

THE WALL STREET JOURNAL.

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MONDAY, APRIL 19, 2004 - VOL. CCXLIII NO. 76 - ★★ ★★ \$1.00

Northrop Papers Indicate Coverup

Documents From '80s Show Accounting Irregularities Were Hidden From Pentagon

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LOS ANGELES—Posing fresh legal and financial problems for a company that has worked hard to cleanse its image, internal documents show that Northrop Grumman Corp. covered up major accounting irregularities during the late 1980s to stay in the Pentagon's good graces.

The documents, which haven't been made public, form the heart of a U.S. government lawsuit against Los Angeles-based Northrop Grumman that could result in penalties of hundreds of millions of dollars. They suggest questionable behavior stretching through the end of the Cold War, when the company's B-2 Stealth bomber and electronic systems it built for military aircraft epitomized former U.S. President Ronald Reagan's massive defense buildup.

The Justice Department's False Claims Act case has been pending for years, but a federal district-court judge in Chicago is about to unseal some files and a trial could start later this year. The lawsuit accuses Northrop Grumman's Rolling Meadows, Ill., facility of defrauding the government by overcharging for advanced radar-jamming devices and other protective equipment installed on some of the Pentagon's advanced jets, including F-15 fighters and B-1 bombers.

Managers at what was then Northrop

Accounting Issues

Internal Northrop Grumman documents from the 1980s offer a rare glimpse of accounting lapses and how the company allegedly covered them up as it billed the Pentagon for equipment on some of the military's most advanced aircraft.

"What will the customer accept as reasons? (We can't tell the truth)"

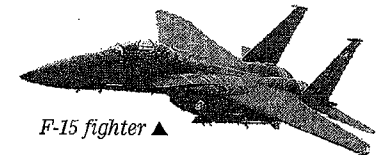
Excerpt from internal 1986
Northrop document about
explaining accounting problems

"We are now approaching the second anniversary of [data clean-up efforts]. It is time to find out what is really wrong...and fix it."

Excerpt from internal 1987
Northrop memo about
inventory management



▲ B-1 Lancer bomber



F-15 fighter ▲



▲ B-2 Stealth bomber

What's News—

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Business and Finance

A GROUP REPRESENTING broadcast media is petitioning the FCC to overturn a March ruling finding remarks by singer Bono "indecent" and "profane," in the first major industry challenge to a recent crackdown. Broadcast interests are concerned that they will be at a disadvantage against rivals not bound by indecency laws, including cable and satellite outlets.

(Article in Column 5)

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■ **Shell is expected** to announce that its chief financial officer, Judy Boynton, is stepping down, in the latest fallout from the energy-reserve accounting debacle.

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■ **Northrop Grumman covered** up major accounting irregularities during the late 1980s to stay in the Pentagon's good graces, internal documents indicate.

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Corp.'s Defense Systems Division in Rolling Meadows recognized the pervasive cost-accounting and material-tracking problems and sought to conceal them from Pentagon auditors, the documents show. A Feb. 21, 1986, memo distributed to 37 managers had explicit instructions on explaining accounting faults. "We can't tell the truth," it said.

The revelations in the internal documents come at a time when U.S. military spending is again on the rise. The alleged improprieties also emerge after Northrop Grumman has largely overcome a troubled past in which it was the target of

several high-profile criminal and civil cases involving improprieties. The company recently has won investor praise for its growth strategy. Without admitting wrongdoing, the company in the past year has paid a total of \$191 million to settle three other federal False Claims Act suits alleging Pentagon overcharges during the 1990s.

In a March filing with the Securities and Exchange Commission, Northrop Grumman said the government is seeking "damages of approximately \$369 million, which could be trebled," plus mil-

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Northrop Papers Indicate Coverup

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lions of dollars in other potential fines and interest related to the pending case. "The company denies the allegations and continues to vigorously defend" itself, the filing said. Many of the people involved in the case no longer work at Northrop Grumman.

A Northrop Grumman spokesman, citing company policy, said he couldn't comment further on pending litigation. Over the years, its lawyers have challenged the basis for the government's case, the interpretation of some documents and the company's maximum liability.

Originally filed in 1989 by two former Northrop employees, the case was taken over by the Justice Department three years ago. The suit alleges, among other things, that Northrop "falsely inflated, recorded and presented costs that were not actually incurred," including scrapping more parts than it had ordered. The company, according to the suit, also "engaged in a secret effort to alter" inventory records "to mislead and defraud" the government.

The internal reports and memos reviewed by The Wall Street Journal portray Northrop managers regularly fretting that procedures for keeping track of everything from production materials to project costs were unreliable. But that isn't what they told the government. The documents disclose that some of the same company officials, determined to fend off threats of reduced payments by the military or potentially harsher punishment, misled Pentagon auditors about the extent of the problems while they scrambled to fix them. Still, every month the company certified to the Pentagon that its billing was accurate.

Northrop Grumman long fought to keep many of the internal documents under wraps. The papers date from 1986, when the Northrop division was already under scrutiny for noncompliance with certain Pentagon accounting standards.

Documents show that Northrop man-

agers in Rolling Meadows held a meeting on Feb. 21, 1986, a day after the Pentagon's Defense Contract Audit Agency cited their unit for accounting failures that had cost the government an extra \$27 million. The minutes of the meeting include a memo that counseled lying about so-called problem-analysis reports dealing with accounting lapses under scrutiny by the Pentagon.

"What will the customer accept as reasons," the memo asked, adding, "We should train the [cost-accounting managers] to violate the system" within certain guidelines. In parentheses, the memo stated, "We can't tell the truth." In sworn statements, former Northrop officials have said that internally, the term "customer" referred to the government.

Wallace Solberg, who was then general manager in Rolling Meadows, didn't attend the meeting but was among the officials on the distribution list for the minutes. Asked in a 2002 deposition about that sentence, Mr. Solberg replied, "I've not seen this before. I'd have killed somebody for that." Mr. Solberg, who rose to serve on Northrop's board of directors before retiring in 1997, declined to comment.

Duane Emling, then head of Northrop's material-accounting department in Rolling Meadows, assured the Pentagon in writing in the summer of 1987 that the unit's accounting system didn't contain major deficiencies. Yet in a 1999 deposition, he said that his previous statements were "accurate, not necessarily complete," because the document "doesn't address issues that might exist with respect to noncompliance." Mr. Emling left Northrop in 1998 amid layoffs. He didn't respond to calls or e-mails requesting comment.

In 1988, the Pentagon's audit agency threatened to withhold 10% of monthly payments to Northrop. It backed down in early 1989 after fierce Northrop protests. The memos show that Northrop felt singled out by the Pentagon's rigorous audits.