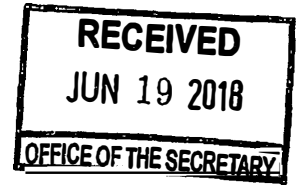


**HARD COPY**

**UNITED STATES OF AMERICA  
Before the  
SECURITIES AND EXCHANGE COMMISSION**

**ADMINISTRATIVE PROCEEDING  
File No. 3-17950**



**In the Matter of**

**David Pruitt, CPA**

**Respondent.**

**DIVISION OF ENFORCEMENT'S MEMORANDUM IN OPPOSITION  
TO RESPONDENT'S MOTION TO THE COMMISSION TO AMEND THE  
ORDER INSTITUTING PROCEEDINGS**

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The Division of Enforcement (the “Division”) respectfully submits this memorandum in opposition to Respondent David Pruitt’s motion to the Commission to amend the Order Instituting Proceedings (the “OIP”) in this matter and to stay this proceeding pending the Commission’s decision. Respondent argues that the OIP contains factual allegations that are now known to be false and misleading and must be removed from the OIP. Respondent does not, however, identify new matters of fact or law that would permit a motion under Rule of Practice 200(d)(1). Because the motion addresses facts within the scope of the original OIP, the Division respectfully submits that the Commission should deny the motion with leave to refile it before the hearing officer under Rule of Practice 200(d)(2), or refer the motion to the hearing officer. The proposed amendments relate to facts that will be disputed at the hearing such that, at this juncture, the hearing officer is better situated to make the initial determinations regarding the content of the OIP.

With the exception of one sentence, the most that can be said of the allegations that are the subject of the motion is that they are in dispute. The Division submits that the overall factual allegations in the OIP are supported by the record, as the Division will establish at the hearing in this matter, scheduled to begin on October 15, 2018. The OIP has served its purpose to put Respondent on notice of the basis of the charges against him. As to the one sentence, because a witness has now provided a different version of events described in the sentence than statements made previously to the Division, the Division would not oppose a slight amendment to paragraph 21 of the OIP to change “denies” to “denied” and “does recall” to “did recall”— but aside from this cosmetic correction, no other amendments are warranted.

Accordingly, the Commission should deny the motion to amend the OIP and should deny the motion to stay pending resolution of the motion.

## BACKGROUND

### *1. The Allegations in the OIP*

On April 28, 2017, the Commission issued the OIP in this matter against Respondent David Pruitt (“Pruitt” or “Respondent”). In 2013, Pruitt was the principal accounting officer of a division of L3 Technologies, Inc. (“L3”), a major U.S. government contractor. The OIP alleges that Pruitt caused L3 improperly to recognize revenue by directing subordinates to generate invoices but withhold them from delivery to L3’s customer, the U.S. Army. The OIP alleges that Pruitt later took steps to mislead L3’s senior corporate accounting staff and L3’s auditor into believing that the invoices were delivered to the Army. The revenue associated with the invoices was improper because the criteria for recognizing revenue under Staff Accounting Bulletin 104 (“SAB 104”) had not been satisfied when the invoices were generated.

The OIP alleges that, as a result of his misconduct, Pruitt caused L3’s violations of Section 13(b)(2)(A) of the Securities Exchange Act of 1934 (“Exchange Act”), and that he violated Rule 13b2-1 of the Exchange Act, by causing L3 to fail to maintain accurate books, records and accounts that in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company. The OIP also alleges that Respondent violated Section 13(b)(5) of the Exchange Act by knowingly circumventing a system of internal accounting controls or knowingly falsifying the books, records or accounts of the company.

### *2. Pruitt’s Motion to Amend the OIP*

At issue on this motion are three allegations contained in paragraphs 21, 30, 36, and 27 of the OIP. Specifically, Pruitt challenges the following allegations in the OIP:

*Allegation 1 (OIP ¶ 21):* Pruitt challenges as materially false the allegation he acted without the approval and direction of his accounting supervisor, Timothy Keenan.

OIP ¶ 21: Pruitt and the Aerospace Systems CFO [Timothy Keenan] had a telephone call on or about Friday, December 20, 2013. Pruitt claims they discussed a one-page list of the revenue recovery claims that he purportedly emailed the Aerospace Systems CFO prior to the call. Pruitt claims that he and the Aerospace Systems CFO went down the list and the Aerospace Systems CFO instructed Pruitt which items to invoice and which to accrue. The Aerospace Systems CFO denies giving Pruitt blanket authority to invoice for the claims, but does recall a conversation in which he told Pruitt that he could invoice for work performed during option year 3 (i.e., 2013).

*Allegation 2 (OIP ¶ 30 & 36):* Pruitt challenges the allegation that the U.S. Army did not request invoices from L3.

(OIP ¶ 30): The Controller's office requested through the Aerospace Systems CFO that ASD obtain a letter from the U.S. Army indicating that ASD had permission to bill for the \$3.2 million Option Year 3 claims. In connection with seeking this letter, Pruitt received from the C-12 Contract Manager two separate email chains from late December and early January, neither of which Pruitt had been copied on previously, discussing whether L3 should invoice for all of the revenue recovery items (i.e., not just the \$3.2 million). Both email chains suggest that the U.S. Army intended for L3 to send invoices that would be paid if justified or denied. In one of the email chains, the C-12 Contract Manager specifically asks, "[j]ust to be clear . . . are you telling me to invoice (bill) the government for what we believe we are owed to start the conversation? Or are you telling me to file a claim? I see those as two different actions." The response was, "I think the first step is to invoice the Government, then a claim will follow if the invoice is denied." Neither email chain mentioned invoicing in L3's SAP system but withholding the invoice from the U.S. Army.

(OIP ¶ 36): The modified e-mail that Pruitt and the President of ASD procured from the Army Contracting Officer is deceptive, however, because it gave L3 Corporate and L3's auditor the impression that ASD had permission to invoice the U.S. Army for unresolved claims, when that was not actually the case. Pruitt knew, based on his prior conversations with the General Counsel of ASD, as well as the Army Contracting Officer's original e-mail, that the U.S. Army was not prepared to accept invoices.

*Allegation 3 (OIP 27):* Pruitt challenges the allegation that he was motivated by a potential year-end bonus.

OIP ¶ 27: ASD, with the revenue from the invoices, met the required 75% of their plan to make bonuses. Pruitt received a bonus of \$62,100 on a base salary of \$189,673 attributable to ASD achieving 75% of plan. This bonus was later rescinded by L3.

As described below, Pruitt's motion to amend the OIP does not seek to add any new facts

or law. Rather, he is in essence seeking a prehearing ruling that certain facts are not in dispute. But, aside from the tense of two verbs in one sentence, the allegations he is challenging are in dispute, as evidenced by Pruitt's own motion.

## ARGUMENT

### **I. THE ALJ IS BETTER POSITIONED TO DETERMINE THE MOTION IN THE FIRST INSTANCE**

Rule 200(d)(1) of the Commission's Rules of Practice provides that, on motion by a party, the Commission can amend an order instituting proceedings "to include new matters of fact or law." Rule 200(d)(2) provides that the hearing officer may amend an order instituting proceedings to include such new matters of fact or law "that are within the scope of the original order instituting proceedings." The Commission has stated that requests to amend an OIP to reflect "subsequent developments" "should be freely granted, subject only to the consideration that other parties should not be surprised nor their rights prejudiced." *Matter of Siming Yang*, Admin. Proc. File No. 3-15928 (Nov. 19, 2014).<sup>1</sup>

As described below, Pruitt does not in fact point to any new matters of fact or law. Rather, he essentially wants 3 allegations in the OIP to be resolved in his favor. Because those facts are within the scope of the original OIP and are so specific to facts that will be disputed at the hearing, the Division believes that the hearing officer is better situated to make the initial determinations regarding the content of the OIP. Accordingly, the Division respectfully submits that the Commission should dismiss the motion with leave to refile it before the hearing officer,

---

<sup>1</sup> Pruitt cites three cases in support of his motion. In each of those, the Division moved for the relief sought, including two cases where the motion was made under Rule 200(d)(1). Pruitt does not cite, and the Division has not identified, any prior instance of a respondent making a motion to amend an order instituting proceedings. Notably, Pruitt had previously made motions for a more definite statement (June 7, 2017) and for a ruling on the pleadings (July 18, 2017).

or refer the motion to the hearing officer.

**II. THERE ARE NO NEW MATTERS OF FACT OR LAW REQUIRING AMENDMENT TO THE ORDER INSTITUTING PROCEEDINGS**

Respondent's motion is also facially defective because, as noted above, it fails to identify any *new* matters of fact or law to be added to the OIP. Rather, Pruitt wants three allegations removed from the OIP because he contends there is no factual basis in the record for the allegations. In essence, Respondent wants a pre-hearing determination that the three allegations at issue should be resolved in his favor. This is an insufficient basis for a motion to amend the OIP under Rule 200(d).

**A. Allegation 1 that Pruitt acted without his supervisor's approval is in dispute.**

*Allegation 1 (OIP ¶ 21):* Pruitt challenges as materially false the allegation he acted without the approval and direction of his accounting supervisor, Timothy Keenan.

OIP ¶ 21: Pruitt and the Aerospace Systems CFO [Timothy Keenan] had a telephone call on or about Friday, December 20, 2013. Pruitt claims they discussed a one-page list of the revenue recovery claims that he purportedly emailed the Aerospace Systems CFO prior to the call. Pruitt claims that he and the Aerospace Systems CFO went down the list and the Aerospace Systems CFO instructed Pruitt which items to invoice and which to accrue. The Aerospace Systems CFO *denies* giving Pruitt blanket authority to invoice for the claims, but *does recall* a conversation in which he told Pruitt that he could invoice for work performed during option year 3 (i.e., 2013). (emphasis added).

Pruitt does not contend that the last sentence was untrue when the OIP was filed, but that the witnesses identified in this paragraph, Timothy Keenan, has recanted his prior statement and now has affirmed and testified that he “direct[ed] Mr. Pruitt to invoice most of the revenue recovery items and accrue for two others,” which direction “included invoicing for option years 1 and 2 of the C-12 Contract, not just option year 3.” (Respondent's Br. at 13.)

At issue is the final sentence of Paragraph 21. Had the sentence been written in the past tense, Pruitt would not have an argument that it is not accurate. But because it is written in the



present tense, Pruitt points to Keenan's recent affidavit and testimony recounting this December 20, 2013 conversation, to say that the allegation is now unfounded.

The Division contends that there is a dispute of fact as to what Keenan said to Pruitt in December 2013. Keenan's current version of events recounting that December 2013 conversation contradicts multiple prior versions Keenan provided shortly after the events occurred. Specifically, Keenan told L3 counsel, criminal investigators, and the Division's staff that, when he spoke with Pruitt in late December 2013 about invoicing revenue recovery items, he only spoke about option year 3. (H. Gregory Baker Decl. dated June 18, 2018, Ex. A, B, C.) Moreover, Keenan is subject to being impeached at trial<sup>2</sup> and it is the providence of the finder of fact at trial – the Administrative Law Judge – to determine which of Keenan's versions is factual.

Finally, Keenan's new version of events raises substantial issues of fact as to *what Pruitt told Keenan* in this conversation. While Keenan testified (at varying times in his testimony) that he instructed Pruitt to invoice for all three option years based on Pruitt having said that the customer would "accept" "valid invoices" and in fact "pay" for them. (Baker Decl. Ex. D, at 116, 121, 132.) Exactly what this means is entirely within the province of the finder of fact at the hearing, and not in the nature of a "subsequent fact" that should be amended in the OIP.

Keenan also testified that on January 7, 2014 he found out from L3's corporate controller that items for option years 1 and 2 could not be invoiced (Baker Decl. Ex. D, at 118), and that he informed Pruitt of this (Baker Decl. Ex. D, at 118), but that Pruitt did not, however, go back and

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<sup>2</sup> For example, Keenan was fired from L3 for misleading L3 corporate about a subsequent question about the revenue recovery project. Keenan also asserted his Fifth Amendment privilege against self-incrimination both during the investigation that preceded this proceeding and in a related class-action deposition. Lastly, Keenan fully understood the importance of making truthful statements when he was interviewed by criminal investigators and the Commission staff, yet his new version of events is at odds with what he said during those interviews closer in time to the events.

reverse the revenue recognized for option years 1 and 2 despite Keenan's instruction. While Keenan also testified that he "must not have been clear" when he gave this instruction, what credence and import to apply to any of this new testimony is, again, something for the finder of fact at the hearing to determine.

Most significantly, however, the fact that Keenan may have directed Pruitt to generate invoices concerning all of the revenue recovery items is a red-herring. Pruitt was the L3 employee who was responsible to ensure that L3's revenue recognition policy was followed. The Division contends that the policy was not followed. L3's accounting policy for fixed-price service contracts, such as the C-12 contract, was that revenue could be recognized only when the four requirements of SAB 104 were satisfied. SAB 104, which was embodied in generally accepted accounting principles ("GAAP"), required that revenue only be recognized when: (i) persuasive evidence of an arrangement exists (legally-binding revenue arrangement); (ii) delivery has occurred or services have been rendered; (iii) the sales price to the customer is fixed or determinable; and (iv) collectibility of the sales price is reasonably assured. (Baker Decl. Ex. E.) Even if services had been rendered for all of the revenue at issue in this case, which the Division does not concede, none of the other three criteria had been met at the time Pruitt generated the invoices at issue. Pruitt, as a certified public accountant and the principal accounting officer of ASD, was the person responsible to ensure ASD complied with SAB 104, L3's accounting policy and GAAP. Put another way, even if Keenan had directed Pruitt to generate invoices, Pruitt should not have followed such direction in contravention of SAB 104, L3's policy and GAAP.

To avoid any further dispute, however, the Division believes a slight amendment to the allegation in ¶ 21 of the OIP to change "denies" to "denied" and "does recall" to "did recall" is

appropriate to properly reflect Keenan's new version of events.

**B. Allegation 2 that the U.S. Army requested L3 to issue invoices is in dispute.**

*Allegation 2 (OIP ¶ 30 & 36):* Pruitt challenges the allegation that the U.S. Army did not request invoices from L3.

