

**A Closer Look at the
Future Combat Systems Agreement with Boeing:
A High Risk Program with a Higher Risk Agreement**

**Testimony Before the
Subcommittee on Airland
of the
Senate Committee on Armed Services
March 15, 2005**

**Kenneth F. Boehm
Chairman
National Legal and Policy Center
107 Park Washington Court
Falls Church, VA 22046
www.nlpc.org**

Mr. Chairman and Members of the Subcommittee, thank you for this opportunity to testify.

My name is Ken Boehm and I serve as Chairman of the National Legal and Policy Center (NLPC). My legal center promotes accountability in public life and has been critical of the actions of the Boeing Company during the recent series of defense procurement scandals. In October 2003, NLPC filed a complaint with the Defense Department's Office of Inspector General detailing former Air Force official Darleen Druyun's ties to Boeing through her daughter's job with that company and the sale of her house to a Boeing official while she was overseeing significant acquisition matters for the Air Force involving Boeing.¹

The complaint went on to question whether Druyun was negotiating for future employment with Boeing while she was representing the Air Force in multi-billion dollar business issues affecting Boeing contracts.

The next day, the *Wall Street Journal* ran a front-page story on the NLPC complaint, "Air Force Ex-Official Had Ties to Boeing During Contract Talks," and Boeing disingenuously told the media that Druyun was not working on the tanker deal as part of her employment for Boeing.² The Air Force weighed in with an equally disingenuous statement to the effect that Druyun had recused herself from decisions affecting Boeing but declined to specify when Druyun had recused herself.

The following month Boeing terminated employment for both Darleen Druyun and its Chief Financial Officer Michael Sears, citing violation of the company's standards in the hiring of Druyun.³

Today, Darleen Druyun is in federal prison and Michael Sears will be entering federal prison shortly, both in connection with their conspiracy to violate conflict of interest laws.

NLPC turned its attention to the Army's Future Combat Systems program because it was the largest military procurement project involving Boeing and - much like the tanker case - featured many anomalies which appeared to favor Boeing at the expense of the Army.

The conclusion reached was that while there appeared to be a consensus that the Future Combat System (FCS) program was high risk because of its ambitious plan to coordinate so many as yet undeveloped technologies into a coordinated weapons program of the future, these risks were compounded by the decision to use Boeing as the Lead

¹ See Letter to Defense Department Inspector General and Defense Criminal Investigative Service, Oct. 6, 2003, at www.nlpc.org.

² See "Air Force Ex-Official Had Ties to Boeing During Contract Talks," *The Wall Street Journal*, Oct. 7, 2003, p. 1.

³ See, e.g., "Boeing Dismisses Two Executives for Unethical Conduct," Boeing news release. Nov. 24, 2003, available at <http://www.boeing.com/news/releases/archive2003.html>.

System Integrator and to structure the legal agreement for FCS through a wholly inappropriate Other Transaction Agreement (OTA) in a way that minimized oversight and accountability.

The OTA exempted Boeing from most of the standard statutes which apply to major military procurement contracts to deter waste, fraud and abuse. Moreover, the use of an OTA in the FCS program was unprecedented insofar as OTAs were intended by Congress to attract non-traditional suppliers to deal with the Defense Department without the cost of the bureaucratic procedures associated with major defense contracts. Even a cursory examination of the FCS program shows that the highest amount of funding by far goes to Boeing with very little to any non-traditional suppliers and the \$20 billion dollar cost of the FCS development phase dwarfs any previous use of an OTA for prototype development purposes.

FCS: A High Risk Project

“FCS is at significant risk for not delivering required capability within budgeted resources. Three-fourths of FCS’ needed technologies were still immature when the project started.”

Paul Francis, Director, Acquisition and Sourcing Management, GAO⁴

There is a consensus that the FCS is an ambitious project which faces significant risks. This view has been expressed in both legislative hearings and within the defense community.

Even the FCS Other Transaction Agreement signed on Dec. 10, 2003 acknowledged:

*“The complexities and risk associated with the FCS SDD Increment I Program are significant.”*⁵

Among the risk factors cited by the GAO’s acquisition expert, Mr. Paul Francis, in testimony to the House of Representatives’ Subcommittee on Tactical Air and Land Forces of the Committee on Armed Services on April 1, 2004 were the following:

- The first FCS prototypes will not be delivered until just before the production decision.
- Full demonstration of FCS’ ability to work as an overarching

⁴ See Defense Acquisitions: The Army’s Future Combat System’s Features, Risks, and Alternatives, by Paul Francis, Director, Acquisition and Sourcing Management, April 1, 2004, GAO-04-635T.

⁵ See Agreement Between the Boeing Company and U.S. Army Tank-Automotive and Armaments Command Concerning Future Combat Systems System Development and Demonstration Phase, Agreement No. DAAE07-03-9-F001, at page 14

system will not occur until after production has begun. This demonstration assumes complete success – including delivery and integration of numerous complementary systems that are not inherently a part of FCS but are essential for FCS to work as a whole. When taking into account the lessons learned from commercial best Practices and the experiences of past programs, the FCS strategy is likely to result in cost and schedule consequences if problems are discovered late in development.

- Because the cost already dominates its investment budget, the Army may find it difficult to find other programs to cut in order to further fund FCS.⁶

These conclusions were explicitly understood by the Chairman of the House Armed Services Subcommittee on Tactical Air and Land Forces when the GAO presented its findings at a hearing on April 1, 2004. Chairman Curt Weldon (R-Pa.) summed up the problem succinctly when he stated, “If FCS experiences the technical difficulties that every major development program seems to experience, the cost overruns will consume the Army budget.”⁷

Rep. John Spratt (D-S.C.) accepted this assessment as well when he told Army Lt. Gen. Joseph Yakovac, who testified about the program as deputy to the Army acquisition secretary, “I can’t think in the 23 years I’ve sat here of a system more fraught with risk. It’s going to be a Herculean task to bring it together on the ambitious schedule you’ve set.”⁸

The technological challenges were summed up by Chairman Weldon at the hearing when he stated:

“Unfortunately, however, the Future Combat Systems program also carries high risk. The Army has never managed any program the size and complexity of FCS. Eighteen systems, 32 critical technology areas, 34 million lines of code, 129 trade studies, 157 programs being developed independent of FCS, and all in five-and-a-half years.”⁹

While the testimony of GAO Acquisition and Sourcing Management Director Paul Francis has already been cited, his analysis of the underlying management judgment associated with the FCS program was especially harsh:

⁶ See *Defense Acquisitions: The Army’s Future Combat System’s Features, Risks, and Alternatives*, by Paul Francis, Director, Acquisition and Sourcing Management, April 1, 2004, GAO-04-635T

⁷ See “GAO hoists red flag over costly Boeing Army project,” by Darrell Hassler and Tony Capaccio, Bloomberg News, *The Seattle Times*, April 2, 2004, p. E1.

⁸ See *Id.*

⁹ See Hearing of the Tactical Air Land Forces Subcommittee of the House Armed Services Committee on Future Combat Systems and Force protection Initiatives, April 1, 2004, Federal News Service transcript, p.3.

“In our more than 30 years of analyzing weapons systems, we have not found concurrent strategies to work, particularly when advanced technologies are involved. Delaying the demonstration of knowledge results in problems being discovered late in development. FCS is susceptible to such problems as a demonstration of multiple technologies, individual systems, the network and the system of systems will all culminate late in development and early production.”¹⁰

Mr. Francis further concluded that even modest delays and cost increases could end up costing the government billions of dollars and that such funds would be very difficult to find since the FCS was already consuming such a considerable portion of Army funding.¹¹

Boeing: A High Risk Lead System Integrator for FCS

The FCS program – which the Army has called its “greatest technological and integration challenge ever undertaken” – is a system of manned and unmanned ground vehicles, air vehicles, and munitions all connected with a cutting-edge communications and information system. Boeing became the Lead System Integrator on the SDD phase of FCS when it received, along with partner Science Applications International Corp. (SAIC), \$14.8 billion to oversee the eight-year effort in December 2003.¹² In August 2004, a modification to FCS added \$6.4 billion to the cost of the program.¹³

Boeing’s initial selection as LSI for FCS “shocked defense observers”¹⁴ and raised serious questions. As LSI, Boeing functions very much like a general contractor in overseeing other key suppliers and contractors to ensure that program objectives are met. That aspect of the LSI role has caused controversy for reasons touched upon in a *Financial Times* article:

“Boeing’s ability to defend its reputation will be critical. It has positioned itself as a ‘systems integrator’ for many of the big defence contracts it has secured – such as missile defence and the Future Combat Systems project – acting as the middleman, piecing together often complex technology from rivals, and **treading a fine line about managing access**

¹⁰ See Hearing of the Tactical Air Land Forces Subcommittee of the House Armed Services Committee on Future Combat Systems and Force Protection Initiatives, April 1, 2004, Federal News Service transcript, p. 8.

