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FEATURE COMMENT: Emerging Issues In Iraq Reconstruction Contracting—Audits, Investigations, And The Transition Of Sovereignty

The reconstruction of Iraq has become outsourced nation-building. Tens of billions of dollars are flowing to thousands of prime contractors and subcontractors, creating an unprecedented level of private-sector involvement in a diplomatic and military mission. At the same time, the risks to contractors—from the attacks on contractor personnel, to high-profile audits and investigations, to the June 30 transition of sovereignty from the Coalition Provisional Authority (CPA) to an Iraqi-led government—have received worldwide attention.

This article focuses on two distinct categories of emerging issues of concern to contractors: (1) the rising tide of audits and investigations targeting Iraq contracts, and (2) the impending government transition, including the continuing role of the United States in security activities and reconstruction activities.

The Rising Tide of Audits and Investigations—Contracting in Iraq has been described as a “gold rush,” with tens of billions of dollars up for grabs to companies that choose to participate in the process. At the same time, solicitations are requiring proposals to be submitted within a period of days—not weeks or months—and award decisions are being made in minutes or hours, often without the benefit or a complete evaluation of offers. This state of affairs is generating a wave of audits and investigations at almost every level of the contracting process.

The rapid buildup of contracting activities in Iraq presents an atmosphere similar to that expe-

rienced by the defense industry in the 1980s. Following a surge in defense spending, a number of procurement scandals and investigations arose. The most notable was Operation Ill Wind, a vast criminal investigation into procurement fraud conducted between 1986 and 1990. That investigation targeted corrupt procurement practices infesting the defense industry, and it resulted in the conviction of more than 90 companies and individuals in dozens of defense programs. The continual public reports of fraud and waste severely eroded public confidence in the defense industry.

The acquisition process and business environment involved in the reconstruction of Iraq are ripe to produce a similar circumstance. While the Government has shifted the bulk of tasks to contractors, it has also leanly staffed its contracting activities. The acquisition officials on the ground in Iraq are few in number, rotated frequently, and overworked. The contracts produced by this skeletal contracting apparatus have been harshly criticized. In one instance, the Army approved a contract worth \$587 million to Halliburton in just ten minutes.

At the same time, the Government has dramatically increased the audit and investigation resources dedicated to uncovering improprieties in Iraq reconstruction contracting. This comes on the heels of the corporate scandals that began occurring in 2001, and which have heightened this country’s focus on ethical violations, accounting irregularities, and illegal conduct. The headlines concerning Halliburton and a handful of other companies speak for themselves. To those of us heavily involved in Iraq reconstruction, it is regrettably apparent that many contractors in Iraq—even the most principled corporations and organizations—will not be immune from intense scrutiny.

As Dr. Dov Zakheim, the former under secretary of defense (comptroller) recently stated in testimony before Congress:

Many contractors that have not had problems in performing their domestic [Department of Defense] contracts are having difficulties in adjusting to the unique environment in Iraq and

to their own firms' influx of new business. We believe that contractor financial and internal control problems will resolve themselves, but in the meantime, we will take whatever actions are necessary to protect the Government's financial interests. DOD has enforced and will continue to enforce the highest standards for contracts in Iraq and anywhere else.

Contracts for Rebuilding Iraq: Hearing of the Committee on House Government Reform, Mar. 11, 2004 (Statement of D. Zakheim).

Broadly speaking, the audits and investigations focusing on Iraq reconstruction contractors are targeting three areas: fraud, corruption, and costs and pricing compliance.

- *Fraud.* Government auditors and investigators are instructed to “think fraud” when examining the activities and records of contractors. The Government has a wide range of civil and criminal laws for combating fraud, with remedies including monetary penalties, contract suspension and debarment, and imprisonment. This section describes the Government's enforcement tools to combat fraudulent activity.

First, the false statements statute makes it illegal for anyone “knowingly and willfully” to make a false statement or representation concerning a matter within the jurisdiction or agency of the United States. See 18 USCA § 1001. A “statement” includes any oral statement or written document, both sworn and unsworn. The statement must be material, meaning that it must have a natural tendency or capability to influence a decision or function of the Government. The false statements statute also prohibits concealing or covering up, by means of some trick, scheme, or device, a material fact where there is a duty to disclose.