(OIP ¶ 30): The Controller's office requested through the Aerospace Systems CFO that ASD obtain a letter from the U.S. Army indicating that ASD had permission to bill for the \$3.2 million Option Year 3 claims. In connection with seeking this letter, Pruitt received from the C-12 Contract Manager two separate email chains from late December and early January, neither of which Pruitt had been copied on previously, discussing whether L3 should invoice for all of the revenue recovery items (i.e., not just the \$3.2 million). Both email chains suggest that the U.S. Army intended for L3 to send invoices that would be paid if justified or denied. In one of the email chains, the C-12 Contract Manager specifically asks, "[j]ust to be clear . . . are you telling me to invoice (bill) the government for what we believe we are owed to start the conversation? Or are you telling me to file a claim? I see those as two different actions." The response was, "I think the first step is to invoice the Government, then a claim will follow if the invoice is denied." Neither email chain mentioned invoicing in L3's SAP system but withholding the invoice from the U.S. Army.

(OIP ¶ 36): The modified e-mail that Pruitt and the President of ASD procured from the Army Contracting Officer is deceptive, however, because it gave L3 Corporate and L3's auditor the impression that ASD had permission to invoice the U.S. Army for unresolved claims, when that was not actually the case. Pruitt knew, based on his prior conversations with the General Counsel of ASD, as well as the Army Contracting Officer's original e-mail, that the U.S. Army was not prepared to accept invoices.

Pruitt contends this allegation is now known to be false because Alex Cummins (the L3 business manager on the C-12 contract) and Roderick Hynes (the program manager on the C-12 contract) have testified that the Army had requested that L3 invoice the Army (Respondent's Br. at 14-16).

Again, Pruitt is simply seeking a pre-hearing determination that an issue at the hearing should be resolved in his favor. The issue as framed in the OIP is whether the specific invoices Pruitt created or about December 27, 2013 – that were never delivered to the Army – met L3's requirements for revenue recovery. Ancillary to that issue is whether the Army had agreed to

pay for any of the amounts in the revenue recovery initiative and would accept invoices for those amounts. At the hearing, the Division will present the Army contracting officer, Karen Fletcher, who has stated in an interview with the criminal authorities and the staff that it was premature to invoice. As discussed at OIP paragraphs 33-36, she made it clear that it would be premature to send invoices as late as January 17, 2014. Specifically, Fletcher stated that “It would be an exercise in futility to submit invoices for these requested contract funding adjustments at this point, as they would be rejected by the DCMA<sup>3</sup> Administrative Contracting Officer.”

Moreover, Karen Fletcher did *not* direct L3 to submit invoices to her “instead” of through Wide Area Word Flow (“WAWF”),<sup>4</sup> as Pruitt contends at (Respondent’s Br. at 7), but directed that L3 submit “proposed invoices” to her to review, along with supporting documents, and, if approved, then the actual invoices could be submitted into WAWF.

As to the supposed “new” facts Pruitt claims warrant amending the OIP, what inferences should be made from that evidence will be contested. Specifically, Hynes testified in his affidavit that, at a December 18, 2013 meeting, the Army stated that if L3 believed it was owed money for services, then L3 should submit invoices and supporting documentation to the Army “for review.” (Aff. of Jimmy Fokas, Ex. E (emphasis added).) Pruitt cites to no evidence supporting that he was even informed of this undocumented oral request prior to creating the invoices at issue here. (See Respondent’s Br. at 7-8, 14-15.) In contrast, when Pruitt was questioned at the time he ordered the creation of the invoices by key witnesses who will appear at the hearing, he did not refer to this request. (Baker Decl. Ex. F.) Moreover, Pruitt’s reliance on Lieutenant Colonel Jonathan Frasier’s December 30, 2013 email is of dubious relevance

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<sup>3</sup> DCMA refers to the Defense Contract Management Agency. See <http://www.dcma.mil>.

<sup>4</sup> WAWF refers to the government’s web-based system for electronic invoicing, receipt and acceptance. See <https://wawf.eb.mil/xhtml/unauth/web/homepage/functionalInfo.xhtml>.

given that it requests that L3 “*submit*” invoices, *i.e.*, actually deliver them, and that the invoices be submitted through the “*appropriate channels*” (emphasis added) whereas Pruitt, the Division will argue, did not submit the invoices created in December 2013 through appropriate channels or at all. But this is all argument, subject to adjudication by a fact finder, which is the province of the ALJ, not appropriate for a motion to amend the OIP.

**C. Allegation 3 that Pruitt was motivated by the possibility of receiving an incentive bonus is in dispute.**

*Allegation 3 (OIP 27)*: Pruitt challenges the allegation that he was motivated by a potential year-end bonus.

OIP ¶ 27: ASD, with the revenue from the invoices, met the required 75% of their plan to make bonuses. Pruitt received a bonus of \$62,100 on a base salary of \$189,673 attributable to ASD achieving 75% of plan. This bonus was later rescinded by L3.

Pruitt’s position on Allegation 3 is as follows: Keenan has provided testimony that it is “not accurate for anyone to say that in December 2013, the issuance of invoices by Mr. Pruitt solely caused ASD to reach the 75% bonus threshold,” because the threshold was reached as a result of management’s decision to shift costs and expenses. (Keenan Aff. ¶ 16.) Further, Keenan has stated that “Pruitt was not involved in these discussions, nor could he have known in advance what, if any, adjustments would be made.” (Keenan Aff. ¶ 15.)

Pruitt’s argument is simply illogical. Pruitt’s motive must be assessed at the time the invoices were created (*i.e.*, December 2013) and not some later time when adjustments may have been made by others to achieve that number. The fact that Pruitt “could [not] have known in advance” of the specific later adjustments only shows that Pruitt had every incentive to do what he could at the time to attain the key 75% of plan number. As the OIP alleges, and as the Division will prove at trial, Pruitt was keenly aware of the threshold ASD needed to make and in

fact spoke with Keenan concerning the process of making adjustments so he and others would receive management incentive bonuses. Pruitt even memorialized the discussion in an email on January 8, 2014. (Baker Decl. Ex. G.)

Keenan's own recent testimony establishes this fact. Keenan states that the issuance of invoices by Pruitt did not "solely" cause ASD to reach the 75% bonus threshold and that Pruitt did not know what adjustments were made in order for Pruitt to receive a bonus. But at his subsequent deposition, Keenan said that the issuance of the invoices "certainly" played a part in reaching the bonus threshold, that he discussed with Pruitt proposed adjustments that Pruitt wanted to make to reach the threshold, and that the only thing he did not discuss with Pruitt was which adjustments were actually made. (Baker Decl. Ex. D, at 179, 197-98.)

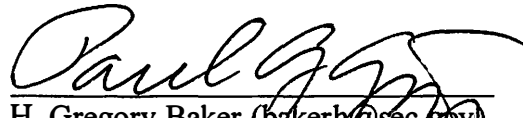
In light of this, it is clear that the hearing officer will be asked to make findings concerning whether Pruitt was motivated by the potential for a bonus in deciding to run the disputed invoices. Pruitt's motivation cannot be resolved pre-hearing.

**CONCLUSION**

For the foregoing reasons, the Division respectfully requests that Respondent's motion to amend the OIP and to stay this proceeding pending a decision on the motion to amend be denied. Alternatively, the Division respectfully requests that Respondent's motion be denied with leave to refile before the hearing officer, or be referred to the hearing officer. Finally, if the Commission (or hearing officer) deems that any change is warranted to the OIP, the Division would not object to changing the words "denies" to "denied" and "does recall" to "did recall" in paragraph 21 of the OIP.

Dated: June 18, 2018  
New York, NY

DIVISION OF ENFORCEMENT

By:   
H. Gregory Baker (bakerh@sec.gov)  
Paul G. Gizzi (gizzip@sec.gov)  
David Oliwenstein (oliwensteind@sec.gov)  
Securities and Exchange Commission  
200 Vesey Street, Suite 400  
New York, NY 10281  
212-336-1100

**CERTIFICATE OF SERVICE**

I hereby certify that on June 18, 2018, I caused the original and three copies of the foregoing DIVISION OF ENFORCEMENT'S MEMORANDUM IN OPPOSITION TO RESPONDENT'S MOTION TO THE COMMISSION TO AMEND THE ORDER INSTITUTING PROCEEDINGS and accompanying Declaration of H. Gregory Baker to be filed:

Brent J. Fields  
Secretary  
Securities and Exchange Commission  
100 F Street NE, Mail Stop 1090  
Washington, DC 20549

I further certify that I caused to be served a copy of the foregoing via email upon:

David Pruitt  
c/o John J. Carney, Esq.  
BakerHostetler  
45 Rockefeller Plaza  
New York, NY 10111

I further certify that I caused a courtesy copy of the foregoing to be provided by email to:

The Honorable James Grimes  
Administrative Law Judge  
Securities and Exchange Commission  
100 F Street NE, Mail Stop 2582  
Washington, DC 20549

  
Paul G. Gizzi



**UNITED STATES OF AMERICA  
Before the  
SECURITIES AND EXCHANGE COMMISSION**

**ADMINISTRATIVE PROCEEDING  
File No. 3-17950**

**In the Matter of,  
  
David Pruitt, CPA,  
  
Respondent.**

**DECLARATION OF H. GREGORY BAKER, ESQ. IN SUPPORT  
OF THE DIVISION OF ENFORCEMENT'S OPPOSITION TO  
RESPONDENT'S MOTION TO AMEND THE ORDER INSTITUTING PROCEEDINGS**

I, H. Gregory Baker, pursuant to 28 U.S.C. § 1746, declare as follows:

1. I am presently employed as Senior Counsel in the Division of Enforcement in the New York Regional Office of the Securities and Exchange Commission. I submit this declaration in support of the Division of Enforcement's Opposition to Respondent's Motion to Amend the Order Instituting Proceedings.

2. A copy of a memorandum, dated April 18, 2016, reflecting the Division's summary of an interview with Timothy Keenan that occurred on April 12, 2016, is attached hereto as Exhibit A.

3. A copy of the [REDACTED], is attached hereto as Exhibit B.

4. A copy of the [REDACTED], is attached hereto as Exhibit C.

5. A copy of relevant excerpts from the transcript of the May 2, 2018 Deposition of Timothy Keenan is attached hereto as Exhibit D.

6. A copy of a document entitled "Corporate Accounting Policy No. 102" is attached

hereto as Exhibit E.

7. A copy of a December 31, 2013 email from [REDACTED] to Robert Hayes, bates-stamped L3-DOJ-SEC-0000000210-11, is attached hereto as Exhibit F.

8. A copy of a January 8, 2014 email from David Pruitt to Mark Wentlent, bates-stamped L3-DOJ-SEC-0000457693, is attached hereto as Exhibit G.

I declare under the penalty of perjury under the laws of the United States of America that the foregoing is true and correct, to the best of my knowledge.

Executed on June 18, 2018 in New York, NY.



H. Gregory Baker  
U.S. Securities and Exchange Commission  
200 Vesey Street, Suite 400  
New York, NY 10281  
Phone: (212) 336-9147

# EXHIBIT A



UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
NEW YORK REGIONAL OFFICE  
200 Vesey Street  
Suite 400  
NEW YORK, NY 10281

MEMORANDUM

To: Files  
From: Adam Dwyer, Intern  
Date: 04/18/2016  
Re: (NY-09140) L-3 Communications, Inc. Proffer meeting with Tim Keenan on 04/12/16.

**I.e Introduction**

This memorandum summarizes a proffer meeting with Tim Keenan on April 12, 2016. This meeting was conducted from the SEC's New York Regional Office ("NYRO") located at 3 World Financial Center in New York, New York. This is the author's account and summary of the conversation, and is not a verbatim transcript. Mr. Keenan spoke directly to NYRO attorneys; however, he was represented by his attorney John Teakell. Steve Rawlings, Greg Baker, David Oliwenstein, Paul Gizzi, Chris Mele and I were present for the Commission. At the start of the interview, Mr. Keenan was provided with a copy of his proffer agreement, and reminded that statements could be used for impeachment purposes in the event of a trial, or as a basis for investigation other evidence. Mr. Baker also clarified that information could be shared by the Commission with groups such as the U.S. Attorney's Office to be used under the same terms as those found in the proffer agreement. Mr. Keenan was also provided SEC Form 1662. Mr. Baker asked if Mr. Keenan had any questions pertaining to Form 1662, and he did not. Mr. Keenan was informed that his answers, though voluntary, must be truthful.

**II. Background**

**a. Personal**

Mr. Keenan attended The University of California at Northridge, graduating in 1987 with a degree in accounting. Mr. Keenan worked for Menasco from 1985 until 1997, beginning as an intern in Burbank, CA, and later taking a position as a staff accountant. Mr. Keenan was transferred to Ft. Worth in 1990. From 1997 to 2000 Mr. Keenan worked for Hamilton Sundstrand in East Windsor, CT.

**b. L-3 Communications**

1 EXHIBIT 19 PLTF.  
WITNESS Keenan DEFT.  
CONSISTING OF 17 PAGES  
DATE 5-2-18  
BEHMK READING AND VIDEO SERVICES, INC.

SEC-SEC-E-0006584



UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
NEW YORK REGIONAL OFFICE

200 Vesey Street  
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In 2000 while visiting former co-workers at Manesco, Mr. Keenan was told by a former employee of his Cheryl Pugh that a headhunter had called her about a job with L-3 Communications which she could not take. Mr. Keenan contacted the headhunter, and was hired as an accounting manager in the Link Simulation and Training division. Mr. Keenan was promoted to Assistant Controller, then Controller and finally VP of Finance. In 2011 Mr. Keenan moved to the Aerospace group taking the title of Senior VP of Finance and CFO. Mr. Keenan was terminated by L-3 Communications on July 30, 2014 when he was stripped of his stock and pension, but no bonus was clawed back. Mr. Keenan does not hold any professional licenses (including CPA). He does not sit on any boards or hold other positions except as VP of his wife's real estate company which is his current employer in Dallas, TX.

L-3 was structured with four sectors, Aerospace, National Security Systems, Communication Systems and Electronics Systems. Aerospace was the second largest and second most profitable sector. The President of Aerospace was John McNellis to whom Mr. Keenan reported. Under Mr. McNellis were three groups, ISR headed by Mark von Schwarz, Platform Systems headed by Nick Farah and Logistics Systems headed by Gordon Walsh. Logistics Systems had been the home of Vertex and Army Fleet Supply (AFS) until Mr. Walsh split Army out of Vertex to create Army Sustainment Division (ASD). Logistics Systems was probably the smallest of the three groups at \$1B- \$1.2B; Platform had similar revenues, while ISR had roughly \$2B-\$2.2B in revenue.

