



United States  
General Accounting Office  
Washington, D.C. 20548

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Accounting and Information  
Management Division

B-282531

May 19, 1999

The Honorable William J. Lynn  
Under Secretary of Defense (Comptroller)

Subject: Foreign Military Sales: Recovery of Nonrecurring Research,  
Development, and Production Costs

Dear Mr. Lynn:

Last October, we reported to Senator Charles E. Grassley on the results of our review of the Department of Defense's accounting and reporting on the costs of the foreign military sales (FMS) program.<sup>1</sup> In that report we noted that the Air Force and Navy were not promptly collecting nonrecurring research, development, and production costs from the FMS trust fund as major defense equipment items were delivered to FMS customers. Specifically, we identified over \$183 million of nonrecurring costs related to items that were delivered to FMS customers—some as long ago as 1989—that had not been charged to the foreign customers' trust fund accounts.

To address these issues, we recommended that the Air Force and Navy (1) recover the amount identified in our report that had not yet been charged to FMS customers' trust fund accounts and (2) review all other open FMS cases that require foreign customers to pay a proportionate amount of nonrecurring research, development, and production costs for major defense equipment and recoup nonrecurring costs that have not yet been recovered for items that have already been delivered to FMS customers. The Air Force and Navy have now collected the over \$183 million identified in our report.

While the collection of this amount is a positive first step, our recent visit to the Air Force Materiel Command's headquarters, as part of another audit, disclosed that the Air Force has not collected nonrecurring costs owed for items related to other open FMS cases. Specifically, we found that \$152,101,014 of nonrecurring research, development, and production costs had not been collected from Saudi Arabia's trust

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<sup>1</sup>Foreign Military Sales: Millions of Dollars of Nonrecurring Research and Development Costs Have Not Been Recovered (GAO/AIMD-99-11, October 20, 1998).

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GAO/AIMD-99-148R FMS Nonrecurring Costs

fund account for 26 F-15 aircraft that were delivered to the country between December 1997 and March 1999.

Volume 15 of DOD's Financial Management Regulation 7000.14-R, entitled Security Assistance Policy and Procedures, states that "Charges for nonrecurring costs are earned as items are physically delivered to the FMS customer." As we noted in our October 1998 report, not recovering nonrecurring costs promptly from an FMS customer's trust fund after items are delivered represents poor financial management practices. It also raises the risk that amounts will never be recouped and that these funds, deposited in advance into the FMS trust fund for this purpose, will be erroneously returned to FMS customers.

We recommend that you take the actions necessary to ensure that the Air Force promptly bills and collects the over \$152 million of outstanding nonrecurring costs owed by Saudi Arabia for the 26 F-15 aircraft. We also recommend that you reemphasize to the military services the need to expeditiously complete the review of other FMS cases involving nonrecurring costs to ensure that all amounts owed have been collected.

In written comments on a draft of this letter, the Defense Deputy Chief Financial Officer stated that the Air Force had deferred the collection of nonrecurring costs based on directions from the Defense Security Cooperation Agency (DSCA). He further stated that the Under Secretary of Defense (Comptroller) had issued a memorandum on April 29, 1999, to the Director, DSCA, emphasizing the department's financial policy requirements for such collections and requested DSCA to provide the Under Secretary with a plan for collecting all outstanding amounts owed by Saudi Arabia.

With respect to the review of other FMS cases involving nonrecurring costs, the Deputy Chief Financial Officer cited a December 11, 1998, memorandum that the Under Secretary issued in response to a recommendation in our October 1998 report. Because we found, in April 1999, that the Air Force was still not fully complying with the recoupment requirements of the December 1998 memorandum, we are now recommending that the Under Secretary reemphasize his December 1998 position to the military services. The Deputy Chief Financial Officer's written comments are reprinted in the enclosure.

Within 60 days of the date of this letter, we would appreciate receiving a written statement on actions taken to address our recommendations.

