

# CORD

## The AEY Investigation

Item Type	House Majority Staff Report
Download date	2025-02-14 23:24:04
Link to Item	<a href="https://hdl.handle.net/20.500.14300/2391">https://hdl.handle.net/20.500.14300/2391</a>



UNITED STATES HOUSE OF REPRESENTATIVES  
COMMITTEE ON OVERSIGHT AND GOVERNMENT REFORM  
MAJORITY STAFF ANALYSIS  
JUNE 24, 2008

---

# THE AEY INVESTIGATION

---

## **TABLE OF CONTENTS**

<b>EXECUTIVE SUMMARY .....</b>	<b>1</b>
<b>I. BACKGROUND .....</b>	<b>3</b>
<b>II. THE COMMITTEE’S INVESTIGATION.....</b>	<b>5</b>
<b>III. QUESTIONABLE NEED FOR CONTRACT.....</b>	<b>6</b>
<b>IV. FAILURE TO CONSULT ARMS TRAFFICKER WATCH LIST .....</b>	<b>7</b>
<b>V. INADEQUATE ASSESSMENT OF AEY’S PAST PERFORMANCE.....</b>	<b>10</b>
<b>A. AEY’s Performance under Other Defense Department Contracts.....</b>	<b>10</b>
<b>B. AEY’s Performance under State Department Contracts.....</b>	<b>14</b>
<b>C. The Defense Department’s Evaluation of AEY’s Past Performance ...</b>	<b>16</b>
<b>D. AEY’s Possible Concealment of Contract Terminations .....</b>	<b>18</b>
<b>VI. POOR CONTRACT EXECUTION AND OVERSIGHT .....</b>	<b>19</b>
<b>VII. USE OF CHINESE AMMUNITION AND OTHER GOODS .....</b>	<b>22</b>
<b>VIII. CONCLUSION .....</b>	<b>26</b>

## **EXECUTIVE SUMMARY**

On January 26, 2007, the U.S. Army awarded a \$300 million contract to supply ammunition to the Afghan Security Forces to AEY, Inc., a Florida company owned by 21-year-old Efraim Diveroli. On May 23, 2008, after payments of \$66 million, the Army terminated AEY's contract for cause. On June 19, 2008, a federal grand jury indicted AEY, Mr. Diveroli, and three other individuals affiliated with AEY on criminal charges arising from AEY's procurement of ammunition under the contract.

At the request of Chairman Henry A. Waxman, the Committee initiated an investigation to answer a basic question: Why did the federal government award a military contract worth \$300 million to a company run by an inexperienced 21-year-old? In the course of the investigation, the Committee has received to date 9,500 pages of documents from AEY, 14,000 pages from the Defense Department, and 2,600 pages from the State Department. The Committee staff also interviewed Army contracting officials who oversaw the contract, Defense and State Department contracting officials who oversaw other contracts with AEY, the State Department official in charge of its arms trafficker "watch list," and other individuals. This staff analysis summarizes the information received by the Committee.

The AEY contract can be viewed as a case study in what is wrong with the procurement process. The record before the Committee indicates that there was questionable need for the contract in the first place, a grossly inadequate assessment of AEY's qualifications, and poor execution and oversight of the contract. The result is that U.S. taxpayers have paid over \$66 million to a contractor who provided "unserviceable" ammunition, much of it apparently of illegal Chinese origin.

### ***Questionable Need for Contract***

When the Defense Department awarded the \$300 million ammunition contract to AEY in January 2007, the contract may have been unnecessary. There appear to have been several options available to the Defense Department to obtain the ammunition without cost to the taxpayer. At the time the AEY contract was awarded, the Eastern European countries from which AEY purchased its ammunition, such as Bosnia, Bulgaria, and Hungary, had offered to donate weapons and ammunition without charge. Albania, one of AEY's main suppliers, had been seeking ways to dispose of tons of stockpiled weapons and ammunition as a condition of gaining membership in NATO and the European Union. In fact, the President of Albania traveled to Iraq in December 2007 and made a personal offer to General David Petraeus and Ambassador Ryan Crocker to provide ammunition free of charge.

There is no evidence that the Defense Department considered the option of obtaining the ammunition supplied by AEY through donations, despite that fact that this could have saved U.S. taxpayers the cost of the contract.

### ***Failure to Consult Arms Trafficker Watch List***

When the Defense Department awarded the AEY contract in January 2007, all of the primary actors in the transaction — AEY and its president, AEY’s middleman, and AEY’s supplier — were listed on the State Department’s watch list of potential arms traffickers. The State Department official in charge of the watch list described this as “a perfect trifecta.”

Both AEY and its president, Efraim Diveroli, had been placed on the watch list in April 2006 because they were under investigation by U.S. Immigration and Customs Enforcement for “numerous violations of the Arms Export Control Act and contract fraud.” The watch list warned that “future license applications involving Diveroli and/or his company should be very carefully scrutinized.” The watch list also had entries for Heinrich Thomet, the president of Evdin, Ltd., a company based in Cyprus that acted as AEY’s middleman; and Ylli Pinari, the head of the state-run Military Export Import Company (MEICO), which supplied the ammunition from Albania.

There is no evidence that the Defense Department checked the State Department watch list prior to executing the AEY contract.

### ***Inadequate Assessment of Past Performance***

Documents produced to the Committee show that federal agencies terminated, withdrew, or cancelled at least seven previous contracts with AEY, as well as four additional delivery orders under an eighth contract. Under these contracts, AEY provided potentially unsafe helmets to Iraq, failed to deliver at least 10,000 pistols to Iraq, and shipped poor quality ammunition to U.S. Special Forces. Government contracting officials repeatedly warned of “poor quality,” “damaged goods,” “junk” weapons, and other equipment in “the reject category,” and they complained on several occasions that AEY was “hurting the mission” and had “endangered the performance” of government agencies.

One Defense Department contracting official interviewed by the Committee recalled that when AEY failed to deliver Beretta pistols for the Iraq Security Forces, Mr. Diveroli offered excuses that were false, such as blaming AEY’s failure to perform on a hurricane in Florida that never occurred. A contracting official stated: “It’s not like we didn’t have the Internet in the Green Zone and couldn’t check on this.”

Based on a review of the documents, it appears that AEY’s method of operation was to underbid competitors without a secured source for products, attempt to locate suppliers and goods after the contract award, and provide nonconforming substitute products when it was unable to locate goods required under the contract. One Defense Department official interviewed by the Committee called this a “bait and switch” tactic. When asked whether AEY was the worst company he encountered in Iraq, this contracting officer responded: “yeah, that was my lemon I had to make lemonade out of.”

When the Defense Department was evaluating bidders for this \$300 million contract, a source selection team raised concerns with AEY’s proposal, rating the company as

“Unsatisfactory” in its ability to conduct international shipments and manage subcontractors. But the Defense Department contracting officer who awarded the contract changed that rating to “Good” and also gave AEY an “Excellent” rating for quality and timeliness, stating that previous contracting officers “indicated no quality issues.” The contracting official concluded: “There is essentially no doubt that AEY would perform in accordance with the delivery schedules and has no history of quality related problems.”

### ***Poor Execution and Oversight***

When the Defense Department awarded its \$300 million contract to AEY, it failed to establish adequate standards for the age, quality, or shipping of the ammunition. The documents indicate that AEY took advantage of the inadequate standards, informing suppliers: “there is no age restriction for this requirement so please take that into consideration when you look around,” and “Please be advised, there is no age restriction for this contract!!!”

The Department also failed to monitor AEY’s performance adequately. The contracting officer told the Committee that the Defense Contract Management Agency did not conduct inspections of the AEY ammunition before it was shipped. Inspections were also overlooked in Afghanistan after the arrival of the ammunition.

When inspections did occur, they found serious problems in the quality of the ammunition being provided. Defense Department officials described shipments that showed “significant corrosion” and were “unserviceable.” They described crates that “disintegrated from extensive termite damage” and were “no longer safe for transportation.” In some cases, the ammunition was over 60 years old. After being reprimanded by the Defense Department, an AEY official acknowledged that the company had delivered “shit ammo” to the Afghan security forces.

### ***Shipment of Illegal Chinese Ammunition***

AEY appears to have violated federal law banning the acquisition of Chinese munitions. Kosta Trebicka, an Albanian businessman hired by AEY, told the Committee that his job was to remove ammunition from wooden crates with Chinese markings and repack it into cardboard boxes before shipment to Afghanistan. According to Mr. Trebicka, Mr. Diveroli asked him “if there were any Chinese writings on the top of the packaging or inside the metallic cans” and instructed him to “make sure no written papers get inside the carton boxes.” AEY, Mr. Diveroli, and three others now face criminal charges arising from the procurement of Chinese ammunition.