Within the three groups there were between seven and nine divisions. Platform included WAC, MAS, Crestview and Aeromet while Logistics included ASD, AFS and Vertex. ASD was the smallest of the three divisions and in the bottom third of all Aerospace divisions. The division culture was fairly autonomous and Mr. Keenan was rarely involved in division level work; mostly he dealt with divisions after he got reports up the chain. He did not have an SAP logon, his role was to provide support for the various divisions and interact with corporate on their behalf.

Mr. McNellis was an officer of the company, Mr. Keenan understood Holly Clark the General Counsel of Aerospace to also be an officer as she could sign on behalf of the company. Kevin Coffman who was in charge of Business Development was not an officer, nor was Mr. Keenan. Mr. Keenan was not sure where it would be memorialized that Ms. Clark and Mr. McNellis could sign on behalf of the company.

Mr. Keenan also had dotted line reporting to Ralph D'Ambrosio the Corporate CFO and Dan Azmon the Controller and Chief Accounting Officer. Mr. Keenan interacted with both men,



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though more often with Mr. Azmon, he met Mr. D'Ambrosio at least at the quarterly meetings. Mr. D'Ambrosio was responsible for the strategic decisions such as buybacks of stock, and earnings reports. Mr. Azmon was responsible for making sure the corporation's books were in order.

According to Mr. Keenan, Mr. D'Ambrosio and Mr. Azmon were never involved on the division level. Mr. Keenan's staff would use something called Hyperion to process SAP data and report to Azmon. Mr. Keenan also reported at Corporate Business Reviews originally held quarterly and then switched to three times a year with the fourth folded into the budget meeting. These meetings took place at the corporate headquarters in New York and included Mr. Keenan, Mr. McNellis and the other three Sector Presidents.

Mr. Keenan was asked about Mr. Walsh, and replied that Walsh did not report to him, but directly to Mr. McNellis. Mr. Walsh had previously held the position that became Mr. Keenan's for five or six years and was a CPA. Mr. Walsh told Mr. Keenan that he wanted to move from finance into operations, which he could not do at Link because the head of Link only wanted engineers for those positions. Mr. Keenan believes that Mr. Walsh was "pretty good" at his operations role in Logistics Solutions. He did not believe that Mr. Walsh could have headed either of the other groups because of the technical awareness needed for the job.

### III. The Army C-12 Contract

According to Mr. Keenan he first learned of the C-12 contract in 2011 when he joined Aerospace and toured all of the divisions. C-12 was a fairly new contract, and Rich Nordstrom had put the first Estimated at Completion (EAC) report together four or five months earlier. Mr. Nordstrom was an expert in EACs, and had been with L-3 for many years; Mr. Keenan described him as "a bull in a china shop." An EAC is created by gathering the contract requirements in terms of people, materials and support required by Contract Line Item Number (CLIN), combining that information with revenue to be received and create estimates to help recognize revenue. An EAC is created at the beginning of the option year usually with a lower level of detail, and then is monitored and updated at least quarterly. The EAC is only good for that year, so in the case of C-12 which is a base year plus four option years a new EAC is created for each option year taking into account the previous year.

According to Mr. Keenan the problems with C-12 began with the heavy maintenance CLIN. Under the contract a certain amount of fixed maintenance on aircraft was done in the field, called A and B checks. Heavier maintenance such as a D check which involved stripping down an aircraft was done at a facility under the heavy maintenance CLIN. Heavy maintenance



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was supposed to be done on a cost plus basis (labor cost is paid plus a premium, materials are part of a separate billing) with six months' notice from, the Army.

What began happening was that the Army would send planes with six days or sometimes even no notice. According to Mr. Keenan this unscheduled heavy maintenance would have gone into the over and above CLIN, which held excess (mostly labor) for other CLINs. The repair facility should have given the Army a list of what needed to be fixed, with a cost and gotten approval in the form of an Authorization to Proceed (ATP).

Mr. Keenan said that what was happening is that when the plane was stripped down, ASD would find problems and tell the Army what needed fixing and ask for over and above hours. The Army would say that the problems should have been noticed in the field and not authorize the hours. Since the plane needed to go out and ASD can't send out pilots in planes with problems, or certify the planes under the contract the repairs would be made. The next step according to Mr. Keenan would be to put in a claim for the work with the Army. However, ASD was not doing a good job of following up with the Army. Work was being done for which ASD was not paid. This was a point where ASD maintenance and the ASD contracts group should have gotten together with the Army to show why L-3 was entitled to be paid, this was not happening according to Mr. Keenan.

After the second quarter of 2013, Mr. Keenan, Mr. McNellis, Ms. Clark and Mr. Coffman went to the various division locations to get a quarterly review of the division. Mr. Keenan says that in one of these meetings (sometime between July and September) in trying to figure out how ASD was losing money on a cost plus contract, Mr. Walsh brought up the issue of the field not properly following the contract. The C-12 contract was low profit from the beginning with an expectation of 1% to 2%, compared with Ft. Rucker which was at 4% to 6% at the time.

According to Mr. Keenan, Mr. Walsh told his people at ASD that they needed to find documentation for the work done. Mr. Walsh and Mr. Wentlent formed a team in July or August to go through the contract, get a legal opinion of reimbursement options, file claims, and put the contracting officer on notice that going forward they needed to make changes to how they received approvals. The team was made up of Ken Lassus, Rick Schmidt, Dave Pruitt and Alex Cummins. Mr. Wentlent was in charge of the team, but most of the actual supervision was done by Mr. Schmidt.

The project was presented as a way to turn around a struggling contract, as Mr. Walsh and Mr. Wentlent had found the billing issues when they were looking for a way to make C-12 profitable. To make a claim ASD would present the relevant contract clause to the Army with



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documentation supporting that the work had been done and was subject to the clause. This would be submitted for an equitable adjustment, and after negotiations the money would be put into the over and above CLIN. This process could take as much as six months to two years depending on the client and who involved wanted to slow it down. The over and above CLIN was initially given only token funding, and funding would then be added once the customer approved a charge.

Another concern at this meeting which led to re-examining the C-12 program was a building WIP (Work in Progress) balance, something that had been addressed with Mr. Pruitt at previous meetings. According to Mr. Keenan, he would find out much later that one reason for the problems was that Mr. Pruitt was not producing the EACs that he was supposed to. The EAC was necessary to create the annual operating plan; it allowed ASD to project and record revenue, and see if there were losses so that they could be addressed. The EAC should have been produced for each option year (L-3 would know usually 60 days ahead of time that there would be a renewal), and Mr. Pruitt was representing to everyone at the group meetings that they were done, including signing the certifications required under Sarbanes Oxley.

Mr. Keenan said that he found out about the EAC issue in May of 2014 when he and Mike Miller went to look into other issues. Mr. Schmidt said that they hadn't claimed to have EACs, that there hadn't been one done since the 2011 EAC by Mr. Nordstrom. According to Mr. Keenan, Mr. Schmidt claimed that they used sales and cost on slides they produced, so Mr. Keenan assumed that Schmidt knew and didn't tell anyone. The slides presented at the meetings did have columns for EAC and contract value according to Mr. Keenan. Paper "EACs" were produced to Mr. Keenan, but they were not what they should have been, and Mr. Miller discovered that they had never been entered into SAP anyway. Mr. Keenan said that he remembered being upset because there was no justification to not have an EAC, as it was company policy and representations were made to PWC that they were done.

Mr. Keenan noted that if Mr. Pruitt's team was unsure how to handle an EAC they could have told Mr. Keenan and he could have gotten someone to help them whether from another division or by having Mr. Nordstrom brought in. Mr. Keenan said that he asked Mr. Schmidt why he didn't call about the EAC issues, and Mr. Schmidt told him that he "didn't want the retaliation from Walsh." Mr. Keenan noted that he had a good relationship with Walsh because he was always straight with him and never overpromised but also never slacked off. Mr. Keenan categorized Mr. Walsh as very intelligent, but also without any patience for people he felt weren't getting things done.





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Mr. Keenan was asked how Mr. Wentlent could have missed that his division was not correctly producing EACs, he answered that Mr. Wentlent doesn't know anything about accounting and could be easily confused by the documents produced.

WIP includes unbilled receivables, labor, and materials and overhead; by not writing them off in terms of revenue the WIP builds up, and eventually at year end hits profits, reduces margin. Not producing the EAC builds up the WIP because projections are being overstated. However some of the WIP could be matched with a legitimate claim, which would allow ASD to eliminate the WIP once the Army agreed to pay.

#### IV. The Revenue Recovery Plan

According to Mr. Keenan, once the team was established Mr. Walsh encouraged them to go back and find all the money that ASD might be entitled to under the contract. Mr. Keenan recalled only being involved in approximately three update calls during the summer and early fall. The team's findings were discussed on October 8, 2013 for which a PowerPoint was produced (BATES ending 35322). The WIP showed a very high balance for the Cost per Flight Hour (CPFH) CLIN for Option Year 2 (OP2) which covered February of 2012 through January of 2013. CPFH is the hourly fee for flights under the C-12 contract, if the hours are too low ASD can't make a profit. The high number is surprising since you should know where you are on CPFH every month. The operations people in the program would say "they fly what they fly", but anything outside a threshold of +/-10% should have been brought to the contracting officer to deal with. The program management team of Mr. Schmidt, Mr. Lassus (who would deal with contracts) and the business manager Mr. Cummins should have known about the buildup and told someone.

The presentation included a summary of WIP exposure, which showed a number of ATPs where the Army had agreed to pay, as well as a category of recoveries that the team had determined they were entitled to at a rate they expected to get out of the claim. Mr. Pruitt put the final numbers together, and it included EAC. Mr. Keenan is not sure where the numbers used for EAC profit and cost came from as there was no EAC produced. Cummins was responsible for assisting in making the EAC, but according to Mr. Keenan his idea of an EAC was not what an EAC was. In May Mr. Cummins provided his EACs to Keenan, they were summary in nature, contained no real backup and had not been entered into SAP. The recovery of CPFH was to be handled by a team led by Mr. Cummins and including Delayna Shepard. It was projected that there would be agreements on some elements allowing ASD to bill as receivable before the end of the year. Mr. Keenan said that he was not optimistic due to the time involved and changing



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schedule. He pointed to a projection of closing a matter in a week which estimated 100 hours needed to close. The data needed to be culled manually which was a time consuming process.

**a. Cash Variance**

Mr. Keenan was showed a pair of emails from Shannon Nichol the Director of Financial Planning and Analysis on which he was copied (BATES ending in 218250 and 335549). Mr. Keenan explained that Mr. Nichol was providing a variance analysis that was done on the division and group level to Mr. Miller. The October 24, 2013 email was about Mr. Miller wanting more detail on why there was a -\$24M variance in cash flow for Logistics Solutions. Mr. Keenan stated that he usually gets a book after this process so he isn't very involved unless Mr. Miller asks him to go to a division and figure out an issue. Groups tend to be judged on four criteria: bookings, sales, profit and cash. Mr. Miller was looking for more clarity in case he needed to talk about the cash variance.

Mr. Keenan noted that the explanation from Mr. Pruitt was strange, in that it accounted \$20M due to delays in "definitizing" C-12 Army proposals and REAs. Proposals refer to a situation where the Army has yet to make a decision on what they are going to do on over and above expenses. Mr. Keenan stated that unless almost all of the \$20M was from proposals and not REAs it was a bad decision to include it in Q3 numbers. Mr. Keenan knew that the REAs had not been submitted yet, and with the turnaround time involved would not be paid in Q3.

Mr. Keenan was not sure if this explanation from Mr. Pruitt was supplied to investors. He believes it is possible that it was mentioned on a monthly conference call, but usually division level numbers were not discussed unless there was very large scale variance such as \$70M or more.

**b. October Group Operations Meeting**

Mr. Keenan believes he attended the ASD meeting and saw the slideshow presented (BATES ending 0003). Mr. Keenan stated that most of the presentation was more of a marketing plan of going out and looking for new business. He did not that there was some information of the STF, an as of date projection for Q4 and full year projections from the AOP. They were projecting an actual cash number of \$-12.6M. Mr. Keenan did not remember any discussion of why there was an estimate of Q4 receipts of \$54.4M, but looking back at the presentation and seeing the REAs listed on downside he did think it unusual to project a number \$12M above the best quarter. Mr. Keenan recalled that in this time period there were several meetings where Mr. Walsh was upset about WIP and asked why the process wasn't going faster and going further, he also would say



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that there were no excuses not to get it done. During this time Mr. Keenan and Mr. Walsh discussed doing a new physical inventory.

**c.a Accrual and Legal Entitlements**

According to Mr. Keenan in November Mr. Pruitt and ASD were determining what to recognize and how. On November 15, 2013 they sent new numbers to Laurie Gandy who worked for Mr. Nichol doing much of the heavy lifting in terms of computer work. ASD wanted those changes to go into the Phase I and Phase II reports that were going to be given in New York. Mr. Keenan refused because it was too close to one of the three dry runs he was doing. Mr. Pruitt wanted to accrue additional revenue recovery, but Mr. Keenan told them to wait so that it could be looked at after the dry run.

Mr. Keenan noted that this was followed by a conference call on the legal entitlement issue on November 22, 2013. The process discussed at that meeting was that the contract experts would find clauses in the contract that entitled ASD to payment show that the government did not follow the clause and then determine what to submit as an REA, and estimate based on the history what will actually get paid. Once there had been a legal determination that ASD was entitled to payment then an REA would be submitted.

According to Mr. Keenan Mr. Pruitt and Mr. Walsh asked if revenue could be recognized based on this legal entitlement. Mr. Keenan asked Mr. Azmon who told him that because this was not SOP 81-1 but instead under SAB 104 it could not be recognized. The contract was not SOP 81-1 because of a number of factors including that it was only one year, it did not include design or development and it mostly dealt with staffing or labor. Mr. Azmon told Mr. Keenan that ASD could only recognize revenue for what they could invoice, Mr. Keenan passed this information to Mr. Pruitt and Mr. Walsh. Under SOP 81-1 ASD would have been able to change the EAC based on what was earned and record it as unbilled revenue until the Army signed off on it being invoiced so long as ASD was legally entitled and it was more probable than not that it could collect.

