

**TAXPAYERS CARRY
THE LOAD:
THE C-130J CARGO PLANE DOES NOT**

March 15, 2005

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INTRODUCTION

The Pentagon called for the cancellation of the U.S. Air Force's C-130J transport aircraft procurement contract in a December 23, 2004, internal memo signed by Deputy Secretary of Defense Paul Wolfowitz. (Appendix A) This move by the Pentagon to cut its losses on the overpriced, unneeded, and problem-plagued C-130J, would allow nearly \$5 billion in funding to be directed to other program areas, such as properly equipping the nation's fighting men and women.

Unfortunately, the C-130J supporters almost immediately began a disinformation campaign in response to the Wolfowitz memo. A group of U.S. Senators, motivated by parochial interests and those of a powerful defense contractor, (Appendix B) rushed off a letter to President Bush asking that he overrule the Secretary of Defense and put the money for the C-130J back in the 2006 fiscal year budget. (Appendix C) Desperate supporters of the C-130J have been claiming it will cost the taxpayers up to \$2 billion¹ to terminate the contract "at the convenience" of the government, when in fact, the cancellation cost ceiling specified in the contract is less than one quarter of that amount. (Appendix D) Lockheed Martin wants all the benefits of both commercial and traditional procurement with none of the risk. They want the benefits of commercial acquisition by keeping government auditors at arm's length, and the benefits of traditional contracting by coming hat-in-hand when the customer, in this case the government, walks away. Due to the deficiencies in the design and procurement of the aircraft, the government would be justified in cancelling the program for cause, avoiding paying any cancellation fee.

In their letter to the president, the Senators lumped the "J" model with the older tried-and-true versions of the C-130. The older models of the C-130 Hercules enjoy an excellent reputation as dependable workhorses, but the new "J" has instead become a legend in the acquisition community as an example of bad weapons development and procurement contracting.

These two aircraft, sharing the same name, could hardly be more different. The "J" model may look like its predecessor, but is actually a different aircraft – with 70 percent of its features being unique. In fact, the old C-130s and the newer C-130Js are so different "pilots cannot be qualified on both aircraft, which causes additional financial and personnel burden on units that must operate both aircraft."²

The Air Force has fueled the debate by temporarily grounding 30 of its older C-130 "E" models and restricting the flights of 60 other C-130s, claiming they had developed cracks near their wings.³ The fact that this development came at the same time the "J" model was being threatened with cancellation is highly suspect, reminiscent of an eleventh-hour claim last year that the Air Force's existing tanker fleet had serious corrosion problems as a ploy to lease 100 new tankers. That claim was

¹ *Inside the Air Force*, "Senior USAF Officer: C-130J Termination Costs Could Exceed \$2 Billion," March 14, 2005.

² *Audit Report, Acquisition: Contracting for and Performance of the C-130J Aircraft*, Department of Defense Office of Inspector General, Report No. D-2004-102, July 23, 2004, p. 10.

³ "Air Force Finds Cracks, Grounds C-130E," United Press International, February 11, 2005.

later refuted as an exaggeration in a Defense Science Board task force study that concluded the corrosion of the current tanker fleet was manageable and that the Air Force has a “robust” control program in place.⁴

The C-130J contract cancellation has even resulted in the aircraft’s manufacturer, Lockheed Martin, creating new restrictions on its employees’ communication with the Pentagon’s C-130J program office, following what it called “a recent flurry” of requests from the program office. (Appendix E) In a February 7, 2005, internal e-mail, Lockheed’s chief C-130J systems engineer, Michael A. Reed, suggested that future communications between Lockheed and the program office be limited to only those required by contract, and that “all recently requested non-contractual data” be removed from Lockheed’s computer system which communicates with the program office. “Until further notice, there will be but one channel for information requests on the C-130J program, and that will be by Contracts letter,” Reed wrote.

Now a high-stakes dogfight is shaping up between Defense Secretary Donald Rumsfeld and the Air Force and some Members of Congress. The facts are on Rumsfeld’s side: Since its inception in the mid-1990s, the C-130J transport aircraft program has proven itself a disaster for both the U.S. taxpayers and the military. The aircraft, a so-called modernized version of the legendary 1950s-era C-130 Hercules cargo and troop airlifter, was developed and purchased using a misguided and highly suspect “commercial” acquisition strategy that essentially doubled the cost of the aircraft and left government auditors powerless to do anything about it.

