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UNITED STATES  
GENERAL ACCOUNTING OFFICE

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JUL 1 1975

# REPORT TO THE CONGRESS

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Balance Of Payments Deficit  
For Fiscal Year 1974  
Attributable To Maintaining  
U.S. Forces In Europe  
Has Been Offset

Department of Commerce  
Department of Defense

**BY THE COMPTROLLER GENERAL  
OF THE UNITED STATES**

ID-75-75

JULY 1, 1975

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COMPTROLLER GENERAL OF THE UNITED STATES  
WASHINGTON, D.C. 20548

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To the President of the Senate and the  
Speaker of the House of Representatives

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-  
We have fulfilled our consultative role as required under section 812 (the Jackson-Nunn Amendment) of the Department of Defense Authorization Act, 1974 (Public Law 93-155). Subsection 812(a) of the act states that the fiscal year 1974 balance-of-payments deficit incurred as the result of deploying U.S. Forces in Europe in fulfillment of U.S. treaty commitments and obligations shall be determined by the Secretary of Commerce in consultation with the Secretary of Defense and the Comptroller General of the United States. 74 # 5

Subsections 812(a) and (b) require full offset of any fiscal year 1974 balance-of-payments deficit incurred as a result of deploying U.S. Forces in Europe in fulfillment of our NATO commitments. To the extent that the deficit is not fully offset, proportional troop reductions are required. Subsection (a) provides for determining the 1974 deficit. Subsection (b) specifies time periods for offsetting the deficit and for implementing troop reductions if it is not fully offset and provides a formula for determining such troop reductions.

In our consultative role, we participated in a working group on the NATO balance of payments with representatives of Commerce and Defense and provided a legal analysis on the application of the legislation to Commerce. Our report to the Congress of February 7, 1975, reviewed the status of efforts to offset the balance-of-payments deficit for fiscal year 1974 attributable to maintaining U.S. Forces in Europe (ID-75-43).

BALANCE-OF-PAYMENTS DETERMINATION

The working group determined that, based on balance-of-payments methodology and concepts, the NATO balance was in deficit by \$684 million in fiscal year 1974. (See app. I.)

This deficit was calculated by determining the foreign exchange costs directly associated with deploying U.S. Forces in Europe for NATO treaty commitments and obligations and netting against that figure the receipt items considered valid according to balance-of-payments concepts and definitions.

Direct Defense Department expenditures in NATO countries, adjusted for items determined not to be the result of NATO treaty commitments and obligations, totaled \$1,997 million in fiscal year 1974. The military receipt items accepted as valid by the working group included (1) U.S. Government cash receipts associated with military sales contracts, (2) commercial sales of military material, and (3) interest income forgone as the result of negotiated concessional rates on purchases of U.S. Government securities or deposits of funds with the U.S. Government. These three items totaled \$1,313 million in fiscal year 1974.

#### PRESIDENT'S REPORT TO THE CONGRESS

As required by subsection 812(d) of the act, the President submitted his final report on section 812 on May 27, 1975. He reported that our allies have fully offset the fiscal year 1974 deficit and that the troop reduction provision will not have to be implemented. This report accepted the working group's determination that the balance on military transactions with NATO countries was in deficit by \$684 million.

In the President's report, the following offsets were applied.

1. Remaining 1974 portion of 1974-75  
Offset Agreement

(millions)

a. Troop facilities rehabilitation	\$112
b. Real estate taxes and airport fees	4
c. U.S. Government securities	<u>445</u>
	<u>561</u>
2. European Allies (less West Germany) procurement of U.S. military-related items through commercial channels in 1974 not separately identifiable in Commerce balance-of-payments accounts	 <u>248</u>
Total	 <u><u>\$809</u></u>

The working group rejected the inclusion of the face value of loans (\$445 million) to the U.S. Treasury under military expenditure offset agreements because, since the loans had to be repaid, no permanent balance-of-payments gain accrued to the United States. However, the economic benefits from such loans were recognized. The working group determined that interest income forgone by West Germany, because of purchasing securities from or depositing funds at concessional interest rates with the U.S. Government under military expenditure offset agreements, was a proper credit item in a NATO balance of payments, although such amounts are not entered into the balance-of-payments accounts. This income forgone represented the excess interest accrued at an imputed market interest rate that was more than interest accrued at the stated rate received by West Germany.

