

**Congress of the United States**  
**Washington, DC 20515**

To: Members, Committee on Veterans' Affairs, Subcommittee on Oversight and Investigations;  
Members, Committee of Small Business, Subcommittee on Investigations, Oversight and  
Regulations

From: Committee Staff

Date: June 20, 2015

Re: Hearing: "Manipulation and Fraud in the Reporting of VA Small Business Goals"

---

On Tuesday, June 23, 2015 at 4:00 pm in Room 334 of the Cannon House Office Building, the Subcommittee on Oversight and Investigations of the Committee on Veterans' Affairs and the Subcommittee on Investigations, Oversight and Regulations of the Committee of Small Business will meet for the purpose of receiving testimony on allegations of fraud and manipulation in small business contracting and goaling at the Department of Veterans Affairs.

I. Introduction

In 2006, then-Senators Barack Obama and Tom Coburn introduced the Federal Funding Accountability and Transparency Act of 2006 (FFATA).<sup>1</sup> The law required that details on all federal contract awards be entered into a publicly searchable database.<sup>2</sup> When speaking of the bill on the floor of the Senate, Senator Obama stated:

The American people have a right to know how Federal resources are being used. Congress and the President should make it as easy as possible for taxpayers to see how well we are doing our jobs as stewards of Federal revenues and administrators of Federal spending. All of us should have adequate tools to monitor and evaluate how departments and agencies are performing their important functions.<sup>3</sup>

It is not surprising, therefore, that the Obama Administration has continued to emphasize the importance of data. According to Data.Gov, a website launched by President Obama in 2009, "[o]pen government data is important because the more accessible, discoverable, and usable data is the more impact it can have. These impacts include, but are not limited to: cost savings, efficiency, fuel for business, improved civic services, informed policy, performance planning, research and scientific discoveries, transparency and accountability, and increased public participation in the democratic dialogue."<sup>4</sup> This comports with

---

<sup>1</sup> This became Pub. L. No. 109-282. 120 Stat. 1186 (2006).

<sup>2</sup> FFATA at §2(b), 120 Stat. at 1187.

<sup>3</sup> Congressional Record, vol. 152, S9211 (Sept. 7, 2006).

<sup>4</sup> <http://www.data.gov/impact/>

the President's earlier statements that, "[w]e should do everything we can to ensure that the American public can easily access and track how the Federal government does its business,"<sup>5</sup> because "[w]e can't reduce waste, fraud and abuse without knowing how, where and why federal money is flowing out the door."<sup>6</sup>

However, on March 19, 2015, Mr. Jan Frye, the Senior Procurement Executive and Deputy Assistant Secretary for Acquisition & Logistics at the Department of Veterans Affairs (VA) sent a letter to Secretary Robert McDonald alleging that VA had been engaged in illegal contracting since 2008, and that it had intentionally withheld data required by FFATA in order to conceal those illegal transactions.<sup>7</sup> Mr. Frye made the allegations public at a hearing of the Subcommittee on Oversight and Investigations (O&I) of the Committee on Veterans' Affairs (HVAC).

HVAC O&I has held two hearings examining Mr. Frye's allegations, one of which addressed the abuse of the VA's purchase card program, and one of which examined VA's failure to comply with the Federal Acquisition Regulations (FAR).<sup>8</sup> Rather than reexamine the issues raised at the prior hearings, the Subcommittees will examine the effect of this fraud upon small businesses. Specifically, while the memorandum will briefly review the prior findings, it will examine violations of the small business reserve provisions of the Small Business Act (the Act), violations of the small business goaling provisions of the Act, and the effect on the federal procurement scorecard.

## II. The Frye Allegations

The March 19, 2015 letter (March letter) made numerous allegations pertinent to this hearing. Most of these allegations relate to low dollar value purchases – those between the micro-purchase threshold and the simplified acquisition threshold (SAT). Most of these purchases were made using Governmentwide commercial purchase cards (purchase card) and some of were against the multiple award schedules (schedules) program. Therefore, this memorandum will briefly explain the rules for micro-purchases, purchases below the SAT, the use of purchase cards, and the schedules.

### a. Micro-Purchases, SAT, Purchase Cards and Schedules

Micro-purchases are those with an aggregate value of less than \$3,000, while SAT purchases have an aggregate value of less than \$150,000.<sup>9</sup> Given the relatively low dollar values of these purchases, there are fewer procurement rules to be followed. Micro-purchases do not require competition if the purchaser requires the price to be reasonable, although agencies are directed that, "[t]o the extent practicable, micro-purchases shall be distributed equitably among qualified suppliers."<sup>10</sup> Buyers are not required to report the transactions into the Federal Procurement Data System (FPDS), nor to verify the eligibility of a

---

<sup>5</sup> <http://fas.org/sgp/news/2008/06/obama-coburn.html>

<sup>6</sup> <http://www.govexec.com/oversight/2007/12/web-site-on-federal-grants-loans-and-contracts-debuts/25957/>

<sup>7</sup> Letter on file with the Committees.

<sup>8</sup> *Waste, Fraud, and Abuse in VA's Purchase Card Program*, Hearing before the H. Comm. on Veterans' Affairs, Subcomm. on Oversight and Investigations, Contracting and Workforce Hearing, 114-XXX (May 14, 2015) [hereinafter, *Purchase Card Hearing*]; *Circumvention of Contracts in the Provision of Non-VA Healthcare*, Hearing before the H. Comm. on Veterans' Affairs, Subcomm. on Oversight and Investigations, Contracting and Workforce Hearing, 114-XXX (June 1, 2015) [hereinafter, *Circumvention Hearing*].

<sup>9</sup> FAR § 13.305-3(b); FAR § 2.1.