From a technical standpoint, too, the aircraft has a checkered history. None of the first group of 50 “J” models delivered between 1999 and 2003 have yet been declared fully ready for combat.⁵ A 2004 Rand study for the Air Force called the C-130J a “contractor-initiated” idea that was at first supposed to be a simple and routine upgrade, but in the end was far from simple or routine.⁶

In fact, the Department of Defense’s Office of Inspector General found that, rather than being available for combat, the C-130J should only be used in a “permissive,” non-hostile environment. “The evaluation did not include aircraft survivability equipment; therefore, the aircraft should only be employed in a permissive threat environment until aircraft survivability equipment testing is completed,” the report said. The Inspector General report said the DoD defines a permissive threat environment “as an operational environment in which the host country’s military and law enforcement agencies have control as well as the intent and capability to assist operations that a unit intends to conduct.”⁷

⁴ Summary of Aerial Refueling, Defense Science Board Task Force, May 2004. <http://www.pogo.org/m/cp/cp-dsbtaskforcereport-2004.pdf>

⁵ *Audit Report, Acquisition: Contracting for and Performance of the C-130J Aircraft*, Department of Defense Office of Inspector General, Report No. D-2004-102, July 23, 2004, p. i.

⁶ *Test and Evaluation Trends and Costs for Aircraft and Guided Weapons*, RAND Corporation, 2004, p. 38. http://www.rand.org/pubs/monographs/2004/RAND_MG109.pdf

⁷ *Audit Report, Acquisition: Contracting for and Performance of the C-130J Aircraft*, Department of Defense Office of Inspector General, Report No. D-2004-102, July 23, 2004, p11.

POGO's report supports the decision to cut the program. Attempts to reinstate funding for the C-130J program are nothing more than another scheme to keep on the table a plate of federal pork cooked up by a defense contractor and force-fed to the Pentagon by Congress.

CONGRESS AND LOCKHEED CREATE A NEED FOR THE C-130J

The C-130J was first introduced in the mid-1990s as an improvement to earlier C-130 models – not by the Pentagon, but by defense contractor Lockheed Martin Aeronautics Company.⁸ Until it faced the recent threat of program cancellation, the Air Force had never really expressed an overwhelming need for more, or upgraded, versions of the C-130 transport aircraft. A 1998 Government Accountability Office (GAO) report suggested that Congress was calling the shots when it came to buying new C-130s. “For the past 21 years, with the exception of five aircraft, Congress has directed the procurement of C-130s for the Air National Guard and Air Force Reserve units.”⁹

As of December 31, 2004, 180 “J” models had been ordered and 120 delivered worldwide to the U.S. and other countries’ air forces, including the U.K. Royal Air Force, Royal Australian Air Force, Italian Air Force, and the Royal Danish Air Force.¹⁰ Lockheed ordained the “J” model as its transport aircraft of the future by closing the production line for its predecessor, the C-130H model.¹¹

Now the Pentagon has a chance to stand up to Congressional pressure and save the taxpayers \$5 billion by cutting Air Force procurement of the “J” model. History would support such an action. In 1998, the GAO concluded that Congress was giving the Air Force more C-130s than it needed:

The Air Force has retired C-130s with service life remaining on the aircraft. Program officials told us that such retirements have generally been driven by congressional direction to buy more C-130s than the Air Force requested in its annual budget requests. Program officials told us that, accordingly, it was difficult to control the retirement of C-130 aircraft. They stated that, since retirement from the fleet had been based on congressionally directed acquisitions replacing existing C-130 aircraft, they were not retiring aircraft because the service life had expired.¹²

⁸ *Audit Report, Acquisition: Contracting for and Performance of the C-130J Aircraft*, Department of Defense Office of Inspector General, Report No. D-2004-102, July 23, 2004, pp. 1-2.

⁹ *Intratheater Airlift: Information on the Air Force's C-130 Aircraft*, Government Accountability Office, GAO/NSIAD-98-108, April 21, 1998, p. 6.