¹¹ See *Id.*

¹² See, e.g., “U.S. Army Signs Milestone FCS Contract,” Dec. 10, 2003, www.boeing.com/defense-space/ic/fcs/bia/031212_nr_armyannounce.html.

¹³ See “Army Boosts Boeing’s Future Combat Program Value By Up to \$6.4 Billion,” Aug. 17, 2004, <http://www.spacedaily.com/news/milspace-04x.html>.

¹⁴ See, e.g., “Boeing Plays Defense: Beset by Airbus and rocked by scandal, the aircraft maker turns to a new CEO – and the Pentagon – for help,” *Fortune*, April 19, 2004.

to proprietary information from rivals.¹⁵ (emphasis added)

Boeing's reputation for illegally obtaining proprietary information from its rivals is arguably the worst of any in the defense community. Since January 2003, Boeing has been implicated in three major cases involving improper access to competitors' proprietary information.

Raytheon Case

A report by the General Accounting Office (GAO) concluded that Boeing had obtained and misused Raytheon proprietary information in the course of a competition to provide a "kill vehicle" for the missile defense system. Boeing's actions violated Pentagon regulations for a project that was described as "the core of the missile defense system."¹⁶ When the misuse of Raytheon proprietary documents by Boeing came to light, Boeing was forced to withdraw from the competition. Boeing's actions hurt the government because the default award of the contract resulted in a design said by experts to be flawed in that the kill vehicle could not adequately distinguish between warheads and decoys. Also at issue was whether the government took appropriate steps to punish Boeing and recoup some of the \$800 million invested by the Pentagon in the design competition.

Especially important in considering Boeing's role in the Raytheon case is the fact that when Boeing illegally used Raytheon's proprietary documents in an attempt to win a major contract, Boeing was the LSI of the National Missile Defense Program.¹⁷ The GAO report also stated that the Army had recommended debarment against the Boeing employees involved in the wrongdoing and against Boeing's Electronic Systems and Missile Defense Group.

Ultimately, the Ballistic Missile Defense Organization "abandoned recovery efforts because of litigation risks associated with proving damages, as well as anticipated litigation costs, and the belief that litigation was inconsistent with its partnership with Boeing as the LSI contractor."¹⁸

It is difficult to imagine a more clear-cut example of a defense contractor abusing its Lead System Integrator role in a major project. Yet, in the end, Boeing received a mere slap on the wrist. There was no debarment of the company, no lawsuit to recoup the \$800 million lost on the tainted competition and no criminal prosecution.

¹⁵ See "Condit focuses on domestic problems," by Caroline Daniel, *Financial Times*, June 19, 2003, p. 29.

¹⁶ See "Antimissile Contract Won on Technicality, GAO Report Finds; Award Made After Boeing Spy Case," by Bradley Graham, *The Washington Post*, Jan. 30, 2003, p. A21.

¹⁷ See "Missile Defense: Events Related to Contractor Selection for the Exoatmospheric Kill Vehicle," General Accounting Office-03-324R Missile Defense, Jan. 27, 2003.

¹⁸ See "Missile Defense: Events Related to Contractor Selection for the Exoatmospheric Kill Vehicle," General Accounting Office-03-324R Missile Defense, Jan. 27, 2003, p. 11.

Boeing's selection by the Army as LSI for its largest procurement project ever, the high risk FCS program, is especially difficult to understand in that the Army was not only aware of Boeing's intentional misconduct in the case involving Raytheon's proprietary information but had recommended far more appropriate sanctions against Boeing than was finally meted out. The following excerpt from the GAO letter regarding the matter underscores this point:

"Concurrently, the Army recommended debarment proceedings against the Boeing employees involved in the wrongdoing, and against Boeing's Electronics Systems and Missile Defense Group. The Army also considered the alternative recommendation on a monetary settlement commensurate with the damages suffered by the government.

*The Army's assessment of damages focused on: the loss of the Integrity of a planned competition that had been carefully maintained for 8 years at great administrative expense; the loss of the benefit of a head-to-head "best value" comparison of two technical approaches developed at the cost of approximately \$400 million each; and the loss of the potential savings that might have been achieved by the abandoned competition, which the Army suggested should be valued at approximately 25 percent of the cost of Raytheon's EKV."*¹⁹

Lockheed-Martin Case

Boeing's ethical problems with proprietary documents belonging to its competitors also figured prominently when Boeing was discovered to have some 25,000 proprietary documents belonging to Lockheed Martin Corp. while the two companies competed for a major Pentagon rocket launch contract.

The Air Force stripped Boeing of approximately \$1 billion in potential revenue as a penalty in the case and also suspended three Boeing subsidiaries for an unspecified period. The Air Force stated that the suspension was appropriate for the "serious and substantial violations of federal law" involving the illegal acquisition of the Lockheed documents. The fallout continued with a civil racketeering case filed against Boeing by Lockheed, a Justice Department investigation and the indictment of two former Boeing employees. Speaking of the case, Air Force Undersecretary Peter B. Teets stated, "I have never heard of a case of this scale."²⁰

The suspension was not lifted until Mar. 4, 2005, making it the longest suspension of a major defense contractor ever.²¹

¹⁹ See "Missile Defense: Events Related to Contractor Selection for the Exoatmospheric Kill Vehicle," General Accounting Office-03-324R Missile Defense, Jan. 27, 2003, p. 11.

²⁰ See "U.S. Strips Boeing of Launches; \$1 Billion Sanction Over Data Stolen From Rival," by Renae Merle, *The Washington Post*, July 25, 2003, p. 1.

²¹ See "Air Force Lifts Boeing Suspension," Reuters, *Los Angeles Times*, Mar. 5, 2005, Part C, p. 3

Coming just months after the discovery of Boeing's misdeeds in the Raytheon case, the Lockheed Martin case represented one of the largest penalties ever assessed against a defense contractor. But the year was not yet over.

Airbus Case

Proprietary information involving a Boeing competitor was also an issue in the Boeing tanker lease scandal. E-mail messages written by Boeing executives and found by members of Congress suggested that "Darleen Druyun, who handled acquisitions for the Air Force at the time, might have shared confidential details of the Airbus offer with Boeing officials – thus giving them competitive advantage in crafting their own proposal."²²

The Department of Defense Inspector General's office initiated an investigation of the allegations.²³ An attorney for the Airbus parent firm, European Aeronautic Defense & Space Co. (EADS), raised additional questions with the allegation that if Druyun did pass along proprietary information to Boeing, that could have unfairly influenced a competition underway in Britain for the same kind of tankers.²⁴

All doubt as to Druyun's actions with respect to Airbus proprietary information was removed on October 1, 2004 when Druyun was sentenced to 9 months in federal prison. In a document released by the U.S. Attorney's office, it was stated that Druyun "acknowledges providing to Boeing during the [tanker] negotiations what she considered to be proprietary pricing data" from the European plane maker Airbus, which was competing to build the planes.²⁵

The cases involving Raytheon, Lockheed and Airbus all involve allegations of misconduct by Boeing in connection with proprietary information belonging to Boeing's competitors. All cases arose during major defense procurement competitions and all stories broke in 2003. But the ethical problems associated with Boeing's conduct as a defense contractor were not limited to proprietary information issues. A recent study by the Project on Government Oversight, a well-respected watchdog group, determined that Boeing "committed 50 acts of misconduct and paid \$378.9 million in fines and penalties between 1990 and 2003."²⁶

²² See "Pentagon to probe how Airbus lost refueling tanker deal to Boeing," AFX.COM, September 18, 2003.

²³ See "Pentagon to probe how Airbus lost refueling tanker deal to Boeing," AFX.COM, September 18, 2003.

²⁴ See "Boeing Deal on Tankers Again on Hold; Rumsfeld Orders Review After Executives are Fired," by Renae Merle, *The Washington Post*, Nov. 26, 2003, p. E1.