The person need not make the statement directly to a Government agent for it to relate to some matter within the jurisdiction of the United States; it need only be a statement that could affect some aspect of an agency's function. For example, a subcontractor that submits an invoice with wrong product numbers to a prime contractor may be liable under the false statements statute, even if the prime does not submit the invoice to the Government, because the invoice could affect the Government's audit of contract performance.

Second, there are two False Claims Acts: the criminal False Claims Act at 18 USCA § 287, and

the civil False Claims Act at 31 USCA § 3729. The criminal False Claims Act makes it illegal for anyone to make or present any claim upon or against the U.S. that the person knows is “false, fictitious, or fraudulent.” The definition of the term “claim” includes any request or demand for payment of money or credit or the transfer of property; as a practical matter, any attempt to get money from the Government is a claim. The claim need not be made directly to the Government, and there is no requirement to show an intent to defraud the Government. This statute has become especially relevant in Iraq contracting, primarily due to inflated invoicing and product substitutions.

The civil False Claims Act also addresses the presentation of a false claim to the Government, but it focuses on conduct that is reckless or done in deliberate ignorance of the truth; the Government does not have to prove that the person had actual knowledge of the falsity of the claim. Additionally, the Government need only prove a violation by a preponderance of the evidence, rather than the “beyond a reasonable doubt” standard for the criminal act. This civil statute provides for civil prosecution with penalties and treble damages.

The civil False Claims Act also contains a *qui tam* provision that allows a private individual to file a lawsuit in the name of the U.S. Government charging fraud by a contractor. The whistleblower bringing such an action has an opportunity to share in any award against the contractor. Statistics indicate that more than 4,000 *qui tam* suits have been filed since 1986, when the statute was strengthened to make it easier and more rewarding for private citizens to sue. The Government has recovered over \$6 billion as a result of the suits, of which over \$960 million has been paid to whistleblowers.

Third, the Major Fraud Act, an outgrowth of Operation Ill Wind, makes it a separate criminal violation to defraud the Government in connection with contracts of \$1 million or more. The act makes it illegal to knowingly execute or attempt to execute any scheme or artifice with the intent to defraud the U.S. or to obtain money or property by false or fraudulent pretenses, representations, or promises. See 18 USCA § 1031. The penalties for violation of the Major Fraud Act are significantly greater than those of the other statutes discussed in this section. The Act also permits the Attorney General to pay a \$250,000 bounty to a whistle-

blower that furnishes information relating to a possible prosecution for a major fraud.

In addition to the statutes described above, there are various civil and administrative remedies available when a person commits fraud in the context of a Government contract. The Program Fraud Civil Remedies Act allows federal agencies to impose administrative monetary penalties for false statements and false claims of \$150,000 or less. See 31 USCA § 3801. The Government may also suspend or debar a contractor that is found to be dishonest, unscrupulous, or otherwise irresponsible. See Federal Acquisition Regulation (FAR) 9.405. A suspended or debarred contractor is excluded from receiving any additional Government contracts—the harshest penalty for a company whose primary customer is the Government. Finally, the Government may void or rescind a contract that is based on fraud. See, e.g., FAR 3.703.

- *Corruption.* Several corruption statutes applicable to U.S. Government procurements are also being actively applied in the context of Iraq reconstruction contracting.

First, the bribery statute prohibits the corrupt offering, promising, or giving of anything of value to a Government official (1) to influence any official act, (2) to influence the public official to participate in any fraud on the Government, or (3) to induce the public official to do or to refrain from doing anything in violation of his lawful duty. See 18 USCA § 201(b). The law also prohibits the official from soliciting or receiving the bribe. It is still a bribe if the payment is made to someone other than the public official, as long as it is paid on behalf of the public employee. See *U.S. v. Kelly*, 748 F.2d 691, 699 (D.C. Cir. 1984).

Second, the gratuity statute, like the bribery statute, is a criminal law that applies to offers and solicitations of gifts. The gratuity statute prohibits any gift or payment of a thing of value for or because of any official act performed or to be performed by the public official. See 18 USCA § 201(c). Even “wining and dining,” a common marketing tool within the commercial world, can violate the statute if it is given as a reward for a specific official act that the official would have regularly done. Gratuities are prohibited so as to discourage attempts to gain favor with a public employee, even if corruption is not intended by the donor or the recipient.