<sup>10</sup> FAR § 13.203(a).

vendor in the System for Award Management (SAM).<sup>11</sup> SAT purchases do require that they be reported in FPDS, and do require that the vendor be eligible in SAM, but the solicitation procedure is again simplified – oral bidding, soliciting from only one source, and other efficiencies are available to buyers under the SAT.<sup>12</sup> However, even under the SAT, contracting officers “must promote competition to the maximum extent practicable to obtain supplies and services from the source whose offer is the most advantageous to the Government, considering the administrative cost of the purchase.”<sup>13</sup> However, the contracting officer must not “[s]olicit quotations based on personal preference” or “[r]estrict solicitation to suppliers of well-known and widely distributed makes or brands.”<sup>14</sup> Contracts and orders above the SAT have more substantial requirements for competition.

Purchase cards resemble commercial credit cards, and may be used by trained and authorized federal employees to “mak[e] or pa[y] for purchases of supplies, services, or construction.”<sup>15</sup> They are the preferred method of payment for purchases below the SAT or micro-purchase thresholds. However, the “card may be used only for purchases that are otherwise authorized by law or regulation.”<sup>16</sup> When the purchase is under the micro-purchase threshold of \$3,000, the use of the purchase card is itself considered the contract vehicle. If the purchase exceeds \$3,000, warranted contracting officers may use the purchase card “to place orders and to pay for purchases against contracts established under Part 8 [of the FAR] procedures, when authorized; and to place orders and/or make payment under other contractual instruments, when agreed to by the contractor.”<sup>17</sup> A contracting officer cannot split a large purchase up into several small payments to take advantage of the micro-purchase or SAT rules, since it is the aggregate amount of the purchase that determines which set of rules apply to a specific procurement.<sup>18</sup>

The General Services Administration (GSA) establishes contracting vehicles that other federal agencies may use to purchase goods and services, and the most well-known of the contract vehicles established by GSA are the schedules. GSA delegates its authority for some schedules to VA. These schedules are broken up into broad categories of goods and services, each of which is known as a Schedule. While a vast oversimplification, it is perhaps easiest to compare this to the Amazon website, where Amazon will present multiple resellers of the same product, often at different price points. Amazon’s search features, much like the Schedules, organize the various offerings under subtabs, subdividing them into common groups like the Schedules, and then into subgroups. The contracts themselves are Indefinite Delivery, Indefinite Quantity (IDIQ),<sup>19</sup> so the contracts serve as frameworks, including all necessary clauses and the maximum price negotiated between the vendor and GSA or VA. Awardees are not guaranteed any set amount of sales during the five year base period of the contract, but instead, each is simply guaranteed a

---

<sup>11</sup> FAR § 4.6; FAR § 13.201.

<sup>12</sup> FAR § 4.6; FAR § 13.106.

<sup>13</sup> FAR § 13.104.

<sup>14</sup> *Id.*

<sup>15</sup> FAR § 13.301.

<sup>16</sup> *Id.* at (a).

<sup>17</sup> *Id.* at (b).

<sup>18</sup> FAR § 13.000.

<sup>19</sup> IDIQs means that the contract will list a variety of goods and services that can be purchased, but will not guarantee any actual task orders over the five year base period for the contract.

minimum sale of \$2,500 over those five years, or during any of the three successive five year option periods.

The fundamental tenet of federal procurement law is that competition leads to the government obtaining the best value. The existence of the schedules does not undermine that principle. However, since each schedule contract is based on the “best” prices from each particular contractor, these do not utilize open competition in the same ways as other contracts. Task orders under \$3,000 may be placed with the schedule holder without additional competition<sup>20</sup> Contracting personnel considering purchases greater than \$3,000 but less than the SAT<sup>21</sup> must review the price lists or obtain quotes from at least three schedule holders, in order to preserve a modicum of competition. Contracts in excess of the SAT may only be issued after the agency issues a Request for Quotations (RFQ) or a Request for Proposals (RFPs).<sup>22</sup> The contracting officer may issue the RFP or RFQ to specific Schedule holders, but must ensure that at least three offers are received by the agency. For any of these task orders, the ordering agency can request additional discounts.

b. Abuse of the SAT, Purchase Cards and Schedules at VA

The March 2015 letter provides a great deal of insight into the lack of competition for contracts at VA in each of the four categories mentioned. First, VA has a long history of purchase card abuse.<sup>23</sup> For example, as discussed at the Purchase Card Hearing, HVAC O&I reviewed purchase card data between October 2014 to February 2015, and found that VA was splitting purchasing to procure prosthetic devices to keep them under the micro-purchase threshold, and thereby circumvent the competition requirements. Specifically, they documented multiple purchases just under \$3000 on the same date to the same vendor.<sup>24</sup> Further, the HVAC O&I investigation established that a single contracting officer bought over \$31 million in goods and services but avoided the requirement for full and open competition by structuring multiple purchases just under \$25,000.<sup>25</sup> Through a review of VA purchase card data from October 2010 to August 2011, O&I observed duplicative purchases for \$24,900 on the same dates, to the same vendors,

---

<sup>20</sup> FAR § 8.405-1.

<sup>21</sup> FAR § 8.405-1, § 8.405-2.

<sup>22</sup> FAR § 8.405-2. RFQs are simple quotes for defined products, RFPs include more detail, such as the proposed approach for meeting the requirement.

<sup>23</sup> *See, e.g.*, VA Office of the Inspector General (OIG) REVIEW OF UNAUTHORIZED COMMITMENTS WITHIN VA Report 13-00991-154 (2014) (OIG substantiated that VA purchase card holders made 15,600 potentially unauthorized commitments valued at approximately \$85.6 million due to inadequate warrant information, insufficient verification of cardholder limitations, and insufficient training. VA OIG indicated that each unauthorized commitment should be reviewed for possible ratification as necessary. As of the December, 2014, there was no indication that the Heads of Contracting Activities had begun ratification action.); VA OIG AUDIT OF VHA’S ENGINEERING SERVICE PURCHASE CARD PRACTICES AT THE CHARLESTON VAMC Report 13-02267-124 (2014) (OIG substantiated that the Charleston VAMC Engineering Service employees split purchases from October 2011 to December 2013 to avoid single micro-purchase limits for acquiring services and lacked sufficient documentation to support card payments in the amount of \$660,000. The OIG recommended better oversight at the VISN level).