²⁵ See "Ex-Pentagon Official admits to more illegal help to Boeing," by David Bowermaster, *Seattle Times*, Oct. 2, 2004, p. A1

²⁶ See "U.S. Strips Boeing of Launches; \$1 Billion Sanction Over Data Stolen From Rival," by Renae Merle, *The Washington Post*, July 25, 2003, p. A01.

An excerpt from the Project on Government Oversight Federal Contractor Misconduct Database detailing Boeing misconduct in defense cases from 1990 through 2003 is appended at Exhibit A. It is all the more striking in that it leaves out many of the billions of dollars in tainted procurement contracts involving Boeing which have been disclosed in the past 18 months. When former Air Force official and former Boeing executive Druyun was sentenced on Oct. 1, 2004, U.S. Attorney Paul McNulty revealed that Druyun, after failing a polygraph, had confessed to:

- providing Boeing with proprietary information about a competitor as a parting gift to Boeing
- negotiating an excessive \$100 million payment to Boeing from NATO
- awarding Boeing a \$4 billion contract in 2001 to modernize more than 500 C-130 aircraft built by Lockheed-Martin, disclosing that “an objective selection authority may not have selected Boeing.”
- negotiating a \$412 million payment to Boeing in 2000 tied to its production of C-17 transports because a senior Boeing executive at the time was helping secure a job for her future son-in-law, Michael McKee²⁷

And as recently as Feb. 14, 2005, the Department of Defense revealed that it was turning over to the Inspector General for investigation eight additional questionable contracts overseen by Darleen Druyun worth billions of dollars. Four of the eight contracts involved Boeing, including a \$1.5 billion KC-135 Programmed Depot maintenance contract from 2000-2001.²⁸

The Future Combat Systems project with Boeing as LSI has already generated controversy after it was learned that Boeing executives had gotten access to secret information of companies competing with Boeing for FCS contracts:²⁹

- Boeing executives James Albaugh and Roger Krone were brought inside the so-called fire-wall, causing competitors and senior Army officials to worry that “Boeing could get an unfair advantage on the work it bids for.”
- “Concerns about Boeing’s role in the project come against the backdrop of recent allegations that the Chicago-based aerospace titan on at least two

²⁷ See “Ex-Pentagon official admits to more illegal help to Boeing,” by David Bowermaster, *The Seattle Times*, Oct. 2, 2004, p. A1.

²⁸ See “Department of Defense Announces Contract Reviews,” DoD News Release No. 157-04, Feb. 14, 2005.

²⁹ See “Boeing’s Role in Defense Project Worries Pentagon, Competitors,” by Anne Marie Squeo, *The Wall Street Journal*, June 16, 2003.

occasions inappropriately obtained a rival's information while competing for military contracts.”

The article went on to state that Army officials were “unhappy with the fire-wall situation” and that “any further controversy could undercut the Pentagon’s emerging practice of using a ‘lead system integrator’ from the private sector on big military programs.” While Boeing was quick to deny any problem with the revelations, that may be small comfort insofar as Boeing also misrepresented the extent of the wrongdoing in both the Raytheon and Lockheed cases.³⁰

By all accounts, an LSI for a major Pentagon project must have a reputation beyond reproach because the LSI has access to sensitive proprietary information from companies with which it is in competition on a regular basis. As this is a defining feature of the LSI role, a strong argument can be made that not only is Boeing a questionable selection for LSI in the FCS project, but given its documented reputation for illegally misusing proprietary information of competitors, Boeing is the worst possible choice for the role.

Boeing’s FCS OTA: Where Are the Nontraditional Defense Contractors?

The agreement between the Army and Boeing structuring the legal relationship for the FCS program’s System Development and Demonstration (SDD) Phase is known as an “other transaction agreement” or OTA. The legal authority for the FCS OTA is derived from 10 U.S.C. § 2371 and Section 845 of the Public Law 103-160, as modified by Section 804 of Public Law 104-201, and as modified by Section 803 of the Floyd D. Spence National Defense Authorization Act for FY 2001.³¹ These agreements are also sometimes referred to as Section 845 agreements. One of the distinguishing features of an OTA is that they are not generally subject to the federal laws and regulations which are applicable to procurement contracts.

One of the principal purposes of removing the legal requirements associated with standard procurement contracts for major defense contractors is in order to attract nontraditional defense contractors to consider working with the Defense Department.

The rationale for this purpose was expressed in a recent GAO Report on defense acquisitions:

“In an era of shrinking defense industrial base and new threats, DoD views ‘other transaction’ prototype authority as a key to attracting nontraditional defense contractors.”³²

³⁰ See “Boeing’s Misconduct is Detailed in Memo,” by Peter Pae, *The Los Angeles Times*, April 23, 2004.

³¹ See Agreement Between the Boeing Company and U.S. Army Tank-Automotive and Armaments Command Concerning Future Combat Systems System Development and Demonstration Phase, Agreement No. DAAE07-03-9-F001, at page 1.

³² See Defense Acquisitions: DoD Has Implemented Section 845 Recommendations but Reporting Can Be Enhanced, Report to the Chairman and Ranking Minority Member, Committee on Armed Services, U.S. Senate, Oct. 2002, GAO-03-150, p. 3

The GAO Report went on to cite as an example of a benefit to these agreements “attracting business entities that normally do not do business with the government.”

Despite the intent of Congress that OTAs be used to reach out to the newer high tech companies which might not otherwise consider dealing with the Pentagon, all too often prototype funds associated with OTAs do not flow to the nontraditional suppliers but to major defense contractors.

Such is the case with the FCS OTA. Boeing is the second largest defense contractor in the country and most of the other firms participating in the FCS program do not fit the description of a nontraditional defense contractor.

This fact was readily conceded in a report prepared last year for Acting Army Secretary Brownlee on FCS management issues:

“One intended benefit of OT authority – attracting nontraditional suppliers – has not been realized to date; the initial round of subcontracts has gone almost exclusively to traditional defense suppliers.”³³

A closer look at the funding of the FCS SDD program shows that just four large defense contractors account for most of the funding. The cost share of the planned work shows Boeing receiving \$4.9 billion, SAIC receiving \$1.3 billion, and General Dynamics and United Defense together receiving \$4.6 billion. The 21 Tier 1 competitive subcontracts combined total \$1.7 billion.³⁴

Boeing’s FCS OTA: Less Accountability and Oversight for America’s Most Dishonest Defense Contractor

In recognition of potential problems with using an OTA in lieu of a standard procurement contract, Congress was very careful in the extension of legal authority to the Department of Defense to utilize OTAs. The conference report accompanying the National Defense Authorization Act for Fiscal Year 1999³⁵, which extended the OTA authority, cautioned that any further extension would be contingent on the congressional defense committees concluding that OTAs had been used in a responsible and limited manner:

“[S]ection 845 authority should only be used in the exceptional cases where it can be clearly demonstrated that a normal grant or contract will not allow sufficient access to affordable technologies. The conferees are **especially concerned that such authority not**

³³ See Review of FCS Management Issues, Final Report to Acting Secretary of the Army Hon. R. L. Brownlee, Institute for Defense Analyses, Aug. 17, 2004, p. ES-3.

³⁴ Op cit

³⁵ See Pub. L. 105—261, 112 Stat. 1920, 1954 (1998).

be used to circumvent the appropriate management controls in the standard acquisition and budgeting process.”³⁶ (emphasis added)

Because the use of OTA authority can result in an agreement that is virtually exempt from most of the statutes and regulations governing Defense Department R&D or prototyping efforts, repeated efforts have been made to identify and clarify exactly which legal authorities might apply to an OTA. Paul G. Kaminski, as Undersecretary for Acquisition and Technology in December 1996, identified 21 statutes relating to procurement that “are not necessarily applicable to ‘other transactions.’”³⁷

While the objectives of cutting government red tape to empower the Defense Department to have increased flexibility in dealing with high-tech companies for advanced technology projects is clearly desirable, the fact that many of the statutes inapplicable to OTAs were specifically enacted to deter waste, fraud and abuse – a very real and persistent problem for government contracting – calls for very careful analysis. Simply stripping out decades of protective statutes without protecting the government’s interests in dealing with contractors is a formula for financial disaster. Put simply, such a process would leave the government vulnerable to almost any kind of waste, fraud and abuse and – adding insult to injury – an unethical company could say its actions were “legal” because laws restricting its unscrupulous activities simply did not apply.