## **I. BACKGROUND**

AEY, Inc., was founded by Michael Diveroli in 1999.<sup>1</sup> The company is located in Miami, Florida, and is run by Mr. Diveroli’s son, 22-year-old Efraim Diveroli, who serves as

---

<sup>1</sup> Florida Department of State, Division of Corporations, *Articles of Incorporation, AEY, Inc.* (Nov. 30, 1999) (online at [www.sunbiz.org/search.html](http://www.sunbiz.org/search.html)).

president of the company. Other company officials have included David Packouz, a 25-year-old former masseur, who served as vice president.

AEY received its first government contract in 2004. At that time, the company president, Efraim Diveroli, was 18 years old. The majority of AEY's contracts have been with the Defense Department or the State Department for the procurement of weapons, ammunition, or other military equipment. From 2004 through 2006, AEY received \$11 million in federal contracts, including \$2.4 million in contracts in 2006.<sup>2</sup>

AEY's largest government contract was awarded on January 26, 2007, by the U.S. Army to buy ammunition for the Afghan Security Forces.<sup>3</sup> The contract had a value of \$298 million. It was awarded to fulfill a centerpiece of U.S. foreign policy: the effort to train and equip Afghan security forces so that U.S. troops could return home. At the time, company president Efraim Diveroli was 21-years-old.

Between the award of the contract on January 26, 2007, and the termination of the contract on May 23, 2008, AEY was paid \$66 million under the contract. At that time, AEY had received five task orders worth a total of \$155 million, but had failed to deliver on \$88 million of the ammunition it had committed to procure.<sup>4</sup>

On March 25, 2008, the Department of Defense suspended AEY from future contracting with any federal agency based on evidence that under the Afghan Security Forces contract, AEY illegally purchased ammunition in Albania that was "manufactured in the People's Republic of China between 1962 and 1974" and that AEY had made a "false or misleading" representation that some of this Chinese ammunition had been manufactured in Hungary.<sup>5</sup> On May 23, 2008, after the Oversight Committee had scheduled a hearing relating to AEY, the Army terminated the contract for failure to deliver the ammunition in conformance with the terms and conditions of the contract.<sup>6</sup> On June 19, 2008, a federal grand jury returned a 71-count indictment charging

---

<sup>2</sup> This data comes from the Eagle Eye Federal Prime Contracts Database, a federal procurement database application published by Eagle Eye, Inc. The database contains data from 1999 to 2008 that is compiled from the Federal Procurement Data System, the federal contract tracking system established by the General Services Administration. *See also*, USASpending.gov, *Database Search for AEY, Inc.* (FY 2000-2008) (online at [www.usaspending.gov](http://www.usaspending.gov)).

<sup>3</sup> Procuring Contracting Officer, Source Selection Authority Decision Document for Request for Proposal W52P1J-06-R-0129: Non Standard Ammunition for Iraq (Jan. 22, 2007) (estimating AEY bid to be \$298,004,397); *\$298 M to AEY for Ammo in Afghanistan*, Defense Industry Daily (Mar. 21, 2007).

<sup>4</sup> House Committee on Oversight and Government Reform, *Transcribed Interview of Kim M. Jones* (June 19, 2008).

<sup>5</sup> Letter from Robert N. Kittel, Army Suspension and Debarment Official, to Efraim Diveroli, President, AEY, Inc. (Mar. 25, 2008).

<sup>6</sup> Letter from Kim M. Jones, Procuring Contracting Officer, U.S. Army Sustainment Command, to Efraim Diveroli, President, AEY, Inc. (May 23, 2008).

AEY, Inc., Efraim Diveroli, David Packouz, and two other individuals associated with AEY with 35 counts of procurement fraud under 18 U.S.C. § 1031, 35 counts of making false statements to the U.S. Army relating to the country of origin of the ammunition under 18 U.S.C. § 1001, and one count of conspiracy under 18 U.S.C. § 371, all relating to AEY's procurement of Chinese ammunition under the Afghan Security Forces contract.<sup>7</sup>

Questions have also been raised about the involvement of the U.S. Embassy in Albania in AEY's activities. On June 23, Chairman Waxman sent a letter to Secretary of State Condoleezza Rice raising concerns about the role of the Embassy in concealing the Chinese origins of ammunition shipped by AEY to Afghanistan.<sup>8</sup>

## II. THE COMMITTEE'S INVESTIGATION

On March 27, 2008, the *New York Times* published a long article describing AEY's procurement of "junk" ammunition under the Afghan Security Forces contract, its use of middlemen "suspected of illegal arms trafficking," and its use of illegal Chinese ammunition.<sup>9</sup> The same day, Chairman Waxman opened an investigation to learn (1) "the scope of AEY's contracts" with the Defense Department, (2) the Department's efforts "to determine whether AEY is a responsible contractor," (3) the Department's "efforts to investigate" allegations of legal violations by AEY, and (4) actions taken against the company as a result of the investigation.<sup>10</sup>

In the course of the investigation, the Committee has received 9,500 pages of documents from AEY, 14,000 pages from the Defense Department, and 2,600 pages from the State Department. None of these entities has completed its document productions to date. The documents include contracts, certificates of conformance, correspondence between AEY and agencies, and internal e-mails and correspondence. The Defense Department did not produce the contract file for the Afghan Security Forces ammunition contract until June 23, 2008, even though the contracting officer informed Committee staff that she submitted it for production in early April.<sup>11</sup>

The Committee staff has also interviewed Army contracting officials who oversaw the contract, Defense and State Department contracting officials who oversaw other contracts with

---

<sup>7</sup> Indictment, *United States v. AEY, Inc. et al.*, S.D. Fla. (No. 08-20574) (June 19, 2008).

<sup>8</sup> Letter from Henry A. Waxman, Chairman, to Condoleezza Rice, Secretary of State (June 23, 2008).

<sup>9</sup> *Supplier Under Scrutiny on Aging Arms for Afghans*, *New York Times* (Mar. 27, 2008).

<sup>10</sup> Letter from Henry A. Waxman, Chairman, to Robert M. Gates, Secretary of Defense (Mar. 27, 2008).

<sup>11</sup> House Committee on Oversight and Government Reform, *Transcribed Interview of Kim M. Jones* (June 19, 2008).



AEY, the State Department official in charge of its arms trafficker “watch list,” and other individuals.

This document is a staff analysis of the information received by the Committee. The evidence before the Committee shows that the AEY contract can be viewed as a case study of a dysfunctional procurement process. At nearly every turn, Defense Department officials made serious mistakes that have cost the taxpayers tens of millions of dollars. The documents and interviews show that there was a questionable need for the contract, an inadequate assessment of AEY’s qualifications, and poor execution and oversight of the contract.

### III. QUESTIONABLE NEED FOR CONTRACT

One of the first questions a federal agency should ask before entering into a contract is whether a contract is necessary to obtain the good or services sought. In the case of AEY, it is unclear that there was a need for the \$300 million contract.

Because Afghanistan had previously used weapons designed for former Warsaw Pact nations, the Department of Defense made a determination to supply the Afghan security forces with ammunition for those types of weapons rather than providing new weapons and ammunition manufactured by U.S. companies.<sup>12</sup> This old Warsaw Pact ammunition is not difficult to obtain. In fact, some countries from which AEY procured ammunition have been actively seeking ways to give away or dispose of their munitions. For example, Bosnia, Bulgaria, and Hungary have offered their weapons and ammunition to Afghanistan as donations to help aid the war effort.<sup>13</sup> The United States worked directly with Bosnia until 2004 to procure donations of weapons.<sup>14</sup>

Albania was a principal source for the ammunition provided under the AEY contract. When Albania sought membership in NATO and the European Union, both organizations imposed as a condition of entry the destruction of Albania’s stockpiled weapons and ammunition.<sup>15</sup> As a result, Albania has been destroying ammunition similar to the ammunition

---

<sup>12</sup> Government Accountability Office, *Afghanistan Security: Efforts to Establish Army and Police Have Made Progress, but Future Plans Need to Be Better Defined* (June 2005) (GAO-05-575).

<sup>13</sup> NATO, *Progress in Afghanistan: Bucharest Summit* (Apr. 2-4, 2008); Erwin Kauer, *Weapons Collection and Destruction Programmes in Bosnia and Herzegovina* (undated) (online at [www.bmlv.gv.at/pdf\\_pool/publikationen/small\\_arms\\_weapons\\_collection\\_destruction\\_e\\_kauer.pdf](http://www.bmlv.gv.at/pdf_pool/publikationen/small_arms_weapons_collection_destruction_e_kauer.pdf)).

<sup>14</sup> *Bosnia’s Leftover Guns: Sell, Give, Destroy?*, Christian Science Monitor (July 10, 2006).

