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CENTRAL INTELLIGENCE AGENCY

Office of Congressional Affairs

Washington, D.C. 20505

Telephone: [Redacted] 16 Aug 89

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TO: Jack Russ
Sergeant at Arms
House of Representatives

Attached is additional background information on Air America. I hope it is helpful.

If we can be of further assistance, please do not hesitate to call.

[Redacted]

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FORM 2-86 **1533** OBSOLETE PREVIOUS EDITIONS.

(40)

14 August 1989

MEMORANDUM FOR THE RECORD:

SUBJECT: Air America, Inc.

1. This memorandum concerns two related matters: (1) recognition for Americans who were either killed or were listed as missing and presumed dead while engaged in activities on behalf of Air America, Inc. or associated companies in Southeast Asia, and (2) general background information of the history of Air America.

2. Turning first to the issue of recognition, an informal task force was convened by the Director of Central Intelligence in 1987 to consider an appropriate remembrance. Discussions were held with numerous officers within the Agency, including many with personal experience in Air America operations, and extant Air America proprietary records were also reviewed. As a result, it was concluded that while individual honors or an honor roll would be ideal, the incompleteness of our records -- both as to the identity of those Air America employees who were killed or are presumed dead in the line of duty, as well as the circumstances of their death or disappearance -- would preclude the creation of any individualized commemoration which would be complete and thus equitable. It should be noted that substantially identical reasons have also precluded individualized honors for those members of the Office of Strategic Services (OSS), the World War II predecessor to the CIA, who were killed in the line of duty.

3. In light of these factors, the then Director of Central Intelligence determined that a commemorative and honorary plaque for Air America employees killed in the line of duty should be commissioned and erected in the lobby of the CIA Headquarters Building near the commemorative display for those CIA officers killed in the line of duty. That plaque is available today for viewing.

4. Turning to the issue of background information on Air America and its operations in Southeast Asia, we are able to provide the following precis of the creation, operation and functions of this activity. We might also recommend a recent book on Air America by William M. Leary entitled Perilous Missions. While this book neither is an official history of Air America nor bears any official imprimatur, it appears to be an

example of fine scholarship as well as interesting reading.

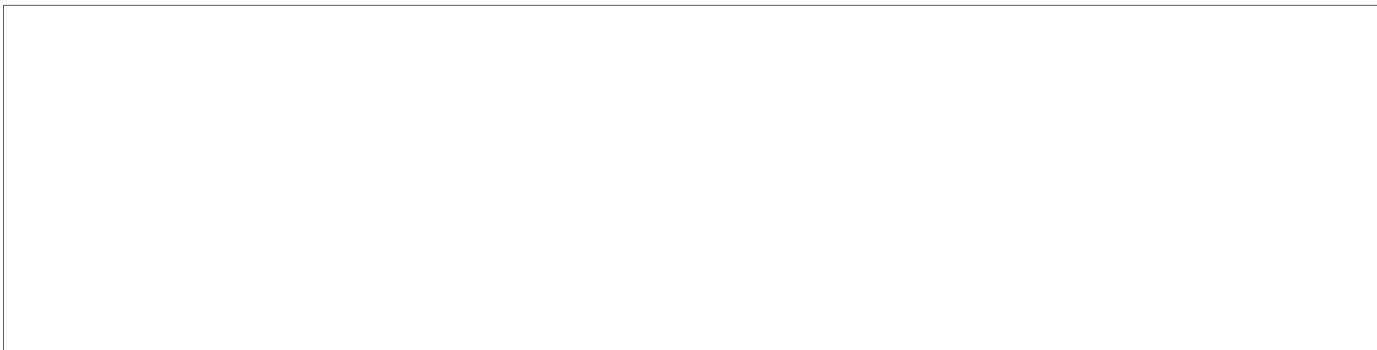
5. Air America was the largest of the CIA's proprietaries and functioned primarily to provide air support for U.S. operations in Southeast Asia under cover of a commercial flying service fulfilling, inter alia, United States Government contracts. By way of definition, proprietaries are companies or businesses lawfully formed, which ostensibly appear to be private, but which are owned by the CIA and which function in the interests of U.S. national defense and foreign policy. Corporate headquarters for Air America and associated companies including the overall holding corporation were in Washington, D.C., with field headquarters in Taipei, Taiwan.

6. To fully appreciate the *raison d'etre* of Air America as well as its work in support of U.S. interests requires that this background begin in 1946 in Mainland China. There, General Claire L. Chennault and Whiting Willauer formed a company (known by various names but generally referred to as Civil Air Transport or "CAT") to haul relief supplies and other cargo in war-ravaged China and to encourage the development of an anti-communist, western-oriented regime. After facing numerous bureaucratic, political, financial and operational problems to establish their airline, Chennault and Willauer were then caught in the middle of the civil war in China in the late 1940's. Allied on the side of the Nationalist Government, they used CAT as a paramilitary asset in support of Chiang Kai-shek and the civilian populations in the areas of China under his control. Operating a fleet of well-used C-46 and C-47 aircraft, and flying with the most primitive support facilities and with non-existent navigational aids, CAT pilots were truly responsible for saving the lives of hundreds of thousands of Chinese. Their exploits of flying into unimproved 2000 foot runways hacked from a mountain side while under fire from communist forces in order to bring food and medical supplies to beleaguered cities is worthy of the greatest praise. From the evacuation of Mukden to the siege of Taiyuan, CAT unfailingly supported and aided the Nationalist population and forces and was, in the opinion of many, responsible for saving thousands if not millions of lives and for insuring the survival of a free Chinese government.