A group of contract experts assembled as an ad hoc working group sought to analyze exactly which statutes were exempted from OTAs and the ramifications of those exemptions, publishing an excellent treatise on the subject in January 2000.³⁸ The group concluded that inapplicability of certain statutes and regulations “may raise significant questions of accountability for the public fisc and other matters of public policy.”³⁹ Increased risks and uncertainties in areas such as funding limitations and dispute resolution were identified.⁴⁰ And there was a warning that, “Confusion over OT’s statutory exemption can be costly either in litigation or in the misuse of OTs.”⁴¹

The signal contribution made by the ad hoc working group to the understanding of potential risks and benefits of OTAs comes from its analysis of the question as to whether OTAs are exempt from the 21 statutes identified in the Kaminski memo⁴² as well as an additional 11 statutes identified by the working group.

³⁶ See H.R. Conf. Rep. No. 105-736, at 590 (1998).

³⁷ See “Memorandum from Undersecretary of Defense for Acquisition and Technology Paul G. Kaminski to Secretaries of the Military Departments and Directors of Defense Agencies,” Dec. 14, 1996 reprinted in full in *Department of Defense Other Transactions: An Analysis of Applicable Laws*, a project of the Ad Hoc Working Group on Other Transactions Section of Public Contract Law, American Bar Association, 2000, Attachment 1.

³⁸ See *Department of Defense Other Transactions: An Analysis of Applicable Laws*, a project of the Ad Hoc Working Group on Other Transactions Section of Public Contract Law, American Bar Association, 2000.

³⁹ See *Id.* at 2.

⁴⁰ See *Id.* at 2.

⁴¹ See *Id.* at 2.

⁴² See *Id.* at Attachment I

Among the statutes determined to not apply to OTAs are the following:

- Competition in Contracting Act
- Contract Disputes Act
- Extraordinary Contractual Authority and Relief Act
- 10 U.S.C. § 2313, Examination of records of contractor
- 10 U.S.C. § 2403, Major Weapons Systems: Contractor Guarantees
- 10 U.S.C. § 2408, Prohibition on persons convicted of defense contract related felonies and related criminal penalty as defense contractors
- 10 U.S.C. § 2409, Contractor employees: protection from reprisal for disclosure of certain information
- 31 U.S.C. § 1352, Limitation on the use of appropriated funds to influence certain Federal contracting and financial transactions
- 41 U.S.C. § 423, Procurement Integrity Act
- 41 U.S.C. §§ 701-707, Drug-Free Workplace Act of 1988
- 41 U.S.C. §§ 10a-10d, Buy American Act
- 41 U.S.C. § 2306a, Truth in Negotiations Act
- 41 U.S.C. § 422, Cost Accounting Standards
- 10 U.S.C. § 2334, Cost Principles

The statutes just listed, along with their enabling regulations, represent a partial list of the statutory exemptions for OTAs. While an OTA may incorporate some of the missing statutory protections and terms by writing them into the agreement, any omissions can easily become loopholes through which an unscrupulous contractor can extract financial benefits not typically available to other contractors who are subject to the standard procurement contract.

A more detailed listing is appended to this testimony as Exhibit B: Applicability of Specific Statutes to Other Transaction Agreements.

Also of concern is the fact that the lack of major procurements handled through OTAs has meant that there is a distinct lack of case law interpreting possible ambiguities.

This means additional uncertainties and costs in the event of disputes that may occur between the contractor and the government with the burden of proof being on the government in most instances.

While there has never been an OTA as large as the FCS OTA, problems of accountability have arisen in recent OTAs such as the Evolved Expendable Launch Vehicle (EELV) project. A great deal of financial information about the project is off-limits to the public and, among other issues, the public and the media have no practical way to assess whether claims of government savings are credible.

A recent article on the EELV raised issues directly relevant to the FCS project:

“In its audits, the General Accounting Office warned the Other Transaction Agreement approach was risky for a billion-dollar-project. It’s a tool previously reserved for far smaller contracts. The GAO said it posed considerable challenges because it exempted the project from normal rules for spending tax dollars, limited Defense Department oversight and did not give the military the authority to conduct audits, GAO said.

‘The use of Other Transaction instruments for Evolved Expendable Launch Vehicle development will challenge (the Defense Department) in determining how to protect the government’s Interests,’ GAO said.

The Defense Department inspector general also challenged whether there was enough ‘visibility’ into the program’s spending in its 1999 review of the EELV program, according to the agency’s Congressional testimony.

‘The EELV other transactions agreements included technical safeguards but provided limited insight into the financial aspects of the program,’ assistant auditor Don Mancuso told Congress in the spring of 2000.”⁴³

The lack of transparency and accountability is a serious issue in its own right but, as indicated in the EELV case above, disclosure acts as an important deterrent to unscrupulous behavior by contractors:

“However, government auditors and taxpayer watchdog groups cautioned one side effect of the new way of doing business is far less public disclosure of what the companies and the military are doing with public money.

⁴³ See “\$1 billion question – Taxpayers may never know how companies spent Air Force rocket money,” by John Kelly, Chris Kridler, and Kelly Young, *Florida Today*, August 25, 2002, p. 1

‘Anything that removes financial transparency is not a good deal for the taxpayers,’ said Eric Miller, a defense industry investigator for the Project on Government Oversight, which has spent two decades investigating deals between the Defense Department and its contractors. ‘Time and again defense contractors have shown they will sometimes take advantage of these types of situations. When you eliminate that kind of oversight, you’ve got a potential disaster.’⁴⁴

Mr. Miller went on to state that the Other Transaction Agreement strategy was never intended for big companies to avoid scrutiny on nine- and ten-figure contracts. “We don’t think such large contracts should come without financial oversight. It’s a dangerous practice.”⁴⁵

Boeing’s FCS OTA: How Sweet a Financial Deal?

By all accounts the FCS deal has been an exceptionally good one for Boeing. The \$14.8 billion initially being spent on the development phase has already been augmented with an additional FCS modification in August 2004 which added approximately \$6 billion to the program and will probably grow to more than \$100 billion when production gets underway.⁴⁶ And it comes at a time when Boeing has been losing market share to Airbus, making its defense business all the more important. The year 2003 marked the first time in decades that more than half of Boeing’s revenues came from defense.⁴⁷

Financially, the importance of FCS to Boeing has been cited by such defense experts as Jacques Gansler, Undersecretary of Defense for Acquisition, Technology and Logistics in the Clinton Administration, who recently stated, “This [FCS] is a big plum, from Boeing’s perspective.”⁴⁸ One of the reasons such a Lead System Integrator deal can be lucrative is that it does not require a significant amount of new capital spending so the return on investment can be quite high. George Muellner, president of Phantom Works, Boeing’s research and development arm, has described the LSI role as being a “high-margin, low-overhead area.”⁴⁹

Far and away, the most important factor to be analyzed in determining whether the FCS program was negotiated in Boeing’s interest at the expense of the government is the OTA signed on Dec. 10, 2003.⁵⁰

⁴⁴ See Id.

⁴⁵ See Id.

⁴⁶ See “Boeing-SAIC Team gets \$14.8 billion Army pact,” *San Diego Union-Tribune*, Dec. 11, 2003.

⁴⁷ See “Boeing Plays Defense; Beset by Airbus and rocked by scandal, the aircraft maker turns to a new CEO – and the Pentagon – for help,” by Judy Cresswell, *Fortune*, April 19, 2004, p. 90.

⁴⁸ See Id.

⁴⁹ See Id.

⁵⁰ See Agreement Between the Boeing Company and U.S. Army Tank-Automotive and Armaments Command Concerning Future Combat Systems System Development and Demonstration Phase, Agreement No. DAAE07-03-9-F001.

While obtaining a copy of a government procurement document is generally relatively easy insofar as most are public information, Boeing has shown itself to be unusually sensitive in opposing public scrutiny of its FCS arrangement with the Army. When the National Legal and Policy Center filed a request under the Freedom of Information Act for a copy of both the draft and final versions of the FCS OTA, NLPC's counsel was informed that Boeing opposed disclosure, even to the point of claiming the documents were "classified." To their credit, the Army's professional FOIA staff disclosed the requested materials once it became apparent that Boeing had no legal grounds to prevent such disclosure.