¹⁰ Discussion in Business Segments, Form 10-K, Lockheed Martin Corporation, February 28, 2005, p. 5.

¹¹ *Audit Report, Acquisition: Contracting for and Performance of the C-130J Aircraft*, Department of Defense Office of Inspector General, Report No. D-2004-102, July 23, 2004, p. i.

¹² *Intratheater Airlift: Information on the Air Force's C-130 Aircraft*, Government Accountability Office, GAO/NSIAD-98-108, April 21, 1998, p.8.

So even if the Air Force could justify a need for additional C-130 aircraft, any future needs could be filled by taking those older retired C-130 aircraft out of mothballs and putting them back into service, rather than buying the expensive and problem-plagued C-130Js. The Air Force could also do a Service Life Extension Program (SLEP) on the C-130E, C-130H, and possibly C-130F models, which involves adding new skin panels and other structures to extend the life of the aircraft. This will put people to work, continue C-130 E&H (possibly F) versions' serviceable life for several years and will save millions, possibly billions, of dollars. This will eliminate any argument that the C-130J is needed to replace older versions of the C-130 with wing cracking problems.

The 1998 GAO audit also suggested that the standard contracting process was turned upside down. "Additionally, during our review, some Air Force officials expressed concern that the normal requirements process was not followed in the recent J buys," the audit said. "They stated that requirement documents for the EC-130Js and WC-130Js were written after the Air Force had made a commitment to buy the aircraft."¹³ This is a highly unusual way of procuring weapons systems. Typically, each military service determines its weapons-systems needs first, writes a requirements document outlining precisely what it wants, and then seeks out defense contractors qualified to fill those requirements in an open-bid competition.

As recently as February 9, 2005, the Department of Defense's acting acquisition chief, Michael Wynne, made a speech that appeared to contradict the Air Force's current position that there is a compelling need for more C-130Js. Wynne told an investment conference in New York City that changing transportation requirements and capabilities prompted the department's decision to terminate the C-130J program, according to *Inside Defense*. Wynne noted that some studies are now suggesting that the U.S. military may not need to rely on transport aircraft like the C-130J to haul its equipment worldwide. New options for getting weapons and supplies to the battlefield include high-speed ships and increased reliance on prepositioned stocks, *Inside Defense* quoted Wynne as saying.¹⁴

COMMERCIAL PROCUREMENT FAILURE

At the heart of the C-130J debacle is the contracting scheme used to acquire it. A July 2004 Department of Defense Office of Inspector General (OIG) report was highly critical of the Air Force's decision to designate the C-130J a "commercial item." Declaring an item "commercial" is a contracting strategy that absolves the defense contractor of responsibility for providing detailed and important cost data, and restricts the government's ability to audit the contractor's books. The use of the commercial acquisition strategy, never before used to purchase a military aircraft, was so out of bounds that the OIG recommended that "civilian and military managers" involved in managing acquisition programs read its audit to learn the do's and don'ts of commercial acquisition. It told managers that the audit "discusses an unjustified decision to use a commercial item acquisition strategy and other problems that occurred because of poor management."

¹³ Ibid., p. 10.

¹⁴ *Inside Defense*, "Wynne: Changing Transportation Needs Triggered C-130J Cancellation," February 10, 2005.

The OIG flatly stated that the Air Force did not properly justify the use of a commercial acquisition strategy, did not properly manage the program, and did not provide the contractor with an incentive to deliver aircraft that worked properly. The audit also criticized the Office of the Secretary of Defense for not providing effective oversight of the program to correct C-130J deficiencies.

The OIG recommended that the Air Force immediately stop the system program office from “contracting for additional block upgrades until a contract-compliant aircraft is designed, developed, and delivered.” It also strongly encouraged the Air Force to modify any future contracts to employ a more traditional procurement method, increase the amount of money withheld from contractors when the government accepts “noncompliant aircraft,” and develop a schedule for fixing problems with the “J” models already in the fleet.