<sup>24</sup> For the period 2010-2011, this same vendor received business from VA despite being associated with an individual who had been debarred due to his felony conviction for conspiracy to distribute prescription narcotics for non-medical purchases.

<sup>25</sup> Within VA, low level warrants only allow contracting personnel to commit up to \$25,000 per purchase.

for the same product code. O&I investigators then identified the vendors from the Federal Procurement Data System (FPDS) and contacted them to determine whether they had contracts with VA for these products. None were identified.<sup>26</sup>

Mr. Frye's allegations in the March 2015 letter make it clear that VA officials first knew as early as 2010 that purchase cards were being abused.<sup>27</sup> Most of the abuse alleged by Mr. Frye relates to the purchases of pharmaceuticals, prosthetic devices, and fee-for-service healthcare by the Veterans Health Administration (VHA). The March 2015 letter details how VHA and VA conspired to perpetuate violations of federal procurement law, limit competition, and conceal their transactions, including misleading HVAC.<sup>28</sup>

While Mr. Frye states that "[t]o the credit of all, the [purchase card] program for micro-purchases appears to be well administered across the VA,"<sup>29</sup> the same cannot be said of purchases below the SAT. Instead, Mr. Frye will testify that he informed numerous high ranking VA officials on multiple occasions that procurements under the SAT were being made in violation of the FAR, as they were not applying even the simplified requirements for competition applicable to SAT purchases.<sup>30</sup> Furthering this problem, the goods and services – usually pharmaceuticals, medical goods, prosthetics or fee basis care – were being paid for using purchase cards even though there was no underlying contract and the contracting personnel were not authorized to make the purchases.<sup>31</sup>

For example, Mr. Frye will state that VA has issued thousands of purchase cards for micro-purchases to persons without adequate training or delegated authority. He will testify that thousands of warranted contracting officers at VHA have made purchases above the micro-purchase threshold without contracts and then paid for them with purchase cards without ratification of the unauthorized commitments. He will note that the primary reasons to split purchases are to evade single purchase amount limitations or to avoid competition requirements.

Mr. Frye contends that in all cases where unauthorized commitments take place, individual ratifications are required before payment is made. He asserts that Mr. Edward Murray, the interim Chief Financial Officer, has routinely ordered payment before ratifications are executed, in violation of the FAR. While VA has attempted to institutionally ratify these purchases, the Inspector General found that the FAR does not allow for institutional ratification, and holds no one accountable for breaking the law.<sup>32</sup>

Finally, the March 2015 letter alleges that rather than purchasing from the schedules program using the mandatory regulatory procedures, VA officials were simply picking orders off of a "shopping list."<sup>33</sup> This shopping list "is estimated to contain nearly 400,000 items, and is often being used indiscriminately and

---

<sup>26</sup> In a letter to O&I Chairman Coffman, dated July 29, 2013, VA admitted that no contract files could be found for the subject purchases.

<sup>27</sup> March 2015 letter at p. 8.

<sup>28</sup> *Id.* at pp. 6-7, 21, 25.

<sup>29</sup> *Id.* at p. 17.

<sup>30</sup> *Id.*

<sup>31</sup> *Id.* at pp. 12-17.

<sup>32</sup> VA Office of the Inspector General (OIG) REVIEW OF UNAUTHORIZED COMMITMENTS WITHIN VA at 6.

<sup>33</sup> *Id.* at pp. 27-28.

not in accordance with the FAR,” meaning that the fair opportunity provisions of the schedules program have been violated and that each task order is “blatantly illegal.”<sup>34</sup>

### III. Small Business Contracting

Not previously discussed are the ramifications of the Frye allegations on small business contracting. The Act provides preferences and goals for the use of these small businesses in federal contracting.<sup>35</sup> The March 2015 letter raises two serious issues for small businesses: (1) compliance with the small business reserve; and (2) reporting of small business goals. The small business reserve will now be addressed, and the next section will address goaling.

Under the small business reserve, all contracts below \$150,000 are reserved exclusively for small businesses unless the contracting officer determines there is not a reasonable expectation of obtaining offers from two or more firms.<sup>36</sup> While it is the responsibility of the contracting officer to comply with this rule, the Act also provides that a Senior Executive known as the Director of the Office of Small and Disadvantaged Business Utilization (OSDBU) shall be responsible for ensuring compliance within the agency.<sup>37</sup> Tom Leney is the VA OSDBU.

Given that at least \$5 billion per year is allocated against the Fee Basis Care program using purchase cards,<sup>38</sup> and that in 18 months alone, Mr. Frye can document \$1.2 billion in prosthetics purchased without contracts but exceeding under the SAT,<sup>39</sup> and that as much as an addition \$6 billion to \$10 billion of VA purchase are not reported annually,<sup>40</sup> it is suggested that at a minimum \$5 billion per year for the last five years should have been reserved for small businesses but was instead spent simply at the discretion of the contracting personnel. Even assuming that each of these procurements was for \$150,000, the maximum allowed under the SAT, that means that over 166,000 small business contracts were diverted.

Indeed, SAM indicates that there were small businesses able to fulfill this work. As of June 15, 2015, there were 982 companies in SAM registered to provide prosthetics, including 18 that are service-disabled veteran-owned small businesses (SDVOSBs), 79 that are veteran-owned small businesses (VOSBs), and 407 that are small businesses. Likewise, there are 396 registered pharmaceutical companies, including 9 VOSBs and 112 small businesses. There are nearly 7,000 registered medical providers, of whom 4,611 are small businesses, 873 are VOSBs, and 364 are SDVOSBs. For medical supplies, there are nearly 11,000 registered vendors, including nearly 9,000 small businesses, 1,844 VOSBs, and 992 SDVOSBs. In each case, if the VA were actively soliciting companies, more small businesses would be likely to

---

<sup>34</sup> *Id.* at p. 27.