An analysis of the FCS OTA confirmed what others had already suspected – that the FCS OTA negotiated by Boeing lacked many of the standard legal protections that accompany major Defense Department acquisitions. Because OTAs are not contracts and were originally designed to streamline regulatory procedures, many legal terms and conditions needed to deter or detect waste, fraud and abuse must be individually incorporated into an OTA or they simply will not apply.

The first round of public controversy addressing the legal shortcomings of the FCS OTA began when Reuters ran an article disclosing that two months before the Army signed the FCS OTA with Boeing, a private consulting firm, CommerceBasix, Inc., hired to improve the Army acquisition process, recommended that the Army rework the draft agreement. Among the consulting firm's findings was that a delay of six months in the project under the terms of the May 31, 2003 draft OTA could result in a \$1 billion financial risk to the government.⁵¹

While Army officials were dismissive toward the Oct. 14, 2003 consultant's report and signed the OTA on Dec. 10, 2003, the subsequent analysis by the General Accounting Office released on April 1, 2004 before the House Armed Services Subcommittee on Tactical Air Land Forces not only largely corroborated the consultant's claim but even cited the possibility of a multi-billion-dollar cost associated with a fairly modest delay.⁵²

The Reuters article disclosed that concerns about FCS were not limited to the consulting firm:

“The size of the agreement sparked concerns not just at CommerceBasix but among top Future Combat Systems Program officials and defense industry experts as well.

‘This was unheard of,’ said one defense industry official,

⁵¹ See “Boeing deal with Army criticized; Consultant cited \$1 billion risk to government,” *Chicago Tribune*, Feb. 17, 2004, p. 3.

⁵² See Hearing of the Tactical Air Land Forces Subcommittee of the House Armed Services Committee on Future Combat Systems and Force protection Initiatives, April 1, 2004, Federal News Service transcript, p. 8.

who asked not to named. ‘It raised a lot of alarm bells.’”⁵³

The Reuters article went on to report that the decision to opt for the less formal Other Transaction Agreement instead of a standard Defense Department procurement contract “also raised eyebrows, given a spate of ethics scandals at Boeing in recent months.”⁵⁴

Anyone able to obtain and review the FCS OTA would have even greater reason for raised eyebrows.

The consultants only had the May 30, 2003 draft OTA on which to rely for their October 2003 report. However, a review of that draft with the final definitized version signed in December 2003 indicates relatively minor changes in terms and conditions. Indeed, the OTA itself indicates that the definitization process between the May and December versions would deal more with cost issues than business terms and conditions.⁵⁵

Perhaps out of sensitivity to the consulting firm’s allegation about the government’s exposure to financial risk, the final version did substantially augment “Article XXXIII – Termination Liability” from the relatively Spartan treatment of those issues in the May version and some related terms and conditions.

Ironically, the report on FCS management by the Institute for Defense Analyses was critical of the CommerceBasix analysis of the legal weakness of the FCS OTA by citing the fact that they did not see the final December 2003 agreement:

*“TheCommerceBasix review of a draft Army-Boeing agreement, which was critical of the lack of clauses to protect the Army’s interests, did not address all of the clauses that are in the final FCS agreement.”*⁵⁶

This is somewhat disingenuous since it seems to suggest there was a major strengthening of the agreement to protect the Army’s interests before the December draft was signed. There was not, as any reading of the two documents shows. The Army would have been better served had there been a listing of all changes made to the May draft to better protect the Army’s legal interests. Even more helpful would have been a complete analysis of the legal effect of the omission of every statute which covers standard DoD procurement contracts but which are missing from the FCS OTA.

⁵³ See “Boeing deal with Army criticized; Consultant cited \$1 billion risk to government,” *Chicago Tribune*, Feb. 17, 2004, p. 3.

⁵⁴ See *Id.*

⁵⁵ See Agreement Between the Boeing Company and U.S. Army Tank-Automotive and Armaments Command Concerning Future Combat Systems System Development and Demonstration Phase, Agreement No. DAAE07-03-9-F001, May 30, 2003 draft at pp. 13-14.

⁵⁶ See Review of FCS Management Issues, Final Report to Acting Secretary of the Army Hon. R. L. Brownlee, Institute for Defense Analyses, Aug. 17, 2004, p. ES-3.

All too many issues associated with protecting the government's interests against waste, fraud and abuse as well as promoting accountability remain.

Traditionally, resolution of disputes is a critically important part of any major agreement. In the case of a high-risk, multi-billion-dollar project where the GAO already has assessed "significant risk," the resolution of disputes is an area that requires clarity as well as strong protection of the government's interests. The Contracts Disputes Act does not apply to OTAs unless it has been specifically incorporated into the agreement. The FCS OTA has no such incorporation of the Contract Disputes Act.

The issue of dispute resolution is addressed in the FCS OTA at Article XV – Disputes. While Boeing and the Army anticipate resolving disputes through a set of sparsely worded dispute resolution procedures, Boeing is also accorded the opportunity to "bring a claim in a court of competent jurisdiction as authorized by 28 USC 1491"⁵⁷ if Boeing disagrees with the outcome of the dispute resolution.

An apparent shortcoming is the failure to address exactly how the government can bring a claim in the event it disagrees with the outcome of a dispute resolution. Generally, there is federal jurisdiction over civil actions initiated by the U.S. government as stated in 28 U.S.C. § 1345, "Except as otherwise provided by an Act of Congress, the district courts shall have original jurisdiction of all civil actions, suits, or proceedings commenced by the United States, or by any agency or officer thereof expressly allowed to sue by Act of Congress." The Contract Disputes Act represents a way in which Congress has "otherwise provided" for jurisdiction in that it applies to any "express or implied contract...entered into by an executive agency..." The Court of Federal Claims has jurisdiction over claims brought pursuant to the Contract Disputes Act. However, since the FCS OTA is not considered a "contract," a very real issue exists as to whether and how the Army could bring a breach of contract suit against Boeing. Moreover, the Court of Federal Claims has never ruled on its jurisdiction over OTAs.

Throughout the FCS OTA, problems similar to the issue of dispute resolution appear, resulting in both uncertainty as well as legal vulnerability for the government's position. The Army had a professional, legal and ethical obligation to address every such issue so as to protect the government's interest. The guidance provided to the Army through the "*Other Transactions*" (*OT*) *Guide for Prototype Projects*, as revised in August 2002, addresses this obligation clearly:

"...the Agreements Officer is not precluded from and should consider applying the principles or provisions of any applicable statute that provides important protections to the government, the

⁵⁷ See Agreement Between the Boeing Company and U.S. Army Tank-Automotive and Armaments Command Concerning Future Combat Systems System Development and Demonstration Phase, Agreement No. DAAE07-03-9-F001, Dec. 10, 2003, at Article XV (B)(3), p. 53.

participants or participants' employees.”⁵⁸

The guide went on to advise that the Agreements Officer may also want to consider whether whistleblower protections should be included in the agreement, “especially if the prime awardee is a company that typically does business with the DoD.”⁵⁹

The guide is consistent in advising the government to take all appropriate steps to protect the government's interests in an OTA and especially in taking steps to minimize project risk. The linkage of risk to the terms and conditions of the OT agreement is also beyond dispute:

“The risks inherent in the prototype project and the capability of the sources expected to compete should be a factor in the terms and conditions of the OT agreement.”⁶⁰

While the FCS OTA does incorporate a number of statutory provisions as well as Federal Acquisition Regulations, the majority of standard procurement laws and a good number of laws promoting accountability are conspicuous by their absence. Without providing an exhaustive listing, it appears that most of the statutes previously specified in *Department of Defense Other Transactions: An Analysis of Applicable Laws* are not applicable to the FCS OTA.

A review of the FCS OTA found no apparent inclusion of the Procurement Integrity Act. This is especially noteworthy given the allegations involved in the criminal investigation of Darleen Druyun and Boeing. The Procurement Integrity Act⁶¹ imposes two types of obligations on government employees seeking non-government employment who have been involved in procurement. First, for government employees who have been personally and substantially involved in a procurement worth more than \$100,000, it sets forth requirements that must be followed if the employee inquires about or is contacted by the company involved with the procurement. Second, there is a one-year ban on accepting compensation from contractors involved in the procurement. There are civil penalties for violations by both the government employee and the contractor.⁶²

Additionally, the FCS OTA does not include the Truth in Negotiations Act (10 U.S.C. § 2306a). Possible violation of the Truth in Negotiations Act may be an issue in the ongoing audit of the AWACs contract upgrade involving Darleen Druyun.⁶³ At issue

⁵⁸ See “*Other Transactions*” (*OT*) *Guide for Prototype Projects*, Under Secretary of Defense for Acquisition, Technology and Logistics, August 2002, C2.7 – Consideration of Protections Provided in Law, p. 24.