The main difference between the bribery and gratuity prohibitions is the intent requirement: the bribery statute requires a showing of corrupt intent on the part of the offeror and a showing that the gift is a *quid pro quo* made in return for an act by a Government official, whereas the gratuity statute requires only a showing of a wrongful purpose to offer or accept a thing of value because of an official act. Compare *U.S. v. Sun-Diamond Growers of California*, 526 U.S. 398, 414 (1999), with *U.S. v. Tomblin*, 46 F.3d 1369, 1380 (5th Cir. 1995).

Despite these broad prohibitions, there are limited circumstances where giving a thing of value to a public employee is not prohibited. These circumstances are generally confined to situations where giving a nominally valued gift would not realistically produce corruption, such as serving refreshments to guests when public employees are present. The Office of Government Ethics publishes guidelines on this topic. See http://www.usoge.gov/pages/forms_pubs_otherdocs/forms_pubs_other_pg2.html#Anchor—O-42881.

Third, the Anti-Kickback Act, similar to the two statutes described above, prohibits giving anything of value for the purpose of improperly inducing or rewarding favorable treatment in connection with a prime contract or a subcontract relating to a prime contract. See 41 USCA § 52. In the case of this statute, however, the recipient of the “thing of value” would be a prime contractor or a subcontractor—not a Government official. The prohibition extends to all instances of behavior that constitute a commercial bribe in connection with a Government contract. The significant number of subcontracts being awarded in Iraq makes this form of corruption likely to occur, and audit and investigation reports are beginning to bear that out.

Fourth, the Foreign Corrupt Practices Act (FCPA) prohibits bribery of foreign officials in connection with doing business in a foreign country. More specifically, it prohibits “any domestic concern” from corruptly using interstate commerce in furtherance of paying anything of value to any foreign official for the purpose of (1) influencing any act or decision of such foreign official in his official capacity, (2) inducing such foreign official to do or to refrain from doing any act in violation of his lawful duty, (3) securing any improper advantage, or (4) inducing such foreign official to use his influence to affect any act or decision of a foreign government

to assist the domestic concern in obtaining or retaining business for or with any person. See 15 USCA § 78dd-2.

The FCPA defines “any domestic concern” as any U.S. citizen, national, or resident, or any corporation or other business entity organized under U.S. laws or that maintains its principal place of business in the United States. The FCPA also bars domestic concerns from using foreign agents for this same purpose. However, it exempts from coverage “facilitating or expediting payments” whose purpose is to expedite or secure the performance of a routine governmental action. *Id.* at 788dd-2(b); *U.S. v. Kay*, 200 F.Supp.2d 681 (S.D. Tex. 2002). It also excludes payments that are lawful under the foreign country’s laws and regulations. See 15 USCA § 78dd-2(c). FCPA violations may play a significant role as contractors begin dealing more with the Iraqi ministries following the June 30 transition of government (described below).

- *Costs and Pricing Compliance.* Contractors dealing with the Government must submit accurate pricing and cost-related information, both as part of their proposal and during contract performance. Many prime contractors and subcontractors are required to have accounting systems that comply with the Cost Accounting Standards (CAS) and the FAR Part 31 cost principles, and that will support the submission of cost and pricing data under the Truth-In-Negotiations Act (TINA). In the context of Iraq contracting, the Government is scrutinizing compliance with these cost standards, as well as how contractors charge their time and expenses.

When applicable, the CAS requires that the contractor’s cost accounting practices comply with 19 specific standards (if subject to “full” coverage) or four standards (if subject to “modified” coverage). The CAS necessitates changes to the cost accounting systems typically relied upon by commercial businesses and requires disclosure of a company’s current cost accounting practices in a formal Disclosure Statement. See FAR 52.230-2. From a practical viewpoint, these requirements may exclude companies without a CAS-compliant accounting system from competing for contracts.

The cost principles, contained in FAR Subpart 31.2, include general guidance regarding the allocation of costs, provide administrative guidance, and address categories of cost that are either unallowable or for which allowability is qualified or limited

in some respect. These principles require the company to establish an accounting system that identifies and excludes unallowable costs from proposals and invoices to the Government.

