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HEARING TO RECEIVE TESTIMONY ON THE DEPARTMENT OF DEFENSE INSPECTOR GENERAL'S MANAGEMENT ACCOUNTABILITY REVIEW OF THE BOEING KC-767A TANKER PROGRAM

*Oral Testimony of the Honorable Joseph E. Schmitz, Inspector General of the
Department of Defense before the Senate Committee on Armed Services, Washington,
DC, Tuesday, June 7, 2005.*

Thank you Mr. Chairman, Senator Levin, Senator McCain, Senator Collins and
Senator Thune:

I appreciate the opportunity to appear this morning and to answer your
questions regarding our recent "Management Accountability Review of the KC-767A
Tanker Program." As the publicly releasable version of the report has already been
submitted and speaks for itself, I would ask that it be admitted as part of the Record.
This morning I would like to introduce the Report's primary author, Deputy IG
Mr. Thomas Gimble, and very briefly review the Report's genesis, its scope and
methodology, and its bottom-line results. Of course, Mr. Gimble and I are prepared
to answer your questions.

On December 2, 2003, Mr. Chairman, you sent a letter to the Deputy Secretary
of Defense in which you suggested that I conduct an independent assessment that
would "examine the actions of all members of the Department of Defense and the
Department of the Air Force, both military and civilian, top to bottom, who
participated in structuring and negotiating the proposed tanker lease contract" for the
KC-767A Tanker Program.

Subsequently, on November 19, 2004, you and two other Members of this
Committee, Senators Levin and McCain, sent another letter, this time addressed to the
Secretary of Defense, reiterating that I should conduct "an assessment of
accountability" along the same lines of your prior letter, and requesting that my
assessment determine "what happened, who was accountable, and what actions must
be taken to prevent this situation from happening again."

To accomplish this objective, our independent review team analyzed selected e-mails and memoranda from the Department of Defense, the Air Force, and the Boeing Company, and interviewed 88 individuals from the Departments of Defense and Air Force who had been involved in the Boeing KC-767A Tanker Program – to determine what happened and who was accountable during the structuring and negotiating of the proposed lease contract for the Boeing KC-767A Tanker Program.

Our review team did not interview White House officials, Members of Congress, or officials of the Boeing Company because the objective of the review focused on the accountability of members of the Office of the Secretary of Defense and of the Air Force who were involved in the Boeing KC-767A Tanker Program.

What Happened?

Although Boeing had submitted a proposal in February 2001 to the Chief of Staff of the Air Force to convert 36 Boeing 767 commercial aircraft into tanker aircraft, it was not until after September 11, 2001, that Air Force officials began meeting with Boeing Company executives to enter into an agreement to lease 100 Boeing KC-767A tanker aircraft. The proposed lease agreement generally had support of White House officials, Members of Congress, senior officials of both the Department of Defense and the Air Force, and the Boeing Company. At that time, that is, before and immediately after September 11, 2001, the Air Force had neither identified nor funded an urgent requirement for the replacement of its existing fleet of tankers.

The Department of Defense Appropriations Act for FY 2002, enacted January 10, 2002, included Section 8159, titled “Multi-Year Aircraft Lease Pilot Program,” which authorized the Air Force to make payments on a multi-year pilot program “to lease not more than a total of 100 Boeing 767 aircraft” and provided that the “term of any individual lease agreement . . . shall not exceed 10 years.” Without conducting an Analysis of Alternatives, the Air Force used the provisions of Section 8159 to justify an informal acquisition strategy, the focus and goal of which was expeditiously to lease 100 KC-767A tanker aircraft from Boeing through a business trust.

By not following established acquisition procedures contained in DoD Directives, the DoD and Air force officials identified in our report neither applied best business practices nor adhered to prudent acquisition procedures, and failed to comply with five statutory provisions relating to: commercial items; testing [two statutes]; cost-plus-a-percentage-of-cost system of contracting; and leases to satisfy warfighter needs.

Who Was Accountable?

Our report identifies the DoD and Air Force officials who were responsible for failing to ensure the prescribed acquisition rules and procedures were properly followed. In summary, a number of senior DoD and Air Force officials acted as if Section 8159 of the FY2002 Appropriations Act had waived various legal requirements -- statutory checks and balances -- that it had not. Moreover, as our executive summary concludes, "The system of management internal controls was either not in place or not effective because the existing acquisitions procedures were not followed in the proposed lease of the Boeing KC767A tanker aircraft."

What Actions Must be Taken to Prevent This Situation from Happening Again?

- The Department must change the cultural environment in its acquisition community to ensure that the proper internal control environment is reestablished and followed for major weapon-system acquisitions.
- The Secretary of Defense should reemphasize the need to conduct an Analysis of Alternatives for all major systems before major milestone decision points.
- DoD 5000 series guidance should emphasize that leasing is merely a method for financing the acquisition of a program, and that leased programs should be treated the same as any other acquisition programs of like cost.
- Finally, the DoD 5000 series guidance should require, at a minimum, that the decision to enter into a contract to lease a major system must be subject to the results of a Defense Acquisition Board or a System Acquisition Review Council review, as applicable.

This concludes my oral statement. Mr. Gimble and I would be happy to answer any questions you may have.