<sup>35</sup> According to the Act, a small business concern is one that is independently owned and operated, organized for profit, and which is not dominant in its field of operations. 15 U.S.C. § 632(a). For further information, please see the Committee Memorandum, “What is a Small Business for Purposes of Federal Contracting?” (2013). SBA creates specific size standards for each industry, and assigns revenue- or employee-based size standards to each of the more than 1,100 North American Industrial Classification System (NAICS) codes. 13 C.F.R. § 121. These regulations also provide SBA’s affiliation standards, which address the independence of operations.

<sup>36</sup> 48 C.F.R. § 19.502-2(a).

<sup>37</sup> 15 U.S.C. § 644(k)(4).

<sup>38</sup> March 2015 letter at p. 16.

<sup>39</sup> *Id.* at p. 25.

<sup>40</sup> *Id.* at p. 3.

register. However, given the large number of potential vendors, it seems odd that none of these procurements were set aside for small businesses.

Even if VA believed some of the requirements were not suitable to be set aside for small business, it is the obligation of the contracting officer to document why the work was not set aside for small business.<sup>41</sup> This is an affirmative responsibility, and does not seem to have been honored. Further, the VA cannot claim ignorance of the importance of these small dollar purchases to small businesses, as on June 6, 2012, the Administrators of the SBA and the Office of Federal Procurement Policy (OFPP) sent a letter to the Deputy Secretaries, Chief Acquisition Officers, Senior Procurement Officers and OSDBUs at each agency directing them to “maximize opportunities for small businesses when making small dollar awards” ensure that “all agencies review their small business contracting practices for purchases under the SAT and make adjustments where appropriate ... [so that at] a minimum, agencies should remind their contracting components of responsibilities to set aside contracts whose value is equal to or less than the SAT unless the rule of two is not met, to properly document the contract file when a set-aside is not used, and to maintain appropriate internal controls that ensure consistent application of these requirements.”<sup>42</sup> Indeed, the SBA/OFPP letter went so far as to provide a sample memorandum for agencies to send to their workforce.

On June 26, 2012, Mr. Frye sent a letter to each contracting activity in VA that detailed how to treat procurements above \$3,000 but below the SAT.<sup>43</sup> The June 2012 letter states that if a contracting officer chose not to set aside a contract for small business that was below the SAT, the contracting officer had to complete a checklist detailing why the requirement was not set aside, and then obtain written approval from the both the Head of Contracting Activity (HCA) and the Senior Executive Service (SES) member directly within the the contracting officer’s supervisory chain of command.<sup>44</sup> All of this paperwork was then to be uploaded into the VA contract management system, and reviewed by the Acquisition Office Director and a SES level customer.<sup>45</sup> Thus, these decisions should have been well documented, yet Mr. Frye states that there is no evidence these requirements were followed for the subject procurements.<sup>46</sup>

Further, the OSDBU is required by the Act to ensure the agency is complying with the requirements of the small business reserve. The March 2015 letter makes it clear that the VA OSDBU was aware of the

---

<sup>41</sup> “The contracting officer shall review acquisitions to determine if they can be set aside for small business, giving consideration to the recommendations of agency personnel having cognizance of the agency’s small business programs. The contracting officer shall perform market research and document why a small business set-aside is inappropriate when an acquisition is not set aside for small business, unless an award is anticipated to a small business under the 8(a), HUBZone, SDVOSB, or WOSB Programs. If the acquisition is set aside for small business based on this review, it is a unilateral set-aside by the contracting officer. Agencies may establish threshold levels for this review depending upon their needs.” FAR § 19.501(c).

<sup>42</sup> Letter from Karen Mills, Administrator, SBA and Joe Jordan, Administrator, OFPP 1-2 (2012) *available at* [https://www.whitehouse.gov/sites/default/files/omb/procurement/memo/follow-up-april\\_25-2012-meeting-of-the-small-business-procurement.pdf](https://www.whitehouse.gov/sites/default/files/omb/procurement/memo/follow-up-april_25-2012-meeting-of-the-small-business-procurement.pdf) [hereinafter SBA/OFPP letter].

<sup>43</sup> VA Acquisition Policy Letter 2012-03, Mandatory Small Business Set Asides for Contract Actions Up to the SAT (2012), *available at* <http://www.va.gov/oal/docs/business/pps/memoMandatorySBSAforContractActionsUpToSAT.pdf> [hereinafter June 2012 letter].

<sup>44</sup> *Id.* at 2.

<sup>45</sup> *Id.*

<sup>46</sup> March 2015 letter at 23.

issues with procurements below the SAT ignoring the small business contracting rules.<sup>47</sup> However, while Mr. Frye sent acquisition letters to all of the contracting offices, there is no evidence that the VA OSDBU, Mr. Leney, sent a letter to the small business specialists, even though the SBA/OFPP letter provided a sample letter to be sent by the OSDBU.<sup>48</sup>

Thus, while over \$25 billion in procurements over the last five years violated both the letter and the spirit of the Act, the VA continued to tolerate these illegal contracts. However, the actions of the VA had repercussions outside of the agency itself, as will now be discussed.

#### IV. Small Business Goaling

Pursuant to the Act, the SBA reports annually to Congress on the small business accomplishments during the prior year, but the Subcommittees are concerned that based on the statement of Mr. Frye, the information reported by the VA to SBA, and then by SBA to Congress, has been incorrect and does not accurately reflect whether the federal government is meeting the small business goals. This section will discuss those goals, SBA's scorecard methodology, and the discrepancies between the two. Finally, it will examine how VA's misrepresentation of data may have affected the results on the government-wide and VA specific score cards.