<sup>15</sup> *The Munitions Challenges in Albania*, Journal of Mine Action (Spring 2000) (online at <http://maic.jmu.edu/Journal/4.1/munitions.htm>); EU Presidency Statement, *Small Arms and Light Weapons: Weapons Collection and Stockpile Management* (July 13, 2005) (online at [www.europa-eu-un.org/articles/en/article\\_4912\\_en.htm](http://www.europa-eu-un.org/articles/en/article_4912_en.htm)).

that the Defense Department paid AEY to procure. To date, over 40,000 tons of ammunition has been destroyed in Albania, but as much as 85,000 tons remain.<sup>16</sup>

Like Bosnia, Bulgaria, and Hungary, Albania also offered to donate its ammunition without charge to U.S. taxpayers. The Committee has been informed that on December 23, 2007, the Albanian President and Defense Minister traveled to Iraq to meet with General David Petraeus, the commander of Multi-National Force-Iraq, and Ryan Crocker, the U.S. Ambassador to Iraq. According to Major Larry Harrison, the Chief of the Office of Defense Cooperation, he personally accompanied the Albanian officials on this trip and attended the meeting. Major Harrison informed Committee staff that the Albanian officials offered to donate the country's surplus ammunition to Afghanistan and Iraq.<sup>17</sup>

According to Major Harrison, General Petraeus rejected this offer because Albania was known to possess large quantities of Chinese munitions, which cannot be received under United States law.<sup>18</sup>

#### **IV. FAILURE TO CONSULT ARMS TRAFFICKER WATCH LIST**

At the time the Defense Department awarded AEY its \$300 million contract to procure ammunition for Afghanistan, the State Department's "watch list" for suspicious international arms dealers included entries for nearly everyone involved with the transaction, including AEY and its president, Efraim Diveroli; Heinrich Thomet, the head of Cyprus-based Evdin, Ltd., a company that acted as AEY's middleman; and Ylli Pinari, the head official of the Albanian state-run Military Export Import Company (MEICO), which was AEY's supplier. During a briefing with Committee staff, the State Department official in charge of the watch list described this as "a perfect trifecta."<sup>19</sup>

In 1968, Congress passed the Arms Export Control Act to require companies engaging in the brokering of weapons and ammunition to obtain a license for each transaction.<sup>20</sup> The State

---

<sup>16</sup> See EOD Solutions, Ltd., *Demilitarisation Feasibility Study* (1999) (finding in excess of 125,000 tons of ammunition, 90% of which was over 30 years old); see also NATO Partnership for Peace, *Final Report on NATO PFP Trust Fund Project to Demilitarize Small Arms and Light Weapons in Albania* (May 2008) (noting that the Albanian Defense Ministry reported stockpiles of 100,000 tons of ammunition in 2001 and the subsequent destruction of 11,665 tons through NATO-led demilitarization programs).

<sup>17</sup> Majority Staff, House Committee on Oversight and Government Reform, *Interview of Major Larry D. Harrison* (untranscribed) (Apr. 28, 2008).

<sup>18</sup> *Id.*

<sup>19</sup> Briefing by David C. Trimble, Director, Directorate of Defense Trade Controls, U.S. Department of State, to House Committee on Oversight and Government Reform (June 10, 2008).

<sup>20</sup> 22 U.S.C. § 2778.

Department's Directorate of Defense Trade Controls may deny or revoke licenses if it "deems such action to be in furtherance of world peace, the national security or the foreign policy of the United States, or is otherwise advisable."<sup>21</sup> To help make these determinations, the State Department maintains a watch list of suspect individuals and entities based on information it receives from law enforcement, the intelligence community, and other government and non-governmental sources.<sup>22</sup> For each license application, the Department checks this watch list for information about the applicant, its subcontractors, and other parties associated with the transaction, all of which must be identified.<sup>23</sup> The State Department may recommend that the license be allowed, disallowed, or returned without action because of defects in the application.<sup>24</sup>

According to documents provided by the State Department in response to Committee requests, as of January 2007, all three entities involved in AEY's Defense Department contract — the purchaser, supplier, and middleman — were listed on the watch list.

Both AEY and its president, Efraim Diveroli, had been flagged by the State Department in April 2006 because they were under investigation by U.S. Immigration and Customs Enforcement (ICE).<sup>25</sup> According to an e-mail provided by the State Department, this investigation began in July 2005 and involved "numerous violations of the Arms Export Control Act and contract fraud."<sup>26</sup> ICE had described this investigation as involving "illegal firearms or firearm related transactions" by Efraim Diveroli and had therefore instructed U.S. officials encountering Efraim Diveroli to "[p]lease search luggage and photocopy any suspect documents."<sup>27</sup>

On December 12, 2006, the State Department made the following entry to the watch list regarding both Mr. Diveroli and his company, AEY:

There appear to be several suspicious characteristics of this company, including the fact that Diveroli is only 21 years old and has brokered or completed several multi-million

---

<sup>21</sup> International Traffic in Arms Regulations, 22 C.F.R. § 126.7.

<sup>22</sup> Briefing by David C. Trimble, Director, Directorate of Defense Trade Controls, Department of State, to House Committee on Oversight and Government Reform (June 10, 2008).

<sup>23</sup> *Id.*

<sup>24</sup> *Id.*; see also International Traffic in Arms Regulations, 22 C.F.R. § 129.7(d).

<sup>25</sup> AEY, Inc., License Registration, Department of State, Office of Defense Trade Controls (Apr. 4, 2006).

<sup>26</sup> E-mail from Michael C. Mentavlos to Michael C. Mentavlos (Oct. 9, 2007).

<sup>27</sup> U.S. Immigration and Customs Enforcement, *Tech II – Person Subject Display of Efraim Diveroli* (accessed on Aug. 14, 2006).

dollar deals involving fully and semi-automatic assault rifles. Future license applications involving Diveroli and/or his company should be very carefully scrutinized.<sup>28</sup>

AEY's middleman in this transaction was Evdin, Ltd., a Cyprus-based company, which reportedly purchased ammunition from Eastern European countries and sold it to AEY. The State Department placed the president of Evdin, Ltd., Heinrich Thomet, on the watch list on August 22, 2006. According to the watch list entry, the reasons for listing Mr. Thomet were described only in classified documents issued by the Central Intelligence Agency and the Defense Intelligence Agency.<sup>29</sup> AEY's business relationship with Evdin extended over multiple transactions. In responding to an August 2007 solicitation from AEY, Evdin noted that there was "a long lasting and strong relationship between EVDIN Limited and AEY Inc."<sup>30</sup>

The Albanian source for the ammunition was the state-run Military Export-Import Company (MEICO), which was headed by Ylli Pinari.<sup>31</sup> The State Department placed Mr. Pinari on the watch list on November 14, 2005, also based on reasons described only in classified documents.<sup>32</sup>

In addition to entities related to AEY's Defense Department contract to buy ammunition for Afghanistan, the State Department watch list also contained entries for individuals and companies associated with AEY under other contracts with the U.S. government. For example, in 2006, AEY entered into a Defense Department subcontract with Imex Group, Ltd., to provide ammunition to the Iraq Security Forces.<sup>33</sup> Imex is run by Petr Bernatik, a Czech national, who had been placed on the watch list on September 29, 2004, for reasons based on classified information.<sup>34</sup> According to the State Department, the current unclassified watch list entry for Mr. Bernatik states: "Identified arms trafficker in Czech Republic – should be denied."<sup>35</sup>

Checking the State Department arms trafficking watch list would seem to be a basic precaution to take before awarding a company a \$300 million contract to supply ammunition overseas. In the case of AEY, this step was not taken, apparently because AEY did not apply for

---

<sup>28</sup> U.S. Department of State, Directorate of Defense Trade Controls, *Microsoft Access Database Entry for AEY, Inc., Update Watch List Detail* (accessed May 6, 2008).

<sup>29</sup> U.S. Department of State, Directorate of Defense Trade Controls, *Watch List Search of Heinrich Thomet* (Feb. 6, 1991 to Present) (accessed May 6, 2008).

<sup>30</sup> Letter from Evdin, Ltd. to AEY, Inc. (Aug. 13, 2007).

<sup>31</sup> *See Albania Sells Off its Military Hardware*, BBC News (Apr. 17, 2002); *Supplier Under Scrutiny on Aging Arms for Afghans*, New York Times (Mar. 27, 2008).

<sup>32</sup> U.S. Department of State, Directorate of Defense Trade Controls, *Watch List Search of Ylli Pinari* (Feb. 6, 1991 to Present) (accessed May 6, 2008).

<sup>33</sup> *Contract between AEY, Inc. and Imex Group Ltd.* (2006).