⁵⁹ See *Id.*

⁶⁰ See “*Other Transactions*” (*OT*) *Guide for Prototype Projects*, Under Secretary of Defense for Acquisition, Technology and Logistics, August 2002, C2.1.3.1.5 – Risk Assessment, at p. 15.

⁶¹ See 41 U.S.C. § 423.

⁶² See 41 U.S.C. § 423(c),(d),(e).

⁶³ See “Pentagon auditors check Boeing charges; Review part of probe of ex-company exec,” by Tony Capaccio, *The Seattle Times*, May 12, 2004, p. E6.

specifically is whether Boeing overcharged the Air Force by “a significant amount” on a \$1.3 billion contract to upgrade NATO surveillance aircraft. The article stated:

“Contractors are required under the Truth in Negotiations Act to provide accurate data, which serves as the basis for final negotiated prices.”⁶⁴

Boeing is no stranger to allegations that it has mischarged or overcharged the government on Defense Department contracts. In one instance, a Boeing subsidiary paid \$3.8 million to settle claims arising from three Navy contracts in which the subsidiary was said to have “mischarged numerous labor hours or provided inaccurate cost information to the government during negotiations for all of the contracts.”⁶⁵ The Justice Department media release on the case stated:

“Under the Truth in Negotiations Act, companies are required to disclose to the government pricing and cost information in their possession when they negotiate contracts with the government.”⁶⁶

The failure of the FCS OTA to be covered by the Truth in Negotiations Act represents yet another legal vulnerability for the government in the event that Boeing or any of its partners provide inaccurate or padded cost estimates in any negotiation associated with the program. There is little doubt that Boeing as a defense contractor does not like the idea of being legally required to provide the government with accurate cost information under the Truth in Negotiations Act. At a roundtable discussion of government contract issues during 2001 Boeing Vice President John Judy argued that the threshold for coverage of the Truth in Negotiations Act should be raised significantly.⁶⁷ Coincidentally, Mr. Judy’s name surfaced during the Darleen Druyun scandal when the National Legal and Policy Center disclosed that he had contracted to purchase Druyun’s Virginia home while Druyun was still at the Air Force overseeing mult-billion dollar business deals with Boeing.

The fact is that Boeing has a long and well-documented record of blatantly overcharging the Pentagon on defense contracts. In the 1980’s Boeing was caught charging the Air Force \$748 for a pair of pliers to be used to repair KC-135 tanker airplanes. An engineer testified before Sen. Grassley’s Judiciary subcommittee on administrative practice and procedure on the subject and stated that he found similar pliers at a hardware store for \$7.61.⁶⁸

⁶⁴ See Id.

⁶⁵ See “Boeing Subsidiary Pays U.S. \$3.8 Million to Settle Dispute Over Three Navy Contracts,” U.S. Department of Justice U.S. Newswire Release, Dec. 29, 1992.

⁶⁶ See Id.

⁶⁷ See “Plotting Our Defense: The Pentagon Wants Reform, but How Will It Work?” *Legal Times*, march 5, 2001, p. 30.

⁶⁸ See “Air Force Victory is Illusory in the Case of \$748 Pliers; Boeing’s New Charge Offsets Price Cut,” *The Washington Post*, March 22, 1985, p. A1.

There are no shortages of good examples of the impact that deficient agreement language or agreement negotiations can have. A very recent example involves – once again – Boeing and the Department of Defense. In an April 16, 2004 *Washington Post* article titled, “Audit Criticizes Another Boeing Deal; Inspector General Says Air Force Didn’t Negotiate NATO Contract Properly,” a \$1.34 billion contract being negotiated by Air Force official Darleen Druyun with her future employer Boeing failed to have the proper verification of costs. As a result, the parties must sit down and follow the correct procedures to ensure that the costs are appropriate. The audit conducted by the Department of Defense Office of Inspector General concluded, “Air Force contracting officials awarded the contract modifications without knowing whether the \$1.3 billion cost was fair and reasonable.”⁶⁹ Four days after this article appeared, Darleen Druyun pled guilty in the U.S. District Court for the Eastern District of Virginia in conjunction with a federal felony count of conspiracy which arose from her employment dealings with Boeing at the same time the contract in question was being finalized.⁷⁰

U.S. Attorney Paul McNulty summed up his view of the crime by stating:

“The only interest should be the public’s interest. Darleen Druyun placed her personal interest over the interests of the Air Force and American taxpayers. Secretly negotiating employment with a government contractor, at the same time you are overseeing the negotiations of a multi-billion dollar lease from that same contractor, strikes at the heart of the integrity of the acquisition process.”⁷¹

The case just cited raises yet another series of questions regarding the lack of integrity in the manner in which Boeing has pursued Department of Defense business. The pattern of wrongdoing is unmistakable. And there’s more. A recent article in *The Wall Street Journal* by Andy Pasztor reported on another pending procurement scandal involving allegations against Boeing:

“In St. Louis, [Boeing] faces a civil investigation for allegedly using foreign titanium in F-15 fighter jets, certain military transport planes and various other Pentagon programs, contrary to U.S. law. Investigators previously demanded the company pay \$20 million to resolve the claims, but Boeing balked at a settlement. The investigation has been underway for three years, though it hasn’t been reported until now.”⁷²

⁶⁹ See “Defense tags Boeing AWACS Deal for criticism; Report: Contract was Mishandled,” by David Bowermaster, *The Seattle Times*, April 16, 2004, p. C1.

⁷⁰ See “Ex-Pentagon Official Admits Job Deal; Civilian Got Boeing Offer While Overseeing Air-Tanker Contract,” by Renae Merle and Jerry Markon, *The Washington Post*, April 21, 2004, p. 1.

⁷¹ See Statement of U.S. Attorney Paul McNulty, April 20, 2004, United States of America v. Darleen Druyun, Criminal No. 04-150-A

⁷² See “Pentagon Probes Suppliers’ Hiring,” by Andy Pasztor, *The Wall Street Journal*, January 12, 2004.

Perhaps if Boeing had had the foresight to use an OTA in the case just cited, it would not be facing a \$20 million fine. The Buy American Act (41 U.S.C. §§ 10a – 10d) does not apply to OTAs unless it has been specifically added.

In yet another very recent (April 23, 2004) news account, the serial nature of Boeing's misconduct with DoD procurement was underscored:

“An internal Air Force memo suggests a broad pattern of improprieties by Boeing Co. when it bid on Pentagon contracts, contradicting the aerospace giant's assertions that such problems were isolated and that it corrected them quickly.”⁷³

The FCS OTA – on its face – raises very serious questions as to whether the government's legal and financial interests have been well served. There is little doubt that Boeing's interests have been well served by receiving the \$20 billion plus “plum deal.” Even a casual reading of the FCS OTA shows considerable financial incentives for Boeing, including the earlier cited “...maximum possible opportunity to earn fee.”⁷⁴ Also deserving scrutiny is the questionable \$9.8 million incentive award received by Boeing from the Army for completing the agreement by the end of the year.⁷⁵ At a time when Boeing was spending millions of dollars on lobbyists in its push for Pentagon business, a \$9.8 million incentive award for rushing through a lucrative deal hardly seems necessary – or wise.

But there is a human element that also invites scrutiny. The fact that the senior Boeing executive involved in the FCS procurement was Michael Sears, the Boeing CFO terminated for cause in connection with his hiring of Darleen Druyun and also – according to Boeing – in the alleged cover-up of his actions, ought to be considered a red flag. Indeed, Sears, prior to becoming Boeing CFO, was the head of Boeing's Phantom Works, the Boeing R&D operation that played a key role in winning the FCS deal.⁷⁶

After Boeing took an unexpected \$1.1 billion charge in 2003 because of losses in its commercial space business, media accounts listed Michael Sears as leader of a team of experts looking to examine the business cases associated with Boeing's biggest projects. *Financial Times* interviewed Mr. Sears and reported:

“Mr. Sears hinted that the business cases made in some of Boeing's tenders were not satisfactory, and added that the risk management practice of the different

⁷³ See “Boeing's Misconduct Is Detailed in Memo,” by Peter Pae, *The Los Angeles Times*, April 23, 2004.