The President's report correctly indicated that the \$248 million of the European Allies procurement of U.S. military-related items was rejected by the working group because of insufficient documentation. The working group's approach to this problem is described in appendix II.

Although the working group did not adjust the U.S.-reported data on commercial sales between U.S. firms and NATO European governments based on data received by the Economic Directorate, it did include data, substantiated by U.S. sources, on payments from NATO agencies to U.S. firms as reported by the Economic Directorate.

We believe that West German expenditures for improvement of troop facilities and real estate taxes and airport fees would not be relevant in determining the deficit for fiscal year 1974 because, to be so considered, such items would have to be added in as a constructive expenditure and then subtracted to reflect West Germany's absorption of these costs. However, it does appear that such efforts on the part of other NATO members should be encouraged and are in furtherance of the direct cost-sharing objectives of subsection 812(c).

In accordance with the legislation, offsets may be computed for an additional 10-1/2 months--July 1, 1974, to May 16, 1975. Therefore, a period of 22-1/2 months is provided to offset 12 months of expenditures. Commerce figures for transfers under U.S. military sales contracts adjusted to a cash basis for 9 months of the allowable 10-1/2 month period total \$583 million.

In addition a Department of Defense report for July 1 to December 31, 1974, shows commercial sales of military material by United States industry to West Germany other than through U.S. military sales contracts totaled \$204 million. These two items alone total \$787 million and offset the \$684 million balance-of-payments deficit for fiscal year 1974.

Although we do not agree with the appropriateness of some items the President used to offset the deficit, from information available as of March 31, 1975, we agree the requirements of the Jackson-Nunn Amendment are met and, therefore, the troop reduction provisions of subsection 812(b) are not applicable.


  
Comptroller General  
of the United States

TABLE 1.--BALANCE ON MILITARY TRANSACTIONS WITH NATO EUROPE

FISCAL YEAR 1974

(Millions of dollars)

A. Debits (payments)	
1. Direct defense expenditures (included in data published by BEA, standard tables 2, 3, and 9, line 17).....	2,573
a. Less: Expenditures for U.S. activities not related to NATO such as U.S. strategic forces in NATO countries.....	<u>1/279</u>
b. Less: Major equipment purchased in NATO Europe and imported into the United States.....	81
c. Less: Expenditures in Canada.....	156
d. Less: Expenditures in NATO Europe for the afloat operations of the Sixth Fleet for U.S. strategic purposes.....	<u>1/60</u>
e. Equals: Adjusted direct defense expenditures in NATO Europe....	1,997
B. Credits (receipts)	
1. Transfers under U.S. military agency sales contracts (included in data published by BEA, standard tables 2, 3, and 9, line 3).....	773
a. Less: Transfers for foreign activities not related to NATO such as foreign strategic forces.....	<u>2/</u>
b. Less: Transfers to Canada.....	52
Adjustments to shift item B1 to a cash basis, net of refunds: <u>3/</u>	
c. Plus: U.S. Government nonliquid liabilities to other than foreign official reserve agencies, associated with military sales contracts (included in data published by BEA, standard table 5, line B11).....	78
d. Plus: Redemption of U.S. Treasury securities issued in connection with prepayments for military purchases in the United States (included in data published by BEA, standard table 5, line B13).....	-22
e. Less: Military sales contracts financed by U.S. Government credits (included in data published by BEA, standard table 5, line B14).....	132
f. Plus: U.S. Government receipts from principal repayments (included in data published by BEA, standard table 5, line B15).....	80
g. Equals: Adjusted U.S. Government cash receipts from NATO European governments associated with military sales contracts, net of refunds.....	<u>2/725</u>
2. Commercial sales of military material <sup>3/</sup> (unidentified component of merchandise exports).....	533
a. Less: Transfers for foreign activities not related to NATO such as foreign strategic forces.....	<u>2/</u>
b. Equals: Adjusted commercial sales of military material to NATO Europe.....	<u>2/533</u>
3. Interest income forgone by NATO countries as a result of negotiated concessional rates on purchases of securities of the U.S. Government or deposits of funds with the U.S. Government (not in U.S. balance of payments).....	55
C. Balance on military transactions with NATO Europe (net debit -).....	-684

