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Report No. D-2012-091 May 24, 2012

Inspector General

United States Department of Defense

The Army Needs to Recoup Funds Expended on Property Damaged in an Accident at a Development Subcontractor's Facility

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Acronyms and Abbreviations

AMS	Airship Management Services
DCMA	Defense Contract Management Agency
DoD OIG	Department of Defense Office of Inspector General
FAR	Federal Acquisition Regulation
JLENS	Joint Land Attack Cruise Missile Defense Elevated Netted Sensor System
SMDC-JA	U.S. Army Space and Missile Defense Command-Judge Advocate
TCOM LP	Tethered Communications Limited Partnership

INSPECTOR GENERAL
DEPARTMENT OF DEFENSE
4800 MARK CENTER DRIVE
ALEXANDRIA, VIRGINIA 22350-1500

May 24, 2012

MEMORANDUM FOR UNDER SECRETARY OF DEFENSE FOR ACQUISITION, TECHNOLOGY, AND LOGISTICS
DIRECTOR, OPERATIONAL TEST AND EVALUATION
DIRECTOR, DEFENSE CONTRACT MANAGEMENT AGENCY
AUDITOR GENERAL, DEPARTMENT OF THE ARMY

SUBJECT: The Army Needs to Recoup Funds Expended on Property Damaged in an Accident at a Development Subcontractor's Facility (Report No. DoDIG-2012-091)

We are providing this report for your information and use. This report is the first of two reports addressing the Army's acquisition of the Joint Land Attack Cruise Missile Defense Elevated Netted Sensor System. We considered management comments on a draft of this report when preparing the final report.

The comments from the Joint Land Attack Cruise Missile Defense Elevated Netted Sensor System Product Manager and Director of Contracting and Acquisition Management conformed to the requirements of DoD Directive 7650.3; therefore, we do not require additional comments.

We appreciate the courtesies extended to the staff. Please direct questions to Ms. Jacqueline Wicecarver at (703) 604-9077 (DSN 664-9077).

Jacqueline L. Wicecarver
Jacqueline L. Wicecarver
Assistant Inspector General
Acquisition and Contract Management

Report No. DODIG-2012-091 (Project No. D2011-D000AE-0258.000) May 24, 2012

Results in Brief: The Army Needs to Recoup Funds Expended on Property Damaged in an Accident at a Development Subcontractor's Facility

What We Did

This report is the first of two reports addressing the acquisition of the Joint Land Attack Cruise Missile Defense Elevated Netted Sensor System (JLENS). We assessed the Army's conclusion regarding the liability for the JLENS property damaged in an accident at a subcontractor's facility. The accident occurred when high winds caused an Airship Management Services airship to break loose from its mooring and collide with JLENS Platform Number 3 as shown below.

Damaged JLENS Platform

Source: JLENS Program Office, Huntsville, Alabama

What We Found

The U.S. Army Space and Missile Defense Command-Judge Advocate Office (SMDC-JA) attorney DCMA - (b)(5) [redacted] had passed to the Government. The SMDC-JA attorney:

- DCMA - (b)(5) [redacted]
- DCMA - (b)(5) [redacted]

~~(FOUO)~~ As a result, the Army did not seek reimbursement from Raytheon for the estimated DoD OIG - (b)(4) [redacted] expended to design and fabricate the JLENS platform that was damaged. However, we disagree with the legal opinion of the SMDC-JA attorney DCMA - (b)(5) [redacted].

What We Recommend

~~(FOUO)~~ We recommend the Army seek reimbursement for the DoD OIG - (b)(4) [redacted] expended on the destroyed JLENS platform property. We also recommend that the Army make sure that title-passing clauses and risk of loss clauses are included in all future development contracts to protect the Government's interests.

Management Comments and Our Response

We received fully responsive comments from the Army and they will seek reimbursement. Please see the recommendations table on the back of this page.

Recommendations Table

Management	Recommendations Requiring Comment	No Additional Comments Required
JLENS Product Manager		1
Director of Contracting and Acquisition Management, U.S. Army Space and Missile Defense Command		2

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Introduction

Objective

This report is the first of two reports addressing the acquisition of the Joint Land Attack Cruise Missile Defense Elevated Netted Sensor System (JLENS). The overall audit objective was to review the Army's preparation of the JLENS for the low-rate initial production decision. This report assesses the Army's conclusion regarding the liability for the JLENS property damaged in an accident at a subcontractor's facility. We will issue another report discussing the JLENS Product Manager's effectiveness in readying the JLENS program for the low-rate initial production phase of its acquisition process. See Appendix A for a discussion of our scope and methodology.