⁷⁴ See Agreement Between the Boeing Company and U.S. Army Tank-Automotive and Armaments Command Concerning Future Combat Systems System Development and Demonstration Phase, Agreement No. DAAE07-03-9-F001, at p. 14.

⁷⁵ See “Boeing deal with Army criticized; Consultant cited \$1 billion risk to government,” *Chicago Tribune*, Feb. 17, 2004, p. 3.

⁷⁶ See “Contract Gives Boeing a Lift,” by Paul Merrion, *Crain's Chicago Business*, May 13, 2002, p. 13.

business units might not be adequate.”⁷⁷

Mr. Sears went on to specifically name the Future Combat Systems project as one of the Boeing efforts being reviewed.⁷⁸

Despite the Reuters account documenting concern over the FCS deal among both FCS program officers and defense industry experts, not to mention the consultant’s report detailing the serious legal and financial risks with the proposed OTA,⁷⁹ *Defense Daily* reported:

“Originally planned to be signed Nov. 26, the Army reached agreement on the SDD contract with the LSI [Boeing] in a process that went ‘exceedingly smoothly from my vantage point,’ Claude Bolton, assistant secretary of the Army for Acquisition, Logistics and Technology, said last month.”⁸⁰

Indeed, Boeing was receiving a nice incentive award to push through a multi-billion-dollar agreement for itself. For good measure, the agreement had most major statutory and regulatory provisions meant to protect against ethical misconduct and other contractor abuses stripped out. What was not to like?

Recommendations

The Army’s largest procurement project has as a Lead System Integrator Boeing, a defense contractor with the demonstrably worst record of procurement misconduct of any defense contractor. Boeing was penalized for substantial violations of the law in the Lockheed proprietary documents case with a \$1 billion contract sanction and the longest suspension of any major defense contractor. In the tanker case, Boeing tried to mislead Congress on the need for tankers with false information in an attempt to get funding for a program that was over-priced by billions of dollars. Boeing executives have pleaded guilty to felonies and Boeing is currently facing numerous criminal investigations and civil litigation for its misconduct.

Instead of increased oversight, Boeing is managing the Army’s most important procurement project with a legal agreement which meant to attract nontraditional suppliers and which minimizes oversight and accountability.

This is a recipe for disaster.

⁷⁷ See “Boeing Team to Reassess Top Projects,” *Financial Times*, by Caroline Daniel, Sept. 2, 2003, p. 33.

⁷⁸ See *Id.*

⁷⁹ See “Boeing deal with Army Criticized; Consultant cited \$1 billion risk to government,” *Chicago Tribune*, Feb. 17, 2004, p. 3.

⁸⁰ See “Army and Boeing-SAIC LSI Sign \$14.8 Billion SDD Contract for Future Combat Systems,” *Defense Daily*, December 12, 2003.

The broadest recommendations are that Congress should conduct a thorough review of the vulnerabilities to the government's position because of the use of an OTA and that Congress should intensify its oversight of the FCS program.

The FCS program is high risk because of its ambitious embrace of so many new and untested technologies but the failure of the Army to have adequate oversight and accountability through the use of an OTA represents an even higher risk.

The best way to assess the major legal vulnerabilities of the present FCS OTA would be an independent legal analysis of the ways in which the agreement fails to match the legal protections found in standard defense procurement contracts. Starting with an assessment of the statutes listed in Exhibit B: Applicability of Specific Statutes to Other Transaction Agreements, there should be statute by statute analysis of the legal benefits of each statute to the government and a thorough examination of the language in the OTA to determine what benefits are missing and what effect that may have on the government's ability to oversee the program and to protect its legal interests.

Similarly, there should be an independent examination of the financial and fee structure of the FCS program. While Lead System Integrator positions can be very lucrative for defense contractors and this aspect should be closely scrutinized, even closer scrutiny should be given to whether Boeing's compensation in the OTA is appropriate given the shifting of so much of the financial and legal risk for the program to the government as compared with a standard defense procurement contract.

To the degree that the government can modify the existing agreement to protect its interests and promote greater accountability, it must do so. Whatever objections Boeing may have to such a modification pale next to the risk the government is taking in not asserting its right to protect its interests.

Given the poor choice of Boeing as the Lead System Integrator for FCS, especially given Boeing's incredibly poor record with respect to respecting competitors' proprietary information rights, there is no alternative to increased Congressional oversight of the FCS program. As the GAO has pointed out, the cost associated with the FCS program so dominates the Army's investment budget for years to come that any failures in this high risk program will make it extremely difficult to find any other funds to remedy the problem.

The most ethically-challenged defense contractor in the country is in charge of the most expensive high risk defense program using an agreement that minimizes oversight and accountability. If that doesn't call for increased Congressional oversight, what does?

Exhibit A

Project on Government Oversight
Federal Contractor Misconduct Database
www.pogo.org/db/found.cfm

Boeing Defense Misconduct: 1991-2003

Contractor	Case	Amount	Disposition, Date & Source
Boeing --McDonnell Douglass	Defense "Procurement Fraud"	\$1,100,000 (Civil)	Settlement, 3/13/1991 Defense Contracts: Contractor Claims for Legal Costs Associated with Stockholder Lawsuits GAO/NSIAD-95-166 (July 1995)
Boeing --McDonnell Douglas	Defense "... agreed to pay \$1 million to resolve claims that it failed to disclose all information and also misrepresented other costs in negotiating three contracts with the Navy."	\$1,000,000 (Civil)	Settlement, 8/4/1992 Defense Contract Litigation Reporter 08/28/92
Boeing --Argosystem	Defense "Procurement Fraud"	\$868,000 (Civil)	Settlement, 12/23/1992 Defense Contracts: Contractor Claims for Legal Costs Associated with Stockholder Lawsuits GAO/NSIAD-95-166 (July 1995)
Boeing --McDonnell Douglas	Defense Allegedly "failed to disclose required cost or pricing data in negotiating delivery orders for an Army weapon"	\$2,100,000 (Civil)	Settlement, 3/3/1993 Defense Contract Litigation Reporter 03/11/93
Boeing	Defense Accused of "mischarging labor costs on a number of Department of Defense airplane contracts"	United States v McDonnell Douglas, Docket #93-CV-2188, US DC ED MO (Civil)	Pending, 10/12/1993 Department of Justice (DOJ) Press Release 09/08/95; Taxpayers Against Fraud (TAF) Quarterly Review Volume 13 April 1998, Volume 9 April 1997; Court Docket
Boeing	Defense "Procurement Fraud"	\$250,000 (Civil)	Settlement, 4/15/1994 Defense Contracts: Contractor Claims for Legal Costs Associated

with Stockholder Lawsuits
GAO/NSIAD-95-166 (July 1995)

Boeing	Defense	\$75,000,000	Settlement, 4/29/1994
	"Accused of charging the Government millions of dollars in research and development costs that it should have absorbed."	(Civil)	Defense Contracts: Contractor Claims for Legal Costs Associated with Stockholder Lawsuits GAO/NSIAD-95-166 (July 1995); The New York Times 04/30/94
Boeing --Argosystem	Defense	\$3,000,000	Settlement, 12/1/1994
	"Voluntary Disclosure Fraud"	(Civil)	Defense Contracts: Contractor Claims for Legal Costs Associated with Stockholder Lawsuits GAO/NSIAD-95-166 (July 1995)
Boeing --Rockwell	Defense	\$260,000	Settlement, 6/14/1995
	"... during contract price negotiations Rockwell gave the Air Force proposals that failed to account for discounts Rockwell received from its vendor"	(Civil)	Department of Justice (DOJ) Press Release 06/14/95; Settlement Agreement
Boeing --Rockwell	Defense	\$27,000,000	Settlement, 7/31/1995
	"... to settle allegations the company knowingly failed to provide the U.S. with accurate, complete and current information in negotiating multi-billion dollar contracts in 1981"	(Civil)	Department of Justice (DOJ) Press Release 07/31/95; Taxpayers Against Fraud (TAF) Quarterly Review October 1995; Settlement Agreement
Boeing --Space and Defense Group	Defense	\$6,000,000	Settlement, 9/1/1997
	Allegedly, "unallowable costs were ... included in computations used to determine overhead rates used on Government contracts."	(Administrative)	Department of Defense (DOD) Inspector General Semiannual Report to the Congress 04/01/97 - 09/30/97
Boeing --McDonnell Douglas Aircraft	Defense	\$2,000,000	Settlement, 11/19/1997
	Allegedly "overcharged the government to repair equipment used to manufacture aircraft under a military contract"	United States v McDonnell Douglas, Docket #91-CV-3139, US DC CD CA (Civil)	Senator Harkin and Representative DeFazio Press Release 06/07/00; Department of Justice (DOJ) Press Release 11/19/97; Taxpayers Against Fraud (TAF) Quarterly Review Volume 5 April 1996, Volume 12 January 1998
Boeing --McDonnell Douglas	Defense	\$2,000,000	Settlement, 12/1/1997
	"Procurement Fraud"	(Civil)	Senator Harkin and Representative