##### a. Goaling

Recognizing the importance of small businesses to the economy, Congress has established a series of programs to assist small businesses competing for federal contracts.<sup>49</sup> To achieve these aims, the Act establishes three types of small business goals: numerical goals, industrial goals, and maximum practicable utilization. As the SBA's procurement scorecard only considers the numerical goals, this memorandum will restrict itself to those ten goals.<sup>50</sup> Section 15(g) of the Act requires that the federal government have a government-wide goal of awarding "not less than 23 percent of the total value of all prime contracts awards for each fiscal year" to small business concerns. Additionally, there is a goal of awarding three percent of all prime contract dollars to SDVOSBs, and three percent to qualified HUBZone small business concerns.<sup>51</sup> Further, there is a goal of awarding five percent of all prime contract dollars to small business concerns owned and controlled by socially and economically disadvantaged individuals (SDBs) and five percent to small business concerns owned and controlled by women (WOSBs).<sup>52</sup> In large part due to the VA's reported accomplishments, in FY 2013, the federal

---

<sup>47</sup> *Id.* at 21-22.

<sup>48</sup> SBA/OFPP letter at attachment 2.

<sup>49</sup> For information on these programs, please see Committee Memorandum, *Small Business Act Programs for Federal Contractors* (February 2013), available at [http://smallbusiness.house.gov/uploadedfiles/small\\_business\\_act\\_programs\\_for\\_small\\_federal\\_contractors.pdf](http://smallbusiness.house.gov/uploadedfiles/small_business_act_programs_for_small_federal_contractors.pdf) (last accessed February 26, 2015). Congress established these programs in the belief that the use of small businesses as contractors is "in the interest of maintaining or mobilizing the Nation's full productive capacity, [. . .] in the interest of war or national defense programs, [and . . .] in the interest of assuring that a fair proportion of the total purchases and contracts for property and services for the Government in each industry category are placed with small-business concerns." The Act, § 15(a), 15 U.S.C. § 644(a).

<sup>50</sup> For information on the other goals, please see Committee Memorandum, *Contracting and Industrial Base II: Bundling, Goaling, and the Office of Hearings and Appeals* 18-22 (March 17, 2013), available at [http://smbiz.house.gov/uploadedfiles/3-17-2015\\_hearing\\_memo.pdf](http://smbiz.house.gov/uploadedfiles/3-17-2015_hearing_memo.pdf) (last accessed June 8, 2015).

<sup>51</sup> The Act, §§ 15(g)(1)(ii)-(iii), 15 U.S.C. §§ 644(g)(1)(ii)-(iii).

<sup>52</sup> The Act, §§ 15(g)(1)(iv)-(v), 15 U.S.C. §§ 644(g)(1)(iv)-(v).

government met the 23 percent goal, and exceeded the SDB and SDVOSB goals.<sup>53</sup> Initial indications are that the federal government will meet the small business prime contract goal again for FY 2014, although the substance of the Frye letter casts doubts on the legitimacy of this data.

The federal government has subcontracting goals as well as prime contracting goals. The SBA sets the subcontracting goal at 36 percent of subcontracted dollars during the fiscal year, and statute sets the goals for SDBs, HUBZones, WOSBs, and SDVOSBs at the same level as the respective prime contracting goals.<sup>54</sup> In FY 2013, the federal government met only the WOSB and SDB subcontracting goals.<sup>55</sup> Subcontracting goals only apply to contracts awarded to other-than-small business concerns.<sup>56</sup>

SBA negotiates each agency's goals on an annual basis.<sup>57</sup> It then reports annually on the numerical goals through its scorecard process. SBA's scorecard awards a letter grade to the federal government and each agency. Eighty percent of the grade is based on the prime contracting achievements.<sup>58</sup> Subcontracting achievements only account for 10 percent of a grade, and the final 10 percent is based on an agency's plan progress.<sup>59</sup>

To calculate the prime contracting portion of the scorecard, SBA looks at the agency's achievement for each goal relative to the agency's specific goal.<sup>60</sup> Prime contract dollars awarded to small businesses are worth sixty percent of the score, and each of the subcategory goals is worth 10 percent.<sup>61</sup> The resulting number is worth eighty percent of the final grade. The subcontracting portion of the scorecard uses an identical methodology to obtain the final number, which is worth 10 percent of the score.<sup>62</sup> The final 10 percent is based on seven success factors, each of which is worth one point, for a total of seven points.<sup>63</sup>

---

<sup>53</sup> SBA, "FY 2013 Procurement Scorecard" available at [https://www.sba.gov/sites/default/files/files/FY13\\_Government-Wide\\_SB\\_Procurement\\_Scorecard\\_Public\\_View\\_2014-04-28.pdf](https://www.sba.gov/sites/default/files/files/FY13_Government-Wide_SB_Procurement_Scorecard_Public_View_2014-04-28.pdf) (last accessed February 26, 2015).

<sup>54</sup> The Act, § 15(g)(1), 15 U.S.C. § 644(g)(1).

<sup>55</sup> SBA, "FY 2013 Procurement Scorecard," available at [https://www.sba.gov/sites/default/files/files/FY13\\_Government-Wide\\_SB\\_Procurement\\_Scorecard\\_Public\\_View\\_2014-04-28.pdf](https://www.sba.gov/sites/default/files/files/FY13_Government-Wide_SB_Procurement_Scorecard_Public_View_2014-04-28.pdf) (last accessed February 26, 2015).

<sup>56</sup> The Act, § 8(d), 15 U.S.C. § 637(d).

<sup>57</sup> The Act, § 15(g)(1)(B), 15 U.S.C. § 644(g)(1)(B).

