



Comptroller General

of the United States

Washington, D.C. 20548

**DO NOT MAKE AVAILABLE TO PUBLIC READING
FOR 30 DAYS**

B-223224

August 18, 1986

**The Honorable Jack Brooks
Chairman, Committee on Government
Operations
House of Representatives**

Dear Mr. Chairman:

Your letter of April 21, 1986, requested our views concerning the provisions of H.R. 4783, a bill to amend the Anti-Kickback Act, 41 U.S.C. §§ 51-54. We appreciate the opportunity to review this legislation and to comment on its provisions, particularly as it concerns the General Accounting Office's role in the area of kickback investigations, the role of agency inspectors general, GAO's inspection authority, lack of coverage of kickback schemes involving related entities and the potential paperwork and regulatory burdens.

The current Anti-Kickback Act prohibits the direct or indirect payment of any gift or gratuity by or on behalf of a subcontractor to any employee of a prime contractor holding a negotiated contract with the government or to an employee of a higher-tier subcontractor, either as an inducement for the award of the contract, or as acknowledgement of a subcontract previously awarded. Among other things, H.R. 4783 would:

1. extend this prohibition to include attempted or solicited payments in addition to actual payment of a kickback;
2. extend this prohibition to any government contract, removing the Act's present restriction to negotiated contracts;
3. prohibit kickbacks paid to obtain any type of favorable treatment in connection with a government contract, not just those paid to induce or acknowledge the award of a contract as proscribed by the current Act;
4. authorize an agency head to terminate a prime contract for default if the prime contractor or a higher tier subcontractor, or any of their employees, receive any money, gratuity or other compensation of whatever value;
5. require prime contractors to file with the contracting agency an annual report containing sworn statements from employees identifying any compensation received from subcontractor employees during the previous year; and

536465

6. substantially increase civil and criminal penalties for violations of the statute.

In addition, both the Act and H.R. 4783 also provide for set-off against moneys owed a subcontractor under other contracts by the government or by a prime contractor, for court action to recover amounts paid as kickbacks, and for criminal prosecution. H.R. 4783 also provides for a set-off against moneys owed by the government to prime contractors.

Role of the General Accounting Office

The proposed legislation maintains without change a provision authorizing the General Accounting Office to inspect the plants and to conduct audits to investigate violations of the Act and extends the same authority to other federal agencies. It also continues a provision which requires the prime contractor, at the direction of the contracting agency or the GAO, to withhold from subcontractors the amount of any kickbacks. As such, GAO's role under the proposed legislation appears to be the same as under the current Act.

The legislative history of the 1946 Anti-Kickback Act, which was proposed by GAO, suggests that in the absence of "patent evidence of fraud" an active role for the GAO in detecting subcontractor kickbacks was not contemplated. See Hearings on H.R. 131 Before the House Committee on Expenditures in the Executive Departments, 79th Cong., 1st Sess. 39 (1945). Thus, Congress did not anticipate that GAO would actively search for kickbacks.

Coordination with agency inspectors general

H.R. 4783 acknowledges the role of the agency inspectors general in the detection and prevention of violations of the Anti-Kickback Act. Section 8 requires the prime contractor to report possible violations of the Act to the inspector general of the agency involved or the head of an agency if the agency has no inspector general. Section 10 authorizes the inspector general, as well as GAO, to inspect the facilities and audit the books and records of any prime contractor or subcontractor under a prime contract awarded by such agency. The potential conflict which might arise from this overlap of effort is addressed in section 4(c) of the Inspector General Act of 1978 (5 U.S.C.A. App. 3 (Supp. 1985)), which contemplates that the activities of the inspector general offices and the Comptroller General be coordinated to avoid unnecessary duplication.

GAO inspection and audit authority

H.R. 4783 maintains the provision of the current Act which grants GAO the authority to "inspect the facilities and audit the books and records

of any prime contractor or subcontractor under a prime contract" awarded by a federal agency. While this language gives GAO the necessary audit authority, it does not specify the corresponding right of access to the books and records necessary to conduct the audit. This omission would not be a problem in connection with negotiated contracts because 41 U.S.C. § 254(c) and 10 U.S.C. § 2313(b) require that most negotiated contracts and their subcontracts contain a clause which would give the Comptroller General access to and the right to examine certain books and records. However, H.R. 4783 expands the coverage of the Anti-Kickback Act to include all types of contracts. To assure that GAO has authority to access the records covering all types of contracts, H.R. 4783 could be amended to add the following sentence to section 10:

"In order to conduct such audit, the Comptroller General of the United States or any of his duly authorized representatives shall have access to and the right to examine any directly pertinent books, documents, papers and records, including computer tapes, databases and other information generated through the use of automated data processing equipment, of any prime contractor or subcontractor under a prime contract awarded by such agency."

