Good morning, Mr. Chairman and members of the Subcommittee on Oversight and Investigations of the Committee on Veterans Affairs. Thank you for the opportunity to present testimony on improving accountability of the VA-affiliated nonprofit research and education corporations. I am Antonio Laracuente, executive director of the Atlanta Research and Education Foundation (AREF) and chairman of the National Association of Veterans' Research and Education Foundations (NAVREF). NAVREF is the membership association of the eighty-six active VA-affiliated nonprofits.

As you are aware, investigators from the General Accounting Office (GAO) spent the summer conducting in-depth site visits of the foundations in Atlanta, Portland, San Diego, Boston and Indianapolis, and the IG visited two foundations, San Francisco and Palo Alto. Because their findings were not made public in time for me to comment on them before the deadline for written testimony, my statement focuses on my own experience with the GAO auditors and pending legislation that would improve nonprofit accountability: Section 7 of H.R. 3645, and provisions regarding contracting and Federal Tort Claims Act coverage originally contained in S. 2132 that are now in the Senate-passed version of H.R. 3253.

GAO and IG Site Visits

My foundation was the first one the GAO investigators visited. Foundation and medical center staff spent more than 20 hours in focused discussions with the GAO team responding to questions. We arranged briefings with medical center staff including principal investigators, the medical center director, chief of staff and the ACOS R&D, and provided full access to our files. Since ours was the first site, the team began with no prior knowledge of the VA-affiliated nonprofits and being unique, the foundations did not fit into any pre-existing frame of reference. Throughout the visit, we found the auditors to be astute questioners. Ultimately, four themes developed during questioning by the GAO site visitors that I will address in this statement:

1. **Why does VA need the nonprofits?** When I cited the many ways AREF supports the VA research program in Atlanta, the GAO auditors questioned why a nonprofit was needed, maintaining that federal means to accomplish the objective exist. I would be the first to acknowledge that in a perfect world, there would be no need for the foundations. However, two realities make the foundations necessary:

   First, VA funding is inadequate to meet the increasingly complex needs of supporting a research program of the caliber our veterans deserve.

   - You heard in testimony in May that the Richmond nonprofit underwrites the entire cost of that medical center's institutional review board to the tune of $600,000 annually.
   - As discussed in my April 24 testimony on research facilities, there is no designated VA funding stream to meet the increasingly urgent need for research facility maintenance and improvements. Repeatedly, the foundations are called upon to cover the cost of moving walls, upgrading electrical supply and improving ventilation.
   - Appropriated funding to support research related travel simply is not available and last year the foundations expended more than $4 million in travel and related costs so VA investigators could disseminate important research findings, keep current in their fields and interact with their peers.
   - Although VA facilities house a significant number of projects administered by affiliated universities, the universities rarely provide support for the VA research infrastructure.

   Second, time constraints on research grants require quick turnaround on procurement and flexibility in hiring that cannot be accommodated using federal mechanisms such as the General Post Funds

(GPF). Despite changes in the GPF authority that made them more flexible, VA's General Post Funds remain an inadequate, cumbersome and inflexible mechanism to manage private sector and non-VA federal research funds. It is far more efficient and cost effective for a foundation to hire research employees and donate their services to VA, or when appropriate, enter into Intergovernmental Personnel Act assignments. The same goes for procurement. Using private sector funds and non-VA federal grants, nonprofits can purchase goods and services quickly and then can donate them to VA. If Congress eliminated the nonprofits and the funds were managed through the GPF, I can assure you that efficiencies would be lost and ultimately, the funds the nonprofits currently administer would return to universities and the benefits would accrue to the universities, not to the VA research program.

I could give you many more examples, but they would only serve to illustrate my first point: in 1988, Congress recognized the need for a flexible funding mechanism to manage non-VA research funds and the nonprofits have been highly successful in meeting that need.

2. **What rules and regulations apply to the nonprofits?** Accustomed to auditing federal agencies and expenditures of federal funds by other organizations, the GAO site visitors appeared at times uncertain about applicable statutes and regulations for organizations that in most cases administer a mix of non-VA federal and private sector funding. We had some lively discussions when it became apparent that the site visitors were inclined to impose on AREF expenditures the requirements relevant to procurement for federal agencies, hiring federal employees and federal employees' travel. Rather, we must - and do - comply with the regulations that are specific to nonprofits that expend federal funds, OMB Circulars A-133, A-122 and A-110. Also, in the case of expenditures of private sector funds, IRS regulations apply. Nonprofits are **not** required to spend down all the private sector funds they take in, and indeed sound nonprofit management entails maintaining an operating reserve equivalent to at least three months expenses.

   Along the same lines, a nonprofit should not be viewed as deficient if the site visitors conclude that VA's own regulations on conflict of interest disclosure and outside employment are less rigorous than the standards required of GAO investigators. As discussed in my May 16 testimony, the nonprofits are required to follow federal regulations applicable generally to nonprofits as well as a broad array of federal, state and local regulations. At most, nonprofit employees should be held to standards set by VA regarding conflicts of interest.