On the conference call Pruitt provided a draft briefing (BATES ending in 35235) which showed the REA amounts that ASD thought they should get, and the amount that Steve Sinquefield and Mr. Lassus came up with as likely under legal entitlement. Mr. Keenan is not sure if he received this document before or after the first time he spoke with Mr. Azmon. Mr. Keenan did remember that he thought page 6 of the document was the craziest thing he'd ever heard. That was because Mr. Pruitt wanted to book all \$30M of the legal entitlement. It was Mr. Keenan's impression that Mr. Pruitt was the driving force behind the aggressive revenue



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recognition strategy. However, he did think it was possible that Mr. Pruitt went to Mr. Walsh and told him that ASD was not going to make the year, and Mr. Walsh told him to go back and find a way. Mr. Keenan recalls telling Mr. Pruitt that booking all \$30M was not going to fly, and that he could only recognize revenue for things he could invoice.

According to Mr. Keenan, Mr. Pruitt came back and told him that the customer had said that they would allow him to invoice everything in the current year. Mr. Keenan acknowledged that as fine so long as he had confirmation from the contracting officer. He thought that the process of not putting invoices into WAWF but instead walking them over was strange, but believable. Mr. Keenan thought that the only option for the other years being recognized sooner would be to try reversing some of the costs so long as Mr. Azmon approved the plan, which he did not.

Logistics Systems continued to have a cash problem at this time, but Walsh told Mr. Nichol that "Superman is scheduled to show up around Dec. 31..." Mr. Keenan said that he thought this was Mr. Walsh jokingly saying that he was expecting and hoping to have a large amount of cash come in late in the month, he did not recall if this conversation about cash and the \$5.5M in STF increase that Mr. Walsh wanted to include were related to revenue recovery. Mr. Keenan stated that if Mr. Walsh thought he was going to have some increase in sales and cash receipts he could change the STF if he wanted to. Mr. Keenan may have spoken about this in-person with Mr. Walsh, as their offices, while on opposite sides of the building, were not that far apart. However, Mr. Walsh traveled frequently and was usually in the office only 2 days a week.

Mr. Keenan was asked about the ASD operations meeting held on December 3, 2013. He indicated that he would not have attended that meeting or received the PowerPoint presentation given there (BATES ending 00048). Looking at the December STF numbers presented at that meeting, Mr. Keenan noted the large jump in C-12's projected sales of \$8M and EBIT of \$5.4. He speculated that this was estimated so as to not show that ASD was going to miss the year. Mr. Keenan said that he was not in any meetings that discussed achieving those numbers through revenue recognition and only knew that Mr. Pruitt said that he could invoice the current year. Mr. Pruitt also told him at some point that the contracting officer was on Christmas leave so the invoices hadn't been brought over yet.

According to Mr. Keenan on December 5, 2013 Mr. Pruitt sent him a document detailing the legal entitlements and the proposed treatments. Mr. Keenan noticed that in some Mr. Pruitt had proposed accruing more than the legal entitlement and as such made changes and sent it back



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to Mr. Pruitt. Based on the document Mr. Keenan expected Mr. Pruitt to bill for Option Year 3 (OP3) items. The proposed accrual amounts for other option years was under the theory of reversing costs that had been written off, which at this point he had yet to discuss with Mr. Azmon. An REA would then be submitted for those costs and an invoice created after the customer agreed to fund the over and above CLIN. The currently billable matters were the CPFH beyond the 10% threshold and two other OP3 categories which Mr. Keenan had been told the Army would accept invoices with backup on then proceed through the WAWF process.

Mr. Keenan was asked about an email on which he was copied from Mr. McNellis to Fred Piccirillo (BATES ending 00140) in which an entitlement letter was discussed as necessary to document anticipated recovery. Mr. Keenan stated that the email was about the separate physical inventory issue. It had been claimed that the inventory was incorrect so Mr. Keenan and Stuart White looked at the inventory and deemed that it appeared to have been done appropriately. Mr. Keenan and Mr. Azmon decided to do a new physical inventory and not to make adjustments until that inventory was complete. The issue Mr. Keenan remembered was that parts were supposed to be put back into inventory after repair, but there had been a problem with properly accounting for these parts. It was decided not to write off the materials because there was another inventory upcoming. Mr. Keenan stated that he is not sure what was meant by the phrase "recover the cost." Mr. Keenan stated that the revenue recovery project never needed or produced a legal entitlement letter.

During December Mr. Keenan attended meeting about revenue recovery every two weeks. In the PowerPoint for the December 13, 2013 meeting (BATES ending 00141) Mr. Pruitt listed submitted actions. Mr. Keenan noted that three of the claims totaling \$4M were submitted, but the largest, \$9.3M for PMO support had not, and the PowerPoint is internally inconsistent regarding whether it was. Mr. Pruitt also created a list of intended recovery actions totaling an additional \$37.3M. According to Mr. Keenan there was no discussion of invoicing these, only the current year. Pruitt said that he was invoicing approximately \$5M for the current year. Mr. Keenan did not remember Mr. Pruitt saying that he wasn't doing the other years, but Mr. Keenan had told Mr. Pruitt he could only recognize revenue he could legally invoice.

Mr. Keenan stated that he never told Mr. Pruitt to put invoices into SAP but not into WAWF, and did not know that was occurring until April 2014, when Mr. Azmon, Mr. Miller and Kathy Press called him about the practice. According to Mr. Keenan Mr., Pruitt told him that the contracting officer requested that process when she met with him and Mr. Lassus. According to Mr. Keenan, Mr. Pruitt told him that they expected to get everything for OP3 done by the end of Q1, and the rest had to be filed as claims. Mr. Keenan stated that he asked if the contracting



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officer had returned from leave, told that she had he told Mr. Pruitt to get the invoices over to her right away. Mr. Pruitt also told him that they waited to submit invoices until Kim Gilles was replaced as contracting officer. Mr. Keenan stated that he never saw the invoices created but that Mr. Miller told him about them in May. At around this time a replacement for Mr. Pruitt was being sought. It was felt that Mr. Pruitt was over his head, the reasons included his failure to report up the walkover invoice procedure and his delay in executing it. Additionally he had difficulty answering questions he should have had the answers to at operations reviews.

Mr. Keenan discussed with Mr. Azmon sometime around January 7, 2014 the idea of putting some of the written off costs back on the book for the 2013 adjustments. Usually the books can stay open for up to two and a half weeks for adjustments. Mr. Keenan also noted that sometimes PWC will find something in the audit that requires re-opening the books.

Mr. Keenan was shown a series of emails he exchanged with Mr. Pruitt on January 7, 2014 (BATES ending 00218). Mr. Keenan explained that he was telling Mr. Pruitt to reverse entries for accrual based on SAB 104 and telling him to put the invoiced OP3 revenue of \$2.8M and \$450k into the "billed A/R" category. When Mr. Pruitt responded asking if he meant unbilled Mr. Keenan asked for a phone call. According to Mr. Keenan, on that call he reiterated that Mr. Pruitt was only to record those invoices from OP3 which he had invoiced and walked over. Mr. Keenan stated that he told Mr. Pruitt to do what he had said he would and they had discussed earlier. Everything was pulled off the books, and then the period was re-opened and the \$2.8M and \$450k were added to billed A/R.

Mr. Miller asked for a letter from the contracting officer according to Mr. Keenan to verify that the customer would be accepting the two invoices for \$2.8M and \$450k. The letter was not supposed to be about the rest of the legal entitlement that would be claimed. Miller was looking to document that the customer agreed to accept before the recognition would be allowed. According to Mr. Keenan, Mr. Pruitt said that he would get the letter. On January 11, 2014 Mr. Pruitt forwarded two emails to Mr. Keenan from Craig Sabourin. Mr. Keenan was not that happy with the response, he wanted a clear and concise statement that ASD could bill the government. Mr. Keenan stated that he was a little concerned by the language because if it wasn't more firm Miller might say that the \$3.25M had to be removed from the books. The reference to the invoice being denied and followed by a claim was not that concerning because while it was a little different from what Pruitt had explained it was only an issue if the backup wasn't correct. Mr. Keenan did not notice at the time that Mr. Sabourin thought that the invoices had not been submitted, but he probably wouldn't have been concerned because Ms. Gilles was



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supposed to be dealing with them. Ms. Gilles was still the contracting officer until February or March.

Mr. Keenan had a call with Mr. Walsh on January 17, 2014 about the issue of getting a letter from the government. According to Mr. Keenan he was asking why it was so hard to just get a letter saying that ASD could invoice for the \$3.25M in OP3 revenues. Mr. Walsh talked to Mr. Wentlent who said that he would get into it with his staff.

Mr. Keenan was asked about an email from Mr. Pruitt on that day updating him on the process of getting the letter. Mr. Keenan stated that while the items Mr. Pruitt mentions are from OP1 and OP2, he knew that those discussions were ongoing for the purpose of submitting REAs, and he thought that the important part was the contracting officer's impression of the quality of the backup. Mr. Keenan stated that looking back he can see the interpretation that Mr. Pruitt was invoicing those items, but at the time he thought it was a reference to going over REAs with the contracting officer which she could have approved and then would be invoiced.

Mr. Keenan was then sent an email that Mr. Lassus had sent to Karen Fletcher detailing the agreed upon process and approval of invoices which Mr. Keenan understood was only for OP3 items, as well as her confirmation. According to Mr. Keenan he was unaware of a previous draft of the email in which Ms. Fletcher called the process an "exercise in futility." In May he would be told by Mr. Lassus that Mr. Lassus had written the emails and sent them to Ms. Fletcher to copy and paste before sending back. Mr. Keenan stated that as of January he had no concerns; now that the Army had confirmed he expected the process to be completed by the end of January for the \$3.25M. Mr. Keenan stated that if the Army had not confirmed or if he had known at the time that the invoices had not been delivered he would have pulled that revenue out of the 2013 numbers.

Mr. Keenan was asked how something billed in 2014 could be recognized in 2013. He answered that because the revenue was earned in 2013, and the customer had agreed to allow it for OP3 he could have corporate go back and open December of 2013 and book the revenue.

During the conversations about obtaining a letter from the Army, Mr. Walsh asked Mr. Keenan what the impact on bonuses would be if they could not get confirmation. Mr. Keenan sent an email noting that without the \$3.25M the bonus requirement of 75% would be narrowly missed.

At the January 23, 2014 operations review meeting there were discussions of the issues surrounding the C-12 contract, Mr. Keenan believes that both the division and group level



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meetings were together; however his version of the PowerPoint presented at that meeting differs in some ways from the one produced to the Commission. Mr. Keenan stated that Mr. McNellis, Mr. Schmidt, Mr. Walsh, Mr. Wentlent and Mr. Coffman attended. Mr. Lassus was present, but Mr. Pruitt did all of the talking in terms of presenting information according to Mr. Keenan. Mr. Pruitt indicated that the Army had agreed to the invoices and was auditing them. Mr. Keenan understood from this meeting that the OP3 invoices had been delivered and that REAs were being sent. He thought that skipping WAWF was a little strange, but the “chummy” relationships that the contracts people and contracting officers sometimes had made it possible.

According to Mr. Keenan, he took the numbers listed under OP1 and OP2 as invoiced in the division PowerPoint (BATES ending 00261) to mean that an REA had been submitted. He based this on talking with Mr. Pruitt about meetings with the Army going well, he did not notice the use of the word invoice. Mr. Keenan stated that he believed that on these issues the Army had the entire backup and was agreeing so far but had to audit the information.

Mr. Keenan stated that looking back at the data he is not sure why there is a large amount of recovered revenue booked for 2013 as that should all have been reversed by this point. According to Mr. Keenan he had told Mr. McNellis about pulling out the revenue from accruals. Mr. Keenan stated that he did not recall seeing the sales revenue listed, and that he usually cared more about year to date numbers than monthly. He indicated that if he had noticed it he would have asked how so much was recovered. Mr. Keenan later added that at some meetings only the summary information on the PowerPoint was reviewed and the rest of the deck set aside. Mr. Keenan was not sure if that was the case in the meetings on January 23<sup>rd</sup>. Mr. Keenan stated that he isn't sure how he missed \$14M in revenue, and suggested that he was not paying attention to one month of one division, concentrating more on the big picture. Mr. Keenan said that he did not remember hearing in late January that PWC was having difficulty reconciling ASD numbers.

Mr. Keenan was showed a series of emails between himself and PWC employees in late January. He indicated that the emails were related to the issues with the inventory, and not the revenue recovery project.

Mr. Keenan was shown an email on which he was copied between Mr. McNellis and Mr. Wentlent, to which was attached a PowerPoint slide with a chart of invoiced revenue recovery similar to that shown at the January 23<sup>rd</sup> meeting. Mr. Keenan stated that he didn't pay attention to the terminology used in calling the \$14M invoiced; he assumed that Mr. Pruitt and Mr. Lassus were continuing to work with the Army and had sent over REAs for auditing and approval. Mr.





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Keenan stated that the first time he realized that more than the \$3.25M in OP3 items had been invoiced was in April when Mr. Miller brought it to his attention.

According to Mr. Keenan the next time he talked to Mr. Walsh about the revenue recovery project was in April. Mr. Keenan stated that he was concerned that the process was taking so long and he wanted to put a team on it. According to Mr. Keenan he assumed at this time that the next round of item by item REAs should be sent for approval, but he should have known from the January 23<sup>rd</sup> meeting that it had already been recognized.

Mr. Keenan stated that at the operations review meeting on April 17, 2014 where Pruitt represented that REAs had been submitted, he asked why the process was taking so long. Mr. Keenan noted that once an REA had been submitted with the backup he felt the process should only take a month or two at most. According to Mr. Keenan he did not get a satisfactory answer from Mr. Pruitt, Mr. Wentlent and Mr. Lassus; he then asked Mr. Walsh to put together a team to work on it. Mr. Pruitt told Mr. Keenan that he had waited to deliver the invoices until Ms. Gilles had left because Mr. Lassus had a much friendlier relationship with Ms. Fletcher. It was at the April 17<sup>th</sup> meeting that Mr. Keenan claims he first learned of the additional invoices being issued instead of just OP3 items, he was told at the meeting that \$12.4M in invoices were with the contracting officer (this is from p. 35 of the version of the PowerPoint Mr. Keenan had for this meeting.) Mr. Keenan stated that he was slightly concerned at this point that so much had been invoiced, but not overly because he was told that the contracting officer had accepted them.

In response, Brian Sinkule sent Mr. Keenan a spreadsheet with some of the accounting information, Mr. Keenan marked it up and sent it back noting several errors including situations where amounts were booked above the legal entitlement. According to Mr. Keenan he also sent the spreadsheet on the Mr. Azmon. Mr. Keenan stated that he didn't put together that this revenue was recorded in 2013, he was more concerned that he felt nobody was doing anything, and four months in there were items that he was told had been submitted that had not. Mr. Keenan also pointed to as an example a claim for heavy maintenance was being recognized for Q2 when it had not even been submitted yet.

aA conference call was scheduled for April 22, 2014 where according to Mr. Keenan aa team was to be set up to figure out why the process was so slow. Officially it was the responsibility of the contracts employees to submit the REAs, but they needed operations and finance to get everything together.

