to visit the plant, what was very exciting was that the people who showed me around the plant were the workers, the union leaders, and they talked about how jointly they had taken an entire floor in the building and were able to do what they did in four plans into one floor just because they had become so much more efficient, working together, the laborers and management, and then they'd even been able to reduce what happened on that one floor into half a floor.

And I am talking a fairly large building. And it was just amazing. And the productivity of the workers was pretty incredible.

I happen to believe that sometimes the private sector can do it better, and I happen to believe that sometimes the public sector can do it better. What I am struck by your message, Mr. Harnage, is that you're saying basically that the downsizing happened first. It wasn't a team effort to say how can we be more efficient and then no longer need employees. And I think that's pretty clear.

And so I have to take a role in that because it's to my side of the aisle to see if we can reduce the size of the Government, but your message to me is that it's got to be a cooperative effort.

But the other thing is that you urge us to—it seems to me, and I'd like you to expand on this—you urge us to compare what the public can do at cost and how the private sector could do it, to see if sometimes we're farming out something when in fact the public, the employees within house, can do it more efficiently? How do we do that? What's the process that would determine that?

Mr. HARNAGE. Well, an A–76 is the process for doing that, and I think the message that we're giving is sometimes misunderstood because it's a little untraditional. We're not saying we're totally against contracting out. There are times out that contractors can do it better. The private sector can do it better, and we recognize it.

What we're saying is competition—the competition saves the taxpayers money regardless of who wins—and therefore competition should be taking place in every instance where you can do that. It ought to be fair competition, and that's where the debate becomes. Each side argues, "This is not fair. This is fair."

But A–76 is the best we've been able to come up, in cooperation with the private sector, in cooperation with the administration, in cooperation with the unions, and even the public. A–76 was rewritten about a couple of years, and it was improved, and there was a provision put in there to bring it back in-house if it was more feasible. That's not being utilized. In fact the HUD officials didn't even know it was there until this morning.

Where we make a mistake, we make a mistake—an honest mistake but a mistake—it shouldn't be a permanent one. And so, if we're really into competition and we're really into getting the taxpayers the best bargain, why aren't we re-competing that every so

often to determine is it now better to bring it back in-house and save the taxpayers money or should it stay outside, as well as studying those that are in-house, whether or not they should go outside.

Mr. SHAYS. Mr. Carlson, that seems logical to me and reasonable. Would you disagree with what you just heard? You know, I expected Mr. Harnage to come in and basically say, "It's your civic responsibility to make sure that if it's public, it's done by the public."

That's not the message I've heard from him. It's not the message as I've gone through his statement. His response was that the public sector should also be able to compete for it as well as the private. Would that be a statement you're comfortable with?

Mr. CARLSON. I have no philosophical disagreement with that. I think, however, that if a contract has been awarded to someone that is firm fixed-price for 4 years or whatever, that while it may be an interesting exercise it would be a purely academic exercise to test it prior to the end of that contract unless someone were to decide that a contract termination would be appropriate. To change horses in the middle of the stream, so to speak.

But I can tell you from personal experience, because that's what I do for a living, that if you terminate a firm fixed-price contract in that kind of circumstance, someone could put together what is called a termination settlement claim that would knock your socks off.

Mr. SHAYS. Well, it seems to me that if you have a firm fixed-price contract that sometimes the private sector could lose on that, and sometimes it can gain. The benefit to the public is that at least we know we are paying. We are not going to pay more. We are not going to pay less.

Now, but what I am also hearing from the private sector in other areas is that sometimes we bid out to the private sector and then the private sector comes back and asks for more and asks for more and that to me is a legitimate complaint on the part of the public sector employees.

Mr. CARLSON. Well, Mr. Chairman, I don't know if I can speak to the public sector employees. I am just not familiar enough with A–76 and those sorts of things. I think Mr. Kucinich, the gentleman from Ohio, was talking about contract growth but all the contracts that were referred to in the Inspector General's report grew properly at HUD.

Indefinite quantity contracts are just that. If there is a need for more than anticipated, the contract value would grow. You can get very dramatic responses by saying a contract grew from $9 million to $30 million. People's eyes will flutter and their ears will smoke. But in reality it's all legitimate because the requirement was not known at the outset, and if HUD has an IGC contract which is based on competition at the outset, that's what the vehicle is designed for. And I don't know how that relates to Government employees.