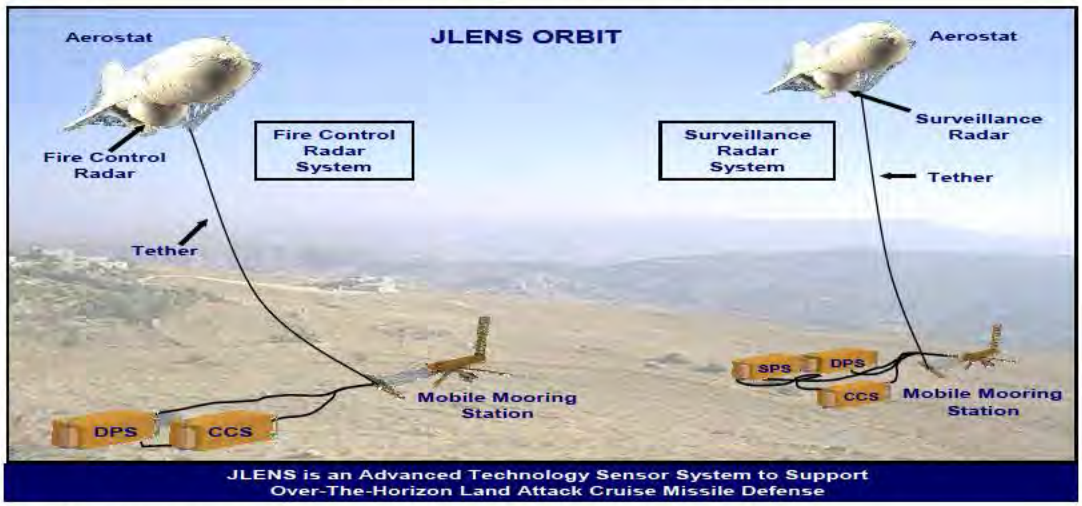
JLENS System

~~(FOUO)~~ The JLENS program is a Major Defense Acquisition Program (Category ID), which is in the Engineering, Manufacturing, and Development phase with an estimated life-cycle cost of about $10 billion. The JLENS is a critical part of the Army's future Integrated Air and Missile Defense force and a key contributor to joint air and cruise missile defense capability objectives. JLENS primary missions include supporting cruise missile defense, contributing to the single-integrated air picture,[1] supporting combat identification and threat characterization. JLENS uses its advanced sensor and networking technologies to provide 360-degree, wide-area surveillance and sectored precision tracking of land attack cruise missiles and other types of aircraft.

~~(FOUO)~~ The surveillance system and the fire control system together make up a JLENS orbit, although each system can operate independently. The surveillance system consists of the surveillance radar, the communications and processing work group, and platform. The fire control system consists of the fire control radar, the communications and processing work group, and platform. A platform is composed of an aerostat (a simple, blimp-like aircraft that cannot be piloted or flown), mobile mooring station, ground support equipment, and tether. The JLENS Orbit can stay aloft up to 30 days, providing 24-hour radar coverage of the assigned areas, and is the only elevated, persistent, long-range surveillance and fire control sensor capability for Army and Joint programs. The surveillance and fire control radar systems are moveable and can be transported by aircraft, railway, ship, or roadway. As shown in Figure 1, JLENS employs a dual, aerostat-based radar sensor system (or orbit) to defend against land attacks from enemy cruise missiles on American military assets.

~~(FOUO)~~ [1] The single-integrated air picture is an operational concept defined as the air track portion of the common tactical picture and consists of common, continuous, unambiguous tracks of airborne objects of interest in area of interest, such as a specified surveillance area.

~~(FOUO)~~ Figure 1. JLENS Orbit



DPS-Data Processing Station
CCS-Communications & Control Station
SPS-Signal Processing Station
Source: JLENS Program Office, Huntsville, Alabama

The JLENS Product Office is procuring two orbits from Raytheon under its engineering and manufacturing development contract (prime contract DASG60-98-C-0001). The contract is a cost-plus-incentive-fee contract valued at $1.8 billion. Tethered Communications Limited Partnership (TCOM LP) is a subcontractor of Raytheon and is responsible for the design, development, procurement, fabrication, integration, testing, demonstration, and delivery of four JLENS platforms.

U.S. Army Space and Missile Defense Command

The U.S. Army Space and Missile Defense Command's mission is to conduct space and missile defense operations and provide planning, integration, control, and coordination of Army forces and capabilities in support of U.S. Strategic Command missions (strategic deterrence, integrated missile defense, and space operations). It serves as the Army force modernization proponent for space, high-altitude and global missile defense, is the Army operational integrator for global missile defense, and conducts mission-related research and development in support of Army Title 10 responsibilities. The JLENS Product Office used the U.S. Army Space and Missile Defense Command's Contracting Office to award the JLENS Program's systems demonstration development contract.

Review of Internal Controls

DoD Instruction 5010.40, "Managers' Internal Control Program (MICP) Procedures," July 29, 2010, requires DoD organizations to implement a comprehensive system of internal controls that provides reasonable assurance that programs are operating as intended and to evaluate the effectiveness of those controls. Although we disagree with the Army's conclusion regarding the liability for the JLENS property damaged in an accident at a subcontractor's facility, we do not consider the issues identified to have resulted from internal control weaknesses in the SMDC-JA office.

Finding. Property Damaged in an Aerostat Accident at Subcontractor's Facility Incorrectly Determined Government Property

The U.S. Army Space and Missile Defense Command Judge Advocate (SMDC-JA) Office attorney DCMA - (b)(5) [redacted]

- DCMA - (b)(5) [redacted]
- DCMA - (b)(5) [redacted]

~~(FOUO)~~ As a result, the Army did not seek reimbursement from Raytheon for the estimated DoD OIG - (b)(4) [redacted] expended to design and fabricate the JLENS platform that was damaged. However, we disagree with the legal opinion of the SMDC-JA attorney when he concluded that FAR 52.245-1(e)(3)(ii)(C) governed when the title passed for the damaged and destroyed JLENS property to the Government.

JLENS Platform Accident

~~(FOUO)~~ USASMDC - (b)(5) [redacted]

~~(FOUO)~~ At the time of the incident, TCOM LP had completed and delivered two JLENS platforms to Raytheon, and the third was at its facility in Elizabeth City, North Carolina. TCOM LP had not completed testing, and Raytheon had not accepted the third platform. The fourth JLENS platform was under construction in a nearby hangar and was not affected by the accident. AMS was not involved in the JLENS program but was simply leasing space from TCOM LP. Although the AMS airship was piloted at the time of the crash, there has been no finding of fact that would indicate pilot error caused the accident. According to the Raytheon contract manager, AMS had only worker's compensation insurance at the time of the accident, which was in breach of the terms of its lease. USASMDC - (b)(5) [redacted]

~~(FOUO)~~ USASMDC - (b)(5) [redacted] In addition, the Raytheon contract manager stated that TCOM LP informed Raytheon personnel that it was not going to file a claim with its insurance company because it regarded JLENS Platform Number 3 to be Government property.