Me. Keenan stated that he emailed Mr. Azmon on April 23, 2014 after Azmon asked for an update (BATES ending 00520). Mr. Keenan's response was based on the information he



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received at the operations meeting with ASD and Mr. McNellis. The language about the invoices not having been rejected was based on Mr. Pruitt's assertion that the contracting officer had the invoices and was auditing them, and that Mr. Pruitt had waited to deliver the invoices until Ms. Gilles had left. This is the first mention of \$24.6M in exposure according to Mr. Keenan as he had just found out from Mr. Sinkule that the \$12.4M he was given at the operations meeting was incorrect and that in fact \$24.6M had been invoiced.

**d. Investigation and Aftermath**

Mr. Keenan stated that when he found that more had been billed and recognized than just OP3 he went to Mr. Azmon, and sent him an email showing what Mr. Pruitt had recognized. According to Mr. Keenan, Mr. Azmon called and told him that he had heard through an ethics complaint that the invoices were not delivered. Mr. Keenan responded that they were not in WAWF, but that they had been hand delivered. Mr. Azmon asked Mr. Keenan to follow up. According to Mr. Keenan, when he talked to Mr. Pruitt and Mr. Sinkule on April 28<sup>th</sup> Mr. Pruitt admitted that he had never delivered the invoices. Mr. Keenan stated that he immediately called Mr. Azmon, and that they along with Mr. Miller went to ASD, where Mr. Miller figured it out in a day. Mr. Keenan stated that when he told Mr. Walsh he was surprised saying "... have to be kidding me" as he also thought the invoices had been delivered. According to Mr. Keenan, Mr. D'Ambrosio was very angry with him for not noticing this, and said he thought that Mr. Walsh ordered Mr. Pruitt to enter the revenue and not deliver the invoices. He could picture Mr. Walsh telling Mr. Pruitt to find a way to fix the shortfall. Mr. Keenan stated that he disagreed and didn't think that Mr. Walsh would order fraud.

Mr. Rawlings asked Mr. Keenan how the addition of \$5.5M to the STF discussed earlier fit in to this issue. Mr. Keenan answered that sometimes what goes in the STF and what you believe in your heart aren't the same, and that Mr. Walsh decided to project more but did not make the projection. Mr. Keenan is not sure how Mr. Walsh could have missed the additional revenue added at the end of the year that helped ASD just make the 75% bonus threshold. However, Mr. Keenan noted that he also missed the addition. Mr. Keenan was asked if he received aging reports from ASD, he answered that he did not.

Mr. Keenan was asked whether he ever instructed Mr. Pruitt to enter invoices into SAP without entering them into WAWF, telling him it was a technique that could be used. Mr. Keenan answered that he had not. Asked if Mr. Pruitt said he did could there have been a miscommunication, Mr. Keenan answered he couldn't imagine that. Mr. Keenan was asked if he told the FBI that he learned that the invoices were not delivered on April 17, 2014. He answered that he had told the FBI that April 17<sup>th</sup> was the date he learned that the invoices had not been



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delivered when Mr. Pruitt had said they were, but instead later. Mr. Keenan stated that on April 23, 2014 he still believed that the invoices had been delivered.

Mr. Keenan was asked if Mr. Pruitt's role changed during the time the invoices and REAs were supposed to be delivered. He answered that he doesn't remember a change at that time, only that later Jeff Kasparites was being considered for the position. According to Mr. Keenan after the first operations review of 2014 Mr. Sinkule was brought in to help at ASD, but he had no responsibilities in handling revenue recovery. Mr. Keenan stated that this was not lost in translation, as Mr. Pruitt was in charge of revenue recovery, while Mr. Sinkule took over everything else because of issues with the books and Mr. Pruitt's inability to answer questions at the operations review.

Mr. Keenan was asked when he had last spoken with a number of people involved with the C-12 issue. According to Mr. Keenan he last spoke with Mr. Pruitt approximately four weeks before he was terminated. Mr. Keenan spoke with Mr. Wentlent three or four times after his termination the last time approximately four months ago. Mr. Keenan spoke with Mr. Walsh a number of times, and he and his wife had considered some business dealings in real estate with Mr. Walsh. However, two or three months ago they spoke about Mr. Keenan receiving a subpoena in the C-12 issue and decided to put the deal on hold and not to talk until the case was settled. Mr. Keenan attempted to contact Mr. Sinquefield several times but was never able to; the last time was more than a year ago.

Mr. Keenan was terminated by Mr. McNellis, who told him that if he did not know what was going on in the accounting for ASD then he should have known. Mr. Keenan stated that he told Mr. McNellis that they all received the same information at the same time, so anything he knew Mr. McNellis and Mr. Nordstrom knew at the same time. Mr. Keenan stated that he learned from Jim Grove who works in resource management in Greenville that Mr. McNellis was frozen out and then retired. Mr. Keenan stated that this was the way L-3 worked; no one would take to Mr. McNellis until he retired. According to Mr. Keenan, Mr. McNellis is now working at the Department of Defense.

**V. Rockwell**

Mr. Keenan was asked who, other than Mr. Walsh, worked at Rockwell that would have known about the C-12 contract. Mr. Keenan answered that Mr. McNellis, Ms. Clark, Mr. Coffman, Mr. Nichol and Dallas Mayfield would likely know about C-12 and ASD's accounting issues. Mr. Keenan was shown a handwriting sample, which he could not identify, but did confirm did not belong to Ms. Clark.



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Mr. Keenan was asked what SFSS stood for, he answered that it was usually called SFS and stood for System Field Services which changed too Integrated Systems before he began there. Mr. Keenan said that it was more likely that someone from Greenville would still use the name, perhaps Bill Hengline or Tom Smith (? VP of HR). Greenville was the location of Intelligence, Surveillance and Reconnaissance, and was located approximately 35 miles further from Dallas than Integrated Systems.

According to Mr. Keenan when Mr. Walsh was CFO his office was located in Greenville, where he is widely disliked because he was constantly pushing his people. Mr. Keenan stated that Mr. Walsh had the record for most ethics investigations filed against a supervisor that were cleared. Mr. Keenan was asked if someone in Greenville would know if Mr. Walsh instructed Mr. Pruitt to recognize the revenue as he did. Mr. Keenan answered that they probably could not, but that wouldn't necessarily stop them from saying that he had, given his unpopularity.

Mr. Keenan noted that anyone who knew could have called him, and he asked several people involved with ASD's accounting why they did not just call him and they told him that they didn't want the retribution from Mr. Walsh for going around him. Mr. Keenan stated that he did not press Mr. Wentlent or Mr. Walsh as he was more concerned at the time with getting back to Mr. Azmon. He did note that Mr. Walsh seemed legitimately surprised that the invoices were not delivered, more so than that they had been issued.

Mr. Keenan stated that in his time at L-3 he had never had any problems before with Mr. Pruitt or the people working on the finances in the other nine divisions. According to Mr. Keenan, Mr. Walsh has a way of being very demanding and he thinks that maybe Mr. Pruitt buckled under that pressure. Mr. Keenan reiterated that he could not see Mr. Walsh actually telling Mr. Pruitt to issue the invoices and not deliver them, and that Mr. Walsh never asked Mr. Pruitt to do anything underhanded when he was his supervisor.

\*\*\*\*\*

Mr. Baker concluded the meeting by thanking Mr. Keenan for his time and for providing information to the Commission. Mr. Baker asked that Mr. Keenan keep this meeting confidential due to the ongoing nature of the investigation. Mr. Baker told Mr. Keenan that if the Commission had any further questions they would reach out to his counsel.

# EXHIBIT B

**REDACTED**

# EXHIBIT C

REDACTED



# EXHIBIT D

**In The Matter Of:**

*In the Matter of  
David Pruitt, CPA*

---

*Timothy Keenan*

*May 2, 2018*

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*Behmke Reporting and Video Services, Inc.*

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Original File 33327KeenanV1.txt

**Min-U-Script® with Word Index**

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1 UNITED STATES OF AMERICA  
2 BEFORE THE  
3 SECURITIES AND EXCHANGE COMMISSION  
4 ADMINISTRATIVE PROCEEDING  
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6 -----  
7 In the Matter of, ) FILE NO.  
8 David Pruitt, CPA, ) 3-17950  
9 Respondent. )  
10 -----  
11  
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13  
14 VIDEOTAPED DEPOSITION OF TIMOTHY KEENAN  
15 WEDNESDAY, MAY 2, 2018  
16 PAGES 1 - 269; VOLUME 1  
17  
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20  
21 BEHMKE REPORTING AND VIDEO SERVICES, INC.  
22 BY: KIM A. MCCANN, TEXAS CSR NO. 5520  
23 160 SPEAR STREET, SUITE 300  
24 SAN FRANCISCO, CALIFORNIA 94105  
25 (415) 597-5600

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7  
8 Videotaped deposition of TIMOTHY KEENAN,  
9 VOLUME 1, taken on behalf of Plaintiff, at 801  
10 Cherry Street, Suite 1900, Unit 18, Fort Worth,  
11 Texas, commencing at 10:00 A.M., WEDNESDAY,  
12 MAY 2, 2018, before Kim A. McCann, Certified  
13 Shorthand Reporter No. 5520, pursuant to Federal  
14 Rules of Civil Procedure.  
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13 ANTHONY MILAZZO, ANKURA CONSULTING  
14 CHRISTOPHER MELE - (TELEPHONICALLY)  
15 STEVE RAWLINGS - (TELEPHONICALLY)  
16  
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1e We really weren't -- I really wasn't sure because I  
2 hadn't -- we had to get our arms around this stuff first  
3 to be able to make sure that we understood what we were  
4 going to do.  
5 But the situation evolved both with us and also  
6 with the customer because of the interaction with Kenny  
7 Lassus going back and forth with the customer trying to  
8 figure out how are we actually, you know, going to do  
9 this.  
10 Q. What do you recall about those discussions?  
11 A. I was not part of the discussions in terms of  
12 -- are you talking about Kenny Lassus's discussions, I  
13 was not part of it, I don't know. It was reported back  
14 to me at one point that the customer had asked for  
15 backup packages with an invoice that totaled up, and we  
16 said, okay, we'll do that. We'll also get a legal  
17 entitlement ruling from our local contracts guys to make  
18 sure that before we go and submit something to the  
19 customer that we are -- we actually had, you know, legs  
20 to stand on.  
21 Q. What do you mean by legal entitlement?  
22 A. Legal entitlement is it was kind of a -- it was  
23 kind of a term that was used under SOP 81-1 where you  
24 would go and you would say, okay, the legal guys would  
25 say, okay, here's what the contract said, here's what

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1e actually happened. We believe you have violated -- you  
2 have violated the contract or breach of contract for  
3 your part of the thing and we have incurred costs  
4 because of that and so we believe we're entitled to this  
5 money.  
6 Q. All right. Well, earlier in the affidavit you  
7 said that you believed the work had been done and you  
8 were entitled to get paid; is that right?  
9 A. Yes, sir.  
10 Q. So is it -- is there any reason to consider  
11 something like legal entitlement when you've believed  
12 the work's been done and --  
13 A. Nobody gives a crap about what I think. What  
14 we --  
15 Q. Sorry?  
16 A. Nobody gives a crap about what I think. What I  
17 -- we needed to do was have a contracts guy has to be  
18 able to say, yes, this is right. If we go through and  
19 we have people saying, Hey, I did this work, and, you  
20 know -- and we go, Okay, fine, prove it. Now we go over  
21 to the legal guy and we say, Okay, we did this work. Is  
22 it over and above of this contract? Is this -- you  
23 know, are they -- were they in breach of what they said?  
24 They told us that they were going to have --  
25 give us six months' worth of -- of notification for this

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1 aircraft. Is that true? And if it's not true, then  
2 what is it and let's find out where -- you know, where  
3 we're entitled to actually say we expended this cash  
4 because of the fact that you didn't do what you said you  
5 were going to do. Now, we would like that money back.  
6 But it's all great that the finance guy thinks  
7 that, but it's not -- it doesn't hold water in a  
8 contractual situation.  
9 Q. Continuing in Paragraph No. 9, you say,  
10 "Mr. Pruitt did not have authority to determine the  
11 accounting treatment to be applied to these items on his  
12 own, and he consulted superiors in the finance groups  
13 and legal counsel regarding the proper treatment to be  
14 applied."  
15 A. Yes.  
16 Q. Okay. Why did you say that Mr. Pruitt did not  
17 have authority to determine the accounting treatment to  
18 be applied?  
19 A. Because this was an unusual situation, and I  
20 would not even begin to suggest that I had the authority  
21 to be able to treat this. I would always go to the  
22 corporate office and make sure I explained the whole  
23 situation to them before we decided to go ahead and  
24 treat this thing.  
25 Q. Okay. Then you say that he consulted superiors

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1 in the finance groups and legal counsel regarding the  
2 proper treatment -- treatment to be applied. How do you  
3 know that?  
4 A. Well, he was telling -- he was asking me, hey,  
5 are we going to -- you know, how are we going to do all  
6 this? And I said, Okay, I'm going to have to get with  
7 Dan and find out what we're going to do. Subsequent to  
8 that, we heard from Kenny Lassus that because this is  
9 what the customer was looking for, was backup and an  
10 invoice. And I said, Okay, backup and an invoice and  
11 it's tied up to the contract. It's a valid invoice.  
12 They have legal entitlement to it. The customer's going  
13 to accept it. It's accurate. And you can invoice it.  
14 Go ahead.  
15 Q. You mentioned Dan in your answer.  
16 A. Yes. Dan --  
17 Q. Who is that?  
18 A. Dan Azmon, yes.  
19 Q. Okay. So when you said that Mr. Pruitt  
20 consulted superiors in the finance groups, besides  
21 yourself, are you referring to anyone else?  
22 A. Well, it would have been myself and then  
23 subsequently that -- you know, Dan Azmon and/or Mike  
24 Miller.  
25 Q. You say "it would have been." Do you know if

