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April 30, 2020

The Honorable Ellen Lord  
Under Secretary of Defense for Acquisition and Sustainment  
U.S. Department of Defense  
1000 Defense Pentagon  
Washington, D.C. 20301-1000

Dear Under Secretary Lord:

I write to request clarification from the Department of Defense (DoD or the Department) on a recent change to its defense pricing and contracting policy in response to the coronavirus disease 2019 (COVID-19) pandemic. As the Department adjusts its business practices to address the COVID-19 pandemic, I seek to ensure that this policy change will result in responsible use of taxpayer funds and that contractors are not profiteering during the crisis.

As a method of contract financing, the Defense Department issues progress payments to contractors for work that is in progress but not yet completed and for costs associated with that work in progress.<sup>1</sup> Typically, the Department sets these progress payments at 80 percent of the work conducted by large contractors and 90 percent of the work conducted by small contractors.<sup>2</sup> On March 25, 2020, DoD Acquisition and Sustainment officials announced a deviation to these progress payments, which “raises the progress payment rates for large businesses from 80 percent to 90 percent, and for small businesses from 90 percent to 95 percent.” According to Kim Herrington, Acting Principal Director of Defense Pricing and Contracting, this change aims to “provide additional and immediate cash flow to industry once incorporated into the contract” and “[a]s far as monitoring, the same processes that are already in place to verify and validate the invoices are continuing to be done.”<sup>3</sup>

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<sup>1</sup> U.S. Department of Defense, “Progress Payments Based on Costs,” [https://www.acq.osd.mil/dpap/dars/dfars/html/current/232\\_5.htm](https://www.acq.osd.mil/dpap/dars/dfars/html/current/232_5.htm).

<sup>2</sup> U.S. Department of Defense, “Progress Payments Based on Costs,” [https://www.acq.osd.mil/dpap/dars/dfars/html/current/232\\_5.htm](https://www.acq.osd.mil/dpap/dars/dfars/html/current/232_5.htm); Space News, “DoD increases progress payments to contractors to shore up cash-strapped suppliers,” Sandra Erwin, March 22, 2020, <https://spacenews.com/dod-increases-progress-payments-to-contractors-to-shore-up-cash-strapped-suppliers/> (“A 90 percent rate means that if \$1 million in expenses are submitted on the program, DoD will reimburse \$900,000.”).

<sup>3</sup> U.S. Department of Defense, “Department of Defense Acquisition and Sustainment Leaders Hold a Press Briefing on the Defense Department's COVID-19 Acquisition Efforts,” March 25, 2020, <https://www.defense.gov/Newsroom/Transcripts/Transcript/Article/2125737/department-of-defense-acquisition-and-sustainment-leaders-hold-a-press-briefing/>.

I recognize that the pandemic has created difficult financial challenges for contractors that the Department relies on for work that contributes to the national defense, and that it is in the national interest to ensure that contractors that perform key national security roles do not go out of business or become vulnerable to capital infusions by foreign adversaries.<sup>4</sup> However, the current playing field of DoD contract financing is already heavily tilted in favor of large contractors,<sup>5</sup> which can invoice, and receive progress payments from, the Department for subcontracted services and products in progress or completed before having to pay their subcontractors. Therefore, the new progress payments policy will allow a large contractor to receive an even greater share – 90 percent – of all its costs reimbursed by the Department before paying subcontractors for the services and products in progress. While prime contractors are encouraged to allocate progress payments received from the Department to subcontractors within 30 days, there is no explicit legal requirement that progress payments be expeditiously passed on to subcontractors.<sup>6</sup>

I am concerned that the change to the progress payments policy may be a cash subsidy that largely benefits big defense companies that can better withstand the economic shock caused by coronavirus – and that already received a bailout of \$17 billion in loans and loan guarantees in the *Coronavirus Aid, Relief, and Economic Security Act* passed by Congress in March 2020<sup>7</sup> - while leaving smaller, less financially resilient companies in the supply chain behind. Furthermore, I am skeptical as to whether large defense contractors will share these extra funds with their smaller supply chain partners in a timely fashion, and whether the Department will hold these industry giants accountable if they fail to do so. Notably, this increase in progress payments could invite waste, fraud, or abuse by expediting the payments of billions of dollars of taxpayer funds to giant contractors that use the funds for stock buybacks or other methods of enriching upper management, or to large contractors whose work may not even be completed due to stop work orders and other mandatory public safety measures issued by state and local governments to stop the spread of coronavirus.<sup>8</sup>

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<sup>4</sup> *Id.* (According to Undersecretary Lord, “It’s critically important that we understand that during this crisis the [Defense Industrial Base] is vulnerable to adversarial capital, so we need to ensure companies can stay in business without losing their technology.”).