The report also stated: “The Air Force bought the C-130J as a commercial item needing minor modification, but in the 8 years since the Air Force began contracting for the C-130J, Lockheed Martin has been unable to design, develop, or produce a C-130J aircraft that meets contract specification.”¹⁵

The C-130J is the only historical example of a military aircraft being declared a “commercial item.” Its flawed history serves as a textbook case of the perils of employing a commercial acquisition strategy for acquiring a major military weapons system. Normally, a commercial acquisition designation is used to obtain any item that the public can purchase such as computers, office equipment, and automobiles. But in the case of the C-130J, Lockheed Martin was permitted to circumvent laws that protect the taxpayer, such as the Federal Acquisition Regulation, the Truth in Negotiations Act, and Cost Accounting Standards.

These laws require transparency in cost or pricing data so that government purchasers know what they are getting for the government’s money. The result has been a doubling of the per aircraft cost – the “H” model cost \$33.9 million when it went out of production in 1997, while the “J” model has an estimated price tag today of \$66.5 million. With oversight regulations waived, the cost of wiring harnesses on the C-130J increased by five times their original price after the aircraft was designated “commercial,” going from \$91 to \$453. The GAO offered this spare part price-hike as a real-world example of the difficulty involved in making the transition from pricing goods and services based on costs incurred to an ineffective commercial model in which factors other than cost are the principal means used to establish price.¹⁶

The trouble is no one, other than Lockheed Martin, seems to be really sure just how much the C-130J should rightfully cost – not even the government. For example, the Rand study noted that it could not do a cost analysis of the “J” model because, “According to the program office, contractor

¹⁵ *Audit Report, Acquisition: Contracting for and Performance of the C-130J Aircraft*, Department of Defense Office of Inspector General, Report No. D-2004-102, July 23, 2004, pp i-ii.

¹⁶ Statement for the Record, Henry L. Hinton, Jr., Assistant Comptroller General, National Security and International Affairs Division, before the House Committee on Government Reform, Subcommittee on Government Management, Information, and Technology, *Federal Acquisition: Trends, Reforms, and Challenges*, General Accounting Office, GAO/T-OCG-00-7, March 16, 2000, p. 10.

T&E [Test and Evaluation] cost data were not available to them because of the nature of the contractor-initiated development effort.”¹⁷

Such commercial agreements also restrict the government’s powers to “routinely” inspect and audit a contractor’s activities. For instance, the 2003 C-130J contract with Lockheed allows the government to inspect and test all supplies, but says that “the Government agrees, consistent with the commercial nature of the C-130J program that such inspections should not be performed on a routine basis, but only where the Government determines in its judgment that inspections are required.”

One Department of Defense auditor-turned-whistleblower who worked at the C-130J plant in Marietta, Georgia, spent months researching the cost of the “J” model, but was frustrated by his attempts to determine an actual, and fair, price for the aircraft. The auditor, Ken Pedeleose, said in a report to Congress that in June 1995 when the government designated the C-130J a “Regulatory Pilot Program,” it “lost all insight into the C-130 operations.” (Appendix F)

In technical reviews for Italy and Norway in late 1996 to early 1997, Pedeleose, an employee of the Defense Contract Management Agency (DCMA), essentially concluded that the prices Lockheed was charging the two governments could not be justified.

“In short, the LMAC (Lockheed Martin) proposed price could not be substantiated based on historical factors and the limited information LMAC provided,” Pedeleose wrote. “Thus the final DCMA evaluation was forced to question the excessive cost and submit the report to the Italian Government for use in negotiations.”

That caused negotiations to stall, and afterward Lockheed complained that DCMA was “interfering” with the company’s negotiations with Italy. After a similar experience with a cost analysis for Norway, Pedeleose concluded that the two projects “verified that LMAC could not support C-130J cost in a commercial marketplace.” He also concluded: “The attitude of LMAC in negotiations and the strenuous nature to which they protect their ‘proprietary’ data for an unjustifiable price is a contributing factor to the poor sales of the C-130J.” Norway never did purchase any C-130Js.

Pedeleose said the history of the C-130J has been one of a “continued trend of excluding technical and financial experts from the process thus allowing further unbridled cost increases, among other issues.”

This became clear by 1998 when Lockheed and the Air Force agreed to keep financial experts in the dark about the program’s costs. For example, in an October 21, 1998, memo about an impending C-130J program review meeting, Lockheed vice president Gene Elmore told an Air Force Colonel on the acquisition team that the discussions could not include any government auditors.