Such a change would simply clarify GAO's right of access regardless of contract type but would not add anything beyond what is currently available for negotiated contracts.^{1/}

We do note that our authority is limited in certain respects which could have a bearing on our ability to investigate kickbacks. Our experience in conducting audits aimed at discovering kickbacks has demonstrated the difficulty of detecting kickbacks by use of traditional audit techniques. This is because kickbacks are conspiratorial in nature and thus frequently are not provable by an inspection of contractor books and

^{1/} Two recent court cases have interpreted access language similar to that above. In Bowsher v. Merck & Co., 103 S. Ct. 1587 (1983), the Supreme Court ruled that GAO lacked the statutory authority to examine records of indirect costs, such as research, development and marketing costs, incurred by contractors operating under fixed-price, non-cost-based negotiated contracts with federal agencies, but GAO could inspect records of direct costs. In contrast, the Court recognized that GAO could have access to indirect cost records in a cost-plus contract. Similarly, in United States v. McDonnell-Douglas Corp., 751 F.2d 220 (8th Cir. 1984), the Court of Appeals allowed GAO to inspect the indirect cost records estimating the "tooling and design engineering costs" incurred under a negotiated cost-plus contract.

records. The chances of success are particularly small where there have been no prior indications or allegations of improprieties. As such, H.R. 4783, like the current Act, does not provide GAO with a full range of tools to carry out what is essentially a fraud investigation. It does not provide GAO with authority to access or subpoena the records of organizations other than the prime contractors or subcontractors involved, such as banking records. Nor does the proposed language authorize GAO to require that employees of prime contractors or subcontractors submit to interviews by GAO auditors.

Although H.R. 4783, like the Act, limits our ability to conclusively prove the existence of kickbacks, in the past it has proven sufficient to permit preliminary investigations of questionable activities to the extent necessary to justify referral to the FBI or to the Department of Justice. However, GAO is currently considering establishment of an investigations unit that will increase our capability to investigate allegations of fraud, including subcontractor kickbacks. In our view, consideration of whether to strengthen GAO's authority under the Anti-Kickback Act should be deferred until such a unit is established and it has had some experience in conducting anti-kickback investigations under the current authority.

Lack of coverage of kickback schemes
involving related entities

The Act and H.R. 4783 do not prevent kickback schemes in which the benefits are provided to entities related to the prime contractor or higher tier subcontractor, such as a parent company or one of its subsidiaries. For example, a subcontractor is a subsidiary of a corporation which has another subsidiary selling products to the prime contractor's parent. The other subsidiary rebates a part of the purchase price of goods sold to the parent. In exchange, the parent directs the prime contractor to provide the subcontractor with additional work under the government contract. Although the prime contractor does not benefit, its parent company has received something of value.

Such a scheme would not be difficult for larger corporations to arrange. To remedy this problem, changes would have to be made to H.R. 4783. Some of the principal changes would include:

- (a) A definition for the term "related person" would be added to Section 2. "Related person" could be defined as "the parent of a corporation which is a prime contractor or higher tier subcontractor, or any of its subsidiaries, or the employees of any such related companies."
- (b) The words "related person" would be added to Section 3(a) after the words "prime contractor" and "higher tier subcontractor."

(c) The definition of "person" in Section 2 would be expanded to add:

"the parent of a corporation which is a prime contractor or subcontractor, or any of their subsidiaries, or the employees of any such related companies."

Similar changes to other provisions in H.R. 4783 would also have to be made to assure that the government has adequate remedies and tools to uncover such complex kickback schemes, e.g., to audit and have access to the books and records of "related persons."

Potential paperwork and regulatory burden

In addition, we believe the bill will result in an increased paperwork burden for individuals, companies and government agencies. Individual employees of prime contractors are required to file annual, sworn declarations with the United States listing any fees, gifts or other compensation received from subcontractors during the previous year (section 9). To do this, such employees will need to maintain records of their contacts or work with subcontractors to assure they know what potential situations involving gratuities would be prohibited by the bill. Companies, as prime contractors, will be required to report possible violations of the bill to the government (section 8). To do this, the companies will need to request their employees to provide the detailed contact information mentioned above, and will have to maintain and review such information to assure that their employees are not violating the intent of the bill. The contracting agencies will have to receive, review and maintain as records these declarations and reports.

As part of its regulatory burden, each contracting agency will have to establish procedures for handling reports submitted under section 8 and the declarations submitted under section 9.

We would be glad to provide any further assistance that you or your staff may desire in considering H.R. 4783 or any proposed alternatives to the bill.

Sincerely yours,


you
Charles A. Bowsher
Comptroller General
of the United States