<sup>58</sup> SBA GRADE CALCULATION METHODOLOGY 2 (2014), available at [https://www.sba.gov/sites/default/files/files/Scorecard-Grade-Calculation-Methodology-FY13\\_FINAL\\_2014-06-04.pdf](https://www.sba.gov/sites/default/files/files/Scorecard-Grade-Calculation-Methodology-FY13_FINAL_2014-06-04.pdf) (last accessed February 26, 2015).

<sup>59</sup> *Id.*

<sup>60</sup> *Id.* at 5.

<sup>61</sup> *Id.*

<sup>62</sup> *Id.* at 6.

<sup>63</sup> The first factor is commitment to small business utilization, which asks whether the agency "has demonstrated, through action and documented evidence, a commitment to utilize small businesses to obtain goods and services." *Id.* at 7. The second factor is effective engagement of senior level management in achieving small business goals, and it requires that the agency's "senior leadership, (i.e. Deputy Secretary, Chief Acquisition Officer, Senior Procurement Executive, senior program managers, and OSDBU Director) demonstrated, through action and documented evidence, that they have clearly communicated the importance of achieving the agency's small business contracting goals through the chain of command to the contracting officer level." *Id.* The third factor is the data quality of small business contracting, and requires that the agency demonstrate "through action and documented evidence, a commitment to small business contracting data quality." *Id.* The fourth factor is training of acquisition staff, and asks if the agency has "demonstrated a commitment to small business utilization through regular training of acquisitions staff on the issues/procedures/policies/regulations impacting small business." *Id.* The fifth factor is outreach to small business, and asks if the agency has demonstrated "a commitment to growing their small business

SBA's letter grade system assigns an A+ to agencies with scores over 120 percent, an A to agencies that exceed 100 percent, a B for a grade of 90 to 100 percent, C for a grade of 80 to 90 percent, a D for grade of 70 to 80 percent, and an F for anything below 70 percent. Based on this system, it is possible for agencies to miss multiple goals and still receive an A.

b. Effect of the Frye Allegations on Goaling

In the March 2015 letter, Mr. Frye states:

Taxpayers have no idea how very sizable portions of VA's Congressional appropriations are being spent, which the law demands. We have effectively "hidden" our illegal transactions from public scrutiny. My estimate above is conservative. **In FY15 I certified the Department FPDS spend to OMB at \$19B. Our reported FPDS spend may be indeed be understated by as much as \$6B - \$10B annually.**

Also, VA small-business goal accomplishments have been and continue to be vastly overstated. Illegal obligations sans contracts are not posted to FPDS, and are thus not properly included in calculations to determine Federally mandated small-business goals. **We have announced each year since 2008 that we have exceeded our directed goals for Veteran-Owned and Service Disabled Veteran-Owned Small Businesses. The stated percentages touted are absolutely false given the immense inaccuracy of denominators used to calculate these annual percentages.** Sadly in my opinion, in addition to our illegal acts, we've duped the veteran-owned business community we are required by law to advocate for.<sup>64</sup>

It is first worth clarifying that agencies do not have the option to exclude data from FPDS. Rather, they are required to report, "[i]n accordance with [FFATA] all unclassified contract actions exceeding the micro-purchase threshold, and any modifications to those actions that change previously reported contract action report data, regardless of dollar value."<sup>65</sup> This failure to report raises several problems, first dealing with VA's grade, and also in addressing the federal government's ability to meet its goals.

For example, in FY 2013 the SBA awarded VA a grade of an A, based on the data input into FPDS. That data showed that VA spent about \$18.227 billion per year. Specifically, the report card provided that for prime contracting, VA received a score of 85.06%, reported as shown in Table 1.

---

supplier base and increasing awareness of contracting opportunities for small businesses." *Id.* The sixth factor is subcontracting, and requires that the agency demonstrate a commitment to expanding subcontracting opportunities for small businesses. *Id.* The seventh and final factor is unbundling, and asks whether the agency has a clearly communicated policy to address and mitigate the adverse effects of contract bundling on small businesses. *Id.*

<sup>64</sup> March 2015 letter at 3 (emphasis added).

<sup>65</sup> FAR § 4.603(a)-(b), *see also* [https://www.fpds.gov/wiki/index.php/FPDS-NG\\_FAQ](https://www.fpds.gov/wiki/index.php/FPDS-NG_FAQ).

**Table 1. Department of Veterans Affairs FY 2013 Procurement Scorecard As Reported by SBA<sup>66</sup>**

<b>Prime Contracting Achievement:</b>			<b>85.06%</b>
	2012 Achievement	2013 Goal	2013 Achievement
<b>Small Business</b>	36.01%	34.00%	36.21% (\$6.6 B)
<b>Women-Owned Small Business</b>	3.30%	5.00%	3.35% (\$612.6 M)
<b>Small Disadvantaged Business</b>	7.91%	5.00%	7.92% (\$1.4 B)
<b>Service-Disabled Veteran-Owned Small Business</b>	19.24%	3.00%	19.38% (\$3.5 B)
<b>HUBZone</b>	1.73%	3.00%	1.72% (\$313.7 M)

When that 85.06% was added to the VA's Subcontracting Achievement Score of 5.87% and the Success Factor Score of 9.91%, VA had a total score of 100.84%, earning itself an A. However, a very different picture emerges if Mr. Frye is correct that the reported spend was \$6 billion less than what VA actually spent. In such a case, the scorecard looks like Table 2 instead.