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1 he did, in fact, consult them?  
2 A. That's what I'm referring to.  
3 Q. Okay. But -- so Mr. Pruitt consulted with --  
4 A. No. He consulted with me, and who in turn  
5 would consult with. So, I mean, he's not specifically  
6 consulting with himself -- I mean, himself consulting  
7 with those guys, but he's asked me to consult with them.  
8 Q. Okay. How -- how did it first -- how did  
9 Mr. Pruitt first raise with you a question about the  
10 proper treatment to be applied?  
11 A. Well, during conference calls, it would be the  
12 question of how are we going to handle this? What --  
13 what are we going to do with this? And I -- I kicked  
14 out several scenarios of this is what we could do.  
15 We -- you know, maybe we do -- maybe this is such that  
16 if it's going to be something that's going to take until  
17 2014 or '15, maybe we reverse the cost of sales on that  
18 and match it with the claim when we get it. And I said,  
19 That -- that's just one item that we can, you know, try.  
20 And, in fact, you can actually create an invoice that is  
21 valid, the customer will take it and has -- you know,  
22 has the ability to pay for it on the over and above  
23 CLIN. Go ahead, let's do that.  
24 So again, it was one of those things that we're  
25 just -- we're just kind of kicking spit ball things

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1 around to -- to try to figure out. And then -- and it  
2 all evolved into eventually me talking with Dan Azmon  
3 and explaining all the -- all of what we were -- what we  
4 were thinking. And he went back and said, Okay, this is  
5 what you can do.  
6 Q. And what did he say that you can do?  
7 A. He said that you cannot invoice for option  
8 years 1 and 2, because those are prior option years and  
9 year -- those years are closed. That's part of the --  
10 what -- what they would call claim accounting, which is  
11 you can re -- you can invoice them, go ahead, invoice  
12 them, but you can't record revenue or cost of sales or  
13 sales on them until we actually get paid for them.  
14 Option year 3, you can go ahead and invoice them if it's  
15 a valid invoice. You can go ahead and invoice those and  
16 take revenue and profit on those.  
17 Q. All right. When did you have that conversation  
18 or that -- when -- when were you having those  
19 discussions with Mr. Azmon?  
20 A. January -- January 7th of 2014.  
21 Q. Why do you remember that date?  
22 A. Because that was the date that I sent an email  
23 to Mr. Pruitt and told him, This is exactly what I just  
24 talked to Dan Azmon about.  
25 Q. All right. We'll show you that document. But

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1 when was -- I'm sorry. When -- when was this first  
2 raised with you that -- that Mr. Pruitt had questions  
3 about the proper accounting treatment to be applied?  
4 A. Well, it was throughout the -- throughout all  
5 the conference calls. It was like going, how are we  
6 going to handle this? How are we going to do this? It  
7 wasn't specific to any, you know, one thing. It was  
8 just a general, how are we going to do this. That's  
9 all.  
10 Q. Now, you -- you talked about reversing costs of  
11 sales for prior years?  
12 A. Yes.  
13 Q. Do you remember that?  
14 A. That was an idea that I brought up that was  
15 shot down.  
16 Q. Okay. So that's not something that was done?  
17 A. No.  
18 Q. All right. Were there any changes that you  
19 made to the draft affidavit in paragraph 9?  
20 A. I don't think so. I don't know, but I don't  
21 think so.  
22 Q. All right. Paragraph 10 says, "I have a  
23 general recollection of speaking with Mr. Pruitt  
24 regarding the revenue recovery items in late December."  
25 Do you see that?

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1 A. Yes.  
2 Q. And what is your recollection about that  
3 conversation?  
4 A. Just here's all of the items we have. Here's  
5 all the back -- the backup that we have. You know, just  
6 talking about the whole package in terms of what we  
7 have.  
8 Q. So who said what in that conversation?  
9 A. I don't recall the exact conversation, but, I  
10 mean, in general terms, it was Dave providing me  
11 information on what they have come up with and me  
12 saying, Okay, that's fine, let's understand, you know,  
13 where we're at.  
14 Q. When did this take place?  
15 A. Probably last 10, 11 days or so of December.  
16 Q. Okay. I mean, that's what you're referring to  
17 by late December?  
18 A. Yeah.  
19 Q. And then you say, "I recall during one  
20 telephone call directing Mr. Pruitt to invoice most of  
21 the revenue recovery items and accrue for two others."  
22 Do you see that?  
23 A. Yes.  
24 Q. And what are you referring to by that?  
25 A. That was what I -- as I was saying before. that

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1 I thought, you know, as long as the customer is going to  
2 accept these invoices, that we could go ahead and put  
3 the backup together, put the invoice on there, put the  
4 legal entitlement together and bring it over to the  
5 contracting officer.  
6 Q. All right. So is this direction dis -- during  
7 -- I recall one telephone -- during one telephone call  
8 directing Mr. Pruitt to invoice.  
9 Is that the same -- is that referring to the  
10 same conversation that you talked about in the first  
11 sentence?  
12 A.e I don't know. I'm not sure. You know, wee  
13 talked, you know, a couple of times -- excuse me -- a  
14 couple of times. It may have been. It may not have  
15 been. I'm not sure.  
16 Q. So the one telephone call where you directed  
17 Mr. Pruitt to invoice, what words did you use to give  
18 that direction?  
19 A. I said something to the effect of, "Dave, if  
20 you have a valid invoice and the customer is telling you  
21 that they will accept the invoice with the backup, then  
22 you can go ahead and invoice that and let's get it  
23 going."  
24 Q. Well, what do you mean, "a valid invoice"?e  
25 A. Well, a valid invoice has to have -- you know,e

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1 has to have -- obviously, customer's exception --  
2 acceptance of, you know, such invoice, the backup that  
3 is required to -- according to the customer, you know,  
4 you have to send me the backup that -- that's required  
5 to it so I can audit it and decide whether or not it's,  
6 in fact, true. And I also requested a -- you know, a  
7 legal entitlement notification from the contracting  
8 people just to make sure that we had something that --  
9 that said, yeah, based on the contract, you owe us this  
10 money.  
11 Q. All right. So you recall discussing -- sorry.  
12 You recall directing Mr. Pruitt to invoice -- you say,  
13 "I directed him to invoice most of the revenue recovery  
14 items."  
15 Which items did you tell him to invoice?  
16 A. I don't recall exactly.e  
17 Q. Which items did you tell him to accrue?  
18 A. I don't recall exactly. I just know that we  
19 talked about accruing. At that -- at one point we had  
20 talked about accruing the cost of sales back on to the  
21 books, which ended up getting reversed.  
22 Q. Did you go -- when you directed Mr. Pruitt, did  
23 you go through each of the invoices or was this a --  
24 withdrawn.  
25 When you say you directed him to invoice most

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1 of the revenue recovery items, were you looking at a  
2 list of items?  
3 A. I don't -- I wasn't looking at a list of, youe  
4 know. specific invoices and backup for any of that kinde  
5 of stuff. I was looking -- I think it was a spreadsheet  
6 there that we talked about, you know, that had all thee  
7 items on there.e  
8 Q. What's the spreadsheet?  
9 A. It was a spreadsheet that had a list of the  
10 items and what we thought we could -- you know, what we  
11 were going to actually recover.  
12 Q. How did you receive --  
13 A. And invoice.e  
14 Q. How did you come to receive that spreadsheet?e  
15 A. I'm sure through email.  
16 Q. From Mr. Pruitt?  
17 A.e Yeah.  
18 Q. Did he say anything in the email attaching thee  
19 spreadsheet?e  
20 A. I don't recall.  
21 Q. Were you looking at that spreadsheet when youe  
22 say in paragraph 10 that you directed Mr. Pruitt toe  
23 invoice most of the revenue recovery items and accruee  
24 for two others?  
25 A.e I'm sure I was.e

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1 Q. But you don't have a recollection that youe  
2 were?e  
3 A.e I was sitting there, I'm sure, when we weree  
4 talking on the phone. I would have -- I would have beene  
5 looking at it. I -- I -- you know, I don't have thate  
6 remembrance of that day specifically. I'm just -- I'me  
7 making a supposition that I would have.e  
8 Q. Right. So just to be clear. So you don'te  
9 recall whether you actually have it, that spreadsheet,e  
10 present with you when you say that you directede  
11 Mr. Pruitt to invoice?e  
12 A.e What I'm telling you is I -- he -- I know hee  
13 sent me the spreadsheet. I'm sure I was looking at it.e  
14 I just don't have remembrance specifically of that daye  
15 or -- you know, doing it. And I know that I did, ine  
16 fact, go through them at one time at least and say, I fe  
17 you have a valid invoice on these items, Dave, go ahead  
18 and invoice them.e  
19 Q. You say, "I believed at the time that it was  
20 appropriate to invoice for the revenue recovery items."  
21 Do you see that?  
22 A. That's true, yes.  
23 Q. Why did you add that statement?e  
24 A. Well, because at the time, we were -- that'se  
25 what we were thinking. We -- we went through and he wase

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1 packages that were put together and invoices that wereo  
2 put together, we could get them over to the contractingo  
3 officer. And at the very least, even if we couldn't doo  
4 something with them, they would have them and they could  
5 start looking at them.  
6 Q. Okay. So in paragraph 10, you're referring to  
7 option -- items -- all of the revenue recovery items?  
8 A. In paragraph 10?o  
9 Q. Yeah. Yeah.  
10 A.o Any ones that they had done.o  
11 Q. Any ones that -- that the full packet --  
12 A. Yeah, the backup package was -- was there.o  
13 Q. All right. And that -- but that -- it was --  
14 okay. Maybe I'm not understanding it.  
15 What direction did you give Mr. Pruitt to -- or  
16 withdrawn.  
17 Which items did you direct Mr. Pruitt to  
18 invoice?  
19 A.o Just the ones that -- any package -- if he --  
20 if they had a backup package and it was -- I'm just  
21 making this up -- just say it was one item for \$400,000  
22 for option year 1, it was altogether and ready to go,  
23 yes, put the invoice together and get it over to them.  
24 Q. All right. So when you made this statement in  
25 the affidavit, you don't recall which items in

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1 particular?o  
2 A. Well, when I say "most," you know, I'm talkingo  
3 about the -- there was a list of, I think, six of them.  
4 Q. Uh-huh.  
5 A. And he may not have, you know -- he may onlyo  
6 have one of them done, but I'm saying, at this point, if  
7 you get them done, send them over. And they were  
8 projecting to be done on almost all of them at one  
9 point, but that didn't happen.  
10 Q. Who is "they" were projecting?o  
11 A. The team, the operations team that was workingo  
12 on putting these things together.  
13 Q. When were they projecting to have them done by?  
14 A. They said that they would all be -- at one  
15 point, they said they'd all be done by end of 2013, but  
16 they backed away from that.  
17 Q. What do you mean, they backed away from that?  
18 A. Well, they weren't ready, you know, and -- ando  
19 they -- we asked them -- you know, you ask them in  
20 December 15th, Where are you -- where are you at on  
21 this? And them, Nowhere, I haven't even gotten anywhere  
22 on that backup yet.  
23 Q. Okay. So it's -- so by saying in paragraph 10  
24 that you directed Mr. Pruitt to invoice most of the  
25 revenue recovery items and accrue for two others, the

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1 ones that he could invoice for, according to your  
2 statement, could have been in option year 1, 2, or 3?  
3 A. Yes.  
4 Q. Is that right?o  
5 A.o Yes.  
6 Q. It was any item where they had the full package  
7 put together?  
8 A. Yes.  
9 Q. So all of the backup?  
10 A.o Yes.  
11 Q. And when the invoice was run, that would  
12 recognize the revenue?  
13 A. Yes. In the SAP system, yes.  
14 Q. What's the SAP system?  
15 A. It's -- I don't know what SAP stands for, buto  
16 it's the financial -- you know, it's the full loop MRPo  
17 system. Closed loop.o  
18 Q. So -- so once invoices are -- once they'reo  
19 invoiced, as you say, then the -- the -- the revenue iso  
20 recognized?  
21 A. In -- yes, that's how it works, unless you turn  
22 around and back it back out.  
23 Q. Okay. And is doing that -- when you -- when  
24 you're directing this, would -- did you believe that --  
25 that that accounting would comply with SAB 104?o

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1 A. I -- I wasn't concerned about that right ato  
2 that point. But yes, I did. If we had actually had ano  
3 invoice that was able to be generated and the customer  
4 would accept it and would pay it, we would be fine.  
5 Q. All right. So -- so to the extent that youo  
6 were giving instruction to invoice, was it youro  
7 understanding that the customer had agreed to pay thoseo  
8 amounts?o  
9 A. Yes.o  
10 Q. If they'd already agreed, why -- why would you  
11 be sending over the full packet?o  
12 A.o They agreed -- what -- what I understood waso  
13 that if they -- if we brought over the invoice and ito  
14 had all the -- the backup for it, that they had done  
15 that -- they had gone through that review earlier and  
16 had that conversation with the customer, the customer  
17 had said, If you've got valid invoices and you've goto  
18 good backup for it, we will pay them. That was -- that  
19 was the answer.  
20 Q. All right. You say that "I believed at theo  
21 time that it was appropriate to invoice for the revenue  
22 recovery items"?o  
23 A. Yes.o  
24 Q. What did you mean when you said that?o  
25 A. Oh, because that was before I had a

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1 A. Yes, sir.  
 2 Q. Whose idea was that to make those adjustments?  
 3 A. It was a discussion that came from John  
 4 McNellis, Gordon Walsh, and myself.  
 5 Q. Was Mr. Pruitt involved in those discussions?  
 6 A. He was not.  
 7 Q. Do you know if he made any requests to anyone  
 8 that those kind of adjustments be made?  
 9 A. I would -- if he made the request, I don't know  
 10 of them, and I -- no, I can't -- I can't imagine that.  
 11 Q. You can't imagine what?  
 12 A. That he would -- I don't think he knew anything  
 13 about how this was being done.  
 14 Q. All right. But as far as you know, he didn't  
 15 request that anything --  
 16 A. No.  
 17 Q. -- along these lines be done?  
 18 A. No.  
 19 Q. You also say that "Mr. Pruitt could not have  
 20 known in advance what, if any, adjustments would be made  
 21 to ASD's financial results."  
 22 Do you see that?  
 23 A. That's correct.  
 24 Q. What are you referring to by that?  
 25 A. The -- the file that we put together on the

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1 incentive compensation by division and all that work was  
 2 closely guarded between myself and John McNellis, Gordon  
 3 Walsh, Nick Ferra for the PIT, and Mark Von Swartz for  
 4 the Mission Integration Division. No one beyond the  
 5 president level would ever get a look at that file.  
 6 Q. In paragraph 16, you say that "If the  
 7 adjustments were not made, ASD management, including  
 8 Mr. Pruitt, would not have received a bonus."  
 9 Do you see that?  
 10 A. Yes.  
 11 Q. Who else in ASD management would not have  
 12 received a bonus?  
 13 A. No one in ASD management would receive a bonus.  
 14 Q. I'm sorry. I guess what I meant by that is who  
 15 are you referring to by ASD management?  
 16 A. It's the -- there's about -- and I can't  
 17 remember the number, but I think it's around six people  
 18 that received incentive compensation from ASD. It may  
 19 not even be that many from ASD. That may be -- may be  
 20 Vertex. But I know Mark went lent would be one. Dave  
 21 Pruitt would be another. I'm sure Rick Schmidt was  
 22 involved in -- in that as the -- you know, for a  
 23 manager. I don't know if I could identified anyone else  
 24 specifically.  
 25 Q. Okay. Then you say, "It is not accurate for

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1 anyone to say that in December 2013 the invoices" --  
 2 sorry -- "the issuance of invoices by Mr. Pruitt solely  
 3 caused ASD to reach the 75 percent bonus threshold,  
 4 because that threshold was only reached when  
 5 Mr. McNellis and Mr. Walsh agreed to make the  
 6 aforementioned adjustments."  
 7 Do you see that?  
 8 A. Yes, sir.  
 9 Q. Okay. So -- so what you're saying is that the  
 10 invoices alone -- just the -- just the issuance of the  
 11 invoices, that alone did not enable ASD to reach the 75  
 12 percent bonus threshold?  
 13 A. That's a correct statement.  
 14 Q. But it played a part in it?  
 15 A. Certainly, you know, it gets to in this level,  
 16 and then we made the arrangements and it got -- and -- I  
 17 mean, the adjustments I should say, and it made it  
 18 happen.  
 19 Q. Did you make any changes to paragraphs 14, 15,  
 20 and 16 from the draft affidavit?  
 21 A. I think so, yes.  
 22 Q. Which paragraphs?  
 23 A. I believe 15 and 16, I think.  
 24 Q. Do you know why you --  
 25 A. I -- I know 16.