Damage to JLENS Platform Number 3

Figures 2 and 3 show JLENS Platform Number 3 before and after the AMS airship collided with it at the TCOM LP facility. Figure 2 shows the aerostat affixed to its mobile mooring station before the accident, and Figure 3 shows the damage that the aerostat, avionics and electronics, and hardware sustained in the accident.

Figure 2. JLENS Aerostat Affixed to Mobile Mooring Station

Figure 3. Damaged JLENS Aerostat and AMS Airship

Destroyed JLENS Aerostat. Mixed JLENS Platform and AMS Airship Debris.

Source: JLENS Program Office, Huntsville, Alabama

~~(FOUO)~~ USASMDC - (b)(4) [redacted]

~~(FOUO)~~ USASMDC - (b)(4) [redacted]

USASMDC - (b)(4) [redacted]

Appendix B provides a detailed itemization of the JLENS platform parts damaged or destroyed in the accident.

DCMA Property Administrator Concluded DCMA - (b)(5) [redacted]

The DCMA property administrator concluded that DCMA - (b)(5) [redacted] On November 1, 2010, DCMA personnel conducted an assessment of the accident. The DCMA property administrator stated DCMA - (b)(5) [redacted] Neither of these actions had occurred at the time of the accident. The property administrator determined that DCMA - (b)(5) [redacted].

DCMA - (b)(5) [redacted]

DCMA - (b)(5) [redacted]

DCMA - (b)(5) [redacted]

DCMA - (b)(5) [redacted]

SMDC Judge Advocate Attorney Issued Legal Opinion

DCMA - (b)(5) [redacted]

The SMDC-JA attorney issued a legal opinion DCMA - (b)(5) [redacted]

Analysis of FAR and JLENS Program Documentation

The SMDC-JA attorney reviewed the FAR to determine what constituted Government property and when the title to property procured under cost-reimbursable contracts passed to the Government. FAR 52.245-1(a), "Definitions," provides the following guidance relating to what constitutes Government property.

> "Government property" means all property owned or leased by the Government. Government property includes both Government-furnished and Contractor-acquired property. Government property includes material, equipment, special tooling, special test equipment, and real property. Government property does not include intellectual property and software.
>
> "Government-furnished property" means property in the possession of, or directly acquired by, the Government and subsequently furnished to the Contractor for performance of a contract. Government-furnished property includes, but is not limited to, spares and property furnished for repair, maintenance, overhaul, or modification. Government-furnished property also includes contractor-acquired property if the contractor-acquired property is a deliverable under a cost contract when accepted by the Government for continued use under the contract.
>
> "Contractor-acquired property" means property acquired, fabricated, or otherwise provided by the Contractor for performing a contract, and to which the Government has title.

The SMDC-JA attorney noted that DCMA - (b)(5) [redacted]

FAR 52.245-1(e)(3) governs when title under Cost-Reimbursable or Time-and-Material Contracts or Cost-Reimbursable contract line items under Fixed-Price contracts passes to the Government.

> (i) **Title to all property purchased by the Contractor for which the Contractor is entitled to be reimbursed as a direct item of cost** under this contract shall pass to and vest in the Government upon the vendor's delivery of such property.
>
> (ii) **Title to all other property, the cost of which is reimbursable to the Contractor,** shall pass to and vest in the Government upon—
> (A) Issuance of the property for use in contract performance;
> (B) Commencement of processing of the property for use in contract performance; or
> (C) Reimbursement of the cost of the property by the Government, whichever occurs first. **[Emphasis Added]**
>
> (iii) All Government-furnished property and all property acquired by the Contractor, title to which vests in the Government under this paragraph (e)(3)(iii) (collectively referred to as "Government property)," are subject to the provisions of this clause.

~~(FOUO)~~ The determination of which paragraph of FAR 52-245-1(e)(3) governs when title passes to the Government depends on whether or not the contractor was being reimbursed for property in question as a direct item of cost. DCMA, USASMDC - (b)(5) [redacted]

~~(FOUO)~~ DCMA, USASMDC - (b)(5) [redacted]

DCMA, USASMDC - (b)(5) [redacted]

DCMA, USASMDC - (b)(5) [redacted]

The SMDC-JA attorney also concluded that DCMA - (b)(5) [redacted] SMDC-JA attorney found:

~~(FOUO)~~ DCMA, USASMDC - (b)(5) [redacted]

~~(FOUO)~~ The contracting officer had not revoked the Government's assumption of risk because of DoD OIG - (b)(4) [redacted] and there was no issue with whether the loss was covered by insurance. Therefore, according to the SMDC-JA, DCMA, USASMDC - (b)(5) [redacted]

~~(FOUO)~~ DCMA, USASMDC - (b)(5) [redacted]

DCMA Property Administrator's Liability Assessment

The DCMA property administrator found DCMA - (b)(5) [redacted] On March 17, 2011, DCMA met with representatives from TCOM LP at its Elizabeth City, North Carolina, facility regarding the incident. According to the TCOM LP representatives, DCMA had not approved the company's property control system. DCMA - (b)(5) [redacted] Furthermore, the subcontract agreement did not require TCOM LP to carry property damage liability insurance. Therefore, after reviewing the terms and conditions, as well as the Government property clause that was included in contract DASG60-98-C-0001, the DCMA property administrator determined DCMA - (b)(5) [redacted]. Consequently, the JLENS Product Office absorbed the cost to repair or replace the JLENS property damaged or destroyed by the AMS airship.