**Table 2. Department of Veterans Affairs FY 2013 Procurement Scorecard if an Additional \$6 Billion is Added to the Base<sup>67</sup>**

<b>Prime Contracting Achievement:</b>			<b>64.09%</b>
	2012 Achievement	2013 Goal	2013 Achievement
<b>Small Business</b>	36.01%	34.00%	27.24% (\$6.6 B)
<b>Women-Owned Small Business</b>	3.30%	5.00%	2.53% (\$612.6 M)
<b>Small Disadvantaged Business</b>	7.91%	5.00%	5.78% (\$1.4 B)
<b>Service-Disabled Veteran-Owned Small Business</b>	19.24%	3.00%	14.45% (\$3.5 B)
<b>HUBZone</b>	1.73%	3.00%	1.29% (\$313.7 M)

In this scenario, the VA only earned a prime contracting score of 64.09%. When that is added to the VA's Subcontracting Achievement Score of 5.87% and the Success Factor Score of 9.91%, VA only has a total score of 79.87%. Such a score only earns a grade of D from SBA, and reflects that VA failed to meet three of its prime contracting goals, plus four of its subcontracting goals. This means that VA only met three of its statutory goals.

Again, this is the optimistic view on the potential fraud perpetrated on small businesses. If \$10 billion were excluded from the base, the results are more dire still, as demonstrated in Table 3.

<sup>66</sup> [https://www.sba.gov/sites/default/files/files/FY13\\_VA\\_SB\\_Procurement\\_Scorecard\\_Public\\_View\\_2014-04-28.pdf](https://www.sba.gov/sites/default/files/files/FY13_VA_SB_Procurement_Scorecard_Public_View_2014-04-28.pdf)

<sup>67</sup> Committee analysis, on file with the Committee.

**Table 3. Department of Veterans Affairs FY 2013 Procurement Scorecard if an Additional \$10 Billion is Added to the Base<sup>68</sup>**

<b>Prime Contracting Achievement:</b>			<b>45.08%</b>
	2012 Achievement	2013 Goal	2013 Achievement
<b>Small Business</b>	36.01%	34.00%	23.38% (\$6.6 B)
<b>Women-Owned Small Business</b>	3.30%	5.00%	2.17% (\$612.6 M)
<b>Small Disadvantaged Business</b>	7.91%	5.00%	4.96% (\$1.4 B)
<b>Service-Disabled Veteran-Owned Small Business</b>	19.24%	3.00%	12.40% (\$3.5 B)
<b>HUBZone</b>	1.73%	3.00%	1.11% (\$313.7 M)

In this scenario, the VA only earned a prime contracting score of 45.08%. When that is added to the VA's Subcontracting Achievement Score of 5.87% and the Success Factor Score of 9.91%, VA only has a total score of 60.86%. This is a failing grade according to SBA, and reflects that VA failed to meet four of its prime contracting goals, plus four of its subcontracting goals. This means that VA only met two of its statutory goals. The reality of what the inflation of the scorecard reflects is sadder still when one reflects that the majority of the dollars absent from the goaling base are for purchases that should have, by law, been made from small businesses. If VA had followed the law both at the time of purchase and at the time of reporting, it would have received an A+.

However, the problems caused by this misreporting do not end with VA. Instead, as VA has the fourth highest level of contract spending of any federal agency, it affects the federal government's ability to meet its goals, and the grade it receives from SBA. If Mr. Frye is correct and VA underreported it goals by \$10 billion, that means that the government did not meet its small business goal for FY 2013, and that it received only a B, rather than the A previously announced. Further, this assumes that VA is an outlier, and that all other agencies are scrupulously including the all covered transactions. However, given that SBA already excludes a large quantity of dollars from the goaling base, the underlying numbers are already suspect. For example, in FY2013, SBA calculated goaling achievements against a total spend of \$356 billion, but in reality the federal government spent over \$471 billion in contracts that year even before the VA discrepancies are addressed.<sup>69</sup>

Misreporting of goaling numbers is more than a paperwork or public relations issue. When the goals are not properly reported, then agencies are not properly incented to structure contracts in a way that creates opportunities for small businesses. Further, as of the FY 2013 National Defense Authorization Act (NDAA), whether an agency meets its goals should be considered before SES are provided with bonuses.<sup>70</sup> Thus, misrepresenting the goaling achievements means that senior executives receive larger bonuses than are merited.

<sup>68</sup> Committee analysis, on file with the Committee.

<sup>69</sup> All data from the Federal Procurement Data System.

<sup>70</sup> Pub. L. No. 112-239 § 1633, 126 Stat. 1632, 2076 (2013).

## V. Issues Before the Committee

### 1. Role of the OSDBU

As previously mentioned, the OSDBU is responsible for ensuring that its agency complies with the Act. However, despite Mr. Frye's documentation that Mr. Leney was aware of violations of the Act at VA, there are no evident actions taken by the OSDBU to address these problems. However, Mr. Leney did boast of the VA's success in meeting its goals in an April 9, 2014 letter to Chairman Coffman, claiming that the VA's level of performance was attributable to its "commitment to providing opportunities for Veterans."<sup>71</sup> Therefore, the Subcommittees wish to know what the OSDBU has done and is doing to prevent abuses of the small business reserve and the small business goaling programs.

### 2. SBA and OFPP Certification Requirements and the Abuse of Bonuses

Until 2011, agencies were required to annually "certify[y] the completeness and accuracy of procurement data" available in FPDS to OFPP and GSA.<sup>72</sup> At that time, the requirement that data be certified was removed, contingent upon "actions that are being taken to improve the quality of procurement data on small business contract awards."<sup>73</sup> Instead, in 2012, agencies were told that to "hold senior leadership accountable for meeting your agency's small business goals, including any of the statutory socio-economic goals . . . [and] include agency small business contracting goals in the performance evaluations of all Senior Executive Service (SES) staff members who oversee your agency's acquisition workforce."<sup>74</sup> While this does address the motivation of agencies to meet the goals, it fails to address data quality issues. Indeed, it may inadvertently encourage agencies to exclude dollars from the goaling base in order to meet the goals.

As previously mentioned, VA officials have been able to take credit for meeting the goals during their performance evaluations. If the Frye allegations are true, it raises questions as to whether unmerited bonuses or salary increases were awarded based on fraudulent data.