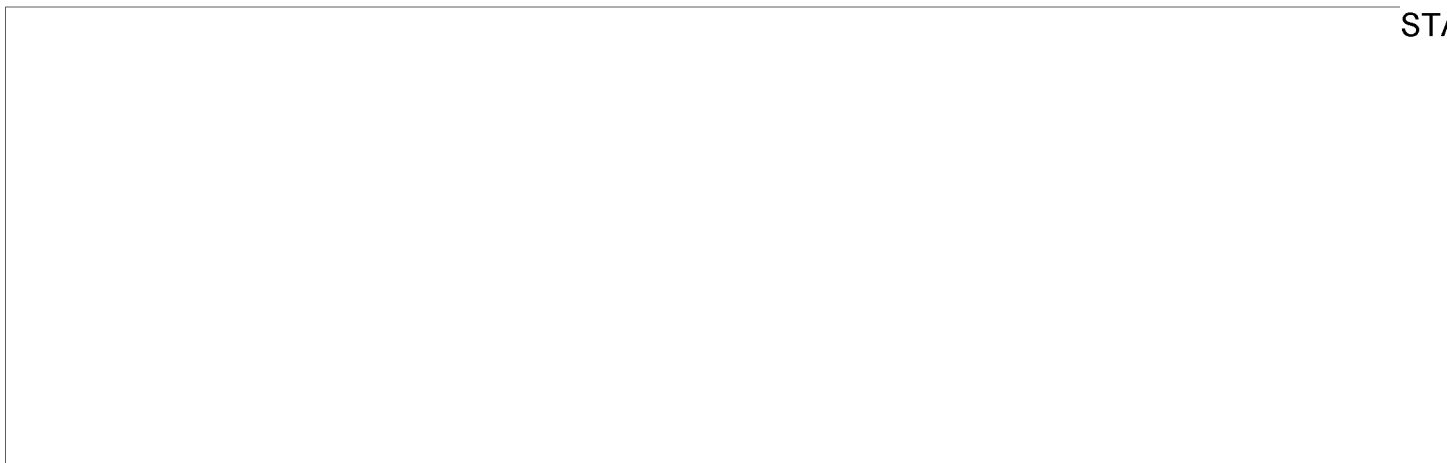
7. When resistance on the Mainland collapsed in 1949, CAT aided in the retreat to Taiwan of the Nationalist Government. It was at this time that the Central Intelligence Agency began its efforts to save CAT and deny its assets to the Communists. The CIA first arranged financial assistance to the company in 1949 and these were eventually credited to the Agency's purchase of the corporation. By summer of 1950, the owners had come to

Washington twice to indicate their desperate needs for additional funds in order to continue operations. With the determination that the CIA did in fact need to contract for air transport in some of its operations and that there would be a continuing need for secure airlift and with there being a general consensus that the loss of this airlift to the Chinese

communists would substantially assist them, the CIA made the decision to exercise their purchase option. In so doing, the CIA also sought and obtained approval from the Department of State.



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10. Through the years of the Viet Nam buildup, Air America and, at the same time Air Asia, the maintenance arm of the company, performed outstanding service both to American interests in general and the U.S. Air Force in particular. Flying in support of the U.S. mission in Southeast Asia, Air America employees, many of them formerly with CAT, distinguished themselves and were responsible for saving the lives of thousands of Laotians and others involved in the long conflict.

11. At its peak, Air America had total assets of some \$50 million and directly employed more than 5,000 individuals. The employment figures for the entire air complex exceeded 8,000. With the wind down of the war in Viet Nam a decision was made to liquidate the Air America complex and the Agency conducted an intensive search for competitive bidders. Air Asia was sold as a going concern on 31 January 1975 while Air America and the remainder of the complex were liquidated by the sale of assets and the surrender of their corporate charters.



CENTRAL INTELLIGENCE AGENCY

Office of Congressional Affairs
Washington, D.C. 20505
Telephone: 482-6136

TO:

A copy of the attached document was
handcarried to Jack Russ, Sergeant at Arms,
House of Representatives, on 10 August 1989.



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94TH CONGRESS }
2d Session }

SENATE

{ REPORT
No. 94-755

FOREIGN AND MILITARY INTELLIGENCE

BOOK I

FINAL REPORT
OF THE
SELECT COMMITTEE
TO STUDY GOVERNMENTAL OPERATIONS
WITH RESPECT TO
INTELLIGENCE ACTIVITIES
UNITED STATES SENATE
TOGETHER WITH
ADDITIONAL, SUPPLEMENTAL, AND SEPARATE
VIEWS



APRIL 26 (legislative day, APRIL 14), 1976

U.S. GOVERNMENT PRINTING OFFICE

WASHINGTON : 1976

69-983 O

For sale by the Superintendent of Documents, U.S. Government Printing Office
Washington, D.C. 20402 - Price \$5.35

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December 31, 1974, this corporation had invested more than \$30,000 in a certificate of deposit.²³ An investment proprietary, which was later dissolved, had invested about \$100,000 in Mexico as of March 31, 1973. A Delaware corporation, which has provided secure air support for Agency employees and classified pouches between Headquarters and other Agency facilities in the United States, has nearly \$150,000 invested in a certificate of deposit.

A former youth activity proprietary, in which the Agency no longer retains an interest, had approximately \$50,000 invested in time deposits as of March 31, 1972. Another proprietary is part of a complex managed by the Cover and Commercial Staff which provides operational support for foreign operations. It is a Delaware corporation used to collect proceeds from the sale of Agency proprietary entities and to refund such proceeds to the Agency. Its total assets were nearly three-quarters of a million dollars and its total stockholders equity was in excess of \$15,000 as of December 31, 1973. It has no employees. As of December 31, 1974, it had invested almost half a million dollars in a convertible subordinated debenture from the sale of a company and almost \$50,000 in notes receivable.