> *The JLENS Product Office absorbed the cost to repair or replace the JLENS property damaged or destroyed by the AMS airship.*

Army Did Not Seek Reimbursement of the Funds Expended to Repair or Replace the Property Damaged in the Accident

~~(FOUO)~~ DCMA, USASMDC - (b)(5) [redacted] the Army did not seek reimbursement for the funds expended on the property damaged in the accident. In accordance with 10 United State Code § 2307, the question of whether title to goods in production passes to the Government depends on the terms of the contract. The United States Court of Claims examined this issue in *Boeing* v. *United States*, 168 Ct. Cl. 109 (CtCl 1964). In this case, the Court found that ownership of the work-in-process inventory passed to the Government when the parties' contract contained both a title-passing clause and a partial payment clause. The contract contained the following provision, which specifically passed title to the Government:

> (b) Upon the making of any partial payment under this contract, title to all parts, materials, inventories, work in process and non-durable tools theretofore acquired or produced by the Contractor for the performance of this contract, and properly chargeable thereto under sound accounting practice, shall forthwith vest in the Government; and title to all like property thereafter acquired or produced by the Contractor for the performance of this contract and properly chargeable thereto as aforesaid shall vest in the Government forthwith upon said acquisition

> or production; Provided, that nothing herein shall deprive the Contractor of any further partial or final payments due or to become due hereunder; or relieve the Contractor or the Government of any of their respective rights or obligations under this contract.

However, despite the fact that the title passed to the Government under the specific contract provision, the contractor retained the risk of loss under the following contract provision:

> (e) The article of this contract captioned "Liability for Government Property" shall be inapplicable to property to which the Government shall have acquired title solely by virtue of the provisions of this Article. The provisions of this Article shall not relieve the Contractor from risk of loss or destruction of or damage to property to which title vests in the Government under the provisions hereof.

~~(FOUO)~~ The SMDC Contract and Acquisition Management Office cited only FAR 52.245-1 in the JLENS System Development and Demonstration contract it issued to Raytheon and did not include a clause that addressed the risk of loss for the JLENS property while under development. Therefore, the title for the property in question passed in accordance with the terms and conditions of FAR 52.245-1(e)(3). However, we disagree with DCMA, USASMDC - (b)(5) [redacted] Furthermore, we disagree DCMA - (b)(5) [redacted]

The determination of whether paragraph (i) or paragraph (ii) of FAR 52-245-1(e)(3) governs whether the title for the destroyed JLENS property passed to the Government depends on whether the contractor was being reimbursed for the property in question as a direct item of cost under its contract. In this case, the JLENS Product Office contracted with Raytheon to design, develop, procure, fabricate, integrate, test, and deliver two System Development and Demonstration JLENS systems under Raytheon prime contract DASG60-98-C-0001. Raytheon, in turn, subcontracted with TCOM LP to design, develop, procure, fabricate, integrate, test, demonstrate, and deliver four JLENS platforms under subcontract 4400042420. According to FAR 4.1001, "Policy," contracts may identify the items or services to be acquired as separately identified line items. Contract line items should provide unit prices or lump-sum prices for separately identifiable contract deliverables and associated delivery schedules or performance periods. The Raytheon prime contract required all the costs associated with the two JLENS systems to be charged against contract line item number 0017AA, "SDD [System Development and Demonstration] JLENS System." In addition, Section 2.6.1, "Integrated Program Management Reporting," of TCOM LP's subcontract states:

> **TCOM shall report EVM [Earned Value Management] data. All reporting shall correspond to applicable CWBS [Contract Work Breakdown Structure] elements. TCOM shall prepare and provide a Contract Performance Report (CPR) and a Contract Funds Status Report (CFSR). TCOM shall provide assistance to**

> **Raytheon to reconcile the cost/schedule data elements in the CFSR with the CPR at Raytheon's request**. TCOM shall provide any reconciliation of the CFSR and CPR as an addendum to the CPR. **To maintain necessary visibility, data reported shall be separated in the CPR via the CWBS structure.** TCOM shall support Raytheon in generating a quarterly Estimate at Completion (EAC). **[Emphasis Added]**

~~(FOUO)~~ Furthermore, the billings that Raytheon submitted to the Government for payment of work related to the JLENS platform reported the costs consistent with the work breakdown structure and cited contract line item number 0017AA. As such, we find it difficult to support the rationale used by the SMDC-JA attorney to determine DCMA - (b)(5) [redacted]. Therefore, the only conclusion that can be drawn from the above facts is that TCOM LP was being reimbursed for the costs associated with the damaged and destroyed JLENS property[2] as a direct item of cost. In addition, because TCOM LP had not delivered the JLENS Platform Number 3 to Raytheon and the Government had not accepted JLENS Platform Number 3, the title to the damaged property never passed to the Government. Therefore, the JLENS product manager should request that Raytheon reimburse the Army for the DoD OIG: (b)(4) [redacted] expended on the damaged and destroyed JLENS platform property. See Appendices C and D for copies of the work breakdown structure and Raytheon's billings.

> *Because TCOM LP had not delivered the JLENS Platform Number 3 to Raytheon and the Government had not accepted JLENS Platform Number 3, the title to the damaged property never passed to the Government.*

Conclusion

~~(FOUO)~~ DCMA, USASMDC - (b)(5) [redacted] The determination of which paragraph of FAR 52-245-1(e)(3) governs when title passes to the Government depends on whether or not the contractor was being reimbursed for property in question as a direct item of cost. In this case, the JLENS Product Office contracted with Raytheon to develop and deliver two JLENS systems. Raytheon, in turn, subcontracted with TCOM LP to fabricate the four JLENS platforms. All the costs associated with the platforms were charged against contract line item number 0017AA. Clearly, both Raytheon and TCOM LP were entitled to be reimbursed for the costs associated with the platforms as direct items of cost. In addition, the title for damaged JLENS Platform Number 3 property never passed to the Government because the JLENS was never delivered to nor accepted by either Raytheon or the JLENS Product Office.