“As I am sure you understand, we are not trying to hide anything, merely attempting to preserve the commerciality of the program,” Elmore wrote. The letter also prohibited Air Force acquisition team members from sharing any cost data with auditors. (Appendix G)

¹⁷ *Test and Evaluation Trends and Costs for Aircraft and Guided Weapons*, RAND Corporation, 2004, p. 38. http://www.rand.org/pubs/monographs/2004/RAND_MG109.pdf

One Senator who questioned the “commercial item” designation for the C-130J was Tom Harkin (D-IA). In 1997, Harkin fired off a letter of protest to then-Secretary of Defense William Cohen:

How can Atlas rockets and C-130J aircraft be considered ‘commercial’ items? Obviously, these are not items found in the commercial sector. More importantly, they are not items that are priced due to the forces of supply and demand. Items bought solely or primarily by the federal government should not fall under the ‘commercial’ definition. (Appendix H)

Real commercial items are acquired where a real market with competition exists, giving an assurance of fair and reasonable prices. For non-commercial items, contractors are required to submit cost or pricing data for negotiated procurement. However, in the case of the C-130J, there was no competition to set the price.

One of the Air Force’s reasons for exempting Lockheed from providing cost or pricing data on the C-130J was because Lockheed said the aircraft would be available in the commercial marketplace by the time of delivery. The commercial process is designed to speed up the acquisition process. Ironically, the C-130J’s commercial designation actually delayed the process. The reason: Lockheed had to justify the aircraft’s commercial item status by obtaining a Federal Aviation Administration (FAA) certification to sell it on the commercial market. But technical problems with the aircraft delayed the certification, which was not obtained until September 1998. In 1995, the Air Force contracted for two C-130Js to be delivered in 1997. However, they were not delivered until 1999 – two years behind schedule.¹⁸

The thinly-veiled attempt to justify the C-130J as a commercial item ended up taking a toll on Lockheed’s balance sheet. In June 1999, Lockheed announced it was reducing its earnings outlook for 1999 and 2000, in part due to the cost growth in the C-130J’s development and slower-than-anticipated sales of the aircraft. The company claimed its first profit on the C-130J program in 2004.¹⁹

The FAA certification process and plan to sell the aircraft commercially turned out to be a smokescreen to get the “commercial item” designation from the Air Force. Lockheed has not sold a single C-130J commercially and, in fact, has allowed the FAA commercial certification to expire. (Appendix I) Yet, Lockheed continues to benefit from selling the aircraft as a commercial item to the government, while government auditors still have no capacity to review cost or pricing data.

FAILING PERFORMANCE

The C-130J’s history of problems has kept it from getting a passing grade from the Pentagon’s independent weapons tester, the Director of Operational Test and Evaluation (DOT&E). In the first

¹⁸ *Audit Report, Acquisition: Contracting for and Performance of the C-130J Aircraft*, Department of Defense Office of Inspector General, Report No. D-2004-102, July 23, 2004, p. 6.

¹⁹ Discussion in Business Segments, Form 10-K, Lockheed Martin Corporation, February 28, 2005, p. 5.

phase of testing, DOT&E declared the C-130J as not operationally “effective” or “suitable,” and has yet to change that designation.²⁰ Not one C-130J was delivered to the Air Force meeting program requirements and, eight years into the program, the aircraft still has not been fully tested by DOT&E. When the Department of Defense Office of Inspector General graded the C-130J’s performance, the report card was clearly less than satisfactory. In uncharacteristically stinging language, the OIG’s July 2004 audit flatly concluded that Lockheed was not meeting its contract specifications and, therefore, that the C-130J was unable to perform its mission of transporting and dropping troops and equipment in combat zones.

Specifically, the OIG report said the Air Force unwisely paid 99 percent of the \$2.6 billion contract price for the first 50 defective aircraft, leaving the contractor little incentive to correct the problems on its own dime. “As a result, the government fielded C-130J aircraft that cannot perform their intended mission, which forces the users to incur additional operations and maintenance costs to operate and maintain older C-130 mission-capable aircraft because the C-130J aircraft can be used only for training,” the audit said.

