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

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Honorable Dan Daniel, Chairman
Special Subcommittee on NATO Standardization,
Interoperability and Readiness
Committee on Armed Services
U.S. House of Representatives
Washington, D.C.

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Dear Mr. Chairman:

In line with your request of August 14, 1978, regarding H.R. 11607 and H.R. 12837 (95th Cong., 2d Sess.), we are forwarding our comments on H.R. 4623 (96th Cong., 1st Sess.), the "NATO Mutual Support Act of 1979."

The predecessor to H.R. 4623--H.R. 11607, which was submitted by the Department of Defense (DOD) for consideration last year--would have provided very broad authority to the Secretary of Defense to enter into agreements with NATO countries and subsidiary bodies to further operational cooperation and cross-servicing of forces. In commenting on that bill, we stated that, while sympathetic to DOD's problems in these areas, we felt that specific legislative relief, in lieu of H.R. 11607, could be provided to allow DOD the flexibility it might need to meet goals in these areas. We commented further that H.R. 11607 (1) did not provide adequate management and internal controls over costs and (2) did not provide adequate Congressional oversight of complex issues.

The Department of Defense was requested to redraft and resubmit its proposal to more simply and concisely cover the needed authority. Unfortunately, in our judgment, H.R. 4623 fails to meet that objective. Its terms are broad and sweeping, as was true of its predecessor. The authority to be conferred is not closely or explicitly tailored to the Department's stated needs. Furthermore, its impact upon other legislation, such as the Arms Export Control Act, would be significant. Accordingly, we do not believe that its enactment, as drafted, would be advisable. Many of our objections to H.R. 11607 (and its companion H.R. 12837) apply with equal force to H.R. 4623. In addition, we have enclosed our detailed comments and questions regarding H.R. 4623 for use by the Committee in considering the legislation.

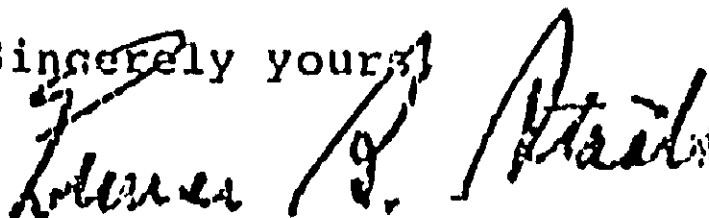
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We wish to state that we remain sympathetic to the Department's needs in the area of NATO logistical support and cross-servicing. H.R. 4623, however, goes well beyond what is needed. A far better approach, discussed with DOD during last year's hearings on H.R. 11607 and H.R. 12837, would be to state with clarity and particularity each and every provision of existing law that needs modification, and to state those modifications in clear language. We believe this is perfectly possible.

Because H.R. 4623 also was referred to the Committee on Foreign Affairs, and because the bill could have a serious impact on the Arms Export Control Act, we are sending a copy of this letter to the Chairman of that Committee.

If we can be of further assistance in analyzing the proposed legislation, please let us know.

Sincerely yours,



Comptroller General
of the United States

cc: Chairman, House Committee
on Foreign Affairs (w/enclosure)

DETAILED GAO COMMENTS AND QUESTIONS
on H.R. 4623 (96th Cong., 1st Sess.),
"North Atlantic Treaty Organization
Mutual Support Act of 1979"

I. DOD Supporting Statements for H.R. 4623:

H.R. 4623 was proposed to Congress by the Department of Defense (DOD) as part of its legislative program for the 96th Congress. DOD outlined its justification for this bill in a letter to the Speaker of the House from the General Counsel, DOD dated April 30, 1979, DOD 96-4. In addition, DOD prepared an undated Fact Sheet "Rationale for DOD 96-4" summarizing DOD's position. The statements in these documents should be carefully compared with the provisions of the bill.

Referring first to the DOD fact sheet "Rationale For DOD 96-4," DOD asserts that some countries, particularly Germany and the Netherlands, can no longer accept U.S. contracting conditions because they find them "distasteful even insulting." What evidence is there to substantiate this assertion and what effect would this bill have on the off-shore procurement agreements (OPA) entered into with NATO member countries in the 1950s? Most of those agreements specifically incorporate some of the "distasteful" U.S. Government contract terms. Have these nations repudiated these agreements or will the bill, if passed, effectively supersede those agreements? If so, what will be the effect

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upon the U.S. European Command (USEUCOM) procurements in Europe that might be outside the scope of this bill? In order to assist Congress in evaluating the merits of the bill, we believe DOD should provide, for the record, evidence of the specific objections raised by the NATO members and by NATO and its subsidiary bodies to continued acceptance of standard U.S. government contract clauses. This would help identify the changes needed to address the specific objections, in lieu of overly broad language.