Furthermore, as outlined previously, the title to goods passes in accordance with the terms of the contract. In this case, because the SMDC Contract and Acquisition Management Office cited only FAR 52.245-1 in the JLENS system development and

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[2] TCOM was contracted to design and procure the aerostat platform, which consists of: the aerostat, the mobile mooring system hardware, the tether, and the ground system equipment.

demonstration contract, the determination regarding when title passed was left to interpretation. As a best practice going forward, the U.S. Army Space and Missile Defense Command should make sure that future contracts include both a title-passing clause and a risk of loss clause specifically stating when the title for work-in-process passes to the Government to put the risk of loss for property in the possession of the contractor with the contractor.

Product Office and Contracting and Acquisition Management Office Comments on the Finding and Our Response

The Product Office and Contracting and Acquisition Management Office provided comments on the finding. We addressed the significant issues and made other minor changes to the report where appropriate.

Comments on DCMA Property Administrator Conclusion

~~(FOUO)~~ DCMA, USASMDC - (b)(5) [redacted] The agency noted that the determination was thoroughly coordinated and agreed to by responsible DCMA personnel after extensive collaboration, coordination, and discussion.

Our Response

We discussed the DCMA property administrator's determination in a September 14, 2011, teleconference between the audit team and the SMDC-JA acquisition attorney that rendered the legal advice on whether the title to the damaged property passed to the Government. During the conversation, DCMA - (b)(5) [redacted].

Comments on Legal Interpretation of FAR 52.245-1 (e)(3)

The SMDC-JA attorney stated that DCMA - (b)(5) [redacted]

Our Response

~~(FOUO)~~ DCMA, USASMDC - (b)(5) [redacted] As stated in the report, the costs associated with the damaged JLENS property were direct items of cost. Therefore, subparagraph (e)(3)(i) applies in the current situation, not subparagraph (e)(3)(ii). Because TCOM LP had not delivered the JLENS Platform to Raytheon and the Government had not accepted the JLENS platform, title to the damaged property never passed to the Government.

Comments on Ambiguous Nature of FAR 52.245-1 (e)(3)

The Product Office and SMDC-JA stated that as noted in the Department of Defense Office of Inspector General (DoD OIG) draft report, FAR 52.245-1(e)(3) is ambiguous and cannot be read in isolation from the entire clause.

Our Response

The draft report did not state that FAR 52.245-1 (e)(3) was ambiguous. The draft report stated that the decision to cite just the FAR instead of using specific contract language to delineate when title passed left it open to interpretation. The contract should have specifically stated when title and risk of loss passed to the Government.

Recommendations, Management Comments, and Our Responses

We recommend that the:

1. ~~(FOUO)~~ Product Manager, Joint Land Attack Cruise Missile Elevated Netted Sensor System Product Office, request payment from Raytheon for the DoD OIG - (b)(4) **expended on the damaged aerostat.**

2. Director of Contracting and Acquisition Management Office, U.S. Army Space and Missile Defense Command, make sure that title-passing clauses and risk of loss clauses are included in all future development contracts.

Product Manager and Director of Contracting and Acquisition Management Response

The JLENS Product Manager and the Director of Contracting and Acquisition Management, U.S. Army Space and Missile Defense Command, agreed with the intent and will coordinate with DCMA to seek reimbursement from the prime contractor. Specifically, the Deputy Director of Army Contracting Command stated that the Contracting and Acquisition Management Office will ensure that the appropriate title-passing and risk of loss clauses are included in future development contracts. In addition, after further consultation with DCMA concerning the FAR property clauses, the Command requested that the DoD OIG assist in seeking recovery from the prime contractor.

Our Response

The JLENS Product Manager and the Deputy Director of Contracting and Acquisition Management, U.S. Army Space and Missile Defense Command, comments were responsive. The actions meet the intent of the recommendations and the DoD OIG will assist the Command in seeking recovery as long as it does not conflict with our responsibility with the Inspector General Act 1978 as amended or DoD policy. No further comments are required.

Appendix A. Scope and Methodology

We conducted this performance audit from July 2011 through April 2012 in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

Our review focused on the Army's conclusion regarding the liability for the JLENS property damaged in a September 30, 2010, Aerostat accident at the TCOM LP facility in Elizabeth City, North Carolina. We interviewed staff from the JLENS Product Office and SDMC Office in Huntsville, Alabama, and DCMA Andover, Massachusetts. We reviewed provisions of the FAR and DFARS and the case law relating to passage of title. We also collected, reviewed, and analyzed program and contract documents dated from November 1991 through September 2011. Specifically, we reviewed JLENS contract DASG60-98-C-0001, TCOM LP subcontract 4400042420, various memoranda prepared to document communications between the contracting officer, Raytheon, and TCOM LP; the DCMA accident investigations; and the SMDC-JA attorney's legal conclusion concerning whether the title for the damaged JLENS platform had passed to the Government. We also relied on advice from the Office of Inspector General, Office of General Counsel.

Use of Computer-Processed Data

We did not use computer-processed data to perform this audit.

Prior Coverage

No prior coverage has been conducted on the subject during the last 5 years.