3. **Are the nonprofits private or federal entities?** NAVREF has long maintained that the nonprofits are private organizations, albeit subject to federal oversight and regulation. The NAVREF view is based on three items:

   - The opening clause of the statute that authorizes the nonprofits clearly states that " . . . any such corporation, and its directors and employees, shall be required to comply only with those Federal laws, regulations and executive orders and directives which apply generally to private nonprofit corporations."
   - Other clauses in the authorizing statute [7366(a)(1)(A) and (B)] assign to the Inspector General responsibilities regarding the nonprofits and specify that nonprofit records shall be made available to the General Accounting Office. If the nonprofits were federal agencies, there would be no need for the statute to make these points.
   - Further, House Report 100-373 which accompanied H.R. 3449, the original nonprofit legislation, states, "These corporations would not be considered for any purposes as corporations owned or controlled by the United States, except for limitations made applicable to these corporations by this Act."

Also, in a letter dated July 17, 2002, VA General Counsel ". . . concluded that it is unclear whether the Economy Act, which our predecessors had relied upon as authorizing OGC to bill the corporations for its legal services, is sound authority for that purpose." As you may be aware, the Economy Act allows one federal agency, or a major organizational unit within an agency, to place an order with and to make a payment to another agency or organizational unit. It is our understanding that GC determined that the nonprofits are not sufficiently federal to allow use of the Economy Act as the basis for billing between VA and the nonprofits. (Note: NAVREF does not object to such billing and urges VA to determine the appropriate mechanism so billing can resume.)

4. **Does VA need 86 nonprofits?** Again and again the GAO site visitors questioned why each VAMC needs its own nonprofit. I am uncertain whether this question was motivated by a desire to have fewer nonprofits to oversee or to engender cost efficiencies. Regardless, my unequivocal answer was "yes." The nonprofit has tremendous value for the research program at each facility. The many advantages of a one-to-one relationship between a VAMC and a nonprofit include:

   - Local oversight by the board
   - Management that is invested in the success of the medical center's research program
   - Responsiveness to facility and individual investigator needs
   - On site services resulting in convenience for investigators and quick turnaround on procurement and hiring
   - Direct access to the VA personnel and committees who conduct research administered by the nonprofit

   The only advantage of consolidating nonprofits that we can envision would be a cost saving on accounting, insurance and some administrative functions, although we are not sure that these would provide long-term, tangible savings. However, these costs are already minimal and in our view the benefits of the current one-on-one relationship far outweigh the value of the possible savings.

Recommendations Regarding Increased Accountability

NAVREF has given consideration to concerns about accountability expressed by members of the Health and Oversight Subcommittees during the May 16 hearing. I wish to remind the Subcommittee that even though the IG has not been routinely auditing the foundations, the foundations have been subject to many other types of ongoing oversight and review since their inception. As provided in the authorizing statute, our records are open to the IG and GAO at any time. A great deal of information is already provided to VA in the nonprofits' annual reports which include the audit and IRS nonprofit informational return, Form 990. Each board of directors provides continuous, local oversight. And each nonprofit has an independent accountant and auditor. Depending on the nonprofit's revenues and activities, an audit is required every one to three years and the level of scrutiny for those administering federal funds is very high.

That said, the May 16 hearing clarified the Subcommittee's key concerns: 1) No one in VA is responsible for a critical review of the information provided in the annual reports; and 2) The IG has not been conducting routine reviews of the nonprofits. In our view, two pieces of relevant legislation are pending.

1. HR 3645, the *Veterans* ***Health Care and Procurement*** *Improvement Act of 2002*, Section 7, ***Improved Accountability of Research Corporations Established at Department of Veterans Affairs Medical Centers*.**

   NAVREF has serious concerns about the content of this bill. As passed by the House on July 22, it imposes on the nonprofits numerous burdensome requirements, some of which provide no discernible

improvement in accountability. We are dismayed that NAVREF was not made aware that the Chairman planned to introduce legislation affecting the corporations prior to receipt of the GAO report on the corporations and this follow up hearing. We would have been pleased to participate in the development of the original bill, H.R. 5084, and to comment on drafts.

Our detailed comments on the bill passed as section 7 of H.R. 3645 are provided as Attachment A. On July 24, NAVREF representatives met with Subcommittee staff to discuss our concerns. However, because we do not know what changes are under consideration or what may be added as a result of this hearing, our comments in Attachment A are based on Section 7 of H.R. 3645 as passed by the House on July 22.

To summarize our comments, we strongly recommend that at a minimum, H.R. 3645, Section 7 should be amended to accomplish the following:

- Impose on **all** of the VA-affiliated nonprofit research and education corporations a requirement that within three years of enactment, the annual audit conducted in accordance with 38 USC §7366 (b) shall be performed in accordance with generally accepted government auditing standards.
- Require that the Inspector General of the Department of Veterans Affairs shall each year review the most recent audit under 38 USC §7366 (b) of at least 10 percent of the corporations
- Impose on VA a requirement to respond to congressional requests for information about one nonprofit within 30 days and within 90 days for requests requiring compilation of information from all the nonprofits.
- Set a June 1 deadline for the nonprofits' annual reports to VA and an October 1 deadline for the VA report to Congress.