Another company in this complex is a foreign company which has been used as an investment vehicle for funds earmarked for new commercial operations requiring Agency investments. This investment project has been terminated and all funds were returned to the Agency. The company has no employees. As of December 31, 1973, it had invested nearly a quarter of a million dollars in a Security Note of a private domestic corporation.

A proprietary which was part of the air support complex had invested over \$200,000 in a certificate of deposit as of December 31, 1974. This entity was later sold. Another is part of the management and accounting complex. As of December 31, 1974, it had nearly half a million dollars invested in time deposits.

The Air Proprietaries

History.—Lawrence R. Houston, former CIA General Counsel, was involved in the establishment of the first set of Agency proprietaries, and has concluded that they should be a mechanism of last resort. Houston maintains that the Agency learned this "the hard way and almost all of the lessons involved probably came out one way or the other in connection with a major aviation proprietary in the Far East. Others had their own special problems, but I think the Air America complex had pretty near everything."²⁴

The Agency acquired Air America in 1949 ostensibly to deny the assets of this company to the Communist Chinese. The CIA first arranged cash advances to the company in 1949. These advances were eventually credited to the Agency's purchase of the corporation. At that time, Houston described the airline as follows:

This normal aviation organization, this would have no meaning at all, was completely at all, it would have no standing

²³ The Agency today uses this firm for the purchase of airline tickets for travel in support of sensitive projects. It is estimated by the Agency that CIA business represents about 30 percent of the gross airline ticket sales of the entity on an annual basis.

²⁴ Houston, 1/15/76, p. 5.

in international law, aviation rights, or any of that. But it worked for what they wanted, which was to take supplies up-country into inland China and then to bring back whatever cargo they could get commercially: tallow, hides, bristles, all that sort of trade, and then they traded that off for their own account. And for awhile the operation was fairly successful, the C-47's and C-46's.²⁵

To finance this activity the lawyer for the airline organized a company, Civil Air Transport, which was funded by a Panamanian corporation. The two owners of Air America approached the Agency in connection with a foreign operation in the spring of 1959, and indicated that unless they received financial assistance, the airline would go out of business.

A series of meetings were held subsequently in which it was determined that the Agency needed to contract for air transport in some of its operations, particularly those involving arms and ammunition.

And so we entered into an arrangement, I think in about September of 1949 whereby we would advance them, the figure of \$750,000 sticks in my mind, against which we could draw for actual use of the planes at an agreed on rate. . . . And we did draw down. I think, all the flying time and expended the \$750,000 between September and about January, at which time we suspended any further payments or draw-downs. I think the money was exhausted.²⁶

The owners came to Washington in early 1950 for a series of discussions with the CIA. As a result of these negotiations, the Agency agreed to advance more funds, and received an option to purchase the assets of Civil Air Transport. Any unused portion of the advances was to be credited toward the purchase price. Air America operated under this arrangement until the owners "came in in the summer of 1950 and said again they were in desperate straits for funds."²⁷ Another series of meetings was held at the Agency in which it was concluded that the operations in the Far East would have a continuing need for secure airlift. There was also a general estimate that the loss of this airlift to the Chinese Communists would substantially assist them. Thus "the Agency then made the decision that they would exercise the option given there was no objection otherwise."²⁸

The Agency felt that it was necessary to obtain approval from the Department of State, so the head of the CIA's Office of Policy Coordination (who was responsible for conduct of covert actions) and Mr. Houston visited the Assistant Secretary of State for the Far East:

He and I went to see [the Assistant Secretary] and explained the situation. And [he] reminded us that it was basic U.S. policy not to get the government in competition with U.S. private industry. But under the particular circumstances, in particular as there was really no U.S. private industry in-

²⁵ *Ibid.*, p. 6.

²⁶ *Ibid.*, pp. 7-8.

²⁷ *Ibid.*, p. 8.

²⁸ *Ibid.*, p. 9.

volved in the area, and they agreed it was important to deny the assets to the Red Chinese. State would go along on the understanding that we would divest ourselves of the private enterprise as soon as such a divestment was feasible, and all of the circumstances that might obtain.²⁹

The divestiture of these air proprietaries was not initiated until 1975, and some of the entities have not yet been fully divested. Mr. Houston noted, however, that:

We did not disregard that guidance because after very considerable use of this asset during the early '50's, there was a question of whether to continue it, and the matter was taken up in the National Security Council. And Allen Dulles, as Director, proposed that we continue the ownership and control of the assets of Air America, as it then was known including the subsidy as needed. And there was a subsidy at that time. . . . It was about \$1,200,000 per year.³⁰

The National Security Council considered whether this asset should be retained in 1956 and, on Dulles' recommendation, decided to continue the subsidy to Air America.

The air proprietary's business consisted almost entirely of Agency cargo carriage under contracts carrying military designations. The company was not organized, according to Houston, to fly common carriage and had no status in the international air business. The evidence indicates that during the early 1950s, there were two internal struggles: one was where control should lie in the Agency, and the other was what policies should apply to the operation of the company itself:

The struggle within the Agency ranged all the way from sort of quiet management discussions as to what was good management, to sometimes rather vociferous arguments of who's in charge here. And the operators always said, "Well, we need to call the shots because it's our operation. . . . And this is what we were running into all the time, of red hot operators opposed to what we would consider good management."³¹

The air proprietary was managed by elements of the Office of Policy Coordination. From the very outset there were problems in this management structure. One such example is the acquisition of Air America in August 1950. Houston was participating in the negotiations at the invitation of the Head of the Office of Policy Coordination.