<sup>1/</sup>Department of Defense estimates.<sup>2/</sup>Reported data or estimates not available for B1a or B2a.<sup>3/</sup>Excludes transactions with Canada.

Source - Final report of the Working Group on the NATO Balance of Payments - May 9, 1975.

DETERMINATION BY WORKING GROUP OF AMOUNTFOR COMMERCIAL SALES OF MILITARY MATERIAL TO NATO EUROPE

The working group decided to include commercial sales of military equipment and services to the extent that transfers of goods and services or payments for them could be identified in U.S. balance-of-payments statistics. Because payments for these commercial sales could not be disaggregated from the capital accounts in balance-of-payments statistics, or could not be identified in any single report, the working group agreed to use a report issued by the Office of Munitions Control, U.S. Department of State, as the basis for estimating commercial sales of military material to all NATO European countries except Germany. This report presented the aggregate value of all arms, ammunitions, and other implements of war, and the aggregate dollar value of each category of such arms, ammunition, and implements of war, exported under an export license, to each foreign country and each international organization, by fiscal year. Data were based on export licenses returned to the Office of Munitions Control after use. Data on these exports are not separately identified in balance-of-payments statistics but are assumed to be commingled with merchandise exports. It should be noted that this report is somewhat incomplete for fiscal year 1974. Licenses used may be returned up to one year later, and, therefore, a full return for fiscal year 1974 would not be available until after June 30, 1975. Also, the report of the Office of Munitions Control does not include data on services performed by U.S. industry for NATO European governments or agencies. The working group was unable to locate a report that separately identified these transactions.

Because the report from the Office of Munitions Control was somewhat incomplete, the working group agreed to review a report prepared by the Economic Directorate, NATO, which showed estimates of defense and defense-related expenditures made in the United States by member countries for fiscal year 1974.

The initial report prepared by the Economic Directorate, however, was incomplete in that not all countries responded to the request of the Economic Directorate for information. Therefore, in some instances, estimates based on the previous year's data were used. Furthermore, of those countries responding, only a few provided sufficient category detail for meaningful analysis. Because of the questions raised by the working group concerning these data, a meeting was arranged between representatives of the working group and representatives of the Economic Directorate.

The Economic Directorate was asked by the working group to provide more detailed and complete information on government-to-firm transactions for those countries which did not provide required data. The working group agreed that such information, if substantiated by U.S. contractors, could be used to adjust reported data on U.S. commercial sales of military material. Furthermore, the working group agreed that substantiated information on valid service transactions (not covered in data on U.S. commercial sales), and on advance cash payments made in fiscal year 1974, for which no export or service performance was effected by the end of fiscal year 1974 would be acceptable as valid credit items in the NATO balance of payments.

The working group received no subsequent information from the Economic Directorate, NATO, at a level of detail sufficient enough to obtain substantiation. Therefore, the working group accepted the data in the report provided by the Office of Munitions Control.

An addition of \$11.9 million was made, representing a loan repayment received from the United Kingdom for a previous commercial sale (1967-69) of military material financed by an Export-Import Bank loan. This repayment was substantiated by Commerce's records.

The working group recognizes that the Office of Munitions Control report represents a narrowly defined series on commercial sales of military material to NATO European countries. It does not include, for example, any transactions in services such as research and development and technical assistance, or any prepayments that might have been made by a NATO European government to a U.S. firm. However, the working group was unable to receive any substantiated information on such transactions and therefore did not include any estimates for them.

Source - Final Report of the Working Group on the NATO Balance of Payments, May 9, 1975.



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