<sup>34</sup> U.S. Department of State, Directorate of Defense Trade Controls, *Watch List Search of Petr Bernatik* (Feb. 6, 1991 to Present) (accessed May 6, 2008).

<sup>35</sup> *Id.*

a broker's license and because the Defense Department did not require one. The Defense Department contracting official who awarded the AEY contract told the Committee that she was not aware of the existence of the watch list and did not inquire with the State Department regarding potential watch list entries prior to the award.<sup>36</sup> She acknowledged, however, that it "may be useful" to arrange for a check of the watch list for contracts for nonstandard ammunition.<sup>37</sup>

## V. INADEQUATE ASSESSMENT OF AEY'S PAST PERFORMANCE

The evidence before the Committee indicates that the Defense Department's review of AEY's past performance was inadequate. By the time the \$300 million contract to AEY was awarded, the company had accumulated a long record of failed and dubious performance under other Defense Department and State Department contracts. This record was overlooked by contracting officials who awarded the contract to AEY.

### A. AEY's Performance under Other Defense Department Contracts

Documents obtained by the Committee show that AEY's performance on other Defense Department contracts was poor. Under these contracts, AEY provided potentially unsafe helmets to Iraq, failed to deliver at least 10,000 pistols to Iraq, and shipped poor quality ammunition to U.S. Special Forces. In all, the Defense Department has terminated at least five previous contracts with AEY due to the company's failure to perform adequately.<sup>38</sup> Additionally, the Defense Department had terminated four delivery orders under a separate contract.<sup>39</sup>

In October 2005, AEY delivered a shipment of damaged helmets to the Multi-National Security Transition Command-Iraq (MNSTC-I). A U.S. inspector who examined the shipment wrote:

---

<sup>36</sup> House Committee on Oversight and Government Reform, *Transcribed Interview of Melanie A. Johnson* (June 18, 2008).

<sup>37</sup> *Id.*

<sup>38</sup> U.S. Department of Defense, *AEY, Inc. Contract H92239-05-T-0010* (Feb. 25, 2005); U.S. Department of Defense, *AEY Inc. Contract W911RX-05-P-0267* (Sept. 27, 2005); U.S. Department of Defense, *AEY, Inc. Contract W911RX-05-P-0284* (Sept. 30, 2005); U.S. Department of Defense, *AEY Inc. Contract H92239-05-P-0034* (date unknown); U.S. Department of Defense, *AEY Inc. Contract W9124Q-06-P-0493* (Sept. 29, 2006).

<sup>39</sup> U.S. Department of Defense, *AEY Inc. Contract W914NS-05-D-9012* (Apr. 25, 2005).

The helmets came to Abu Ghraib by mistake. They are not very good. They have peeling paint and a few appear to have been damaged such as having been dropped. When I first saw them, I put them in the reject category.<sup>40</sup>

The same inspector later wrote to AEY about the helmets:

Some people at MNSTC-I got a little wound up when they saw the daily receiving report. They remembered the 10,000 helmets you sold them earlier this year and the junk AKs we still have in the warehouse. The concern was that, if they break and crack, are they ballistically correct? In other words, will they stop a bullet and what do we do if they don't? Several scenarios were being planned for you, none of them pleasant.<sup>41</sup>

Another MNSTC-I official was more blunt, writing: "Bottom line, the helmets are damaged goods and we don't want them."<sup>42</sup>

During an interview with Committee staff, the contracting officer for the helmet contract stated that AEY failed to provide proof that the helmets were safe. Instead, AEY submitted a document written in Chinese that did not reference the proper safety standards and "didn't even look like it ... matched up" with the shipment of helmets.<sup>43</sup> The contracting officer told the Committee that AEY was "nonperforming" on this contract and that he had a "particular issue" with Mr. Diveroli, explaining: "I just don't trust the guy."<sup>44</sup>

In late 2005, AEY failed to deliver more than 10,000 Beretta pistols under a \$5.6 million delivery order under a larger contract to supply the Iraq Security Forces. The contracting officer overseeing this contract pressed AEY to deliver the goods, writing: "I need immediate resolution on all outstanding 9 mm pistols. ... we are running critically low with inventory."<sup>45</sup> He subsequently concluded that Mr. Diveroli had provided a series of false excuses for failing to deliver. These excuses included claims that a plane crash destroyed key documents, that the German government was interfering with the delivery of Italian pistols, and that a hurricane hit Miami, Florida, where AEY is located, depriving Mr. Diveroli of water and making "his life ...

---

<sup>40</sup> E-mail from Richard Emmert, Quality Assurance Representative, Defense Contract Management Agency, to Lieutenant Commander Frank Futcher, Contracting Officer, Joint Contracting Command Iraq/Afghanistan, *et al.* (Oct. 16, 2005).

<sup>41</sup> E-mail from Richard Emmert, Quality Assurance Representative, Defense Contract Management Agency, to Efraim Diveroli, President, AEY, Inc. (undated).

<sup>42</sup> E-mail from Andrew Griffith, Multi-National Security Transition Command – Iraq, to Richard Emmert, Quality Assurance Representative, Defense Contract Management Agency, *et al.* (Oct. 18, 2005).

<sup>43</sup> House Committee on Oversight and Government Reform, *Transcribed Interview of Commander Frank Futcher* (June 13, 2008).

<sup>44</sup> *Id.*

<sup>45</sup> E-mail from Commander Robert Brooks, Joint Contracting Command-Iraq/Afghanistan, to Efraim Diveroli, President, AEY, Inc. (undated).

just terrible.”<sup>46</sup> According to another contracting official: “[W]e could tell there was no hurricane in Miami. It wasn’t like we didn’t have the Internet in the Green Zone.”<sup>47</sup>

After months of delays, the contracting officer concluded, “I couldn’t take anything [Mr. Diveroli] said credibly,” and he terminated the contract for cause.<sup>48</sup> He explained to the Committee:

All his reasons continued to build and build. And then it just got to the point where it was the straw on the camel’s back. And I said, look, no amount of consideration on your contracts to get these delivered are going to take care of the fact that you have been unable to deliver. You have not had one delivery order come in.<sup>49</sup>

The contracting officer also terminated AEY’s remaining delivery orders under the contract and declined to allow AEY to compete for future delivery orders under another contract for Iraq work.<sup>50</sup> He told the Committee that AEY repeatedly engaged in “bait and switch” tactics by substituting nonconforming goods in place of those required by the contract. He concluded that AEY’s performance was “extremely poor.” When asked whether AEY was the worst company he dealt with in Iraq, he responded: “Yes, they were. ... AEY, yeah, that was my lemon I had to make lemonade out of.”<sup>51</sup>

AEY also performed poorly on past contracts for ammunition, including the same type of ammunition AEY later delivered to Afghanistan. In April 2005, U.S. Army Special Operations Command (USASOC) partially terminated an ammunition contract with AEY because the company “failed to deliver acceptable goods,” “provided no notice of an excusable delay,” and “provide[d] inadequate assurance of future performance.”<sup>52</sup> A few weeks later, USASOC partially terminated a second ammunition contract due to “failure to deliver acceptable goods.”<sup>53</sup>

---

<sup>46</sup> House Committee on Oversight and Government Reform, *Transcribed Interview of Commander Robert Brooks* (June 13, 2008); House Committee on Oversight and Government Reform, *Transcribed Interview of Commander Frank Futcher* (June 13, 2008).

<sup>47</sup> House Committee on Oversight and Government Reform, *Transcribed Interview of Commander Frank Futcher* (June 13, 2008).

<sup>48</sup> House Committee on Oversight and Government Reform, *Transcribed Interview of Commander Robert Brooks* (June 13, 2008).

<sup>49</sup> *Id.*

<sup>50</sup> *Id.*

<sup>51</sup> *Id.*

<sup>52</sup> U.S. Department of Defense, *Amendment of Solicitation/Modification of Contract No. H92239-05-P0072* (Apr. 4, 2005).

<sup>53</sup> E-mail from Major Michael Taylor, Contracting Officer, U.S. Army Special Operations Command, to Efraim Diveroli, President, AEY, Inc. (Apr. 26, 2005).