OPC was a curious organization, determined as being attached to the Agency for quarters and rationing with policy

²⁹ *Ibid.*, pp. 9-10.

³⁰ *Ibid.*, p. 10.

Houston indicated that there had been a subsidy running to the entities since 1949. "\$1.2 million represented about the maximum subsidy given until. I believe, about 1958 was the turning point, and from 1958 on, there was no subsidy as such that went into it." The reason for that, of course, was that the air complex had become "money-making."

³¹ *Ibid.*, pp. 12-13.

guidance from State, which was an impossible situation. Very nice fellows were doing the negotiating with [OPC] . . . quite unknown to me, when they made the agreement to purchase carrying out the option, they gave the vendors the right to repurchase at any time within two years. And I thought this was really inconsistent with our whole position. And during the next two years they negotiated out that repurchase agreement and in its place substituted an agreement to give them a first refusal, if we were to dispose of the airline. That first refusal plagued us for years. They used to make all sorts of extraordinary claims under it and it was never exercised and eventually it was sort of forgotten when [the owners] died. It ran to them personally, whether it ran to them and two others personally, and they all are dead now. But this shows a part of the learning curve, which was the thing we were going through.³²

In the summer of 1954, Houston and a consultant traveled to the Far East to observe the operation. The consultant went "specifically to look at the organization of the airline." At the time of the airline's purchase, the Agency had formed a Delaware corporation to buy it. The corporate counsel and the consultant were both very concerned about the technical organization, or lack of it, in the operation. According to Houston, they demonstrated:

to my satisfaction that it was an absolute situation and that no one out there had the slightest understanding of the problem or what they were up against, or wanted to do anything about it [in terms of airline management].³³

Following this review, a new organization, designed to be more responsive to the Operations Directorate, was created.

Pacific Corporation held title to 40 percent of the equity in Air America, while the remainder was ostensibly owned by Chinese, who gave deeds of trust to the Agency for their shares. For purposes of international law this overt arrangement demonstrated that the company was majority-owned and controlled by Chinese.

Air America originally had several DC-4's and began modest operations between Hong Kong, Taipei and Tokyo. The corporation soon acquired DC-6's, and it was at this time that the question of competition with private corporations first arose. Northwest Orient Airlines was then flying to Tokyo, Seoul, and Manila. A Northwest executive had noted the Agency's interest in this area when he was Chairman of the Civil Aeronautics Board in the late 1940s and early 1950s. Houston told the Committee:

He became head of Northwest, a very tight manager, a very capable fellow, and he used to complain that we were interfering, we were taking passengers off his airline, and we would go to him and say, we have to keep the airline in this business because the Chinese say they need an international airline. They're not ready to start their own yet. And it is

³² *Ibid.*, pp 13-14.

³³ *Ibid.*, p. 17.

necessary to its overall cover status as a going commercial concern.³⁴

By 1959 the executive had decided to ask the Civil Aeronautics Board for a decision. A meeting was held with the entire Board, where the executive maintained "that he was a private industry, he should not be interfered with by government competition."³⁵ The Agency explained its situation, the need for cover, and their efforts to restrict carriage to the minimum necessary to retain their cover.

And it ended up by one of the members of the Board turning to [the executive] and saying, "You ought to be glad that you don't have a really good, reliable competitor in there." He said, "If you were being competed with by private business, you'd have real headaches. You ought to be real glad that it's not worse than it is."³⁶

In these proceedings, Houston conceded that some passengers were traveling on CIA aircraft rather than Northwest planes, but maintained that the impact was minimal and unavoidable. The CAB participated in discussions with both the Agency and Northwest. After hearing both sides, the CAB "came down on the side of the Agency after making a reasoned judgment."³⁷

By 1960 the airline's international commercial business was not making money. Maintenance work in Taiwan, however, was "normally a money-maker, and this was [contracted] primarily, although not exclusively, with the U.S. Air Force."³⁸

There were management problems in the maintenance operation, which originally stemmed from the fact that field personnel were not particularly astute in setting costs for their contracts. Houston cited one instance when the Agency consultant replaced a corporation comptroller who was very able, but "had his own ideas of bookkeeping and controls." The consultant insisted that the corporation implement bookkeeping practices and controls consistent with CAB and FAA regulations. The military maintenance contracts were constantly audited by on-site teams.³⁹

In the early 1960s, the CIA received an exemption from the Contract Renegotiation Board on the grounds that renegotiation personnel might recognize that Air America was not a commercial operation and discover that the CIA was involved. The Agency went to the head of the Contract Renegotiation Board with a letter from the Department of Defense requesting an exemption on what it considered "perfectly legitimate grounds."⁴⁰ There was indeed a basis for exemption under the Renegotiation Act as the business was conducted entirely overseas, and the exemption was granted. The Agency was concerned that it had made a type of profit (over 40 percent on the Air Force maintenance contracts), which may well have been the subject of rene-

³⁴ *Ibid.*, p. 21.

³⁵ *Ibid.*, p. 22.

³⁶ *Ibid.*, pp. 22-23.

³⁷ *Ibid.*, p. 24.

³⁸ *Ibid.*, p. 25.

³⁹ *Ibid.*, p. 26.