The OIG said the transport aircraft has been unable to perform such basic and critical missions that include night vision goggle operations, combat search and rescue, visual formation, global air traffic management, and air-dropping paratroopers and containers. In addition, the hurricane hunter versions of the C-130J have experienced radar problems and the aircraft’s six-blade propellers have become dangerously pitted in bad weather.

The Inspector General audit also noted:

- The mission capable rates for the C-130Js are lower than the rates for the older versions, even though the “J” model has not yet been released to perform all C-130 missions. For the released missions the C-130J achieved a 50.4% rating in 2002 and a 62.4% rating in 2003.
- Although the C-130J was billed as being cheaper to maintain than earlier C-130 models, it had a high rate of “built-in-test false detections.” Such false detections mean that unnecessary maintenance actions are being performed too often, increasing the number of needed spare parts and maintenance hours.
- The immaturity of the “J” model’s design increases “aircraft downtime” and “creates a strain on personnel. The high number of workarounds has caused user personnel frustration and additional maintenance hours and costs.”²¹

Lockheed and the Air Force often try to deflect the critics of the C-130J by pointing to the experience of several other countries who purchased C-130Js prior to the U.S. contract. But nearly all

²⁰ *Annual Report FY2004, Department of Defense, Director Operational Test and Evaluation, Air Force Programs, C-130J Airlift Aircraft, January 2005, p. 251.*
<http://www.pogo.org/m/dp/dp-2004-C130J.pdf>

²¹ *Audit Report, Acquisition: Contracting for and Performance of the C-130J Aircraft, Department of Defense Office of Inspector General, Report No. D-2004-102, July 23, 2004, p. 11.*

of those foreign military buyers have had their share of problems with the aircraft: the British had difficulties dropping paratroopers; the Italians had windshield and horizontal stabilizer cracks; the Australians complained that the powerful engines were creating a dangerous vibration; and the Norwegians unsuccessfully jockeyed behind the scenes to determine if the price they were paying for the aircraft was fair.

As for the U.S. Air Force, all 50 of the first lot of C-130J aircraft delivered to and accepted by the Air Force were deficient in one way or another. Those deficiencies have ranged from propellers that peeled to improperly-functioning radar, and some continue even today. Congressional sources say that as of January 2005, only 11 of 33 major Category One open deficiency reports identified by the OIG have been corrected. Category One deficiencies are those that could cause major loss of equipment or systems, or that could directly restrict combat or operational readiness if not corrected.

To date, only two of the 50 C-130Js have been permitted to fly “limited” missions in Iraq, and are said to be accompanied by an unusually large maintenance and support contingent and extra spare parts – designed to inflate the aircraft’s reliability rate. The remaining 48 “J” models have been restricted to training missions.²²

Despite claims that problems identified in the 2004 OIG audit are fixed, the annual DOT&E report released in January 2005 noted that problems remain. “Major issues confronting the C-130J program include funding of logistics support and training systems; hardware, software, and technical order deficiencies; manufacturing quality; sub-system reliability; failure to meet required measures of system effectiveness and suitability; and resolution of documented deficiencies,” the report said. “A program for the correction of deficiencies is being worked.”

The report also noted that “the airdrop mission cannot be evaluated until deficiency corrections are implemented and the developmental and operational tests are completed as planned in FY06.”²³

Clearly, the taxpayers and fighting men and women have been shortchanged with the C-130J program.

HOLDING THE CONTRACTOR ACCOUNTABLE

C-130J supporters have claimed it would cost the Air Force \$2 billion to terminate the contract. That is contrary to the actual contract language, even if the contract is cancelled “at the convenience” of the government. The contract has a ceiling price that the government must pay if it decides to cancel the contract under those terms: \$439.7 million if it cancels by November 2005 and \$383.3 million if it cancels by November 2006. There are no contractual obligations for the government to pay any other termination costs, something the Air Force has confirmed privately to Congress.

²² Ibid., p. I.