Defense Department documents show that AEY delivered a type of ammunition that “was second-generation reloaded ammunition, and is not acceptable by military standards.”<sup>54</sup> The ammunition had burn marks, corrosion, and defects so serious that “if fired pressure could buildup [and] cause the weapons systems to malfunction.”<sup>55</sup> Rather than correct the defective ammunition, AEY blamed the ammunition inspector, calling her “extremely irritable” and accusing her of “foul play.”<sup>56</sup>

In the two years preceding the award of the Afghanistan contract, AEY experienced a number of other performance problems:

- On December 1, 2006, less than two months prior to the Afghanistan award, the Army terminated an AEY contract for cause after the company failed to deliver 150 mounts for gun scopes. After initially falling behind on deliveries, Mr. Diveroli pleaded with the contract officer not to cancel the contract, writing: “if God Forbid we were to have our contract terminated this would be devastating and possibly crippling to us as a very small business concern.”<sup>57</sup> When AEY failed to deliver the gun mounts after the Army granted two additional extensions, the contract was terminated.<sup>58</sup>
- In February 2006, AEY failed to deliver “J-Point Scopes” under an Army contract. The contract was terminated for cause.<sup>59</sup> The contracting official wrote that after initial delays, he had given AEY the benefit of the doubt because it was a small business. AEY then sent a “sample” product that was rejected as “cheap copies of an actual patented J-Point system.”<sup>60</sup> After repeatedly receiving “excuses and invalid reasons” for AEY’s failure to deliver, he realized the Army “was being strung along by a vendor who knew he was not able to perform,” and he terminated the contract for default.<sup>61</sup>

---

<sup>54</sup> Memorandum from Richard McArdle, Chief, Plans and Operations, U.S. Army Special Operations Command, to USASOC Contracting Office (Apr. 5, 2005).

<sup>55</sup> *Id.*

<sup>56</sup> E-mail from Efraim Diveroli, President, AEY, Inc., to U.S. Army Special Operations Command (Apr. 5, 2005).

<sup>57</sup> Letter from Efraim Diveroli, President, AEY, Inc., to Jesse Brennan, Contracting Officer, Army Contracting Agency (undated).

<sup>58</sup> Letter from Jesse Brennan, Contracting Officer, Army Contracting Agency, to Efraim Diveroli, President, AEY, Inc. (Dec. 1, 2006).

<sup>59</sup> E-mail from Donald Peters, Contract Specialist, Army Contracting Agency, to Efraim Diveroli, President, AEY, Inc. (undated).

<sup>60</sup> U.S. Department of Defense, *AEY, Inc. Contract W991RX-05-P-0267* (Sept. 27, 2005); E-mail from Major Kim D. Zimmerman to Donald W. Peters (Jan. 12, 2006).

<sup>61</sup> Declaration of Donald W. Peters, Contract Specialist, *Bid Protest (Docket No. 55346)* (Mar. 6, 2006).



- In August 2005, AEY failed to deliver machine guns and pistols to Iraq. In an e-mail obtained by the Committee, the contracting official demanded an explanation for the delay, writing that “over TWO months have elapsed without delivery of the order.”<sup>62</sup>

## **B. AEY’s Performance under State Department Contracts**

AEY also had a history of poor performance of providing munitions and other equipment under contracts and purchase orders with the State Department. As a result, the State Department has terminated or cancelled two contracts due to AEY’s inability to perform.<sup>63</sup>

For example, under a 2006 contract for field equipment for the U.S. Embassy in Colombia, AEY provided the wrong model of laser pointers and rifle attachments as required under the solicitation.<sup>64</sup> In addition, AEY failed to obtain the proper export license for the goods and could not meet the required shipping date.<sup>65</sup> AEY also attempted to provide unacceptable substitute goods under this contract without notifying the Department.<sup>66</sup> In a November 1, 2006, memo, a State Department official noted:

The manufacturer of the product AEY quoted contacted [the Department] to inform us that AEY is not an approved distributor and will not be able to provide the products quoted to Bogota. ... In response, AEY provided information on totally different products by totally different manufacturers. ... All are concerned that if AEY were not questioned, AEY would have provided different products without State’s knowledge. Now State knows AEY plans to provide products untested. ... Is this considered “bait and switch”?<sup>67</sup>

The State Department canceled this order November 2, 2006.<sup>68</sup>

---

<sup>62</sup> E-mail from Vance Jochim, Department of State End State Task Force and Iraq Commission on Public Integrity, to Efraim Diveroli, President, AEY, Inc., *et al.* (Aug. 30, 2005).

<sup>63</sup> U.S. Department of State, *AEY Inc. Contract SAQMPD-06-M-3245* (Sept. 30, 2006); U.S. Department of State, *AEY Inc. Contract SAQMPD-06-M-3139* (Feb. 1, 2007).

<sup>64</sup> U.S. Department of Defense, *AEY, Inc. Contract SAQMPD06M3246* (Sept. 30, 2005); E-mail from Kevin Higgins, Technical Advisor, to Timothy E. Henderson, and Suzanne T. Sharp, Contract Specialist (Oct. 25, 2006).

<sup>65</sup> E-mail from Timothy Henderson to Suzanne T. Sharp, Contract Specialist (Oct. 24, 2006).

<sup>66</sup> Memorandum from Vincent J. Chaverini, Jr., Contracting Officer, to Dennis Gallagher, Legal Advisor (Nov. 1, 2006).

<sup>67</sup> *Id.*

<sup>68</sup> E-mail from Suzanne T. Sharp, Contract Specialist, to Efraim Diveroli, President, AEY, Inc. (Nov. 2, 2006); letter from Vincent J. Chaverini, Jr., Contracting Officer, to Efraim Diveroli, President, AEY, Inc. (Nov. 2, 2006).

Under a 2006 contract with the State Department to deliver holographic weapons systems with night vision scopes to the U.S. Embassy in Colombia, AEY failed to deliver the goods by the deadline because the manufacturer would not sell to them.<sup>69</sup> Again, AEY offered a substitute.<sup>70</sup> The contracting officer rejected AEY's proposal, stating: "you were awarded subject order based on the product you proposed via fedbid auction thus you are hereby directed to comply."<sup>71</sup> AEY failed to deliver any equipment under this contract, and on March 1, 2007, the contract was "terminated for cause" because the weapon system was not delivered "in a timely manner."<sup>72</sup>

Under a 2005 contract for tactical equipment for use in Iraq, including optical sights and weapons adaptors, AEY repeatedly ignored a contracting officer's explicit warnings that only the exact products under the contract would be accepted.<sup>73</sup> AEY delivered only one item by the April 18, 2005, delivery date, and it was rejected as nonconforming.<sup>74</sup> The contracting officer wrote to Mr. Diveroli: "I 'Needed' this equipment by 4/18. So the fact that I still do not have it is hurting the mission."<sup>75</sup> The State Department withdrew its order and obtained much of the equipment from other vendors. In a letter to AEY, the contracting officer wrote:

You are hereby notified that your failure to deliver the below listed items on April 18, 2005 as stated and in accordance with subject has endangered the performance of the Department of State mission. Further, in subsequent correspondence your promises of delivery have not been met. You are hereby informed that the undelivered items are

---

<sup>69</sup> U.S. Department of State, *AEY, Inc. Contract SAQMPD-06-M3139* (Sept. 28, 2006); E-mail from Patrick Fulya, Account Manager, to Doug Stuck, FedBid (May 11, 2007).

<sup>70</sup> Memorandum from Dennis J. Gallagher, Legal Advisor, to Benita D. Williams, Contracting Officer (Jan. 19, 2007).

<sup>71</sup> E-mail from Benita D. Williams, Contracting Officer, to Efraim Diveroli, President, AEY, Inc. (Feb. 15, 2007).

<sup>72</sup> Letter from Benita D. Williams, Contracting Officer, to Efraim Diveroli, President, AEY, Inc. (Mar. 1, 2007).

<sup>73</sup> U.S. Department of State, *AEY, Inc. Contract SAQMPD-05-M-1722* (Apr. 14, 2005); *see, e.g.*, E-mail from Amy Maroney, Weapons Program Coordinator, to Efraim Diveroli, President, AEY, Inc. (Apr. 18, 2005); E-mail from Amy Maroney, Weapons Program Coordinator, to Efraim Diveroli, President, AEY, Inc. (undated); E-mail from Amy Maroney, Weapons Program Coordinator, to Efraim Diveroli, President, AEY, Inc. (Apr. 15, 2005).

<sup>74</sup> E-mail from Randarda R. Mathis, Weapons Program Coordinator, to Benita Williams, Contracting Officer (undated).