### 3. Role of SBA

It is SBA's responsibility to report to Congress on the ability of federal agencies to meet the various small businesses goals, and to ensure that agencies are complying with the requirements of the Act. While the Subcommittees do not expect that SBA has the resources to audit VA's procurement data, presumably there are steps that SBA could have taken to improve the probability of VA's compliance. First, the procurement center representatives assigned to VA have not been reviewing the purchases at issue, raising questions about whether these individuals should be more active in smaller dollar procurements. Second, section 1692 of the FY 2013 NDAA tasked SBA with overseeing peer reviews of the OSDBU

---

<sup>71</sup> Letter on file with the Committees.

<sup>72</sup> Memorandum from SBA Administrator Mills and OFPP Administrator Daniel Gordon, "Improving Small Business Procurement Data – Quality and Process" 1 (2011), *available at* <https://www.whitehouse.gov/sites/default/files/omb/procurement/memo/small-business-data-quality-improvement.pdf>.

<sup>73</sup> *Id.*

<sup>74</sup> SBA/OFPP at 3.

offices, in order to ensure that these offices were fulfilling their statutory responsibilities.<sup>75</sup> SBA has not done so, which may have allowed the lapses in the VA OSDDBU office to go undetected. Third, as the agency responsible for overseeing the report to Congress, SBA should not have consented to removing the data certification requirements. The Subcommittees will examine why these lapses occurred.

#### 4. Role of the Integrated Award Environment

GSA manages the Integrated Award Environment (IAE), an interconnected system of procurement-related databases, for the federal government under delegation from OFPP. As such, it has responsibility for implementing FFATA and for operating FPDS. FPDS is supposed to draw data from an agency's contract writing system, so that all procurements are captured. Therefore, the Subcommittees wish to learn how VA could conceal \$6 billion to \$10 billion or more in procurements each year for over five years. Specifically, the Subcommittees wish to know if the systems need to be modified to capture purchase card data over \$3,000.

#### 5. Role of the Procurement Card Program

GSA also manages the SmartPay2 program, which provides VA with access to its purchase cards. Per GSA, under SmartPay2, “[a]gencies have access to management reports via the Internet [including] standard reports and ad hoc reports [such as] Account Activity reports, Dispute reports, Unusual Spending Activity reports, Lost/Stolen Cards reports, and miscellaneous Ad Hoc reports.”<sup>76</sup> Further, the agency receive a rebate on purchases made using the cards, usually a percentage of the amount spent. Therefore, the Subcommittees wish to learn what data was available to VA to detect the fraud alleged by Mr. Frye. Specifically, the Subcommittees are curious as to whether the rebates on purchases in the magnitude of \$6 billion to \$10 billion would have been detectable by the VA Chief Financial Officer.<sup>77</sup>

#### 6. Financial Controls

The Federal Managers' Financial Integrity Act of 1982, as implemented by Office of Management and Budget (OMB) Circular A-123 - Management's Responsibility for Internal Control (A-123), states management has a fundamental responsibility to develop and maintain effective internal controls.<sup>78</sup> Specifically A-123 requires that agency managers “establis[h] and maintain[n] internal control to achieve the objectives of effective and efficient operations, reliable financial reporting, and compliance with applicable laws and regulations ... [by] consistently apply[ing] the internal control standards to meet each of the internal control objectives and to assess internal control effectiveness.”<sup>79</sup> This requires that agencies assess the effectiveness of internal control over financial reporting and compliance with financial-related laws and regulations, and that annually “management must provide assurances on internal control in its Performance and Accountability Report, including a separate assurance on internal control over financial reporting, along with a report on identified material weaknesses and corrective

---

<sup>75</sup> Pub. Law No. 112-239 at § 1692, 126 Stat. at 2089.

<sup>76</sup> <https://smartpay.gsa.gov/program-coordinators/faq-agencies-organizations>

<sup>77</sup> Rebates governmentwide exceeded \$267 billion last year. <https://smartpay.gsa.gov/program-refunds>.

<sup>78</sup> The Federal Managers' Financial Integrity Act of 1982 was codified at 31 U.S.C. §§ 3511 et seq. OMB Circular A-123 is available at [https://www.whitehouse.gov/omb/circulars\\_a123\\_rev](https://www.whitehouse.gov/omb/circulars_a123_rev).

<sup>79</sup> A-123 at 1.

actions.”<sup>80</sup> Therefore, the Subcommittees wish to know whether any VA managers declined to provide the annual certification, or whether the issues dealt with in the March 2015 letter were in any way addressed through the A-123 process.

#### 7. Where did the Money Go?

While the Subcommittees understand that the dollars spent on fee-basis care, prosthetics, pharmaceuticals and the like were not awarded pursuant to the FAR or the Act, the question still remains as to who fulfilled these contracts, and how were they selected? The Subcommittees expect the witnesses to shed a light on these questions.

#### 8. Consequences

Finally, given that VA has had the information in the March 2015 letter for over three months, and it has been available publicly since mid-May, the Subcommittees wish to learn what corrective actions the witnesses have taken, and whether any malfeasance has been punished.

### VI. Conclusion

Secretary McDonald’s response to the March 2015 is that it is Mr. Frye’s “responsibility to fix it.”<sup>81</sup> he said, adding that the department has “a lot of work to do.” The record suggests that Mr. Frye has not been allowed to do the work he is statutorily charged with performing. Therefore, the Subcommittees will consider what other actions are necessary to ensure the work is indeed performed.

---

<sup>80</sup> *Id.*

<sup>81</sup> Eric Catz, Government Executive, VA Put Vets at Risk by Spending Billions Unlawfully, Whistleblower Says (May 14, 2015) available at <http://www.govexec.com/contracting/2015/05/va-put-vets-risk-spending-billions-unlawfully-whistleblower-says/112828/>.