²³ *Annual Report FY2004, Department of Defense, Director Operational Test and Evaluation*, Air Force Programs, C-130J Airlift Aircraft, January 2005, p. 252.
<http://www.pogo.org/m/dp/dp-2004-C130J.pdf>

Lockheed Martin is trying have it both ways. The only benefits of commercial purchases to the government are that it is not held responsible for ancillary costs associated with selling specifically to the government. Given that this is a “commercial item,” special manufacturing equipment to produce the C-130J should not have been required, nor should a government contracting officer approve such a purchase. With “just-in-time” materials purchasing, Lockheed Martin and its subcontractors should not have purchased materials to build planes in the out-years. Normally, long-lead should not exceed one year’s worth of material. The termination is not scheduled until the end of 2006.

However, no cancellation fees would be paid by the government if the program is cancelled “for cause” rather than “convenience of the government.” Because all of the first 50 C-130Js delivered to the Air Force had serious deficiencies, the government should cancel the contract for new transport aircraft for cause. Lockheed Martin failed to manufacture an aircraft that meets contract specifications, even after eight years of development and testing. The Federal Acquisition Regulation (FAR) states that a contract may be cancelled for cause “in the event of any default by the Contractor, or if the Contractor fails to comply with any contract terms and conditions, or fails to provide the Government, upon request, with adequate assurances of future performance.”²⁴

The FAR also says in the event of termination for cause “the Government shall not be liable to the Contractor for any amount for supplies or services not accepted, and the Contractor shall be liable to the Government for any and all rights and remedies provided by law.”

If the government does cancel the C-130J contract for cause, the Pentagon needs to learn from past mistakes. History has shown that contractors fight vigorously for every dime, even if its weapons system is proven to be substandard.

The Pentagon has cancelled contracts to develop major weapons systems “for cause” on at least two prior occasions. The first such contract termination was in 1985 when the Army procurement contract office notified the Army’s division air defense gun (DIVAD) contractor, Ford Aerospace & Communications Corp., that the performance on the anti-aircraft system was “totally unacceptable.” Unfortunately for the government, the decision to cancel the DIVAD by then-Secretary of Defense Caspar Weinberger was made two years after the so-called Sergeant York Gun went into production. It ended up costing the taxpayers \$1.4 billion.²⁵

The second major Pentagon weapon system to be cancelled for cause came in 1991, when then-Secretary of Defense Richard Cheney canceled a contract with McDonnell Douglas (now owned by Boeing Company) and General Dynamics to build the Navy’s A-12 Avenger medium attack aircraft, a program riddled with huge cost overruns and schedule delays. Cheney’s decision was based on the fact that the contractors could not complete the work on schedule, nor could they meet the contract requirements. At the time of termination, nearly \$3 billion had been spent on the A-12 project, with

²⁴Federal Acquisition Regulation, Part 52, Solicitation Provisions and Contract Clauses, 52.212-4 – Contract Terms and Conditions – Commercial items, (l).

²⁵ *Orange County Register*, “Ford, Defense Department Settle Over Sgt. York,” February 23, 1989.

nearly \$2.7 billion of that amount already paid to the contractors. The Navy demanded that the contractors pay back the government \$1.35 billion.²⁶

The contract cancellation ended up in the federal courts in June 1991, when the contractors filed a lawsuit against the Navy to recover cancellation costs and damages. A federal judge ruled in 1995 that the A-12 Avenger contract was cancelled at the convenience of the government, and in a final judgement in 1998, awarded the contractors \$1.2 billion plus interest. In 2001, a three-judge appeals court panel ruled in favor of the government's decision to cancel the contract with cause. A subsequent appellate court ruling sent the case back to the trial court. Hearings were conducted in June of last year, and a decision on the case is pending.²⁷

Given this history, the Pentagon should learn from past mistakes and ensure it terminates the C-130J program without any excessive cost to taxpayers.

RECOMMENDATIONS

1. Terminate the C-130J transport aircraft program for cause.
2. Authorize an independent study to determine future C-130 requirements.
3. Study the possibility of bringing older C-130 models that were placed into early retirement back into service to replace aircraft taken out of service.

²⁶ Testimony of Neal P. Curtain, Director, Planning and Reporting, National Security and International Affairs Division, Government Accountability Office, before the House Subcommittee on Oversight and Investigations, Committee on Energy and Commerce, October 3, 1991. <http://archive.gao.gov/t2pbat7/144968.pdf>

²⁷ Discussion of legal proceedings, Form 10-K, General Dynamics, March 4, 2005.