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1 Q. 16 -- so 16 you did make a change to?  
 2 A. (Witness nodded.)  
 3 Q. Sorry?  
 4 A. Yes. Sorry.  
 5 Q. Yeah, I know, it's getting --  
 6 A. I'm looking down and reading it.  
 7 Q. And 15 you may have made a change?  
 8 A. It's possible, yes.  
 9 MR. GIZZI: Now, I know why court reporters have the  
 10 toughest job, trying to find a spot for the sticker.  
 11 MR. FOKAS: Over there, maybe.  
 12 (Exhibit 12 was marked.)  
 13 Q. Okay. Mr. Keenan, I'm handing you what's been  
 14 marked as Exhibit 12.  
 15 Exhibit 12 is an FBI Form 302 regarding an  
 16 interview with Elizabeth Warnick of Simpson, Thacher &  
 17 Bartlett.  
 18 A. Agreed.  
 19 Q. Do you know Ms. Warnick?  
 20 A. I don't know. I -- I know one guy there in one  
 21 day.  
 22 Q. If you can turn to page 7 of 9, the page  
 23 numbers are in the upper right-hand corner.  
 24 A. All right.  
 25 Q. In -- you know, the bottom of the page that



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1 (Exhibit 16 was marked.)  
2 Q. Mr. Keenan, I'm handing you what's been marked  
3 as Exhibit 16.  
4 MR. ROCCO: Thank you.  
5 Q. This is a email from Mr. Pruitt to Mr. Wentlente  
6 on January 8th.  
7 Have you seen this document before?  
8 A. No.e  
9 Q. All right. In this it -- it says -- Mr. Pruitte  
10 says to Mr. Wentlent, "I spoke with Tim Keenan and we  
11 reviewed the adjustments and also discussed the process.  
12 We need 75 percent or greater to qualify for MIB and we  
13 are over this number. I'll send you the schedule as  
14 soon as I verify the final numbers."  
15 Did you have that conversation with Mr. -- with  
16 Mr. Pruitt?  
17 A.e Yeah, he had to give me the -- he had -- shee  
18 had to give me all the numbers that they thought would  
19 be -- you know, he gave me a litany of numbers that was  
20 like \$15 million and stuff that -- that he thought  
21 should be adjusted back and forth, and of course, it  
22 wasn't that -- that number at all. So he was the one  
23 that was actually the source of the -- of the documents.  
24 Q. So this is -- I thought we'd talked about these  
25 earlier, and maybe I'm missing something, but I thought

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1 you indicated that Mr. Pruitt was not involved in that  
2 process?  
3 A. He's not involved in the process. All it --  
4 all it was was we said -- you know, Gordon said, you  
5 know, get with Dave and get with Stuart White, who was  
6 on the BLN side, and said, you know, get all the -- get  
7 all the adjustments as I think are -- are required, and  
8 it was just a -- a gross number. Beyond that, he was  
9 not involved. Again, Stuart White shoves stuff back  
10 over to ASD.  
11 Q.e All right. So but you did discuss with  
12 Mr. Pruitt what adjustments were going to be made?  
13 A. No, I did not discuss -- I didn't discuss -- I  
14 discussed with him his -- all the stuff that he wanted  
15 to adjust. I didn't discuss with him which ones were  
16 made.  
17 Q. Okay. So you discussed with him what items he  
18 wanted adjusted?  
19 A. Yeah, he sent me a list of all the things ande  
20 explained to me what they -- you know, why he thought  
21 that they should be adjusted, and Stuart White did the  
22 same thing.  
23 MR. ROCCO: So you know Stuart White is?  
24 MR. GIZZI: Yeah.  
25 MR. ROCCO: The other side of the V.

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1 Q. So just to be clear, Mr. Stewart did want thee  
2 adjustments to be made?  
3 A. He was told by Gordon to give -- get a list ofe  
4 all the stuff together that he -- that the people at ASDe  
5 thought they were being shackled with by Vertex. Hee  
6 also told Stuart White the same thing, give me all this  
7 things that you think is -- you know, back and forth  
8 because of the split that happened in May between thee  
9 two divisions.e  
10 They both gave me a litany of stuff that was,  
11 you know -- you know, everything, and we sat down --  
12 John McNellis, Gordon Walsh, and myself -- sat down and  
13 we said these are the things that are true.  
14 Q.e What did you discuss about the process with  
15 Mr. Pruitt? It says that at the end of the firste  
16 sentence.e  
17 A.e I don't know what it means. I don't know whate  
18 that means. I don't know what process. The process ise  
19 just going through and -- we'll go through and decide  
20 which ones are yay and nay.  
21 Q.e Did you think -- withdrawn.  
22 Was it a red flag to you that Mr. Pruitt ise  
23 asking -- you know, discussing with you the adjustments  
24 that he wants made and discussing the process?  
25 A.e No.e

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1 MR. FOKAS: Objection to form.  
2 A. Okay. When Gordon tells him, okay, give me alle  
3 your grievances, and he goes through and gives me a  
4 litany of \$15 million of the grievances, and he says thee  
5 same thing to Stuart White, give me all your grievances.e  
6 So we went through and looked at that, and then  
7 I got all the information and then we sat down  
8 with Gordon, John McNellis, and myself, and we sat down  
9 and said, okay. this is ridiculous, we're not -- and so  
10 they had no idea what the final number ended up being.  
11 They could have asked for the moon.  
12 (Exhibit 18 was marked.)  
13 Q.e Mr. Keenan, I'm handing you what's been marked  
14 as Exhibit 18.  
15 A. Okay.  
16 MR. FOKAS: So do I have that right? It should bee  
17 17.  
18 MR. ROCCO: Yeah.  
19 MR. GIZZI: How is -- okay. Thank you.  
20 Q. Okay. So regarding Exhibit No. 18, do you  
21 recognize this document?  
22 A. Yes, I do.e  
23 Q.e And what is this?e  
24 A. This is just an email from me to Dave asking ife  
25 he ever got the letter from the customer with respect to

**EXHIBIT E**



CORPORATE ACCOUNTING POLICY NO. 102

**TITLE: Revenue and Cost of Sales Recognition  
for Fixed-Price Service Contracts  
Not Covered by SOP 81-1 (SAB 104  
"Services" Revenue/Cost of Sales Recognition)**

**EFFECTIVE DATE: July 2, 2005**

**1. PURPOSE**

To establish general guidelines for the recognition of revenues and cost of sales for revenue arrangements (contracts) that provide fixed-price services not related to the production of tangible assets. Such fixed-price service contracts are not within the scope of AICPA Statement of Position 81-1, *Accounting for Performance of Construction-Type and Certain Production-Type Contracts* (SOP 81-1). Instead, these revenue arrangements to perform services are covered by SEC Staff Accounting Bulletin No. 104, *Revenue Recognition* (SAB 104).

**2. SCOPE**

This accounting policy applies to all revenue arrangements to provide fixed-price services under which the contractual performance is not essential to the construction, or production of tangible assets to the customer's specifications, and therefore not covered by SOP 81-1.

In general, this accounting policy applies to the fixed-price service revenue arrangements (contracts) or separate Unit of Accounting within a revenue arrangement listed below. The list of "services" below is not intended to be an all-inclusive list, but rather an indicative guide.

- a. Scientific, engineering and technical analysis (SETA), integration support or project management that do not alone produce a tangible product as the principal intended result
- b. Installation services that do not involve customization of product features and do not require proprietary information about the Business Unit's products, which can be performed by other vendors or the customer
- c. Training, teaching and education
- d. Recruiting
- e. Information technology support
- f. Simulation and modeling
- g. Advisory, consulting or concept of operations
- h. Maintenance or repair and overhaul of aircraft or other vehicles/platforms
- i. Contractor logistics support
- j. Depot maintenance
- k. Acquisition management, supply chain and inventory management
- l. Mission support for aircraft, weapons systems and other platforms
- m. Operate or "run" equipment, systems or platforms
- n. Facilities management and maintenance
- o. Human resource (HR) management

EXHIBIT 2 PLTF.  
WITNESS [REDACTED] DEFT.  
CONSISTING OF 6 PAGES  
DATE 5-2-18  
BEHMKR REPORTING AND VIDEO SERVICES, INC.

Services that consist of designing, engineering, fabricating, modifying, upgrading, procuring, constructing, manufacturing, installing, integrating and testing related to the production of complex aerospace, or electronic equipment to a customer's specification are covered by SOP 81-1, and therefore, this accounting policy does not apply to these types of revenue arrangements. This accounting policy also does not apply to services for modifying, or upgrading an aircraft to a customer's specifications.

Fixed-price service contracts not covered by SOP 81-1 will generally be structured as one of the types of revenue arrangements listed below:

- **Type A:** A fixed-price service contract that only contains a fixed sales price (contract value) for the entire service period (e.g., per month, quarter or year) and does not contain separately-priced measurable units work to be performed during the contractual service period. These types of fixed-price service contracts also include separately priced extended product warranty and maintenance agreements, which are within the scope of FASB Technical Bulletin 90-1, *Accounting for Separately Priced Extended Warranty and Product Maintenance Contracts* (FTB 90-1);
- **Type B:** A unit-price service contract that contains separately-priced measurable units of work performed during the service period, for example, "fixed hourly labor rate," "fixed-price level of effort," "fixed-price per flight hour" and "fixed-price per occurrence" contracts; or
- **Type C:** A fixed-price service contract that is effectively treated by the Business Unit and the customer as a "time at marked-up rates," or "fixed-price level of effort" type contract. Such fixed-price service contracts essentially function and are administered as "time at marked-up rates" contracts for customer invoicing purposes due to a formal, or informal arrangement with the customer. For example, in these situations although the contract value is a single "fixed price" amount, it is invoiced to the customer based on actual labor hours expended, using negotiated billing hourly labor rates. In these types of revenue arrangements, it is common for the period of performance to be mutually extended until 100% of the fixed price contract value is invoiced to the customer.

### 3. POLICY

#### 1. General Revenue Recognition Criteria

For all types of revenue arrangements, regardless of the revenue recognition method used, revenue shall be recorded in accordance with the guidelines under SAB 104. Under SAB 104 guidelines revenue shall not be recognized (recorded) until it is realized or realizable and earned, which occurs when all of the criteria listed below are met.

- (i) Persuasive evidence of an arrangement exists (legally-binding revenue arrangement)
- (ii) Delivery has occurred or services have been rendered (i.e., the method and timing of revenue recognition)
- (iii) The sales price to the buyer (customer) is fixed or determinable
- (iv) Collectibility of the sales price is reasonably assured

The policies below address the method and timing of revenue recognition for services rendered under fixed-price service contracts (criteria (ii) above). See L-3 Revenue Recognition Guidelines for a detailed discussion of criteria (i), (iii) and (iv) above.

## 2. Method and Timing of Revenue Recognition for Fixed-Price Service Contracts

The accounting for each type of revenue arrangement within the scope of this accounting policy shall be performed as follows:

- Type A: Fixed-price service contract that only contains a fixed sales price and does not contain separately-priced measurable units of work performed during the service period.
  - A. Revenue Recognition. Revenue shall be recorded each month on a straight-line basis, unless evidence suggests that the revenue is earned, or obligations are fulfilled, in a different manner over the contractual term of the revenue arrangement, or the expected period during which the services will be performed (the "service period"), whichever is longer (the "**straight-line method**"). The monthly revenue amount shall be equal to the total contract value (i.e., the revenue arrangement's consideration) divided by the number of months included in the contractual term of the revenue arrangement or the service period.
  - B. If the services are expected to be performed in a pattern other than on a straight-line basis (e.g., services performed at a lower level of effort (LOE) during the early stages of the performance period because of a "ramp-up" in staffing or for any other reason), the straight-line method shall not be used to record revenue. In these situations revenue shall be recorded each month in an amount equal to the month's percentage of estimated monthly staffing (direct headcount) to the total estimated monthly staffing for the entire performance period, multiplied by the contract value (the "**monthly staffing method**"). Changes in the total estimated monthly staffing for the entire performance period shall be accounted for on a prospective basis.
- Type B: Unit-price service contract that contains separately-priced measurable units of work performed.
  - A. Revenue Recognition. Revenue shall be recorded each month in an amount equal to the total contract value divided by the total units of work to be performed over the service period (yields price per unit) multiplied by the actual units of work performed during the month ("**units-price method**").
  - B. If the unit(s) of work performed contain(s) (i) a customer acceptance provision, (ii) the right to invoice the customer is contingent on the customer acceptance provision, or (iii) there is uncertainty about obtaining the customer acceptance, revenue shall be recorded in the period when the written and properly authorized customer acceptance is obtained.
- Type C: Fixed-price service contract that is effectively treated as "time at marked-up rates" contract due to a formal or informal arrangement with the customer.
  - A. Revenue Recognition. Revenue shall be recorded each month in an amount equal to the direct labor hours expended, multiplied by the contractual billable fixed hourly rate(s) for each specified labor category (the "**time at marked-up rates method**").