⁴⁰ *Ibid.*

gotiation, had it not been subject to the exemption. "So the question was what to do about it. And finally, we made a voluntary repayment against part of the profit on that contract to the Air Force."⁴¹

As noted previously, the commercial airline aspect of the operation operated mostly at a loss. While there were periods when Air America cargo carriers were very busy on CIA contracts, the Korean War, Diem Bien Phu, and other paramilitary operations; there were also periods between these activities when there was nothing for the airlines to do. During these periods of inactivity, the airline was still saddled with expenses such as crews' salaries and the maintenance of grounded aircraft. To alleviate this problem,

. . . we finally organized the stand-by contract, which was an apparent military entity on Okinawa. It was our entity, but it had a military designation. I can't remember the name for it. And that entity contracted with Air America for so many hours of cargo stand-by to be available any time on call, and that they would pay so much for that capability being maintained . . . so that is how we kept the subsidy going to maintain them during periods when there was not profitable flying.⁴²

Another area of concern was the proprietary's relationship with the Internal Revenue Service. From the outset, the company's management was informed that they would be required to pay appropriate taxes. While there were the usual arguments about whether certain items were appropriate for taxation and whether certain deductions should have been granted, the relationship maintained with the IRS was basically a normal one.

Houston recalled that in the mid-1950s Air America received notice of an upcoming audit by the IRS. Company officials came to the Agency and indicated that this might pose a security problem. The CIA went to the Commissioner of the Internal Revenue Service and indicated that they wished to have the audit conducted by an IRS team on an unwitting basis to see what they could learn. "We thought it would be a good test of the security of our arrangements."⁴³ Later, the IRS personnel would be notified that they had begun to audit an Agency proprietary, and the audit would be discontinued:

They put a very bright young fellow on and he went into it. They came up with discrepancies and things that would be settled in the normal tax argument, corporate-IRS argument, and all of these were worked eventually, and then we went to this fellow and said, "Now, this was owned and backed by the CIA, the U.S. Government. What was your guess as to what was happening?"

And he said, "Well, I knew there was something there, and I thought, what a wonderful asset it would be for the Russians to have, but I came to the conclusion that it was Rockefeller money."⁴⁴

⁴¹ *Ibid.*, p. 27.

⁴² *Ibid.*, p. 29.

⁴³ *Ibid.*, p. 30.

⁴⁴ *Ibid.*

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As the operations of Air America developed, problems arose involving large cargo carriers. In the early days of its operation the airline used C-54's, which had an extremely limited range, but were able to perform under demanding circumstances. Discussions proceeded during that period about modernizing the equipment and the Agency, through Air America, bought DC-6AB's. These aircraft were a conversion of the DC-6 with large cargo doors installed. Air America did not maintain any jet equipment at that point.

In the early 1950's Air America became deeply involved in a military Air Transport System. This system was originally known as MATS, and later as MAC.

They got MATS contracts, and Air America got these, and these were very good to keep a constant utilization at a good rate, the MATS rates were usually good, because the policy was not to do competitive bidding for the lowest bidder because then you got the poorest service, but give good rates to the carriers, and then require the carrier belong to the Civil Reserve Air Fleet.⁴⁵

In 1956 MATS changed its policy and required that bidders on their contracts be certified. Because Air America could not become certified, the Agency decided to purchase Southern Air Transport. While this corporation was technically a separate entity, not involved with Air America, it was actually an integral part of the complex from a management perspective. All management decisions for Southern Air Transport were made by the same CIA consultant and advisory team that established Air America policy.

Eventually, MAC decided to require that bidders not only be certified, but that they also have equipment qualified for the Civil Reserve Air Fleet, i.e., jet aircraft. As a result, the Agency acquired Boeing 727's and convinced Boeing to modify the 727 by enlarging the ventral exit, enhancing its airdrop capability.

So the theory was that the 727's would be used on MAC contracts to be available on an overriding basis if needed for major national security operation. They were used, usually when they had spare time. To my recollection, they were only called off once, off the actual contract time, and this was for a possible use which didn't go through. But the White House asked if we had the capability to move something from here to there, I think from the Philippines to somewhere in Southeast Asia. I don't recall, and so they sent word to management that they wanted a plane available at the earliest opportunity at Clark Field. They pulled one of them off the MAC contract and had it available. I think ready to go, in twelve hours, all set for the operation. And the operation was never called. But it showed what the capability was. And what they had to do was get substitute service for the MAC contract.⁴⁶

During the late 1960s several Chinese airlines began operations on a limited scale. With the establishment of these indigenous airlines

⁴⁵ *Ibid.*, 38.

⁴⁶ *Ibid.*, p. 39.

flying Far East routes, the CIA considered reducing its international carriage work. The Agency decided to retain the MAC contracts because they did not compete with the native enterprises, but plans to reduce Air America's international common carriage were initiated.

Another CIA proprietary, Civil Air Transport Company, Ltd., which had been organized in 1954, had been the first Agency entity to engage in common carriage. Later, Air America did the American contracting, followed by Southern Air Transport which also performed MAC and MATS contracts with planes leased from Air America.⁴⁷

Houston noted that in the late 1960s an internal decision was made that:

. . . we probably couldn't justify this major airlift with the big jets, and so we started getting rid of them. See, they had no utilization to speak of down in Southeast Asia. A couple of supply flights went into [another area] and I think we used prop planes for that, to my recollection.^{47a}

So the Agency began to phase out the 727s, which contributed to the decision to divest itself of Southern Air Transport and Air America.