It should be noted that since the introduction of H.R. 11607 last session, the Cost Accounting Standards Board has gone very far toward exempting foreign contracts from its standards. 1/ Also, on the audit question, DOD already has authority to waive audits by the Comptroller General under existing law (10 U.S.C. §2313) if the contract is with a foreign government and DOD has authority to waive applicability of the Truth in Negotiation Act, including audits by DOD, under existing law (10 U.S.C. 2306(f)).

DOD's fact sheet states, "Nation-to-nation support must be provided through agreements as is done throughout NATO." It would be useful to know the status of agreements of this

1/ Contracts and subcontracts with foreign governments are exempt from all standards and rules of the Board. Foreign contractors and subcontractors need only comply with Standards 401 and 402 and the requirements to submit a disclosure statement. 43 Fed. Reg. 52693-4, November 14, 1978.

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nature that now exist within NATO and in what areas DOD has been unable to conclude agreements because of existing law. If DOD can cite specific examples, clearer legislative relief might be possible.

The DOD fact sheet cites 3 items that the bill will not do. First, it will not "affect the way the U.S. Government deals with private contractors." This appears to be incorrect inasmuch as the bill, as we read it, would permit any of the NATO countries or subsidiary bodies of NATO in effect to act as our procuring agent. They, in turn, could make acquisitions from private contractors in Europe or elsewhere on our behalf, and do so entirely outside the normal U.S. procurement system.

Second, DOD asserts that the bill will not "materially reduce USEUCOM procurement from U.S. sources." If DOD is referring strictly to USEUCOM, the level of purchases from U.S. sources is not particularly high; therefore this is not especially material. If, however, DOD means all U.S. forces in Europe, then this assertion may be of doubtful accuracy.

Lastly, the fact sheet states that the bill will not "substitute for contracting in procurement of initial order quantities of major equipment." Our comment with respect to this appears below in connection with section 3, subsections (b) and (c).

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DOD's letter dated April 30, 1979, transmitting proposal DOD 96-4, (on page 2, para. 2) refers to "NATO standard agreements." Again, we believe these agreements should be specifically identified and supplied for the record. Are there agreements beyond STANAG 2135, which was referred to by General Gregg during his testimony last year in support of H.R. 11607? 2/

II. Section-by-Section Analysis of H.R. 4623:

Section 2, Page 2, Lines 11-15.

The term property is broad and general and in its generic definition can include personal property (which includes military hardware), real property, supplies and equipment, furniture and furnishings. Although section 3(c) prohibits transfers of certain military hardware it seems that the provisions of section 2 could cause some misunderstanding and section 3(c) could be ignored. We suggest that Defense be required to define the term "property" as used in the bill or use the word "equipment" in section 2 to be compatible with section 3(c).

Section 2, Page 2, lines 15-20: This language implies that our NATO allies do not now have such laws or procedures.

2/ Hearings before the Special Subcommittee on NATO Standardization, Interoperability and Readiness House Committee on Armed Services, H.A.S.C. No. 95-72, 95th Cong., 2d Sess. at p. 1196.

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DOD in its justification for H.R. 11607 last Congress seemed to suggest that the contrary was true. 3/ What country or countries are to take the lead in this? Is the U.S. to compromise first, hoping that our allies will follow, or have they already compromised so that it is now appropriate for the U.S. to introduce some flexibility into its own system?

Section 3(a), Page 3, lines 6-10: The effect of this language is essentially the same as that contained in H.R. 11607 (which was "Notwithstanding any other provision of law * * *"). GAO last year stated in our comments on H.R. 11607 that we felt that language was overly broad. The Special Subcommittee in its report 4/ last Congress concurred in our view and posed several questions that remain unanswered. While certain aspects of Chapter 137 of Title 10 U.S.C. may pose difficulties, we doubt that the entire chapter should be cast aside. For example, title 10 U.S.C. 2306 contains a prohibition, long existing in U.S. law, against any cost-plus-a-percentage-of-cost system of contracting. Why should such a prohibition be discarded? Similar questions can be raised regarding other sections

3/ Ibid., Statement of Hon. Dale W. Church at page 1152, Hearings on NATO.

4/ NATO Standardization, Interoperability and Readiness, Report of the Special Subcommittee on NATO Standardization Interoperability and Readiness, House Committee on Armed Services, H.A.S.C. No. 95-101, 95th Cong., 2d Sess. at 42.

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of the chapter. Significantly, on line 7 of page 3 appear the words "or other laws." What other laws does DOD have in mind and why is DOD still unable to specify for Congress what laws need to be modified, relaxed or waived? Amendments to those specific laws is preferable to broad language that may go beyond what actually is needed. The language proposed could lead to serious unintended results.

Section 3(b) and (c), Page 3, lines 11-20: This section states that once in the system, replacement of major items and spares could be attained through the agreements that would be established under the authority of this bill.