<sup>75</sup> E-mail from Amy Maroney, Weapons Program Coordinator, to Efraim Diveroli, President, AEY, Inc. (Apr. 20, 2005).

being withdrawn from subject order. The DoS mission can no longer be delayed due to your inability to produce the items as stated in subject order.<sup>76</sup>

Also in 2005, AEY offered nonconforming substitute carbines on three separate but related contracts. The State Department's contracting officers warned AEY repeatedly that the "product requested is for a purpose, and no substitutes will be accepted."<sup>77</sup> After the State Department rejected the weapons offered by AEY in October 2005, it modified the contracts by reducing the price and extending the delivery date, only to have AEY deliver additional nonconforming goods.<sup>78</sup>

In 2006, AEY again offered nonconforming goods on a contract for rail adaptor systems, leading a State Department official to complain that AEY should provide the specific part that the State Department requested rather than "what the vendor is trying to convince us to use."<sup>79</sup> One State Department official wrote to a colleague: "We have had problem[s] with AEY in the past."<sup>80</sup>

### **C. The Defense Department's Evaluation of AEY's Past Performance**

The Defense Department's "source selection team" for the \$300 million Afghan ammunition contract evaluated AEY's past performance based only on three contracts identified by AEY.<sup>81</sup> A review of a database available to the source selection team would have identified the other Defense and State Department contracts awarded to AEY.<sup>82</sup> Apparently, however, AEY's performance under other contracts with the Departments of Defense and State was not considered.

---

<sup>76</sup> Letter from Benita D. Williams, Contracting Officer, to Efraim Diveroli, President, AEY, Inc. (May 25, 2005).

<sup>77</sup> E-mail from Nigel McKenzie to Efraim Diveroli, President, AEY, Inc. (Oct. 26, 2005).

<sup>78</sup> E-mail from Kenneth J. Beaudoin to Nigel A. McKenzie (Oct. 31, 2005); E-mail from Steven R. Frazer, Branch Chief, Mobile Antiterrorist Training Team, to Patrick Villegoueix-Ritaud, Functional Analyst IV and Coordinator Diplomatic Security (Jan. 19, 2006); E-mail from Nigel A. McKenzie to James Hopkinson, Kwan Chun and Troy Shirley (Mar. 28, 2006).

<sup>79</sup> E-mail from Diane E. Toledo-Gaskins, Procurement Specialist, to Russell Dickinson, Weapons Program Officer (Oct. 11, 2006).

<sup>80</sup> E-mail from Russell Dickinson, Weapons Program Officer, to Laverne G. Jones, Contracting Officer (Oct. 11, 2006).

<sup>81</sup> Procuring Contracting Officer, *Source Selection Authority Decision Document for Request for Proposal W52P1J-06-R-0129: Non Standard Ammunition for Iraq* (Jan. 22, 2007).

<sup>82</sup> The Federal Procurement Data System identifies over 90 contracts awarded to AEY prior to January 2007. Information on these contracts was available through the database at the time the \$300 million Afghan ammunition contract was awarded.

The source selection team considered AEY's record of (1) on-time delivery, (2) quality, (3) international movement of ammunition, and (4) success as a "system integrator," which included experience in "the identification of ammunition appropriate for foreign weapon systems," "the ability to establish quality control, safety, and transportation plans," and "adhering to the regulations and policies of both foreign and U.S. Governments."<sup>83</sup> The team gave AEY a mixed rating.

The source selection team rated AEY's past history of on-time delivery and quality as "Excellent." The contracting officer who reviewed the source selection team's evaluation agreed, concluding:

There essentially is no doubt that AEY would perform in accordance with the delivery schedules and has no history of quality related problems. Based on this, AEY's initial rating was "Excellent."<sup>84</sup>

With respect to AEY's history of "international movement" and experience as a "systems integrator," the source selection team concluded that AEY's past performance was "Unsatisfactory." The team found that the contracts submitted by AEY for consideration failed to demonstrate "past performance experience with contracts for large number of varied items and the ability to identify appropriate ammunition to stated foreign weapon systems." The team concluded: "Lacking this experience, there is substantial doubt that AEY could perform in accordance with the solicitation requirements."<sup>85</sup>

After being notified of its unsatisfactory rating, AEY submitted additional information about one contract. The additional information did not change the view of the source selection team, which continued to rate the company's experience as "Unsatisfactory."<sup>86</sup>

On January 22, 2007, the contracting official who ultimately awarded the contract overruled the source selection team and raised AEY's score from "Unsatisfactory" to "Good." During an interview with Committee staff, she stated that she disagreed with the source selection team's conclusion that the contract reviewed was insufficient evidence of prior experience in these categories.<sup>87</sup> She acknowledged that her change made "a difference," and she stated that AEY "would not [have] gotten the award" without this adjustment.<sup>88</sup> In changing the rating,

---

<sup>83</sup> Procuring Contracting Officer, *Source Selection Authority Decision Document for Request for Proposal W52PIJ-06-R-0129: Non Standard Ammunition for Iraq* (Jan. 22, 2007).

<sup>84</sup> *Id.*

<sup>85</sup> *Id.*

<sup>86</sup> *Id.*; House Committee on Oversight and Government Reform, *Transcribed Interview of Melanie A. Johnson* (June 18, 2008).

<sup>87</sup> House Committee on Oversight and Government Reform, *Transcribed Interview of Melanie A. Johnson* (June 18, 2008).

<sup>88</sup> *Id.*

however, she had gathered no additional information about these contracts beyond what was available to the source selection team.<sup>89</sup>

Even given the limited universe of contracts considered by the contracting officer, it is difficult to understand why AEY was rated “Excellent” for on-time delivery and quality and “Good” for experience in international movement and systems integration. One of the three contracts reviewed was AEY’s contract to supply munitions to the Iraq Security Forces, including 10,000 Beretta pistols. As discussed above, this pistol delivery order was terminated for cause, with the contracting officer who terminated it stating that AEY’s performance had been “extremely poor” and that AEY was the worst contractor he dealt with in Iraq.

When the Committee asked the contracting official why she concluded that AEY had “no history of quality related problems,” she explained that she obtained her information from a different official who was not familiar with AEY’s poor performance. She acknowledged: “If I would have been aware of that information, it would have entered into the decision.”<sup>90</sup>

#### **D. AEY’s Possible Concealment of Contract Terminations**

In order to compete for a Defense Department contract, AEY was required to complete and submit a federal form called an Online Certifications and Representations Application (ORCA), which contains questions about the company, its activities, and its contracting history.<sup>91</sup> AEY submitted this form for 2005, 2006, and 2007. On each ORCA form, AEY certified that it “has not, within a three-year period preceding this offer, had one or more contracts terminated for default by any Federal agency.”<sup>92</sup>

Documents provided to the Committee identify at least eleven AEY contracts and delivery orders that were terminated because AEY failed to perform adequately, including at least three that were officially terminated for default. These include two contracts the Defense Department terminated in 2006 and another contract the State Department terminated in 2007.<sup>93</sup>

---

<sup>89</sup> *Id.*

<sup>90</sup> *Id.*

<sup>91</sup> U.S. Department of Defense, *AEY, Inc. Contract W52P1J-07-0004*, Amendment 1 (Jan. 26, 2007).

<sup>92</sup> AEY, Inc., *Online Representations and Certification Application* § 52.209-5 (June 17, 2005) (valid through June 17, 2006); AEY, Inc., *Online Representations and Certifications Application* § 52.209-5 (July 25, 2006) (valid through July 2, 2007); AEY, Inc., *Online Representations and Certification Application* § 52.209-5 (July 2, 2006) (valid through July 2, 2008).

<sup>93</sup> Settlement Agreement, Appeal of AEY, Inc. Under Contract Nos. W911RX-05-P-0284 and W911RX-05-P-0267, Armed Services Board of Contract Appeals No. 55346 and 55363 (Mar. 17, 2006); U.S. Department of State, *AEY, Inc. Contract SAQMPD-06-M-3139* (Sept. 28, 2006).

According to the Army contracting official who awarded the Afghanistan ammunition contract, if AEY's ORCA form had listed these contract terminations, it "may have" affected the decision.<sup>94</sup>

The failure of AEY to report its prior terminations may be a criminal false statement. The ORCA form explicitly states that "a false, fictitious, or fraudulent certification may render the maker subject to prosecution" under the federal false statements statute, 18 U.S.C. § 1001, a crime punishable by up to five years of imprisonment.<sup>95</sup>

## VI. POOR CONTRACT EXECUTION AND OVERSIGHT

In the contract awarded to AEY in January 2007 to supply ammunition to Afghan security forces, the Defense Department provided little or no guidance on the quality or condition of the ammunition required. The contract called for ammunition that was "serviceable," but it gave no further details.<sup>96</sup> The contract also specifically permitted the use of "surplus" ammunition.<sup>97</sup> The contract failed to set an age limit for the ammunition purchased by AEY. A section of the contract in which the contracting officer answered questions raised by bidders addressed this issue specifically:

Question 2: Is there an age limitation on the items to be delivered under this contract?