Mr. SHAYS. Well, but one of the things that I think comes out pretty loud and clear from the IG and GAO is that we have people who aren't qualified to bid out these contracts and oversee them, and frankly I'd be surprised if you would disagree with that.

Mr. CARLSON. Oh, I would not disagree with that, but I think the thing that I would caution is that there are things in the audit that are, I guess inflammatory. For example, that Price Waterhouse, a contractor that big, ought to buy its own computers. There's a cost-standard which talks about consistency that allows a contractor to charge direct for equipment if it's for a different purpose.

If the Government requires a contractor to use a total cost input base for allocating general and administrative expenses, they have to get a markup; otherwise, the general administrative cost comes out of profits. And yet, these proper treatments are characterized as things that are evil, that are the result of incompetence, and it's not.

And for people to think that all of our contracting officers are stupid and our contractors are crooks is unacceptable to me.

Mr. SHAYS. Now, first off, I think you do a disservice to yourself by making that statement and also to the inspector general and GAO because they specifically did not say all of them were.

Mr. CARLSON. Oh, that was Mr. Kucinich's statement.

Mr. SHAYS. Oh, OK.

Mr. CARLSON. I am sorry. And I would be glad to introduce him to a good contractor if he'd like.

Mr. SHAYS. I happen to disagree with Mr. Kucinich.

Mr. TOWNS. You know, you raised a very interesting point. In going over the information, seeing it in terms of how they raised the question of the contract, but then when you look at other agencies in the Government, where they do buy this equipment—I mean it's done all the time and nothing is said.

The inconsistency here sort of bothers me. I think, Mr. Chairman, that maybe we need to look at that as well because for them to be criticized and then to know that other agencies are doing it, and HCFA in particular I mean does it every day. They buy equipment and all kinds of things for people in contracting and then criticize this, I just find that very interesting.

Mr. SHAYS. Well, the inspector general doesn't oversee other agencies. So they got a job to look at their own agency.

Mr. TOWNS. Yes, but I am saying that if it's wrong and inefficient and all these other kind of ugly things, you know, over here. Then, God, it must be really ugly over on the other side. That's all I am saying. That's the only point I am making.

Mr. SHAYS. OK, well, if that's your only point then OK. Let me just say to you that my approach in this first hearing is just to introduce us to this issue and to—Mr. Carlson, I think we'll have more contact, and Mr. Harnage, I appreciate the tone of your testimony because the bottom line is the public sector is going to find itself out of business if it can't compete with the private sector. Therefore, it's important that we make sure the public sector has the tools to adequately compete.

But I do believe in contracting out. I just think sometimes you can be far more efficient. I realize this is kind of a stretch to make an analogy, but our local electric plant in Bridgeport, they're ultimately going to sell it to a smaller company and they'll sell to a larger—and be part of a larger grid because they can't always operate at peak performance. And sometimes they're not operating the

plant at peak performance and peak efficiency, whereas if it was part of a larger grid, they could and reduce costs for everyone.

And I realize that's the private sector actually selling out, and in some cases the private sector contracts out for services. I was meeting with Mr. Walch at GE, and they don't do the food in their cafeteria anymore, and the people who do the laws, they're private contractors, and it's much more efficient for the company and then all the other employees who work in the company can be focused on their primary responsibility.

It just makes me make one more point that I want to make: It seems to me that some of what HUD has to do will be, as we do downsizing in some cases, that the employees who remain will have to have an expertise sometimes in contracting out, but the other part is that the employees who remain also have to have the ability to know how they can compete and actually make a bid presentation and show how they can do it better than the private sector.

So we look forward to having that dialog and I appreciate Mr. Carberry staying and just listening to this testimony as well.

Bottom line, this is just our introduction. Either way, I don't know what party will be in power next year, but I do think that on that side a ranking member that you know—[laughter]—let me say this to you: He did this to me last time and told me he was going to have the gavel, and he didn't get it. And he was duly humble when he came back.

I will say, though, given our record in the last few weeks, I am getting concerned. [Laughter.]

But we'll see how we can change that. At any rate, great to have you here, and we'll be working with you regardless of who's in charge. Thank you. Take care. And this hearing is adjourned.

[Whereupon, at 12:35 p.m., the subcommittee adjourned subject to the call of the Chair.]

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