The TINA and the implementing clauses require contractors to submit “cost or pricing data.” See 10 USCA § 2306a and 41 USCA § 254b. The information embraced by the term “cost or pricing data” includes “all facts . . . prudent buyers and sellers would reasonably expect to affect price negotiations significantly.” See FAR 15.401. The requirement must be flowed down to subcontractors at all tiers unless they separately qualify for an exemption.

Contractors are also required to keep complete and accurate records of their cost accounting practices and the costs incurred in performing each contract. A contractor’s ability to obtain payment often depends upon whether it charges costs to the proper account. Time charging has been particularly difficult in the wartime situation of Iraq, where employees often do not work a regular schedule. Nevertheless, a contractor that cannot substantiate its expenses runs the risk of having them denied for reimbursement by the Government. Worse yet, a contractor that mischarges the Government will have to reimburse it for the mischarged costs and may also be subject to prosecution under the fraud statutes described above.

Several key agencies are enforcing the fraud and corruption statutes and the price and cost-related requirements in the context of Iraq reconstruction. Over the past four months, the Government has significantly ramped up the oversight capabilities of these agencies. Additionally, the unique circumstances of Iraq are increasingly making contractors a focal point for congressional oversight. The following analysis describes the auditors and investigators actively pursuing Iraq contracting improprieties.

- The Defense Contract Audit Agency (DCAA) is responsible for performing all contract audits for DOD. It also provides accounting and financial advisory services regarding contracts and subcontracts to all DOD components responsible for procurement and contract administration. DCAA’s Iraq branch will have 31 auditors by the end of May 2004. Complementing this in-country support, DCAA auditors provide contract oversight at the stateside locations of U.S. firms that have major contracts

in Iraq. To date, DCAA has issued nearly 200 Iraq-related audit reports covering forward pricing proposals, costs directly incurred on existing contracts, and contractor policies and internal controls. These audits have resulted in questioned costs of \$132.6 million, unsupported costs of \$307 million, and suspended costs of \$176.5 million. The U.S. Army Audit Agency performs a similar function in relation to Iraq reconstruction, but its activities are more limited thus far.

- The DOD Inspector General (IG) serves as “an extension of the eyes, ears, and conscience” of the Secretary of Defense on matters relating to the prevention of fraud, waste, and abuse in the programs and operations of the Department. Although the DOD IG has issued only one audit report to date in relation to Iraq contracting, the findings of that report are worthy of note: of the 24 contracts awarded by DOD’s Washington Headquarters Services, almost all involved instances of Government officials circumventing or “liberally interpreting” contracting rules. For almost every contract, officials failed to establish firm contract requirements, to support price reasonableness determinations, or to provide oversight on awarded contracts. See *Contracts Awarded for the Coalition Provisional Authority by the Defense Contracting Command-Washington*, Report No. D-2004-057, Dep’t of Defense Office of the Inspector General, Mar. 18, 2004, available at www.dodig.osd.mil/audit/reports, 46 GC ¶ 138.

- The IG of the U.S. Agency for International Development (USAID) serves a similar role for that agency. As with DOD, the USAID IG has found that its agency has not acted fully in compliance with contract regulations. Findings include the following: selecting a contractor without determining whether it had an official facilities security clearance, failure to adequately document the decisions made for market research in identifying prospective contractors, and failure to make proper notifications to unsuccessful bidders.

- The CPA also has its own IG pursuant to Public Law 108-106. The CPA-IG serves as an independent, objective evaluator of the operations and activities of the CPA, and coordinates the activities of the auditors and IGs from U.S. agencies. Since his appointment in January 2004, the CPA-IG has grown his staff from 2 to 58 employees. That office’s “top priorities” include ferreting out “corrupt or deficient practices” and ensuring “contractor corporate

governance compliance.” See *CPA-IG Report To Congress*, App. L—CPA-IG Audit Planning and Areas of Interest, Mar. 30, 2004, available at www.cpa-ig.org/pdf/cpaig_march_30_report.pdf.

- The Defense Criminal Investigative Service, the criminal investigative arm of the DOD IG’s office, has initiated a Middle East Task Force that focuses on Iraq reconstruction contracting. That office has numerous ongoing investigations involving bribery, kickbacks, improper cost and time charging, product substitution, and other corrupt and fraudulent activities by contractors. Given that the audits and investigations of Iraq contractors is increasing in number and scope, more criminal investigations are also expected.