~~(FOUO)~~ Appendix B. USAMDC-(b)(4) [redacted]

USASMDC - (b)(4)

[redacted]

USASMDC - (b)(4)

[redacted]

~~(FOUO)~~ Appendix C. Work Breakdown Structure

The figure below provides the work breakdown structure for the JLENS platform.

USASMDC - (b)(4)

[redacted]

USASMDC - (b)(4)

[redacted]

~~(FOUO)~~ Appendix D. Raytheon Billing

Below are a billing and related voucher that Raytheon submitted to obtain reimbursement for incurred costs related to contract line item number 0017AA for the JLENS System.

Standard Form 1034
Revised October 1962
Department of the Treasury
1-TFM 4-2000
1034-101

PUBLIC VOUCHER FOR PURCHASES AND SERVICES OTHER THAN PERSONAL

VOUCHER NO. BVN0299

U.S. DEPARTMENT, BUREAU, OR ESTABLISHMENT AND LOCATION
DFAS - COLUMBUS CENTER
NORTH ENTITLEMENT OPERATIONS
P.O. BOX 182266
COLUMBUS OH 43218-2266
USA
Code: HQ0337

DATE VOUCHER PREPARED: 19-SEP-2011

CONTRACT NUMBER AND DATE: DASG60-98-C-0001

REQUISITION NUMBER AND DATE

SCHEDULE NO.

PAID BY

PAYEE'S NAME AND ADDRESS
RAYTHEON COMPANY
350 LOWELL ST
ANDOVER MA 01810
USA

DATE INVOICE RECEIVED

DISCOUNT TERMS

Raytheon Contact: LINDSEY A CONLIN

Document No: 90966855
Contract Ref. No: 40010993

PAYEE'S ACCOUNT NUMBER

SHIPPED FROM | TO | WEIGHT | GOVERNMENT B/L NUMBER

NUMBER AND DATE OF ORDER	DATE OF DELIVERY OR SERVICE	ARTICLES OR SERVICES (Enter description, item number of contract or Federal supply schedule, and other information deemed necessary)	QUANTITY	UNIT PRICE COST	UNIT PRICE PER	AMOUNT
	29AUG2011 through 18SEP2011	For details, see SF1035, Continuation Sheet, total amount claimed transferred from SF1035 Form.				DoD OIG - (b)(4)

(Use continuation sheet(s) if necessary) **(Payee must NOT use the space below)** **TOTAL** DoD OIG - (b)(4)

PAYMENT:
- [X] PROVISIONAL
- [ ] COMPLETE
- [ ] PARTIAL
- [ ] FINAL
- [ ] PROGRESS
- [ ] ADVANCE

APPROVED FOR -$

EXCHANGE RATE -$1.00

DIFFERENCES

BY [2]

TITLE

Amount verified; correct for payment

(Signature or initials)

Pursuant to authority vested in me, I certify that the voucher is correct and proper for payment

(Date) (Authorized Certifying Officer) (Title)

ACCOUNTING CLASSIFICATION

PAID BY

CHECK NUMBER ON TREASURER OF THE UNITED STATES CHECK NUMBER ON (Name of bank)

CASH $ DATE PAYEE [1]

FOR

TITLE

[1] When stated in foreign currency, insert name of currency.
[2] If the ability to certify and authority to approve are combined in one person, one signature only is necessary; otherwise the approving officer will sign in the space provided, over his official title.
[3] When a voucher is prepared in the name of a company or corporation, the name of the person writing the company or corporate name, as well as the capacity in which he signs, must appear. For example: "John Doe Company, per John Smith, Secretary", or "Treasurer", as the case may be.

Previous edition usable NSN 7540-00-900-2234

PRIVACY ACT STATEMENT

The information requested on this form is required under the provisions of 31 U.S.C. 82b and 82c for the purpose of disbursing Federal money. The information requested is to identify the particular creditor and the amounts to be paid. Failure to furnish the information will delay discharge of the payment obligation.

Standard Form 1035 September 1973 4 Treasury TRM 2000 1055-110	PUBLIC VOUCHER FOR PURCHASES AND SERVICES OTHER THAN PERSONAL *CONTINUATION SHEET*	VOUCHER NO. BVN0299 SCHEDULE NO. SHEET NO. 2 of 2

U.S. DEPARTMENT, BUREAU, OR ESTABLISHMENT
DFAS — COLUMBUS CENTER

NUMBER AND DATE OF ORDER	DATE OF DELIVERY OR SERVICE	ARTICLES OR SERVICES (Enter description, item number of contract or Federal supply schedule, and other information deemed necessary)	QUANTITY	UNIT PRICE COST	UNIT PRICE PER	AMOUNT
		0017AA MF MG 0028 DoD OIG - (b)(4) [redacted]				DoD OIG - (b)(4) [redacted]
		TOTAL AMOUNT				DoD OIG - (b)(4) [redacted]

USASMDC - (b)(4)

[redacted]

Product Manager and Director of Contract and Acquisition Management Comments

DEPARTMENT OF THE ARMY
PROGRAM EXECUTIVE OFFICE, MISSILES AND SPACE
5250 MARTIN ROAD
REDSTONE ARSENAL, AL 35898-5000

REPLY TO
ATTENTION OF

SFAE-MSLS-CMDS

22 March 2012

MEMORANDUM FOR Inspector General, Department of Defense, 4800 Mark Center Drive, Alexandria, VA 22350-1500

SUBJECT: Agency Response to Draft Report for Project No. D2011-D000AE-0258.000

1. Reference memorandum, DoD OIG, 22 Feb 12, subject: The Army Needs to Recoup Funds Expended on Property Damaged in an Accident at a Development Subcontractor's Facility (Project No. D2011-D000AE-0258.000).

