

October 5, 2022

The Honorable Bill LaPlante
Under Secretary of Defense for Acquisition and Sustainment
U.S. Department of Defense
1000 Defense Pentagon
Washington, DC 20301-1000

Dear Secretary LaPlante:

I write to express concerns and ask for further clarification regarding reports that the Department of Defense (DoD) plans to implement an industry-written proposal to increase defense contract prices without sufficient safeguards in place to prevent industry profiteering and ensure that the increased costs are appropriate and necessary.¹

I recognize that the pandemic has created some supply chain and financial challenges for defense contractors. But as you noted in your own remarks, “during COVID, one of the best places to be was to be have a contract with the U.S. government. It’s better than being a hotel or being a restaurant or being an airline. Particularly in national security, because of the imperative of what we do, we made sure we tried our best to make [companies] whole.”²

The simple fact of the matter is that DoD contractors – like all contractors – agreed to provide good and services to DoD for the contractual rate. None of these companies offer, nor does DoD request, refunds when a program comes in under budget. These are private sector entities that competed for and voluntarily chose to engage in these agreements – and they should not be bailed out with corporate welfare simply because their profits are lower than anticipated. But I fear that this is exactly what is happening, and that well-intentioned DoD policies to support vulnerable suppliers will instead result in taxpayers underwriting defense contractors’ executives’ lavish compensation packages and pay for stock buybacks and paying out cash dividends.

¹ Defense News, “Defense industry to launch inflation relief push in Congress,” Joe Gould, September 1, 2022. <https://www.defensenews.com/pentagon/2022/09/01/defense-industry-to-launch-inflation-relief-push-in-congress/>; Inside Defense, “LaPlante seeking new policies to grant defense contractors inflation relief,” Tony Bertuca, September 7, 2022. <https://insidedefense.com/daily-news/laplante-seeking-new-policies-grant-defense-contractors-inflation-relief/>.

² Federal News Network, “Pentagon planning new guidance to help contractors squeezed by inflation,” Jared Serbu, September 8, 2022. <https://federalnewsnetwork.com/defense-news/2022/09/pentagon-planning-new-guidance-to-help-contractors-squeezed-by-inflation/>.

We have ample evidence of these fiscal risks. For example, at the beginning of the pandemic DoD adjusted progress payment rates.³ DoD uses these payments as a method of contract financing for work that is in progress but not yet completed and for costs associated for work in progress,⁴ and in March 2020 increased the progress payment rate to 90% from 80%.⁵ I wrote to your predecessor raising my concerns that DoD’s change would lead to waste, including leveraging those funds to enrich stockholders or other methods to enrich upper management.⁶ DoD assured me those funds could not be diverted to share buybacks, dividends, or executive salaries.⁷ But in spite of those assurances, it appears that my concerns were prescient. The Government Accountability Office (GAO) conducted a review of the effect of the increase in progress payment rates and found that, “[m]ost of these funds were provided to large businesses. For DCMA administered contracts, approximately \$40.5 billion of the \$42.9 billion in progress payments—or 94 percent—went to large businesses, with the remaining going to small businesses. Similarly, on shipbuilding contracts, nearly all of the \$12.2 billion in progress payments went to large contractors.”⁸ In that same report, the GAO found DoD “lacked meaningful visibility into the extent to which the increased funds reached all the businesses that would benefit from them.”⁹

To date, \$6.2 billion of \$8 billion disbursed through progress payments has gone to Lockheed Martin, Boeing, Raytheon, Northrop Grumman, and General Dynamics.¹⁰ In 2019, the last year before DoD increased the rate of progress payments, these companies spent \$2.3 billion on stock

³ Federal News Network, “Coronavirus is hitting small defense companies, but there may be a silver lining,” Scott Maucione, April 28, 2020. <https://federalnewsnetwork.com/defense-main/2020/04/coronavirus-is-hitting-small-defense-companies-but-there-may-be-a-silver-lining/>.

⁴ U.S. Department of Defense, “Progress Payments Based on Costs,” https://www.acq.osd.mil/dpap/dars/dfars/html/current/232_5.htm.

⁵ Statement of Lt. Col. Mike Andrews, Department of Defense Spokesperson, “Partnering with the U.S. Defense Industrial Base to Combat COVID-19,” March 22, 2020. <https://www.defense.gov/News/Releases/Release/Article/2121122/partnering-with-the-us-defense-industrial-base-to-combat-covid-19/>

⁶ Letter from Senator Warren to Under Secretary of Defense for Acquisition and Sustainment Ellen Lord, April 30, 2020, <https://www.warren.senate.gov/imo/media/doc/2020.04.30%20Letter%20to%20DoD%20re%20Deviation%20in%20Contractor%20Progress%20Payments%20due%20to%20COVID-19.pdf>.