3. Deferred Revenue. Any deferred fixed-price service revenue shall be reported in "Other Current Liabilities" in the division's Hyperion financial statement submissions.
4. Contract Value Revenue Recognition. During the service period, total inception-to-date (ITD) revenue recorded cannot exceed the negotiated/definitized contract value.
5. Other Direct Costs. Other Direct Cost (ODC) contract line items (CLINs), including materials, shall be accounted as separate units of accounting, with revenue recorded as costs are incurred and become billable.
6. Cost of Sales Recognition. All costs to fulfill (perform) the service obligations, including set-up costs, shall be expensed to Cost of Sales (COS) each month as incurred. Costs include all direct labor costs and allocable indirect (overhead) costs, in accordance with the costing practices and methods of the L-3 Business Unit. The monthly COS shall include "incurred but not invoiced" accruals for services performed by vendors and subcontractors, which have not yet been invoiced to the L-3 Business Unit. A contract estimate at completion (EAC) analysis or similar worksheet (see no. 7 below) may be used to accrue the cost of services performed during the period, which have not been invoiced to the Business Unit, or vouchered/processed for payment, including incurred vendor and subcontractor costs.
7. Estimates at Completion (EACs). The Business Unit should continue to prepare EACs for its fixed-price services contracts in accordance with its existing policies and procedures for the preparation of EACs. The EACs should continue to be used for management purposes (e.g., to manage costs and measure progress towards completion and to estimate total contract profit or loss).
8. Profit and Loss Recognition. The monthly profit for fixed-price service contracts not within the scope of SOP 81-1 shall be equal to the revenues less the cost of sales for the month. However, the following exceptions apply.
  - A. EAC indicates a loss. If the contract EAC indicates a loss on the fixed-price service contract (unit of accounting), the entire loss shall be recorded upon the contract award or when loss becomes known. Thereafter, all revenues shall be recorded at a zero profit<sup>(1)</sup> margin over the remaining service period (i.e., monthly revenue equals monthly cost of sales).

Recorded contract losses shall be reported on the "Loss Contract Reserves" line in the current liabilities section in the division's Hyperion financial statement submissions.

- B. EAC indicates a loss, but the unit of accounting is part of a multiple element revenue arrangement which is profitable. If a loss occurs on a fixed-price service contract (unit of accounting), which is part of a multiple-element arrangement that is profitable<sup>(1)</sup>, the entire loss should not be immediately recorded. Revenue should be recorded at zero profit margin. The loss shall be capitalized into inventory as an "investment in the contract," and amortized to cost of sales on a straight-line basis over the remaining service period.

Notes:

- (1) Contract EAC profits and losses should be determined at the gross margin level, unless the Business Unit is an L-3 U.S. Government contractor business that capitalizes Selling, General and Administrative costs as product/inventory costs, in which case the profit and loss measurement should be determined at the operating margin level.

- C. Two or more separate fixed-price service contracts (units of accounting) cannot be combined to avoid recognition of a loss.

#### 4. DEFINITIONS

Revenue Arrangements or Legally-Binding Revenue Arrangement. A revenue arrangement is a contractually binding revenue arrangements between the Business Unit and its customer, under which the Business Unit performs revenue-generating activities, or deliverables. Contracts consist of legally enforceable (binding) agreements in any form and include amendments, revisions and extensions of such agreements. Contracts executed (signed and dated by all parties) would normally include provisions that clearly specify the enforceable rights regarding goods and services to be provided and received by the parties, the consideration to be exchanged, and the manner and terms of settlement. Listed below are typical revenue arrangements (contracts) for L-3's Business Units.

- definitive basic contract,
- a definitive addition to an existing contract,
- an exercised option to an existing contract,
- a delivery order or task order received on an Indefinite Delivery/Indefinite Quantity (IDIQ) contract,
- a customer purchase order from a published product catalog of the Business Unit.
- a purchase order under a basic ordering (BOA) or purchasing agreement (BPA) with the customer.

Legally binding revenue arrangements also include "Letter Contracts" (FAR 16.603 PAR. 30.209.02). Letter Contracts are typically limited as to length of time and funding. Revenue and profits under a Letter Contract can only be recognized (i) when the signature on the Letter Contract is authorized (usually the contracting officer) (ii) when the source of funds are prescribed and (iii) up to the funding amount limitation.

Unit of Accounting. A unit of accounting is a unit, or "profit center" used for the accumulation of revenues and costs and the measurement of income or loss, for purposes of financial reporting. Usually, a unit of accounting is a single contract. However, a revenue arrangement (i.e., contract) may contain one or more separate units of accounting, depending on how many deliverables are contained in the revenue arrangement.

#### 5. PROCEDURES

All transactions that fall within the scope of this corporate accounting policy shall be reviewed at least quarterly to ensure all criteria required for revenue recognition are met.

The Corporate Controllers Office must be contacted if a Business Unit has a fixed-price service contract not covered by SOP 81-1 that differs from the three types of service revenue arrangements listed above. In addition, any question about how or when to apply this policy to a particular contract or order should be discussed with the Corporate Controller's Office.

Any question about how or when to apply this policy to a particular contract or order should be discussed with the Corporate Controller's Office.

## 6. FORMS AND SCHEDULES

Not applicable.

## 7. REFERENCES

AICPA, Statement of Position 81-1, *Accounting for Performance of Construction-type and Certain Production-Type Contracts*.

SEC Staff Accounting Bulletin No. 104, *Revenue Recognition*.

L-3 Revenue Recognition Guidelines.



# EXHIBIT F

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**From:** [REDACTED]  
[/O=ORGANIZATION/OU=IS/CN=RECIPIENTS/CN=RSCHMIDT]  
**Sent:** Tuesday, December 31, 2013 10:18:54 PM  
**To:** Hayes, Robert @ ISG - SFS  
**Subject:** FW: Phone Conversation

Robert, below is the note that captures the conversation I had with my Business Manager on Friday (he called me).

I do not know--and still would like to believe--there is no intent to deceive; however, there is little trust in more senior leadership or the system right now and I have no good answers. Communications from Dave to me or [REDACTED] are not optimal, not consistent, nor clear. My financials have been changed many times by Division without any discussion with me to explain why. I suppose they can do that--and routinely do before the monthly ops reviews.

Yesterday in a conversation with [REDACTED] over year end close outs, Dave, according to [REDACTED] stated that Army C-12 year end numbers needed to be whatever they had to be in order for Division to make \$40M EBIT. I am sure Dave meant something other than how the comment was taken. However, we, and especially the CFO, need to be careful with what we say--in particular in this current environment.

I discussed all of this (except the .."numbers needed to be whatever..." comment) with Dave on Friday. I also told him that folks in Madison [REDACTED] and others) were questioning our practices and expressing concern over invoice directives from Huntsville. Dave explained that invoicing in SAP with no immediate intent to extend the invoice to the Government was a "technique" to utilize since New York had forbid Division to accrue the designated Army C-12 Revenue Recovery amounts. This technique had the same year end effect on the financials that accrual would have had--potentially up to \$18M revenue and associated EBIT recognition. I asked Dave if this "technique" was known to and approved by New York. Dave answered that he did not know, but that Group had directed him to take this path. I asked if we had this direction in writing and the answer was no.

Hopefully all of this is another colossal miscommunication at one or more levels. I pressed Dave pretty hard on all of this suggesting that the organization was losing confidence and that our approach and some practices may invite closer scrutiny if/when audited. Finally, Dave agreed with all of my concerns, but stated Group was directing the current path forward--invoice in SAP, but not the Government. I have not had to sign the quarterly financial documents verifying my concurrence with accurate financial reporting since I left Madison over a year ago; but, I if I were ever asked to sign a document again like that now I would scrutinize it far more carefully before doing so.

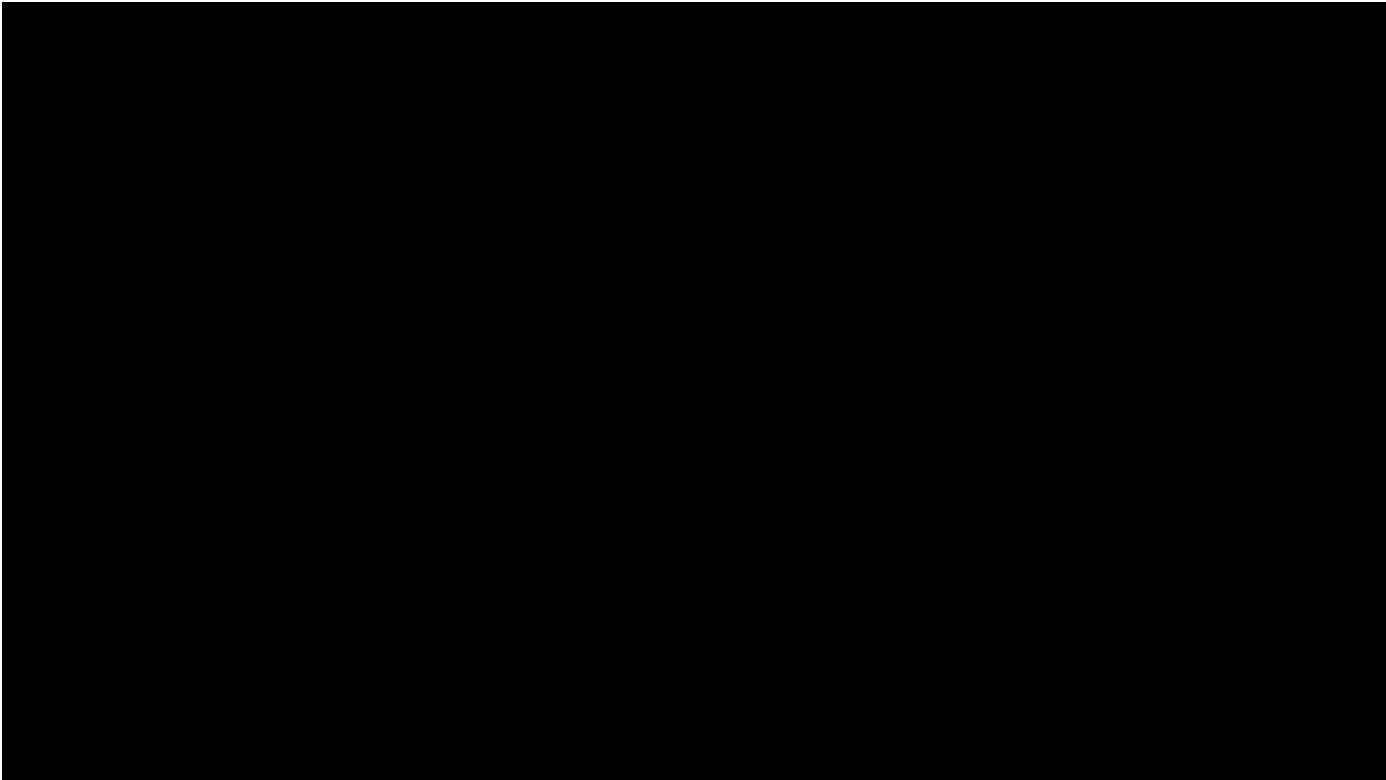
No one wants to make "the numbers" more than I do. I do believe we will recover most, if not all of the amounts of Revenue Recovery that our lawyers have determined we have legal entitlement to, however, there is a right way to do everything and it is not clear to some of us that we are doing that--again, perhaps that is due to poor communication or little understood techniques. But, what if it is not? I cannot afford to be wrong and I am not able to assuage my Business Manager's concerns. Now he wants to file a complaint. If my subordinates feel they need to call a hotline, then I am failing. I have asked [REDACTED] to be patient and suggested that he may have an opportunity to speak with someone in the future who might review our program. If that is not the case, then he and apparently others will make their voices heard. I don't know who the "others" might be--I did not ask.

I provide this to you for the record only. If someone is going to look into the issues previously raised, then I am confident all of the appropriate related processes and procedures will be reviewed and everyone will have a better understanding of our current posture and path forward. However, if the company is not going to address those concerns, then I am afraid one day the ultimate outcome here may not be good.

Thanks,

[REDACTED]

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Thanks,



9301066.00002

# EXHIBIT G

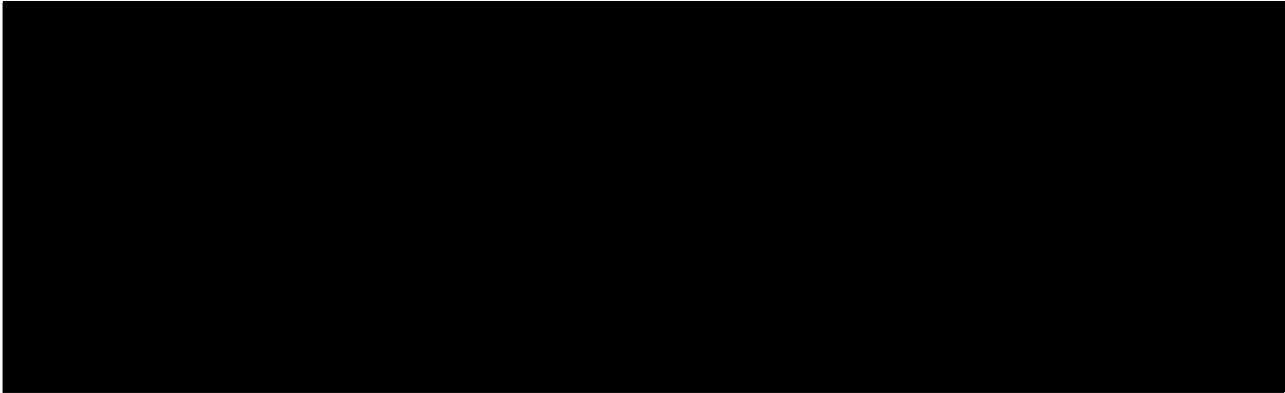



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