<sup>5</sup> USA Today, “These 30 companies, including Boeing, get the most money from the federal government,” Samuel Stebbins and Michael B. Sauter, March 29, 2019, <https://www.usatoday.com/story/money/business/2019/03/27/lockheed-martin-boeing-get-most-money-federal-government/39232293/>.

<sup>6</sup> U.S. Department of Defense, Office of the Under Secretary of Defense, Acquisition and Sustainment, “Class Deviation—Progress Payment Rates,” April 16, 2020, <https://www.acq.osd.mil/dpap/policy/policyvault/USA000801-20-DPC.pdf>.

<sup>7</sup> Coronavirus Aid, Relief, and Economic Security (CARES) Act, Section 4003(b)(3), <https://www.congress.gov/bill/116th-congress/house-bill/748/text>; Washington Post, “Senate aid package quietly carves out billions intended for Boeing,” Aaron Gregg, Jeff Stein, and Josh Dawsey, March 25, 2020, <https://www.washingtonpost.com/business/2020/03/25/boeing-bailout-coronavirus/>.

<sup>8</sup> Defense News, “Pentagon loosens cash flow for industry, more measures likely coming,” Aaron Mehta, March 23, 2020, <https://www.defensenews.com/coronavirus/2020/03/23/pentagon-loosens-cash-flow-for-industry-more-measures-likely-coming/>; Bloomberg, “Pentagon Raises Contractor Payments to Keep Cash Flowing,” Anthony Capaccio, March 22, 2020, <https://www.bloomberg.com/news/articles/2020-03-22/pentagon-raises-contractor-payments-to-keep-cash-flow-buoyant>.

Between 2010-2018, the six largest defense contractors headquartered in the United States – Lockheed Martin, Raytheon, Northrop Grumman, Boeing, L3 Technologies, and General Dynamics – generated \$158.5 billion of free cash flow and spent \$163.9 billion in stock repurchases and dividend payments.<sup>9</sup> Not a single dollar was used to “invest” in the defense industrial workforce.<sup>10</sup> All of this was accomplished when the progress payment rate was 80% for those large businesses. A ten percent increase in the progress payment rate would appear to mean that these companies receive several billion dollars in expedited payments each year.

Accordingly, I request answers to the following questions by May 15, 2020:

1. What analyses did the Department conduct to determine if the additional progress payments are necessary for national security purposes?
2. How much in total payments will be expedited to contractors as a result of this policy, and which five contractors will receive the most funds?
3. What measures are in place to ensure that large defense contractors do not divert the increased progress payments from the Department to share buybacks, dividends, or executive salaries?
4. What measures are in place to ensure that large defense contractors use the more generous progress payments from the Department to financially sustain smaller contractors?
5. Given the Department’s recent guidance<sup>11</sup> designating the defense industrial base as “critical infrastructure” and directing contractors to continue work is apparently not legally binding, what is the Department’s plan to reconcile efforts to continue contract work with mandatory orders by state and local governments to cease work in order to stop the coronavirus?
6. What specific reporting and metrics are the Department putting in place to measure and evaluate how much funding provided to prime contractors is flowing down to subcontractors?
7. How long will this policy last, and what are the criteria for deciding when to end it?

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<sup>9</sup> Figures calculated by staff of Senator Warren based on review of publicly available annual reports from Lockheed Martin Corporation, Raytheon Company, Northrop Grumman Corporation, The Boeing Company, L3 Technologies, Inc., and General Dynamics.

<sup>10</sup> *Id.*

<sup>11</sup> U.S. Department of Defense, “Defense Industrial Base Essential Critical Infrastructure Workforce,” March 20, 2020, <https://media.defense.gov/2020/Mar/22/2002268024/-1/-1/1/DEFENSE-INDUSTRIAL-BASE-ESSENTIAL-CRITICAL-INFRASTRUCTURE-WORKFORCE-MEMO.PDF>; Defense News, “Pentagon declares defense contractors ‘critical infrastructure,’ must continue work,” Aaron Mehta, March 20, 2020, <https://www.defensenews.com/pentagon/2020/03/20/pentagon-declares-defense-contractors-critical-infrastructure-must-continue-work/>.

Thank you for your attention to this matter. I look forward to your response.

Sincerely,

A handwritten signature in black ink, appearing to read "Elizabeth Warren", written in a cursive style. The signature is positioned above a horizontal line.

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Elizabeth Warren  
United States Senator