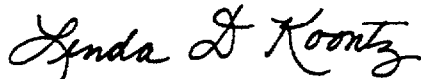
We are sending copies of this letter to Senator Charles E. Grassley. We are also sending copies of this letter to Senator Ted Stevens, Senator Fred Thompson, Senator John W. Warner, Senator Robert C. Byrd, Senator Carl Levin, Senator Joseph I. Lieberman, Representative Dan Burton, Representative Stephen Horn, Representative David R. Obey, Representative Ike Skelton, Representative Floyd D. Spence,

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Representative Jim Turner, Representative Henry A. Waxman, and Representative C. W. Bill Young in their capacities as Chair or Ranking Minority Member of Senate and House Committees and Subcommittees. We are also sending copies of this letter to the Honorable F. Whitten Peters, the Acting Secretary of the Air Force, and the Honorable Jacob J. Lew, Director, Office of Management and Budget. We will make copies available to others upon request.

If you have any questions or need any additional information, please contact me on (202) 512-6240 or Larry W. Logsdon, Assistant Director, on (703) 695-7510.

Sincerely yours,



*for* Jack L. Brock, Jr.  
Director, Governmentwide  
and Defense Information Systems

Enclosure

Comments From the Department of Defense



COMPTROLLER

OFFICE OF THE UNDER SECRETARY OF DEFENSE  
1100 DEFENSE PENTAGON  
WASHINGTON, DC 20301-1100

MAY 10 1999

Mr. Gene L. Dodaro  
Assistant Comptroller General  
Accounting and Information Management Division  
United States General Accounting Office  
Washington, DC 20548

Dear Mr. Dodaro:

This is the Department of Defense response to the General Accounting Office (GAO) draft report, "Foreign Military Sales: Recovery of Nonrecurring Research, Development, and Production Costs," dated April 20, 1999 (GAO Code 511662/OSD Case 1798).

The Department's comments on the recommendations contained in the report are provided in the enclosure.

The Department appreciates the opportunity to comment on the draft report. My point of contact on this matter is Ms. Kay O'Brien. She may be reached by telephone at (703) 697-0586.

Sincerely,

Nelson Teye  
Deputy Chief Financial Officer

Enclosure

**GENERAL ACCOUNTING OFFICE DRAFT REPORT, DATED APRIL 20, 1999  
(GAO CODE 511662/OSD CASE 1798)**

**"FOREIGN MILITARY SALES: RECOVERY OF NONRECURRING RESEARCH,  
DEVELOPMENT, AND PRODUCTION COSTS"**

**DEPARTMENT OF DEFENSE COMMENTS TO  
THE GAO RECOMMENDATIONS**

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**RECOMMENDATION 1:** The GAO recommended that the Under Secretary of Defense (Comptroller) take the actions necessary to ensure that the Air Force promptly bills and collects the over \$152 million of outstanding nonrecurring costs owed by Saudi Arabia for the 26 F-15 aircraft.

**DOD RESPONSE:** The Air Force deferred the collection of nonrecurring costs recoupment charges for the 26 F-15 aircraft based on direction from the Defense Security Cooperation Agency (DSCA). According to the DSCA, this direction was necessary due to the financial position of the Saudi Arabia FMS trust fund account. The Under Secretary of Defense (Comptroller) issued a memorandum to the Director, DSCA, dated April 29, 1999, emphasizing the financial policy requirements of the Department and requesting a plan for collecting payments from Saudi Arabia for all outstanding Foreign Military Sales (FMS) payment requirements and ensuring payments remain current thereafter.

**RECOMMENDATION 2:** The GAO recommended that the Under Secretary of Defense (Comptroller) reemphasize to the military services that they need to expeditiously complete the review of other FMS cases involving nonrecurring costs to ensure that all amounts owed have been collected.

**DOD RESPONSE:** The Under Secretary of Defense (Comptroller), in a memorandum dated December 11, 1998, emphasized the policy requirements involving the recoupment of nonrecurring costs to the military services that failed to recoup nonrecurring research, development, and production costs from FMS customers. In the same memorandum, the Under Secretary of Defense (Comptroller) also directed appropriate actions to occur on a definitive schedule. One of the actions directed was to review all open FMS cases to ensure that amounts owed have been collected.



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