- Finally, congressional committees and certain members are fervently questioning administration officials and contractors on their procurement-related decisions and actions relating to Iraq. The Senate Armed Services Committee, the House Committee on Government Reform, and others have held hearings on the topic over the past two months, and there is talk of a special investigation into waste, fraud, and abuse in the reconstruction contracting process. While some argue that Halliburton has become the poster child for politicization of the reconstruction effort, it is undeniable that the growing scrutiny coming from Capitol Hill is not being confined to that one company.

This increased level of scrutiny shows that the Government will not “overlook” improper conduct merely because it occurs in a wartime environment. Contractors are being judged by the same standards as would normally apply. Accordingly, the prudent contractor must take extra affirmative steps to mitigate the compliance risks inherent in this atmosphere. This effort should include (1) training employees for the common legal pitfalls that they might encounter in the context of Iraq; (2) enforcing the company’s written code of conduct; and (3) self-policing as a means of confirming management’s commitment to abide by ethical and legal standards, and of discovering and correcting instances when conduct falls below these standards.

The Government is also asking contractors with Iraq reconstruction contracts greater than \$5 million to voluntarily provide their internal compliance systems, codes of ethics, and codes of conduct to the CPA-IG. This request was devised to as-

sist in assessing how many of these contractors have current compliance programs, what actions contractors are taking to ensure compliance with federal laws, and whether contractors are actively seeking to identify and remedy compliance deficiencies. The CPA-IG intends to use this data to decide whether to recommend to Congress additional legislation to improve contractor compliance performance. See *CPA-IG Report To Congress*, p. 19, Mar. 30, 2004.

The Transition of Sovereignty—The political-military situation in Iraq brings to mind the words of William Faulkner: “What’s wrong with this world is, it’s not finished yet.”

The fluid situation in Iraq—the impending transition to a sovereign Iraqi government, the pull-out of certain Coalition partners amid security concerns, and the increased level of violence last month—has caused widespread questioning of the reconstruction efforts’ future. The CPA, United States, and United Nations have recently undertaken efforts to quell the “false pessimism about the Iraqi transition” by outlining plans for the transition. This section addresses the three primary issues impacting contractors during this changeover: (1) the structure and leadership of the new Iraqi government, (2) the continuing role of the U.S. Government vis-à-vis Iraq and the reconstruction contracting community, and (3) the security situation.

- *The New Iraqi Government.* On June 30, 2004, the CPA will cease to exist, and a new Iraqi-run government will begin functioning. The CPA, which has served as the temporary government of Iraq since the April 2003 overthrow of Saddam Hussein’s Baath Party regime, was designed to function only until Iraq is sufficiently stable to assume its sovereignty. See *CPA Overview*, available at www.cpa-iraq.org/bremerbio.html. Last November, CPA Administrator L. Paul Bremer and the Iraqi Governing Council collectively chose the June 30th date for the transfer of power.

The plan for establishing the new Iraqi government has been developed by the United Nations’ Special Advisor to the Secretary General, Mr. Lakhdar Brahimi. It involves three stages over the next 18 months. First, a caretaker government will be in place from June 30 until the end of December of this year. Mr. Brahimi is in the process of selecting the leaders of that government. Some members of the Iraqi Governing

Council are expected to play a prominent role under Mr. Brahimi’s plan.

Next, a Transitional National Assembly (TNA) will be elected in December or January. The TNA will then elect a three-person Presidency Council comprised of a President and two Deputies, who will appoint a Prime Minister and a Council of Ministers. Together, the TNA, the Presidency Council, and the Ministers will comprise the Iraqi Transitional Government. In addition to serving as the legislature, the TNA will draft a new, permanent Iraqi constitution, which will be submitted for popular ratification by October 15, 2004.

Finally, elections under the new constitution will be held toward the end of 2005. The newly-elected government, operating under the permanent constitution, will take office by December 15, 2005.

There will be two primary limits on the sovereignty of the interim Iraqi governments. First, the caretaker government may not enact legislation that will have long-term effects. This will be done by the later, democratically-elected government. Second, the country’s military will remain under the control of the Coalition, as described more fully below.