⁷ Letter from Under Secretary of Defense for Acquisition and Sustainment Ellen Lord to Senator Elizabeth Warren, May 15, 2020. https://www.warren.senate.gov/imo/media/doc/US%20Lord%20response%20to%20Warren%20LTR%20Progress%20Payment%20Due%20to%20COVID-19_with%20Enclosure%2005152020.pdf.

⁸ Government Accountability Office, *Defense Contracting: More Insight into Use of Financing Payments Could Benefit DOD in Future Emergencies*, p. 9, <https://www.gao.gov/assets/720/719090.pdf>.

⁹ Government Accountability Office, *Defense Contracting: More Insight into Use of Financing Payments Could Benefit DOD in Future Emergencies*, p. 10, <https://www.gao.gov/assets/720/719090.pdf>.

¹⁰ Bloomberg, “Pentagon’s Covid Speed-Up of Payments Persists as Pandemic Eases,” Anthony Capaccio, September 26, 2022, <https://www.bloomberg.com/news/articles/2022-09-26/pentagon-s-covid-speed-up-of-payments-persists-as-pandemic-eases>.

buybacks.¹¹ In 2021, after DoD spent \$55 billion on progress payments, those same companies spent \$15.6 billion on share buybacks, “the most in any year so far.”¹²

To prevent profiteering and misuse of taxpayer funds, the Senate version of the fiscal year 2023 National Defense Authorization Act includes a provision from my *Stop Price Gouging the Military Act* to create a pilot program to tie progress payments to specific goals, including meeting program schedules and milestones, timely responses to requests to provide certified cost or pricing data, and providing subcontracting opportunities for the blind and disabled.¹³ The purpose of this pilot is to create more accountability for contract performance by rewarding those companies who meet specific goals and objectives while providing consequences for those companies that fail to meet those same goals and objectives. Instead, you appear to be considering the opposite approach: providing massive, unjustified taxpayer bailouts to giant defense contractors with little justification or rationale.

In 2010 then-Under Secretary of Defense for Acquisition, Technology and Logistics Ashton Carter published his “Better Buying Power” guidance.¹⁴ Included in the guidance was a directive to utilize more firm target fixed-price incentive contracts, where both the department and defense contractors would share in both the risk and reward of contract cost performance.¹⁵ Defense contractors rejected this approach, instead insisting on performing under firm fixed price contracts, so they can reap the full benefit of unintended windfall profits that result from overstated contract pricing estimates. But now they are unwilling to accept the risks of this approach, and are instead pushing for a massive taxpayer bailout.

I particularly urge DOD to be circumspect about the industry’s claims about the impact of inflation given their second quarter profits, which show operating incomes that increased over the last quarter and average 11.7%, suggesting there was little or no adverse impact due to

¹¹ 2019 and 2020 data for Northrop Grumman, Lockheed Martin, Raytheon, and General Dynamics obtained via ycharts.com and on file with Senator Warren’s office. L3Harris, *2019 Annual Report*, p. 33, <https://www.l3harris.com/sites/default/files/2020-09/l3harris-2019-annual-report.pdf>; L3Harris, *2020 Annual Report*, p. 32, https://www.l3harris.com/sites/default/files/2021-03/L3Harris_2020_AnnualReport.pdf.

¹² Senator Elizabeth Warren, “After Inquiry from Warren, Department of Defense Says Big Defense Contractors Cannot Divert Increased Progress Payments During COVID-19 to Share Buybacks, Dividends, or Executive Salaries,” July 15, 2020, <https://www.warren.senate.gov/newsroom/press-releases/after-inquiry-from-warren-department-of-defense-says-big-defense-contractors-cannot-divert-increased-progress-payments-during-covid-19-to-share-buybacks-dividends-or-executive-salaries>; Government Accountability Office, *Defense Contracting: More Insight into Use of Financing Payments Could Benefit DOD in Future Emergencies*, p. 8, <https://www.gao.gov/assets/720/719090.pdf>; Bloomberg, “Pentagon Weighs Ending Speedy Payments to Contractors Started for the Pandemic,” Anthony Capaccio, March 9, 2022, <https://www.bloomberg.com/news/articles/2022-03-09/pentagon-weighs-ending-speedy-payments-started-for-the-pandemic>.

¹³ Section 827, S. 4543, the James M. Inhofe National Defense Authorization Act for Fiscal Year 2023. https://www.armed-services.senate.gov/imo/media/doc/fy23_ndaa_bill_text2.pdf.

¹⁴ Office of the Under Secretary of Defense for Acquisition, Technology and Logistics, “Better Buying Power: Guidance for Obtaining Greater Efficiency and Productivity in Defense Spending,” September 14, 2010. https://www.acq.osd.mil/fo/docs/USD_ATL_Guidance_Memo_September_14_2010_FINAL.PDF.

