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National Security and  
International Affairs Division

B-277966

April 10, 1998

The Honorable John McCain  
United States Senate

Subject: DOD's Rationale for Imposing Domestic Source Restrictions

Dear Senator McCain:

This letter responds to your request for information on the criteria and processes used by the Department of Defense (DOD) to impose, retain, or rescind domestic source restrictions on procurement.<sup>1</sup> A later report will provide additional information on the rationale for domestic source restrictions on specific items.

RESULTS IN BRIEF

The justification for imposing domestic source restrictions is generally based on national security concerns. These concerns include the need to retain a unique domestic industrial capability essential to meeting defense requirements, protect information on performance characteristics and vulnerabilities of U.S. systems, and meet surge and replenishment requirements. DOD and the services continually conduct assessments of DOD- or service-imposed source restrictions. However, DOD does not regularly review legislatively imposed restrictions.

CRITERIA FOR DOMESTIC SOURCE RESTRICTIONS

Federal regulations and DOD guidance recognize the need to restrict competition to domestic sources to address national security concerns. The Federal Acquisition Regulation permits competition to be limited to meet mobilization base or other national security needs. DOD's Handbook for Assessing Defense Industrial Capabilities provides guidance for determining

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<sup>1</sup>Restrictions are used to limit the acquisition of items to domestic sources and prohibit the procurement of foreign-manufactured products.

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when competition needs to be restricted to support national security needs. This guidance also indicates that limitations on foreign sources may be needed to (1) avoid dependence on a politically unreliable foreign supplier or (2) protect technologies and products that are classified, offer unique war-fighting superiority, or can enable foreign governments to develop countermeasures that could undermine the effectiveness of U.S. systems.

Competition may also be restricted to meet mobilization base needs. DOD's planning guidance reflects the changes in military missions and requirements that have occurred since the end of the Cold War. The conflicts for which DOD is preparing no longer involve a large-scale mobilization to prepare for global war but instead focus on smaller conflicts that would be fought using readily available defense inventories. To support this strategy, DOD established requirements to produce certain items during a crisis and replenish supplies of these items within a specified period of time after a conflict. In certain cases, DOD has restricted procurement to domestic manufacturers to ensure control over the supplier. These surge and replenishment requirements are limited to munitions, troop support items, and spares.

In addition, domestic source restrictions are mandated by legislation. For example, Congress has restricted DOD-procured items in the Buy American Act, the Berry Amendment, and annual appropriation and authorization language.<sup>2</sup>

#### REVIEWS OF APPLICATIONS OF THE RESTRICTIONS

In response to changes in military policy and industrial base concerns, DOD initiated actions to eliminate agencywide domestic source restrictions imposed by DOD policy. DOD wanted to take advantage of the more competitive global markets when consistent with national security requirements. In 1995 and 1996, DOD, the services, and the Defense Logistics Agency conducted assessments of DOD-wide domestic source restrictions imposed by policy decisions and reported the results of these assessments in DOD's Industrial Capabilities Report to Congress.

As a result of the 1995 and 1996 assessments, DOD rescinded restrictions for miniature and instrument ball bearings, anchor chains, various ferrous forgings, precision components for mechanical time devices, high-purity silicon, and high-

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<sup>2</sup>The Buy American Act is intended to restrict DOD procurement of products to domestic manufacturers. The Berry Amendment restricts procurement of food, textiles, and specialty metals to domestic sources. Annual appropriation and authorization language implements similar restrictions on a variety of items, such as buses, chemical weapon antidote injectors, anti-friction bearings, and naval vessel components.

carbon ferrochrome. DOD retained the restriction for polyacrylonitrile carbon fiber because it considered this technology to be critical for future weapon system procurement. DOD also retained the restriction for selected forgings to prevent foreign access to specifications and manufacturing processes, which could compromise the effectiveness of selected Navy systems.

Since that time, DOD, the services, and the Defense Logistics Agency have conducted additional assessments to examine industrial capabilities in particular sectors. These assessments were reported in DOD's 1997 and 1998 Industrial Capabilities Reports to Congress. As a result of these assessments, the Navy, Air Force, and Defense Logistics Agency have not further restricted procurement to domestic sources. However, the Army continued source restrictions on several items it reviewed. For example, contracts for certain high-performance batteries were restricted to U.S. or Canadian firms to meet surge requirements which could exceed 20 times the peacetime level. In another case, a sole-source contract to a U.S. manufacturer of chemical protective masks was awarded to maintain a sufficient on-hand inventory and the ability to replenish stocks rapidly after a conflict. Finally, the Army used restricted contract methods in three separate cases to meet different munitions needs. In each of these cases, the Army believed that domestic contractors possessed unique equipment or processes necessary to meet surge and replenishment requirements.

DOD does not perform analyses on congressionally imposed restrictions and has no policy for reviewing the need for these restrictions. DOD officials told us that, if statutory restrictions were rescinded, they would assess the need to retain the restrictions using the criteria established in agency policy guidance.

#### SCOPE AND METHODOLOGY

To review DOD's criteria for determining domestic source restrictions, we examined federal and DOD regulations and guidelines for assessing the defense industrial base. We reviewed relevant documentation and reports and discussed DOD's policy and guidance with officials from the Office of the Secretary of Defense, the Defense Logistics Agency, Army and Air Force Headquarters, the Naval Sea Systems Command, and the Department of Commerce, all in Washington, D.C.

We did not obtain written agency comments on this letter. However, we provided a draft of this letter to DOD officials and incorporated their comments where appropriate.

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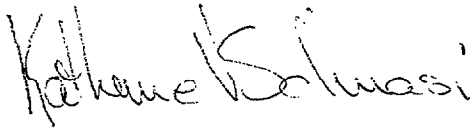
We performed our review from January 1998 to April 1998 in accordance with generally accepted government auditing standards.

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We are sending copies of this letter to the Secretary of Defense. We will also make copies available to others on request.

If you or your staff have any questions, please contact me on (202) 512-4841. Major contributors to this letter are Karen Zuckerstein, Blake Ainsworth, Brian Mullins, and Behn Miller.

Sincerely yours,

A handwritten signature in cursive script that reads "Katherine V. Schinasi".

Katherine V. Schinasi  
Associate Director  
Defense Acquisitions Issues

(707281)

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