These four items would address the primary concerns expressed by members of the Subcommittee during the May 16 hearing regarding oversight of the corporations. As detailed in Attachment A, the other overly burdensome and costly requirements specified in Section 7 should be eliminated. NAVREF has no objection to increased accountability, but feels the requirements put in place to achieve this objective should be reasonable and purposeful.

2. **H.R. 3253 Department of Veterans Affairs Emergency Preparedness Act of 2002 (Engrossed Amendment as Agreed to by Senate), Sections 401-403 regarding the Research Corporations**

As you may be aware, the Senate-passed version of H.R. 3253 contains three provisions regarding the VA nonprofits that are not contained in the House version. We strongly urge your support for all three, but one in particular, Section 401, greatly increases accountability of transactions between VAMCs and the nonprofits.

Section 401. Modification of Certain Authorities on Research Corporations. Our objective in this item is to once again allow VA medical centers and VA nonprofits to contract with each other just as they would with any other service provider, subject to VA's existing contracting authorities. Such contracts were allowed—and supported by two Office of General Counsel opinions—until December 2001 when General Counsel imposed a blanket prohibition on any contracts between VAMCs and the

nonprofits. In Section 401, we are seeking a legislative remedy. As detailed in NAVREF's July 17 letter to you, this provision:

- Clarifies that VA medical centers and NPCs may use VA's existing contracting authorities to acquire research or education services.
- Raises the level of scrutiny of transactions between VAMCs and NPCs.
- Maximizes the benefits of the VAMC/NPC partnership.

We strongly disagree with VA's views on this provision as expressed in General Counsel Tim McClain's written statement before the Senate Committee on Veterans Affairs on May 2.

- A payment pursuant to a VA-approved contract is **not** a "transfer; " it is a fee for a service.
- Contracts executed between VA and a corporation would **not** be "outside the scope of Federal procurement law." Rather, they would be subject to applicable laws, regulations and VA Handbooks, including those pertinent to affiliated institutions under VA's enhanced sharing authority (§8153).
- The nonprofits' primary focus would **not** change – they would remain flexible funding mechanisms to support research and education. Until GC imposed a prohibition on all contracts in December 2001, contracts enhanced the nonprofits' ability to support VA research.
- Because all research projects and education activities supported by the nonprofits must be approved by VA, and contracts under this authority would have to be approved by VA contracting officials, VA would **not** cede control to the nonprofits.

Further, NAVREF has been assured by field contracting officials and VA attorneys that both VA and other federal contracting statutes and regulations are sufficient to manage potential conflicts of interest.

Fees charged by nonprofits under the authority provided in Section 402 are likely to reflect only the foundation's cost of providing the service and would largely be reimbursement. Nonprofits that make a "profit" on an activity are at risk of incurring unrelated business income tax and jeopardizing their tax-exempt status. Therefore, we anticipate that services provided by foundations in support of VA-approved research and education would be both efficient and cost-effective for VA with the added accountability provided by review and approval by VA contracting officials.

A "reimbursement authority" has been suggested in lieu of using VA's existing contracting authorities. However, we feel this would provide less accountability than using VA's existing contracting authorities which have a full body of implementing regulations to ensure adequate controls. Again, we strongly encourage the House to accept the Senate provision regarding contracting between VAMCs and the nonprofits.

Section 402. Coverage of Research Corporation Personnel Under Federal Tort Claims Act and Other Tort Claims Laws. The objective of this provision is to clarify that foundation employees are covered under the Federal Tort Claims Act (FTCA) if they have departmental without compensation (WOC) appointments, work under the supervision of VA employees and perform VA-approved work, subject to certification by the Attorney General.

As you may be aware, in March 2000, the Department of Justice determined that corporation employees are not covered by the FTCA by virtue of their WOC appointments. VA General Counsel strongly disagrees with the Justice position and submitted a formal appeal in October 2001. However, it may take as much as four years to receive a response, and such a response may be negative.

Consequently, NAVREF is seeking a legislative solution and VA supports this remedy. As the Justice letter points out, Congress has extended FTCA coverage to the employees and contractors of a number of organizations that perform government functions or implement government objectives. Since 1989, both VA and the NPCs have been led to believe that NPC employees with WOC appointments working on VA-approved research under the supervision of VA employees would be covered by the FTCA. As a result, an explicit statement to that effect by Congress would impose no new burden on VA or the Department of Justice. Because the VA-affiliated nonprofit research and education corporations exist solely to support the VA research and education missions, in our view it is appropriate to be explicit in providing FTCA coverage to NPC employees engaged in activities that further VA's research and education missions.

Section 403. Permanent Authority for Research Corporations. This provision repeals the sunset clause that prohibits the establishment of new VA-affiliated nonprofits after December 31, 2003. In NAVREF's view, the nonprofits have proven their value to VA and the sunset clause should be eliminated entirely. However, a new expiration date of December 31, 2006 is an acceptable alternative.

Thank you for considering our views. I would be pleased to answer your questions.