Answer: No, but material must be serviceable and issuable to all units without qualifications.<sup>98</sup>

Despite the hazardous nature of the cargo, the contract also had no specific restrictions on the type of packaging to be used in transporting ammunition. The contract had the following instruction, without any elaboration: "Package in cartons in accordance with the best commercial practice for international shipment."<sup>99</sup>

The record does not adequately explain why the Defense Department failed to include proper quality, age, and packaging requirements in the contract. Other military contracts for similar ammunition included such restrictions.<sup>100</sup> For example, contracts to obtain nonstandard

---

<sup>94</sup> House Committee on Oversight and Government Reform, *Transcribed Interview of Melanie A. Johnson* (June 18, 2008).

<sup>95</sup> AEY, Inc., Online Representations and Certifications Application § 52.209-5 (Sept. 25, 2006) (valid through Sept. 5, 2007).

<sup>96</sup> U.S. Department of Defense, *AEY, Inc. Contract W52P1J-07-0004* (Jan. 26, 2007).

<sup>97</sup> *Id.*

<sup>98</sup> *Id.*

<sup>99</sup> *Id.*

<sup>100</sup> Briefing by Lieutenant General William Mortensen, Deputy Commander, U.S. Army Materiel Command, to House Committee on Oversight and Government Reform (Apr. 11,

ammunition for use by the Iraq Security Forces typically include a restriction that the ammunition be 20 years old or newer.<sup>101</sup>

Documents obtained by the Committee show that AEY paid close attention to age restrictions in contracts, including the Afghanistan ammunition contract, and sought to take advantage of the lack of such restrictions in order to obtain older, cheaper ammunition. In one request for price quotes under the Afghanistan contract, AEY wrote to potential suppliers, “there is no age restriction for this requirement so please take that into consideration when you look around.”<sup>102</sup> In another request for ammunition for Afghanistan, AEY wrote, “Please be advised, there is no age restriction for this contract!!!”<sup>103</sup> In a third request, AEY noted, “We remind you that although target prices seem low, we already have the contract with the US Government signed ... and ANY age ammunition is acceptable.”<sup>104</sup>

In July 2007, when a restriction requiring ammunition less than 20 years old was relaxed on a different ammunition contract, an AEY employee wrote on the document: “Wonderful!”<sup>105</sup>

As a result of the lack of appropriate specifications, much of the ammunition AEY provided under the Afghanistan contract was 40, 50, or even 60 years old. AEY purchased ammunition from Bulgaria that had been manufactured as early as 1944.<sup>106</sup> It bought ammunition from Slovakia that was produced in 1956.<sup>107</sup>

AEY also took advantage of the Defense Department’s failure to conduct rigorous inspections. According to the contracting officer, the Defense Contract Management Agency did not conduct consistent inspections of AEY’s ammunition before it was shipped, citing “a plethora of reasons,” including an inability to send inspectors to the various Eastern European countries from which AEY procured ammunition.<sup>108</sup> In Afghanistan, both DCMA and the

---

2008); House Committee on Oversight and Government Reform, *Transcribed Interview of Melanie A. Johnson* (June 18, 2008).

<sup>101</sup> House Committee on Oversight and Government Reform, *Transcribed Interview of Melanie A. Johnson* (June 18, 2008).

<sup>102</sup> AEY, Inc., Request for Quotation for Munitions (undated) (emphasis in original).

<sup>103</sup> AEY, Inc., Request for Quotation for Munitions (undated).

<sup>104</sup> E-mail from Efraim Diveroli, President, AEY, Inc., to “Amit,” *et al.* (undated).

<sup>105</sup> *U.S. Department of Defense, Solicitation W52P1J-07-R-0104, Amendment 2* (July 18, 2007).

<sup>106</sup> *Contract between AEY, Inc. and Arcus Co.* (Nov. 11, 2007).

<sup>107</sup> E-mail from Efraim Diveroli, President, AEY, Inc., to Vladimir Duris, ZVS Holding (Nov. 21, 2007).

<sup>108</sup> House Committee on Oversight and Government Reform, *Transcribed Interview of Kim M. Jones* (June 19, 2008).

Combined Security Transition Command–Afghanistan (CSTC-A) took the position that because of resource limitations “100 percent inspection” of ammunition shipments was not possible.<sup>109</sup>

When military officials did conduct inspections, they discovered serious problems with the ammunition AEY delivered. For example, in one report obtained by the Committee, a Defense Department official described the quality of a shipment of ammunition on March 10, 2008:

Initial inspection showed that significant corrosion, rust and an oily material was evident on the ammunition; CSTC-A ammunition representatives reporting ammo is unserviceable. Munitions from this shipment are judged to be barely within limits of safe storage and transportation.<sup>110</sup>

The Defense Department official also noted that the ammunition was not properly labeled or categorized:

Ammunition was sent in mislabeled ammunition boxes. ... Because a majority of the boxes were mis-labeled, we have no confidence for what is in each box. Every box has to be opened, identified and counted. Several boxes are just a pile of loose rounds. Also, documentation is missing. There were no packing slips, hazardous declaration, nor invoice attached to the pallets of ammunition.<sup>111</sup>

In another report, dated February 28, 2008, the same Defense Department official described how AEY’s packaging was so poor that a shipment of ammunition could not be unloaded from the airplane:

During aircraft movement, three crates disintegrated from extensive termite damage to the wood. Two skids containing fuses show significant damage to packaging crates and termite infestation. An additional skid carrying fuses showed damage from ground-handling movement prior to arrival/delivery at Kabul Intl Airport. Seven wooden crates contained on one skid disintegrated when removed from the aircraft by ground handlers due to significant termite damage. Significant external water and rust damage to metal fuse casings. ... Munitions from this shipment are no longer safe for transportation.<sup>112</sup>

On March 18, 2008, the Army sent a letter to AEY stating that its ammunition “has been found to be unacceptable” and demanding that AEY fix the problems.<sup>113</sup> In an e-mail sent the

---

<sup>109</sup> *Id.*

<sup>110</sup> AEY, Inc., Certificate of Conformance (No. AFG-002-63) (Feb. 29, 2008) (CSTC-A certification statement dated Mar. 10, 2008).

<sup>111</sup> *Id.*

<sup>112</sup> AEY, Inc., Certificate of Conformance (No. AFG-0004-10) (Feb. 19, 2008) (CSTC-A certification statement dated Feb. 28, 2008).

<sup>113</sup> Letter from Kim M. Jones, Contracting Officer, U.S. Army Sustainment Command, to Efraim Diveroli, President, AEY, Inc. (Mar. 18, 2008).



same day, an AEY employee privately acknowledged that the company had delivered “shit ammo” to Afghanistan.<sup>114</sup>

AEY also failed to deliver ammunition on time. A January 8, 2008, letter from the Army stated that AEY was four months late on the shipment of nearly two million rounds of ammunition, and eight months late on the shipment of another three million rounds.<sup>115</sup> In a letter to the Army, AEY blamed its delays on subcontractors and bureaucratic mix-ups, writing:

Unfortunately, several key deals AEY has relied on, have either fell through or suffered serious discrepancies and delays with vendors who are unable to stand by their original commitment, by means of licensing, documentation, and availability.<sup>116</sup>

According to the contracting officer, AEY provided a variety of excuses for its late deliveries, including a supplier who “breached the contract and sold their ammunition to someone else,” “substandard stock,” and “the changing price of the Euro.”<sup>117</sup>

## VII. USE OF CHINESE AMMUNITION AND OTHER GOODS

American contractors are prohibited from obtaining weapons or ammunition manufactured in the People’s Republic of China. The Defense Federal Acquisition Regulation Supplement states:

Any supplies or services covered by the United States Munitions List that are delivered under this contract may not be acquired, directly or indirectly, from a Communist Chinese military company.<sup>118</sup>

The Defense Department solicitation for the \$300 million ammunition contract expressly incorporated this prohibition.<sup>119</sup> AEY had also been awarded other Defense Department

---

<sup>114</sup> E-mail from Joseph Wachtel, AEY, Inc., to Yassen Kounchev, Avair, Ltd. (Mar. 18, 2008).

<sup>115</sup> Letter from Kim M. Jones, Contracting Officer, U.S. Army Sustainment Command, to Efraim Diveroli, President, AEY, Inc. (Jan. 8, 2008).

<sup>116</sup> Letter from Efraim Diveroli, President, AEY, Inc., to Daniel Stackwick, U.S. Army (undated).

<sup>117</sup> House Committee on Oversight and Government Reform, *Transcribed Interview of Kim M. Jones* (June 19, 2008).

<sup>118</sup> Defense Federal Acquisition Regulation Supplement § 252.225-7007, “Prohibition on Acquisition of United States Munitions List Items from Communist Chinese Military Companies” (Sept. 2006).