Internal management was streamlined in 1963 by the establishment of an executive committee consisting of the boards of directors of the Pacific Company, Air America and Air Asia. The overt board of directors in New York City passed a resolution organizing an overt executive committee, which consisted of the CIA consultant and two other directors. Covertly, the Agency added its own representatives to this committee, which allowed representatives of management, Agency and the operators to meet, consider policies, and give guidance to the company. Houston indicated that this mechanism was extremely effective in controlling the company:

So I think for the last, oh, fifteen, eighteen years, the proprietary management system was on the whole pretty effective from the Agency point of view. I think we knew what was going on. I think we were able to get things up for decisions, and if we couldn't resolve them at the staff level, we would take them up to the Director for decisions; quite different from the early days in the early 50's that I described, and the operators at least made the claim that they had the right to call the tune.⁴⁸

During this period of time Operations Directorate personnel

were getting themselves involved in the acquisition of aircraft and which were getting awfully damned expensive at this time, and separate projects were going after some of this expensive equipment without consideration of what might be available elsewhere to the Agency by contract or old aircraft. And so the Director of Central Intelligence set up EXCOMAIR, of which I was Chairman, and had representation from both the operation and management and fi-

⁴⁷ SAT actually owned one 727 and leased two from Air America.

^{47a} *Ibid.*, p. 42.

⁴⁸ *Ibid.*, pp. 46-47.

nance out of the Agency, to try and coordinate the overall control and acquisition and disposition of aircraft.⁴⁹

A February 5, 1963 memorandum entitled "Establishment of Executive Committee for Air Proprietary Operations," noted that the committee was "to provide general policy guidance for the management of air proprietary projects, and review and final recommendations for approval of air proprietary project actions." Houston indicated that this committee, dubbed EXCOMAIR, "was . . . an amorphous group" which worked on a very informal basis. He indicated that EXCOMAIR was an effective method of achieving overall coordination; it was responsible for conducting a thorough inventory of all the equipment that the Agency had in the aviation field and was generally able to keep track of who needed what.⁵⁰

According to Houston, a general shift in thinking at the Agency occurred between 1968 and 1972 as to the desirability of maintaining a substantial airlift capability. The records appear to indicate that Houston convinced the Director in the early 1970s that such a capacity was no longer necessary to retain. Houston commented on this assessment as follows:

Through what knowledge I had of the utilization of the various assets, it seemed to me that utilization, particularly of large assets, that is, heavy flight equipment, was going down to the point where there was very little of it. Consequently, we couldn't forecast a specific requirement. Such requirements as you could forecast were highly contingent. But I also remember a couple of times putting the caveat into the Director that with a changing world and with the complications in the aviation field, once you liquidate it, you could not rebuild, and so you ought to think very, very carefully before getting rid of an asset that did have a contingent capability.⁵¹

Allegation of Drug Trafficking.—Persistent questions have been raised whether Agency policy has included using proprietaries to engage in illegal activities or to make profits which could be used to fund operations. Most notably, these charges included allegations that the CIA used air proprietaries to engage in drug trafficking. The Committee investigated this area to determine whether there is any evidence to substantiate these charges. On the basis of its examination, the Committee has concluded that the CIA air proprietaries did not participate in illicit drug trafficking.

As allegations of illegal drug trafficking by Air America personnel grew in the spring and summer of 1972, the CIA launched a full-scale inquiry. The Inspector General interviewed a score of officers at CIA headquarters who had served in Asia and were familiar with the problems related to drug trafficking. After this initial step, the Office of the Inspector General dispatched investigators to the field. From August 24 to September 10, 1972, this group travelled the Far East

⁴⁹ *Ibid.*, p. 51.

⁵⁰ *Ibid.*, p. 52.

⁵¹ *Ibid.*, p. 57.

in search of the facts. They first visited Hong Kong, then eleven Agency facilities in Southeast Asia. During this period they interviewed more than 100 representatives of the CIA, the Department of State, the Agency for International Development, the Bureau of Narcotics and Dangerous Drugs, the U.S. Customs Service, the Army, Air America, and a cooperating air transport company.

This inspection culminated in an Inspector General's report in September 1972, which concluded that there was

no evidence that the Agency, or any senior officer of the Agency, has ever sanctioned or supported drug trafficking as a matter of policy. Also, we found not the slightest suspicion, much less evidence, that any Agency officer, staff or contract, has ever been involved in the drug business. With respect to Air America, we found that it has always forbidden, as a matter of policy, the transportation of contraband goods aboard its aircraft. We believe that its Security Inspection Service, which is used by the cooperating air transport company as well, is now serving as an added deterrent to drug traffickers.⁵²

But there were aspects of the situation in Southeast Asia which were cause for concern:

The one area of our activities in Southeast Asia that gives us some concern has to do with the agents and local officials with whom we are in contact who have been or may be still involved in one way or another in the drug business. We are not referring here to those agents who are run as penetrations of the narcotics industry for collection of intelligence on the industry but, rather, to those with whom we are in touch in our other operations. What to do about these people is a particularly troublesome problem, in view of its implications for some of our operations, particularly in Laos.⁵³

The Inspector General noted that there was a need for better intelligence not only to support American efforts to suppress drug traffic in Southeast Asia, but also to provide continuing assurance that Agency personnel and facilities were not involved in the drug business.

His report began by placing the allegations against the CIA in historical perspective. It allowed that when the United States arrived in Southeast Asia "opium was as much a part of the agricultural infrastructure of this area as was rice, one suitable for the hills, the other for the valleys."⁵⁴

The record before the Inspector General clearly established that official United States policy deplored the use of opium as a narcotic in Southeast Asia, but regarded it as a problem for local governments. It was equally clear that Agency personnel in the area recognized its dangers to U.S. paramilitary operations and "took steps to discourage

⁵² CIA Inspector General's Report, "Investigation of the Drug Situation in Southeast Asia," 9/72, p. 2.

⁵³ *Ibid.*, pp. 2-3.