2. The Cruise Missile Defense Systems (CMDS) Project Office and the Army Contracting Command-Redstone (ACC-R), U.S. Army Space and Missile Defense Command/Army Forces Strategic Command (USASMDC/ARSTRAT), Contracting and Acquisition Management Office (CAMO), in conjunction with the USASMDC/ARSTRAT Office of the Staff Judge Advocate and Defense Contract Management Agency (DCMA), have reviewed the above-subject report. While not in agreement with all aspects of the DoD OIG final draft report, CMDS and CAMO agree with the overarching intent and will coordinate with DCMA to seek reimbursement from the prime contractor. CAMO will also ensure that the appropriate title-passing and risk of loss clauses are included in future development contracts.

3. In light of above-subject report and recent further consultation with DCMA concerning the Federal Acquisition Regulation (FAR) property clauses, as noted in the DoD OIG final draft report it is recognized that significant ambiguity exists between sections of the FAR that allow for different interpretations regarding when title for property passes to the Government. Therefore, it is requested that the DoD OIG assist in seeking recovering from the prime contractor.

4. Specific comments to the above subject report are enclosed.

Encls

WARREN N. O'DONELL
COL, FA
Project Manager
CMDS Project Office

CHARLES T. KALLAM
Deputy Director
Army Contracting Command-Redstone
SMDC Contracting Acquisition Management Office

Product Manager and Director of Contract and Acquisition Management Comments

Final Report Reference

DoD OIG Final Draft Report (Project D2011-D000AE-0258.000)
Agency Specific Comments – SFAE-MSLS-CMDS Memorandum Enclosure (Dtd 22 Mar 12)

1. Department of Defense (DoD) Office of the Inspector General (OIG) final draft report, p. 3, correction concerning mooring of JLENS PO Platform Number 3. Page 3 of the DoD OIG final draft report, which describes the accident to the JLENS Platform Number 3, incorrectly states that the aerostat was floating above the subcontractor's facility (TCOM LP); instead, the aerostat was moored to the JLENS mobile mooring station located on the TCOM LP facility's flight pad. Recommend rewording the final report as noted above. — Page 3

2. DoD OIG final draft report, Finding #1 and recommendation. [redacted] — Page 14, Page i and Page 3

a. Agency response.

(1) As further discussed below, as evidenced by its extensive coordination with DCMA, DCMA - (b)(5) [redacted]

(2) As discussed during various interviews with the DoD OIG team and detailed below, DCMA's involvement in the underlying matter was crucial. The 14 February 2011 SMDC-JA legal memorandum and CAMO Procuring Contracting Officer (PCO) determination were thoroughly coordinated and agreed to by the responsible DCMA Administrative Contracting Officer (ACO), DCMA PA, and DCMA attorney after extensive collaboration, coordination and discussion. Of importance, as discussed in the [redacted].

(3) During this coordination the DCMA PA provided a 19 October 2010 electronic mail message to the Agency and DCMA attorney that highlights a section taken from the DCMA-Defense Acquisition University (DAU) Intermediate Defense Contract Property Administration and Disposition Fundamentals Course (Course IND 200), which addresses when title passes to the Government under the Government property clause (Encl 2). This authoritative training booklet states that title can pass prior to delivery even when it is charged as a direct item of cost due to the ambiguous language used in FAR 52.245-1(e)(3).

(4) The DCMA PA was also aware of the ambiguous language in FAR 52.245-1(e)(3) and in a 14 December 2010 memorandum to the DCMA ACO the DCMA PA states that she was DCMA - (b)(5) [redacted] DCMA - (b)(5) (Encl 3). Additionally, the DCMA PA provided documentation to the CAMO PCO, SMDC-JA and DCMA legal office showing that the 2007 version of the

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DoD OIG Final Draft Report (Project D2011-D000AE-0258.000)
Agency Specific Comments – SFAE-MSLS-CMDS Memorandum Enclosure (Dtd 22 Mar 12)

Government property clause (with its subcontractor flow-down requirements) had been incorporated into the JLENS contract in September 2010, which was just prior to the accident (Encl 4).

(5) In coordination with the CAMO PCO, SMDC-JA submitted various drafts of the legal opinion to the DCMA attorney for review and comments prior to its issuance on 14 February 2011. In the last draft coordination electronic mail exchange with SMDC-JA, the DCMA attorney DCMA - (b)(5) [redacted] DCMA - (b)(5) [redacted]. Based upon previous extensive coordination with DCMA and the 14 February 2011 SMDC-JA legal advice, on 17 February 2011 the CAMO PCO issued her determination to DCMA (Encl 6).

(6) Subsequently, the DCMA PA issued a 22 March 2011 memorandum to the DCMA ACO stating DCMA - (b)(5) [redacted] DCMA - (b)(5) (Encl 7). Of significance, the DCMA PA opened a DCMA - (b)(5) [redacted] (LTDD) case and asserted that the prime contractor DCMA - (b)(5) [redacted] DCMA - (b)(5) [redacted] considered contractor property. It was not until the CAMO PCO requested clarification from the DoD OIG regarding its assertion that DCMA's advice was rejected, and the DoD OIG provided a 1 November 2010 DCMA PA letter to the DCMA ACO, that the CAMO PCO and SMDC-JA were made aware of the issue (Encls 8 and 9); the 1 November 2010 memorandum was never raised by DCMA to the CAMO PCO or SMDC-JA during their documented DCMA coordination. Furthermore, the 1 November 2010 DCMA PA memorandum was neither discussed nor referred to in the 22 November 2010 DCMA Consolidated Report on JLENS Platform 3 Accident (Encl 10).