Boeing --McDonnell Douglas	Defense "Defective Pricing"	\$1,850,000 (Civil)	Settlement, 8/13/1998 Senator Harkin and Representative DeFazio Press Release 06/07/00
Boeing	Defense "Boeing repeatedly exported defense articles and defense services to Russia, Ukraine, and Norway without required approval from the Department of State."	\$10,000,000 (Civil)	Settlement, 9/26/1998 State Department Charging Letter 09/02/98; State Department Consent Agreement 09/26/98
Boeing	Defense Allegedly "produced defective aircraft and falsely certified parts and workmanship."	United States v Boeing, Docket #98- CV-1716, US DC WD WA (Civil)	Pending, 12/3/1998 Taxpayers Against Fraud Quarterly Review Volume 12 January 1998; Court Docket; National Transportation Safety Board Public Meeting 08/22-23/00; Confirmed by US Attorneys Office WD WA (Seattle) on 04/27/01
Boeing	Defense "Alleged that Boeing placed defective flight-critical transmission gears into CH-47D Chinook helicopters."	\$61,500,000 United States v Boeing, Docket #97-CV-410, US DC SD OH (Civil)	Settlement, 8/1/2000 Department of Defense (DOD) Inspector General Press Release 08/01/00- 08/15/00; Department of Justice (DOJ) Press Release 08/03/00; DOJ Press Release 05/01/97; Taxpayers Against Fraud (TAF) Quarterly Review Volume 14 April 2000, Volume 18 July 2000, Volume
Boeing	Defense "... allegations that Boeing had agreed to pay bribes to officials of the Bahamas government ... as a means of securing a contract ..."	Aviaco v Boeing Canada, Docket #98-CV-159655 CM; Aviaco v McDonnell Douglas, Docket #92-CV- 2401, US DC SD FL & Docket #92-CV-3739, US DC CD CA (Civil)	Pending, 10/1/2000 The Lawyers Weekly 10/06/00; Court Docket; Confirmed by the Superior Court of Justice Clerk's Office, Ontario, Canada on 04/19/01
Boeing	Defense	\$2,025,000	Settlement, 11/13/2000

	Allegedly "concealed fraud by a subcontractor."	United States v Boeing, Docket #00-CV-32, US DC CD CA (Civil)	Department of Justice (DOJ) Press Release 01/12/00; DOJ Press Release 11/9/2000; Taxpayers Against Fraud (TAF) Quarterly Review Volume 18 March 2000; Court Docket
Boeing	Defense "The Department of State charges that The Boeing Company violated the Arms Export Control Act and the International Traffic in Arms Regulations One hundred ten (110) violations are alleged."	\$4,200,000 (Administrative)	Fine, 4/7/2001 State Department Charging Letter 03/30/01; Consent Agreement 03/30/01; Confirmed by State Department Press Office on 04/18/01
Boeing --Boeing Satellite Systems	Defense "Settlement of the 123 charges against them [Boeing and Hughes Electronics] for violations of the Arms Export Control Act and the International Traffic in Arms Regulations."	\$18,000,000 (Administrative)	Settlement, 3/4/2003 Department of State Press Release 03/05/03; Department of State Charging Letter 12/26/02; Boeing Press Release 03/05/03
Boeing	Defense "The settlement resulted from false claims submitted by Boeing to the government for payment."	\$492,163 United States v Boeing, 98-CV-1842, US DC ED PA (Civil)	Settlement, 4/4/2003 United States Attorney's Office Eastern District of Pennsylvania Press Release 4/4/2003; Settlement Agreement
Boeing --McDonnell Douglas Helicopter Systems	Defense "... Boeing allegedly failed to provide [a safety system for the Apache helicopter] with the 28 volts required for proper operation."	\$2,500,000 Swenson v McDonnell Douglas Helicopter, Docket #98-CV-1476, US DC AZ (Civil)	Settlement, 5/16/2003 Department of Defense (DOD) Inspector General Press Release 06/21/00; Taxpayers Against Fraud (TAF) Quarterly Review Volume 19 July 2000; Court Docket
Boeing	Defense "Alleges that Boeing and its employees committed violations of Federal and Florida law resulting from their solicitation, acquisition, and use of Lockheed Martin proprietary information during the competition for launch contract awards under the U.S. Air Force's Evolved Expendable Launch Vehicle program."	Lockheed Martin v Boeing, Docket #03-CV-796, US DC MD FL (Civil)	Pending, 6/10/2003 Lockheed Martin Press Release 06/10/2003; Court Docket

Exhibit B

APPLICABILITY OF SPECIFIC STATUTES TO OTHER TRANSACTION AGREEMENTS

• • •

Department of Defense Other Transactions: An Analysis of Applicable Laws
A Project of the Ad Hoc Working Group on Other Transactions Section of
Public Contract Law, 2000, American Bar Association, from Table 1, p. 27

• • •

Item No.	Statute	Applicability of Statute to OTs
1.	Competition in Contracting Act, Pub L. No.98-369 (1984), as amended	CICA does not apply to OTs
2.	41 U.S.C. §§ 601 <i>et seq.</i> , the Contract Disputes Act, Pub. L. No. 95-563 (1987), as amended	CDA does not apply to OTs
3.	31 U.S.C. §§ 3551 <i>et seq.</i> , Procurement Protest System, Subtitle D of the Competition in Contracting Act, Pub. L. No. 98-369 (1984)	The protest system at GAO does not apply to protests over the award of OTs. However, the GAO will likely review the agency's use of OTs to determine whether the statutory requirements of 10 U.S.C. § 2371 and § 845 are met.
4.	10 U.S.C. § 2306, Kinds of Contracts	Section 2306 does not apply to OTs
5.	10 U.S.C. § 2313, Examination of records of contractor	Section 2313 does not apply to OTs
6.	10 U.S.C. § 2353, Contracts: acquisition, construction, or furnishing of test facilities and equipment [to R & D contractors]	Section 2353 does not apply to OTs
7.	10 U.S.C. § 2354, Contracts: indemnification provisions	Section 2354 does not apply to OTs
8.	10 U.S.C. § 2393, Prohibition against	Section 2393 does not apply to OTs

Item No.	Statute	Applicability of Statute to OTs
	doing business with certain offerors	
9.	10 U.S.C. § 2403, Major Weapons Systems: Contractor Guarantees	Section 2403 does not apply to OTs
10.	10 U.S.C. § 2408, Prohibition on persons convicted of defense contract related felonies and related criminal penalty as defense contractors	Section 2408 does not apply to OTs
11.	10 U.S.C. § 2409, Contractor employees: protection from reprisal for disclosure of certain information	Section 2409 does not apply to OTs
12.	31 U.S.C. § 1352, Limitation on the use appropriated funds to influence certain Federal contracting and financial Transactions	Section 1352 does not apply to OTs
13.	41 U.S.C. § 423, Procurement Integrity Act, § 27 of the Office of Procurement Policy Act	The Procurement Integrity Act does not apply to OTs
14.	41 U.S.C. §§ 701-707, Drug-Free Workplace Act of 1988	The Drug-Free Workplace Act does apply to OTs
15.	41 U.S.C. §§ 10a – 10d, Buy American Act	The Buy American Act does not apply to OTs
16.	35 U.S.C. §§ 200-212 (1980)(Bayh-Dole Act)	The Bayh-Dole Act does not apply to OTs
17.	10 U.S.C. § 2320 and § 2321, Technical data provisions applicable to DoD	These provisions do not apply to OTs
18.	10 U.S.C. § 2306a, Truth in Negotiations Act	TINA does not apply to OTs
19.	41 U.S.C. § 422, Cost Accounting Standards	Cost Accounting Standards do not apply to OTs
20.	10 U.S.C. § 2334, Cost Principles	Cost Principles do not apply to OTs