<sup>119</sup> U.S. Department of Defense, *AEY, Inc. Contract W52P1J-07-D-0004*, Amendment 6 (Jan. 26, 2007).

contracts that explicitly included this prohibition.<sup>120</sup> For example, a contract awarded to AEY from the Defense Department on September 21, 2006, stated:

NOTICE: Prohibited Sources in the People's Republic of China. Any goods delivered under this contract may not be acquired directly or indirectly from a Communist Chinese military company.<sup>121</sup>

Documents obtained by the Committee indicate that the Defense Department terminated AEY's ammunition contract because the company procured ammunition manufactured in China and concealed this information from the Department.

As part of AEY's interactions with the Defense Department on the ammunition contract for Afghan Security Forces, AEY's president, Efraim Diveroli, executed a certification on November 25, 2007, stating that AEY was obtaining its ammunition from MFS 2000, a Hungarian company.<sup>122</sup> On January 25, 2008, however, agents from the Army Criminal Investigation Division inspected ammunition delivered to Afghanistan by AEY and determined that it had been manufactured in China.<sup>123</sup>

On March 25, 2008, the Defense Department suspended AEY "from future contracting with any agency in the executive branch of the United States Government."<sup>124</sup> The stated basis for this suspension was evidence that AEY purchased ammunition in Albania that was "manufactured in the People's Republic of China between 1962 and 1974," and AEY's certification in November 2007 that the ammunition was Hungarian.<sup>125</sup>

On April 16, 2008, the Army issued a show cause letter for AEY's failure to deliver ammunition in accordance with the terms of the contract.<sup>126</sup> On May 23, 2008, the Army

---

<sup>120</sup> See, e.g., contract U.S. Department of Defense, *AEY, Inc. Contract W91GY0-06-M-1252* (Sept. 21, 2006); U.S. Department of Defense, *AEY, Inc. Contract W91GY0-06-M-0819* (June 1, 2006); U.S. Department of Defense, *AEY, Inc. Contract W910Y0-08-M-0005* (Feb. 14, 2007).

<sup>121</sup> U.S. Department of Defense, *AEY, Inc. Contract W91GY0-06-M-1252* (Sept. 21, 2006).

<sup>122</sup> AEY, Inc., Certificate of Conformance (No. AFG-0002-59) (Nov. 25, 2007).

<sup>123</sup> Letter from Kim M. Jones, Procuring Contracting Officer, U.S. Army Sustainment Command, to Efraim Diveroli, President, AEY, Inc. (May 23, 2008).

<sup>124</sup> Letter from Robert N. Kittel, Army Suspension and Debarment Official, to Efraim Diveroli, President, AEY, Inc. (Mar. 25, 2008).

<sup>125</sup> *Id.*; Memorandum from Brian A. Persico, Attorney, Procurement Fraud Branch, U.S. Army Legal Services Agency, to Army Suspension and Debarment Official (Mar. 21, 2008).

<sup>126</sup> Letter from Kim M. Jones, Procuring Contracting Officer, U.S. Army Sustainment Command, to Efraim Diveroli, President, AEY, Inc. (May 23, 2008).

terminated AEY's contract for default.<sup>127</sup> In a letter to Mr. Diveroli, the contracting officer stated that AEY had delivered ammunition "from a prohibited source and admits substantial quantities of the ammunition were, in fact, manufactured in factories in the PRC."<sup>128</sup>

On June 19, 2008, a federal grand jury in Miami, Florida, returned a 71-count indictment against AEY, Mr. Diveroli, and three other individuals affiliated with AEY, charging them with 35 counts of procurement fraud, 35 counts of making false statements to the Army, and one count of conspiracy, arising from AEY's shipment of Chinese ammunition under this contract.<sup>129</sup>

The Committee received information about AEY's actions from Kosta Trebicka, an Albanian businessman hired by AEY to repackage the Chinese ammunition before it was shipped to Afghanistan. Mr. Trebicka provided the Committee with ledgers from the repackaging process that identify China as the country of origin for the ammunition.<sup>130</sup> In a letter to the Committee, Mr. Trebicka explained that in May 2007, an AEY official instructed his employees to remove ammunition from their original Chinese packaging and place the loose rounds into cardboard boxes for shipping.<sup>131</sup>

Mr. Trebicka informed the Committee that Mr. Diveroli asked him "if there were any Chinese writings on the top of the packaging or inside the metallic cans."<sup>132</sup> According to Mr. Trebicka, Mr. Diveroli instructed him to "make sure no written papers get inside the carton boxes."<sup>133</sup>

This was not the only contract under which AEY took steps to conceal the Chinese origin of its military equipment. In July 2007, AEY arranged to purchase bulletproof vests for the State Department to be used by narcotics agents at the U.S. Embassy in Pakistan. E-mails from AEY's supplier reveal that the vests were made in China. The supplier informed AEY the vests were manufactured by "the vendor of choice for the Chinese Liberation Army."<sup>134</sup> The AEY official responded:

---

<sup>127</sup> Letter from Kim M. Jones, Procuring Contracting Officer, U.S. Army Sustainment Command, to Efraim Diveroli, President, AEY, Inc. (May 23, 2008).

<sup>128</sup> *Id.*

<sup>129</sup> Indictment, *United States v. AEY, Inc. et al.*, S.D. Fla. (No. 08-20574) (June 19, 2008).

<sup>130</sup> Business Ledgers from Kosta Trebicka (May 19-20, 2007).

<sup>131</sup> Letter from Kosta Trebicka, to Majority Staff, House Committee on Oversight and Government Reform (Apr. 21, 2008).

<sup>132</sup> *Id.*

<sup>133</sup> *Id.*

<sup>134</sup> E-mail from Harry Chang, Kendoo Technology, to Ronald Didier, AEY, Inc. (July 13, 2007).

As mentioned by Efraim earlier we would like ... to NOT mention China on any of the products.<sup>135</sup>

The supplier responded:

Mr. Jin has notified the factory [sic] before and after the production to 100% inspect the vests to make sure there is no Chinese marking anywhere in the vest or on the box.<sup>136</sup>

The documents suggest that AEY officials also may have concealed the Chinese origin of bulletproof vests they procured by claiming that they were made in South Korea and were merely being shipped through China. An AEY employee wrote to the company's agent:

Harry, I just spoke to Efraim and here is how we could resolve the situation (please advise) 1) the commercial invoice would show that the shipper is a South Korean company (we have the letterhead) and that you or your contact in C. is just the export company.<sup>137</sup>

AEY appears to have used this same approach to conceal the Chinese origin of bulletproof helmets sent to Iraq. As discussed above, AEY delivered bulletproof helmets to Iraq that were substandard and accompanied by test results written in Chinese. After the contracting officer saw these Chinese documents, he contacted AEY's president, Mr. Diveroli, to clarify the origin of the helmets. Mr. Diveroli responded: "The source of these helmets is South Korea, they are then airfreighted out of Shanghai which is the main port of entry into Iraq from Asia."<sup>138</sup>

During an interview with the Committee regarding this episode, the contracting officer stated that he was not satisfied with Mr. Diveroli's explanation. He stated:

The thing that he sent, it was not a certification from South Korea. ... I was looking for something that would attempt to certify where these helmets, the source, was from.<sup>139</sup>

In fact, the Committee has obtained an e-mail to AEY apparently confirming that the helmets were manufactured in the same Chinese factory as the bulletproof vests. The e-mail

---

<sup>135</sup> E-mail from Ronald Didier, AEY, Inc., to Harry Chang, Kendoo Technology (July 11, 2007).

<sup>136</sup> E-mail from Harry Chang, Kendoo Technology, to Efraim Diveroli, President, AEY, Inc. and Ronald Didier, AEY, Inc. (Aug. 9, 2007).

<sup>137</sup> E-mail from Ronald Didier, AEY, Inc., to Harry Chang, Kendoo Technology (Aug. 8, 2007).

<sup>138</sup> E-mail from Efraim Diveroli, President, AEY, Inc., to Lt. Commander Frank Futcher (Oct. 18, 2005).

<sup>139</sup> House Committee on Oversight and Government Reform, *Transcribed Interview of Commander Frank Futcher* (June 13, 2008).

states that “the bullet proof helmet that Efraim had purchased last year was from this same factory.”<sup>140</sup>

## **VIII. CONCLUSION**

The record before the Committee indicates that the AEY contract can be viewed as a case study in what is wrong with the procurement process. The \$300 million contract appears to have been awarded despite a questionable need for the contract. The record shows that the Defense Department established deficient contract requirements and conducted a grossly inadequate assessment of AEY’s background and qualifications. After the contract was awarded, there was poor execution and oversight, resulting in the Afghan Security Forces receiving large quantities of “unserviceable” ammunition.

---

<sup>140</sup> E-mail from Harry Chang, Kendoo Technology, to Ronald Didier, AEY, Inc. (July 13, 2007).