- *The Continuing Role of the United States.* When the CPA ceases to exist on June 30, a new U.S. embassy will begin operating in Baghdad. Contrary to earlier reports, the embassy will not have four thousand employees; there will be approximately 400 positions for Americans, representing the State Department and other cabinet agencies, and another 450 locally-hired support personnel. The embassy most likely will be headed by Ambassador John Negroponte, the current U.S. Ambassador to the United Nations, whose confirmation is expected this week.

The new embassy will take over much of the U.S. operations in Iraq. This will include all traditional diplomatic functions plus responsibility for carrying on the reconstruction program—a key part of the overall strategy to make Iraq a secure and democratic country. The CPA’s Program Management Office (PMO) will continue to oversee and direct the program’s activities, projects, assets, construction, and financial management. On June 30, however, the PMO will come under the chief of mission’s guidance. Most likely, the CPA-IG will also transfer to the embassy with the PMO.

From the inception of the reconstruction program, the U.S. appropriations have been largely programmed and managed by DOD through the PMO. DOD will continue to have a significant role in the reconstruction efforts going forward. The Army will maintain its position as the executive agent for all DOD reconstruction requirements, including the significant construction-related contract activities managed by the U.S. Army Corps of Engineers.

Funding levels are also expected to continue or even increase over the coming months. DOD is spending approximately \$4.7 billion per month on military and reconstruction activities in Iraq. Last year, Congress approved two supplemental spending bills to support the activities in Iraq and Afghanistan, totaling \$167 billion. In February of this year, the Office of Management and Budget told Congress that it likely would need another \$50 billion for the military and reconstruction activities *this fiscal year*. More recent reports indicate that this new sum may be the floor, not the ceiling, for funds needed in Iraq.

Of the funds appropriated to date, approximately \$20 billion is for reconstruction being performed by contractors. At least \$12.6 billion is being spent on construction projects in the sectors of oil, public works and water, security and justice, transportation and communications, buildings, education, and health. Another \$5.8 billion is being spent on non-construction items, such as democracy-building, computers, uniforms, school supplies, and a range of other products and services.

According to the Deputy Assistant Secretary of the Army for Policy and Procurement, more than 1,500 prime contracts have been issued so far at a value of nearly \$10 billion. This leaves significant funds for more prime contracts. Additionally, much of the contracting activities will begin to shift to subcontracts, as it is estimated that the prime contracts will produce 15,000 competitive solicitations within the next 12 months. As a result, prime contractors are experiencing overwhelming subcontractor interest—over 13,000 subcontractors have registered on Bechtel Corp.'s vendor website alone.

- *Security*. Everything else in Iraq is dependent upon establishing security throughout the country. This was the recurring message from Government officials and contractors alike during the Iraq Reconstruction Executive-Level Seminar hosted by the

Army Engineer Association on March 12, 2004. The message has rung true over the past two months, as the level of violence has amplified dramatically in the lead up to the June 30 transition.

Of the approximately 500 American soldiers that have been killed in Iraq, 350 of them have been combat deaths, and one-fifth of those occurred during April alone. Contractors are increasingly becoming the targets of violent attacks, as well, with approximately 60 contractor personnel killed to date. Reconstruction projects have been shut down, food convoys have been unable to reach towns and bases, and fighting has occurred in both Sunni and Shia areas. Contractors are required to hire their own security forces, and some contractors have a security-to-workforce ratio of one-to-one. However, this has not resolved the safety risks, as the attackers have begun targeting the security forces to increase the general level of fear.

The most significant question affecting the security situation in Iraq is this: Is the Coalition winning the hearts and minds of the Iraqi people. The answer, of course, is complicated. The Administration maintains that this is not a popular uprising, but rather a desperate attempt by frustrated, isolated groups of insurgents trying to derail the reconstruction and democratic processes. The majority of the Iraqi people want these processes to succeed, and a "violent minority, a small marginal minority cannot be allowed to defeat the hopes of the Iraqi people." *U.S. Policy and Military Operations in Iraq and Afghanistan: Hearing of the Senate Armed Services Committee*, Apr. 20, 2004 (Statement of Gen. R. Myers). At the same time, a recent poll by CNN and USA Today showed that the majority of Iraqis want the Coalition forces to leave immediately, even if it would make the situation worse.