⁵⁴ *Ibid.*, p. 5.

its use by indigenous paramilitary troops." ⁵⁵ For example, Meo troops were ejected from various camps when they were caught using the drug. But, the I. G. noted:

We did not, however, attempt to prevent its use among the civilian population in those areas where we exercised military control, believing that such intervention would have been resisted by the tribals with whom we were working and might have even resulted in their refusal to cooperate. ⁵⁶

Nor did the Agency interfere with the movement of the opium from the hills to market in the cities farther south. In this regard, the I.G. remarked candidly:

The war has clearly been our overriding priority in Southeast Asia and all other issues have taken second place in the scheme of things. It would be foolish to deny this, and we see no reason to do so. ⁵⁷

Although it maintained this posture, the CIA was reporting information on opium trafficking long before any formal requirements were levied upon it. As far back as the mid-1960s, when CIA case officers began to get a picture of the opium traffic out of Burma as a by-product of cross-border operations, they chronicled this information in their operational reporting. As more information came to light in Laos and Thailand, this information began to appear in intelligence reporting. Indeed, the Agency "had substantial assets [in two Southeast Asian countries, which] could be specifically directed against this target when it assumed top priority in 1971." ⁵⁸

Air America

As early as 1957, Air America's regulations contained an injunction against smuggling. This regulation later came to include opium. The Report indicated that the airline's effort at this time was concentrated on preventing the smuggling of opium out of Laos on its aircraft. Although still not a crime in Laos, shipment of opium on international flights was clearly illegal and was grounds for dismissal of any pilot or crew member involved. The Inspector General stated that:

Air America has had a few cases of this kind (all of which are documented in the files in the Agency) and has, in each case, taken prompt and decisive action upon their discovery. ⁵⁹

Air America was less able to control drug traffic involving its aircraft within Laos. Although it had a rule that opium could not be carried aboard its planes, the only thing that could be done if the rule was violated was to put the opium and its owner off at the nearest airstrip.

⁵⁵ *Ibid.*, p. 6.

⁵⁶ *Ibid.*

⁵⁷ *Ibid.*

The report related a statement of a case officer which typified the CIA position in the matter during the period 1966-1968. The officer said that he "was under orders not to get too deeply involved in opium matters since his primary mission was to get on with the war and not risk souring relations with his indigenous military counterparts by investigation of opium matters."

⁵⁸ *Ibid.*, p. 7.

⁵⁹ *Ibid.*

Moreover, as a charter carrier, Air America did not have full control over its traffic. It hauled what its customers put on the aircraft. Air operations officers, in the case of Agency traffic, were responsible for authenticating the passengers and cargo they wished to put on the plane. In some locations, the air operations officers had to rely on indigenous assistants for much of the actual details of preparing manifests, checking cargo, and supervising the loading of the aircraft. In areas where active military operations were in progress, this process could become cursory if not actually chaotic. In such circumstances, the Inspector General concluded that:

it was hardly fair to blame Air America if opium happened to get aboard its aircraft. There is no question that it did on occasion.⁶⁰

With the realization that drug abuse among American troops in Vietnam was growing and that Southeast Asian heroin was finding its way to U.S. markets, the CIA's early attitude toward the opium problem began to change. The Agency joined the effort that began in 1971 to halt the flow of opium and heroin from Burma, Laos, and Thailand, and pursued a vigorous intelligence program against these targets.

In terms of staff and contract personnel, the Inspector General was impressed that "to a man, our officers overseas find the drug business as distasteful as those at headquarters."⁶¹ Indeed, many of the CIA's officers were restive about having to deal with Laotian officials who were involved in the drug business:

One young officer even let his zeal get the better of his judgment and destroyed a refinery in northwest Laos in 1971 before the anti-narcotics law was passed, thus risking being charged with destruction of private property.⁶²

But, the I.G. reported, CIA officers generally tolerated the opium problem, regarding it as just another of the frustrations one encounters in the area.

From what the Inspector General contingent was able to observe in the field, "the pilots in the employ of Air America and the cooperating air transport company merit a clean bill of health."⁶³ While it was true that narcotics had been found aboard some of their aircraft, in almost every case the small quantity involved could only have been for the personal use of the possessor. The Inspector General felt that

Given the strict anti-contraband regulations under which these two airlines have been operating for years, it is highly unlikely that any pilot would knowingly have permitted narcotics or any other contraband aboard his aircraft.⁶⁴

Although they noted, "if it is a truism to say that they're in the business for the money," the investigators concluded that these pilots

⁶⁰ *Ibid.*, p. 8.

⁶¹ *Ibid.*, p. 11.

⁶² *Ibid.*

⁶³ *Ibid.*, p. 12.

⁶⁴ *Ibid.*

were deeply committed to their job, and that the subject of drugs was as much an anathema to them as it is "to any decent, respectable citizen in the United States."⁶⁵

The Inspector General indicated how one pilot felt about the subject. He stated:

You get me a contract to defoliate the poppy fields in Burma, and I'll take off right now and destroy them. I have a friend whose son is hooked on drugs, and I too have teenage children. It scares the hell out of me as much as it does you and the rest of the people in the States.⁶⁶

The report also established that the pilots were well paid, averaging close to \$45,000 a year. Almost half of their salary was tax-free. In this context the I.G. concluded that

Although the temptation for big money offered by drugs cannot be dismissed out of hand, it helps to know that the pilots are making good money. Further, an American living in Vientiane can bank a substantial part of his salary without much difficulty, and a common topic of conversation among pilots is how and where to invest their fairly substantial savings.⁶⁷

The milieu in which these pilots found themselves did serve to evoke images of them as mercenaries or soldiers of fortune. The Inspector General indicated that a "number of them do like their wine and women, but on the job they are all business and very much like the average American."⁶⁸