The limitation of the acquisition of major items of organizational equipment is specifically tied by the language here to initial issue quantities. Why is there no limitation placed upon follow-on acquisition?

In subsection (c), the bill excludes "aircraft, naval vessels, tracked combat vehicles, torpedoes, strategic, or nuclear capable missiles." (This language differs from that H.R. 11607, page 2, lines 9-10, namely "aircraft, missiles, naval vessels, tracked combat vehicles, other weapons, or naval torpedoes.") Basically, this language leaves open the possibility that DOD could sell or acquire a large number of major items, for example, tactical missiles for ground, air, and naval application (so long as they are not nuclear), radars, communication systems, Electronic Countermeasure

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(ECH) equipment, munitions of virtually all variety, artillery, non-tracked vehicles and so on. DOD should specify precisely what it intends to transfer, or (looking at section 4) acquire under this bill. How much of total U.S. requirements would be satisfied under this authority? Perhaps the language in the bill should be amended so as to provide a greater degree of specificity because, as now written, it is a gigantic "loophole" and would seem to permit far more than mere logistics support.

Section 3(d)(2), Pages 4-5: Our concerns about agreements to provide base operations and/or use of facilities remain the same as expressed in our comments last year on H.R. 11607. (Refer to our report "Planning Host Nation Support for U.S. Forces in Europe" LCD-78-402, August 9, 1978.)

Generally, DOD can enter into multi-year agreements under the provisions of OMB Circular A-34, but cannot record (or incur) multi-year obligations against single year appropriations. (See lines 3-5 and 23-24, page 4.) With respect to the cancellation of provisions there are three options for the cost of cancellation and the payment of those costs. Let us assume that option (A) and (B) do not work and (C) has not gone into effect, in other words that no appropriation has been made for termination payments. This appears to create an exception to what would otherwise be a violation of the Anti-deficiency Act. It would give DOD a very broad selection

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of appropriation accounts from which to draw funds. It is also noteworthy that option (B) makes no reference to reprogramming. This aspect should be considered.

Section 4(a), Page 5: Here it is clear that the bill permits not only "buying" but also "selling." What precisely does DOD contemplate in that regard? Will this supplant the Foreign Military Sales (FMS) aspects of the Arms Export Control Act (AECA) in significant ways? We note, for example, that there are no requirements restricting transfer of equipment to third countries, particularly non-NATO states. If the bill would impinge upon the AECA, there appears to be a significant deprivation of the congressional review function that otherwise would exist under that Act. Reading this section along with section 3(c), which leaves many major items of equipment subject to the bill's provisions, the effect could be significant.

Also, the bill employs the term "transfer" in contrast to "sales". (See section 2, page 2, lines 11-15.) In context of section 2, it may not be clear that such transfers must be for compensation, or short term loan, as provided in section 5.

The Subcommittee may wish to consider whether a dollar or some other limitation should be specified in the bill for these transfers.

Section 4(b): Provision of, or acquisition of services can be priced in accordance with the Economy Act, as it applies between U.S. departments and agencies. What we see is that

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this would essentially permit DOD to waive certain personnel costs (e.g., military and civilian retirement and benefit costs which could constitute an add on of somewhere in the neighborhood of 25 percent.) Similarly, this could permit waiver of asset use charges and other unfunded costs. This apparently is the practice traditionally, at least, by the U.S. departments acting under the Economy Act. Why should this pricing practice be extended to transfers under this bill, especially when GAO has consistently maintained that there should be full cost recovery for equipment and services under FMS transactions?

Section 4(c): While this section appears superficially to provide some controls, it is critical to know how this will be monitored and who will monitor this. Are the inventory levels referred to simply those in Europe or do they include inventory levels in the U.S.? If they are limited to inventory levels in Europe, could transfers be made from increased inventories in the U.S.? Also, couldn't DOD circumvent this provision by the simple mechanism of direct orders from existing production contracts, again circumventing the AECA? In short, there is a substantial question about the definition of the words appearing on page 5, lines 7-10 (section 4(a)), "* * * in the inventory under the jurisdiction and control * * *." Moreover, inventories could be increased so long as this was not "solely" for the purpose of this bill.

The basic thrust of this bill, as advanced by DOD, appears to be aimed at assisting in the routine support type operations wherein the other NATO forces could requisition supplies and parts from U.S. stocks in Europe. If this were to occur, the U.S. inventories in Europe would necessarily have to increase to meet the new demands and to prevent a degradation of supply responsiveness for U.S. forces. Any increases in stock levels will result in increased costs to the U.S. Government. The Committee may wish to question DOD on the following:

A. Will the logistical support provided by the U.S. forces in Europe to other NATO allies be for filling routine supply requirements or be limited only for supply needs required by military exigency? Will the implementing regulations specify the type of requirements permitted to be serviced from the U.S. supply system in Europe?