Regardless of the polls, the Administration is "as firm as ever in [its] resolve to help create a free, prosperous, a democratic Iraq." *Id.* The U.S. will not pull its troops out of Iraq, and an American commander will remain in charge of the Coalition security force despite the June 30 transition. As Deputy Secretary of Defense Paul Wolfowitz recently told Congress, "We will have exactly as many troops in Iraq on July 1st as we have on June 30th." *Security Assistance Appropriations: Hearing of the House Appropriations Committee Foreign Operations, Export Financing and Related Programs*

Subcommittee, Apr. 29, 2004 (Statement of P. Wolfowitz).

This position is unlikely to change regardless of the outcome of the U.S. presidential election this November. Senator John Kerry voted for the congressional authorization of the war in October 2002, and although he has since questioned the basis for the war, he supports providing more troops if needed. He also recently cautioned against retreat and called for a continued U.S. lead in securing the region: “We may have differences about how we went into Iraq, but we do not have the choice to just pick up, leave.” See Jim VandeHei, *Kerry Struggles on Iraq Issue*, Wash. Post, May 1, 2004, at A06.

The legal framework for the continued presence of Coalition forces in Iraq is contained in U.N. Security Council Resolution (UNSCR) 1511 and the Transitional Administrative Law (TAL) agreed upon by the CPA and the Iraqi Governing Council in March of this year. UNSCR 1511 authorizes the Coalition’s continued security role in Iraq. See <http://ods-dds-ny.un.org/doc/UNDOC/GEN/N03/563/91/PDF/N0356391.pdf?OpenElement>. Article 59(B) of the TAL states that Iraqi armed forces will be “a principal partner in the multinational force operating in Iraq under unified command” pursuant to Resolution 1511. See *Law Of Administration For The State Of Iraq For The Transitional Period*, Mar. 8, 2004, available at www.iraqcoalition.org/government/TAL.html.

Perhaps most importantly, Article 26(C) ensures that CPA orders and regulations “shall remain in force until rescinded or amended by legislation duly enacted and having the force of law.” This includes CPA Order Number 17, which provides Status of Forces Agreement-like protections for Coalition forces, and which will stay in effect until an international agreement is negotiated with the sovereign Iraqi government. See *Status of the Coalition, Foreign Liaison Missions, Their Personnel and Contractors*, CPA Order No. 17, available at www.cpa-iraq.org/regulations/.

Finally, although the June 30 transition will be the official transfer of power in Iraq, it is important to recognize that this step is part of a larger process that has already begun taking shape. Mr. Wolfowitz addressed the complications, controversy, and goals of the reconstruction process in recent testimony before the Senate Armed Services Committee:

I can’t sit here today and predict the exact form of government that will result from this process Iraqis will decide to establish the exact provisions of their permanent constitution and who will emerge as the leaders of the new Iraq. Particularly after 35 years of what they’ve been through, it’s a complicated task. But Americans of all people should understand that a democracy does not guarantee specific outcomes; it opens up ideas for debate. One need only look back to our own constitutional convention to be reminded that any attempt to establish rule for the people and by the people will involve uncertainty and controversy.

Throughout the world, particularly in Eastern Europe and East Asia, new democracies have emerged in the last 10 or 20 years in countries that had no historical experience of democracy. They are all different; none of them are perfect. Neither are we. But even an imperfect democracy will be a light years improvement over what the country has been like for the last 35 years.

U.S. Policy and Military Operations in Iraq and Afghanistan: Hearing of the Senate Armed Services Committee, Apr. 20, 2004 (Statement of P. Wolfowitz).

Conclusion—Putting aside arguments as to whether the war in Iraq was necessary, it appears clear that the U.S. will be nation-building in Iraq for years to come, and will continue to outsource much of that effort. Contractors are reaping significant rewards, both financial and otherwise, but the risks of this participation are among the most significant that a company can face. This paper’s treatment of two emerging issues—the increasing audits and investigations, and the June 30 transition of government—hopefully will help contractors to mitigate their risks by providing some insight into the months ahead.



This FEATURE COMMENT was written for THE GOVERNMENT CONTRACTOR by Robert Nichols. Mr. Nichols is an attorney in the Washington, D.C., office of Piper Rudnick, LLP. He is also the pro bono general counsel for the Army Engineer Association, a non-profit organization that represents the U.S. Army Engineer Regiment and serves as a bridge between USACE and industry. Prior to entering

private practice, Mr. Nichols was an attorney at USACE Headquarters.

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