The investigators, however, could not be as sanguine about the behavior of the numerous other individuals who worked for Air America and the cooperating air transport company as mechanics or baggage handlers. The nature of their work allowed these employees easy access to the airplanes, and created real opportunities for concealing packages of narcotics in the airframes. The records indicated that there were several instances where employees had been fired because they were suspected of handling drugs. The Inspector General advised that:

Despite the introduction of tighter security measures, it would be foolish to assume that there will not be any further attempts by mechanics and baggage handlers to conceal narcotics on airplanes.⁶⁹

In a startling revelation concerning indigenous officials in Southeast Asia, the I.G. bitterly reported that

In recent testimony to Agency officers in Vientiane, Laotian officials who had been involved in the drug business stated that there was no need for drug traffickers to use Air America facilities because they had their own. We certainly found

⁶⁵ *Ibid.*

⁶⁶ *Ibid.* p. 13.

⁶⁷ *Ibid.*

⁶⁸ *Ibid.* p. 14.

⁶⁹ *Ibid.*

this to be true. In addition to the Royal Lao Air Force (RLAF), there are several commercial airlines in Laos, including Royal Air Lines, Lao Air Development, Air Laos, and perhaps others, all of which evidently have ties with high Laotian government officials. It is highly problematical whether these airlines have a full platter of legitimate business.⁷⁰

Another factor which had the effect of making Air America a less desirable target for the drug trafficker was that there were virtually no regular, pre-arranged flight schedules for the pilots. Ordinarily, the pilot did not know until he reported for duty which airplane he would be flying or what his flight schedule would be for the day.

Air America's Security Inspection Service, which was established early in 1972, also had five inspection units in Laos. Similar units were eventually established elsewhere in Southeast Asia. Each unit consisted of an American chief and three or four indigenous personnel. The baggage of the pilot and all passengers traveling in CIA-owned aircraft was inspected in the presence of an American official before anyone was permitted to board. All cargo was inspected unless it had been exempted under established procedures. The very existence of the system was considered a deterrent to drug smuggling on Air America aircraft and did result in several discoveries of drugs among the baggage of passengers, although only one or two of these involved quantities of sufficient size to be as commercial.

Agents and Assets

This is one area where the CIA is particularly vulnerable to criticism. Relationships with indigenous assets and contacts are always broad. In Laos, clandestine relationships were maintained in every aspect of the Agency's operational program—whether paramilitary, political action, or intelligence collection. These relationships included people who either were known to be, or were suspected of being, involved in narcotics trafficking. Although these individuals were of considerable importance to the Agency, it had doubts in some instances. For example, the investigators were troubled by a foreign official who was alleged to have been involved in one instance of transporting opium. He was evidently considered "worth the damage that his exposure as an Agency asset would bring, although the Station insists (a) that he is of value to the Station as an agent of influence [deleted] and (b) that his complicity in the [deleted] incident has never been proved."⁷¹

Among liaison contacts, which in the military arena included virtually every high-ranking Laotian officer, the Inspector General warned that the Agency was "in a particular dilemma."

The past involvement of many of these officers in drugs is well-known, and the continued participation of many is suspected; yet their goodwill, if not actual cooperation, considerably facilitates the military activities of the Agency-supported irregulars.⁷²

⁷⁰ *Ibid.*

⁷¹ *Ibid.*

⁷² *Ibid.*, p. 18.

The Inspector General concluded, that

The fact remains . . . that our continued support to these people can be construed by them, and by others who might become aware of the association, as evidence that the Agency is not as concerned about the drug problem as other elements of the U.S. mission in Laos. The Station has recently submitted, at headquarters' request, an assessment of the possible adverse repercussions for the Agency, if its relationship to certain assets were exposed. We think that, on the whole, that assessment was unduly sanguine. We believe the Station should take a new look at this problem, using somewhat more stringent criteria in assessing the cost-benefit ratio of these relationships. We realize that it is impossible to lay down any but the most general kind of rules in judging whether to continue, or to initiate, a clandestine relationship with Laotians. Each case has to be decided on its own merits, but within a framework that attaches appropriate importance to its possible effect on the U.S. Government's anti-narcotics efforts in Laos. It is possible that the Station will need additional guidance from headquarters as to current priorities among our objectives in Laos.⁷³

2. *Nonoperating Proprietaries*

Nonoperating proprietaries vary in complexity according to their Agency task. They are generally corporate shells which facilitate foreign operations and clearly pose no competitive threat to legitimate businesses. The most elaborate are legally licensed and established to conduct bona fide business.

All nonoperating proprietaries do have nominee stockholders, directors, and officers and are generally directed by one of the Agency's proprietary management companies. The company address may be a Post Office box, a legitimate address provided by a cleared and witting company official or private individual or the address of a proprietary management company. The nonoperating proprietaries maintain bank accounts, generate business correspondence, keep books of account which can withstand commercial and tax audit, file State and Federal tax returns, and perform normal business reporting to regulatory authorities. They are moderately capitalized, generally at around \$5,000, and their net worth at any one time varies according to the Agency task they are performing. As of December 31, 1973, more than 60 percent of the combined net worth of these proprietaries was operating capital for companies which provide cover to agency personnel.

Legally incorporated companies require less elaborate commercial administration due to the nature of the tasks they perform for the CIA. This kind of proprietary is directly managed by headquarters specialists operating in alias. No commercial book or accounts are kept, and in the event of a tax audit the Agency has to brief the auditing authority.

Depending on use, administration may be as simple as maintaining bank accounts and filing annual franchise taxes, or as extensive

⁷³ *Ibid*, p. 19.