¹⁵ Office of the Under Secretary of Defense for Acquisition, Technology and Logistics, “Better Buying Power: Guidance for Obtaining Greater Efficiency and Productivity in Defense Spending,” September 14, 2010, p. 6. https://www.acq.osd.mil/fo/docs/USD_ATL_Guidance_Memo_September_14_2010_FINAL.PDF.

inflation.¹⁶ Lockheed Martin, Northrop Grumman, Raytheon, General Dynamics, and L3Harris have indicated on recent earnings calls that they intend to buy back stock or pay cash dividends amounting to over \$20 billion in 2022.¹⁷

As you have noted, financial decisions must be determined by data.¹⁸ Your May guidance to contracting officers made clear that it is incumbent on contractors, not the contracting officer, to ask for and justify financial relief.¹⁹ And despite defense industry trade associations' claims of catastrophic cost impacts, *Defense News* reported that "officials from several of the armed services" said requests for economic adjustments on existing contracts "said it's been a trickle at best."²⁰ Your revised guidance issued on September 9, 2022 appropriately states that:

For extraordinary circumstances where contractors have sought or may seek an upward adjustment to the price of an existing firm-fixed-price contract to account for current economic conditions, each of the Secretaries of Defense, Army, Navy and Air Force has authority under Public Law 85-804, as implemented by Part 50 of the Federal Acquisition Regulation (FAR) and the Defense FAR Supplement (DFARS), to afford Extraordinary Contractual Relief. While the law and regulation have established stringent criteria, the Department will consider contractor requests to employ this authority, subject, of course, to available funding.²¹

Any companies that request price adjustments must meet the stringent criteria established under Public Law 85-804 and should be required to provide certified cost or pricing data to contracting officers to justify any requested adjustment. Without this information, including certified cost or pricing data, DoD cannot protect taxpayers from industry profiteering.

Given my concerns about the defense industry push for more taxpayer handouts, I ask that you please provide, no later than October 21 responses to the following questions:

1. What data and analysis has DoD received from the National Defense Industrial Association, Aerospace Industries Association, and the Professional Services Council to support increasing contract prices due to inflation? Please provide copies.

¹⁶ Data for Northrop Grumman, Lockheed Martin, Raytheon, L3Harris, and General Dynamics obtained via quarterly earnings calls presentations and press releases on file with Senator Warren's office.

¹⁷ Jim McAleese, "Contractor 2Q Results Call Surprises," August 28, 2022.

¹⁸ Federal News Network, "Pentagon planning new guidance to help contractors squeezed by inflation," Jared Serbu, September 8, 2022. <https://federalnewsnetwork.com/defense-news/2022/09/pentagon-planning-new-guidance-to-help-contractors-squeezed-by-inflation/>.

¹⁹ Office of the Under Secretary of Defense for Acquisition and Sustainment, "Guidance on Inflation and Economic Price Adjustments," May 2022, p. 1. <https://www.acq.osd.mil/dpap/policy/policyvault/USA000999-22-DPC.pdf>.

²⁰ Defense News, "Defense industry to launch inflation relief push in Congress," Joe Gould, September 1, 2022. <https://www.defensenews.com/pentagon/2022/09/01/defense-industry-to-launch-inflation-relief-push-in-congress/>.

²¹ Office of the Under Secretary of Defense for Acquisition and Sustainment, "Managing the Effects of Inflation with Existing Contracts," September 9, 2022, <https://www.acq.osd.mil/dpap/policy/policyvault/USA001773-22-DPC.pdf>.

2. If DoD enacts a policy to increase contract prices due to inflation, how will DoD ensure that any increased payments are not used for buybacks, dividends, or bonuses or other compensation for top company executives?
3. If DoD enacts a policy to increase contract prices due to inflation, what metrics will DoD use to determine whether this policy change achieved DoD's policy objectives?
4. If DoD enacts a policy to increased contract prices due to inflation, what role will the Defense Contract Audit Agency and the Defense Contract Management Agency have in overseeing any inflation-related contract adjustments?
5. I am not aware of any study that predated DoD's decision to increase the progress payment rate, what data was utilized by the Department to determine an increase in progress payment rates from 80% to 90% was justified?

There are too many instances where major defense companies made tens of millions, and my office has been made aware of instances of hundreds of millions of dollars, in excess profit on individual firm fixed price contracts.²² I have not seen, however, any instances where industry associations suggested those excess profits be returned to the warfighter and taxpayers. I urge you to make sure DoD's future policies don't further exacerbate this kind of price gouging.

Sincerely,



Elizabeth Warren
United States Senator

²² KGUN9, "Tucson's biggest private employer facing federal investigation on government contracts: Pricing at Issue," Craig Smith, February 14, 2022, <https://www.kgun9.com/news/local-news/tucsons-biggest-private-employer-facing-federal-investigation-for-overpricing-government-contracts>.