(7) However, based upon recent information provided by DCMA, the DCMA ACO has DCMA - (b)(5) [redacted]

b. Agency response, alternative recommendation. Based upon the discussion and information provided above and in the corresponding enclosures, the Agency recommends that the DoD OIG final report reflect that the Agency extensively coordinated with DCMA in formulating the SMDC-JA legal opinion and CAMO PCO determination, and as noted below DCMA - (b)(5) [redacted]

DoD OIG Final Draft Report (Project D2011-D000AE-0258.000)
Agency Specific Comments – SFAE-MSLS-CMDS Memorandum Enclosure (Dtd 22 Mar 12)

3. DoD OIG final draft report. Finding #2 and recommendation. SMDC-JA misinterpreted FAR 52.245-1(e)(3). Title under Cost-Reimbursable or Time-and-Material Contracts or Cost-Reimbursable line items under Fixed- Price contracts.

Page 14
Page i and Page 3

a. Agency response.

(1) Although the Agency and DoD OIG differ with the interpretation of FAR 52.245-1, it remains the Agency position that DCMA - (b)(5) [redacted] DCMA - (b)(5) [redacted] As discussed below, determining whether title passed to the Government cannot rest solely on whether the item is charged as a direct item of cost as set forth in FAR 52.245-1(e)(3)(i) (Encl 11). As noted in the DoD OIG final draft report, as drafted FAR 52.245-1(e)(3) is ambiguous; thus, it cannot be read in isolation from the entire clause, as well as intent of FAR Part 45 that was current at time of inclusion of the clause in the contract.

(2) Under FAR 52.245-1, subparagraph (e)(3)(ii) is not limited or restricted by subparagraph (e)(3)(i) concerning applicability to direct/indirect items of cost, but rather (e)(3)(ii) states "all other property, the cost of which is reimbursable to the contractor", which includes title vesting in the Government at the commencement of processing the property for use in contract performance or, when the cost of the property has been reimbursed by the Government. This ambiguity is noted in the DCMA/DAU training materials provided to the Agency by the DCMA PA (see discussion above and Encl 2). Additionally, prior to the underlying catastrophe the subcontractor had fabricated the property solely for use under a Government contract and was at the last stage of testing before delivering the equipment to the prime contractor (Encl 12), which invokes FAR 52.245-1(e)(3)(ii)(B) ("at the commencement of processing the property for use in contract performance").

(3) Additionally, as noted in the DoD OIG final draft report at the time of the accident the Government had in essence paid for the destroyed property. The contract in question is a cost-reimbursement contract under which the Government had paid the prime contractor seventy-five percent (75%) of the value of the destroyed property, which also invokes FAR 52.245-1(e)(3)(ii).

(4) Finally, the remedies portion of FAR 52.245-1(h)(1), which provides for the remedies available to the Government under the 2007 Property clause, relieves the contractor of liability for destroyed property except for specific circumstances, none of which are applicable (Encl 13). Additionally, the rights and responsibilities of the prime contractor are "flowed down" to the subcontractor under FAR 52.245-1(f)(v) (Encl 14). The accident in question involved a third party contractor (AMS, Inc.), which was leasing part of the facility for its airship. Apparently, a strong wind caused the pilot of the airship to crash into the JLENS aerostat destroying it, damaging the tether securing the aerostat to the ground and damaging most of the supporting ground equipment (Encl 15) (but see paragraph 1 above).

(5) However, as noted above, based upon recent information provided by DCMA, the DCMA ACO DCMA - (b)(5) [redacted] DCMA - (b)(5) [redacted] Thus, as detailed above while during the late 2010 and early 2011 time frame the Agency coordinated and collaborated with DCMA to reach a consensus regarding passing of title, based upon the recent DCMA determination the Agency will further coordinate with DCMA as stated below.

b. Agency response, alternative recommendation. Based upon the discussion and information provided above and in the corresponding enclosures, the Agency recommends that the DoD OIG final report reflect that the Agency extensively coordinated with DCMA in formulating the SMDC-JA legal opinion and CAMO PCO determination that DCMA - (b)(5) [redacted] DCMA - (b)(5) [redacted] Further, as noted below, recommend that the DoD OIG final report does not state that the Agency misinterpreted the cognizant FAR clause, but rather that the DoD OIG disagrees with the Agency's interpretation of that clause.

4. DoD OIG final draft report, recommendations; additional Agency recommendation.

a. 1st recommendation, JLENS PO request payment from the prime contractor for the DoD OIG (b)(4) [redacted] DoD OIG (b)(4) [redacted] expended on the destroyed aerostat; Agency response. Although the Agency does not agree with the DoD OIG final draft report findings regarding property title determination, the Agency agrees to work with DCMA to review and pursue (as deemed appropriate) all available legal remedies. In particular, the Agency will work with DCMA to seek recoupment of the replacement costs of the destroyed aerostat and destroyed or damaged support equipment.

b. 2nd recommendation, CAMO, ensures that title-passing clauses and risk of loss clauses are included in all future development contracts; Agency response. The Agency will ensure that the appropriate title-passing clause and risk of loss clause are included in all future development contracts.

c. Additional Agency recommendation/request; tone of final draft report, word usage. The draft final report's use of a negative tone and word choice stating that the Agency deliberately ignored certain documents, as well as inferences that the Agency failed to draw an obvious conclusion, is inappropriate and not substantiated as discussed above and provided in the enclosures. Therefore, request that the DoD OIG final report not use the wording "rejected" and "misinterpreted" (or otherwise state or infer the same), but rather use the wording "despite detailed coordination with DCMA the Agency was unaware" (Finding #1) and "the DoD OIG disagrees with the Agency's interpretation" (Finding #2).

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Inspector General
Department of Defense

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