B. If the U.S. supply operations in Europe are increased due to the requirements of NATO forces, will the increased costs to operate the system be passed on to the NATO countries or absorbed by the U.S.?

Section 5(iii): Clearly, we could end up with uneven exchanges. Who will monitor this and how will it be monitored? Who will make the valuations to assure the maximum degree

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of equality? If there is a price differential where whatever the U.S. exchanges is more valuable than what the U.S. receives, the U.S. is in effect making a subsidy. On the other hand, if the reverse is true, DOD is in effect augmenting its appropriations. What mode of valuation would DOD use (i.e., replacement cost or acquisition cost)? This has long been a controversial subject area of FMS where there are sales from stock.

Section 6(a): Why shouldn't the regulations go to the committees 60 days in advance and why should there not be some mechanism whereby the regulations may be disapproved? The regulations are likely to be very complicated and 30 days time would appear to be inadequate.

Section 6(b), Page 7, lines 10-12: The use of accounting terms in this section is not technically correct. Accrued revenues and accrued expenditures are not liquidated. We believe DOD meant to say that all accounts receivable should be collected and all accounts payable paid either within 90 days of incurrence or quarterly. In any case, we do not see any valid reason for this type of legislative requirement. It is not always possible or correct to pay all accounts payable or collect all accounts receivable within 90 days or quarterly. Also, 30 days from date of invoice is the generally accepted period for payment of bills or collection of accounts receivable.

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Section 6(c), Page 8: DOD would need to modify its existing accounting system or develop a new system to accomplish this, especially if this works out to involve a significant number of transactions, which it probably will. We believe that modification of the existing accounting systems may be the best alternative to support the accounting requirements of this section as well as sections 4(b), 5, 6(b) and 7. There is a need to know what systems are now in place or will be put into place. Will the systems be approved by GAO? On line 19, page 8, what is meant by "appropriate reimbursement"? In the sentence beginning on line 21 on page 8, why are payments from subsidiary bodies only, not countries, referred to? Also, DOD might in effect end up with more money, or "free money," if DOD sells equipment, etc. but has no need to replace it. This also has been a problem area in FMS transactions. Lastly, why shouldn't funds be covered into miscellaneous receipts of the Treasury and resulting needs for funds by DOD taken care of by subsequent appropriations, thereby retaining greater congressional control?

Section 6(d), Page 9: If these provisions of law as implemented by contractual language are offensive to the sovereignty of the NATO members, wouldn't this continued applicability also be offensive?

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Section 7: The DOD April 30, 1979, transmittal letter indicates that these agreements would be subject to the Case Act. Therefore they should be reported to Congress when concluded. Why shouldn't the reporting requirement specify that the reports also be directed to the Armed Services, Foreign Affairs and Appropriations Committees? Also, in view of the complicated accounting aspects requiring close monitoring, it may be prudent to require that the reports be submitted to the Comptroller General as well.

Section 8, Page 10: Under the Ottawa Agreement, one of the NATO subsidiary bodies is the NATO Maintenance and Supply Agency (NAMSA). If the proposed legislation is adopted, DOD plans to make use of NAMSA for depot maintenance of equipment as well as other logistics support. (Source: DOD's Fifth Report on Rationalization/Standardization within NATO, January 1979, pp. 43, 49). Up to this time the U.S. forces in Europe have made only limited use of NAMSA because in part, NAMSA has declined to enter into contracts requiring full compliance with U.S. procurement laws and regulations. At present, the U.S. may not legally contract with NAMSA. Any extensive use of NAMSA would have an impact on the cost of this program. Also, the use of NAMSA for any extensive maintenance efforts raises a question as to whether corresponding reductions will occur in maintenance programs in

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facilities in the United States. We believe the Committee may wish to question DOD on these matters.

Other General Observations:

There is nothing in the bill to indicate who within DOD (or what activity) is to control the transactions that would occur within the scope of the authority to be conferred. What precisely does DOD have in mind with respect to sales or transfer of U.S. items or services? What cooperation will exist with the Defense Security Assistance Agency?

If the U.S. is to acquire goods and services under this bill, what mechanism will exist to assure the fairness and reasonableness of the prices paid? This question is particularly significant if it is a purchase from NAMSA, who in turn may have made an acquisition from a European or American manufacturer, or if the purchase is to be from a foreign government which has in turn contracted for the goods or services. What administrative and other indirect charges will we have to pay? What provisions for cost and price control will be imposed upon private firms?

Lastly, what will be the implications of this bill for logistical support (spare parts, depot maintenance, etc.) of the F-16 program? The bill excludes only "aircraft", not their parts.