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In the past 7 years, foreign military sales volume grew from \$952 million to over \$8.7 billion. The United States has dominated the world arms market since 1965 and now controls it by almost 50%. Findings/Conclusions: Foreign military sales include some of the most advanced weapons and support systems in the U.S. inventory and represent a large percentage of new weapons and equipment. The chief customers have changed from primarily North Atlantic Treaty Organization countries to Middle East countries. There are indications, based on Department of Defense (DCD) assessments, that foreign deliveries have affected U.S. defense capabilities adversely. Problems affecting arms sales management include: (1) foreign sales agreements providing for future support which could magnify problems of production limitations and competing demands for key components; (2) over 45% of support requirements for spare and repair parts have not been forecasted; (3) management information systems for foreign military sales do not identify future support requirements for U.S. and foreign customers; and (4) inadequate consideration has been given to the cumulative effect of foreign military sales on weapon systems with common components. Recommendations: The Secretary of Defense should require: inclusion of detailed impact statements in the foreign military sales decisionmaking process; a supply support agreement or other mechanism to be a part of any sale when it is feasible, so that DOD can program and fund future support without adverse effects on U.S. defense capabilities; and development of a forecasting mechanism to identify the probable quantities of future critical support items for U.S. and foreign sales customers. (Author/HTW)

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REPORT TO THE CONGRESS

03394



BY THE COMPTROLLER GENERAL
OF THE UNITED STATES

Foreign Military Sales-- A Potential Drain On The U.S. Defense Posture

Departments of Defense and State

This report is the unclassified version of GAO's SECRET report LCD-76-455, dated July 25, 1977. It discusses military sales by the United States to foreign buyers which have grown to dominate the international arms market. This rapid growth has, on one hand, been at the expense of the U.S. Forces; on the other, it has helped maintain employment and has reduced the costs of some weapon systems.

Of equal importance, these sales have created large inventories of U.S. articles in foreign hands. However, there is no experience to suggest that the future support of both foreign and U.S. inventories can be accomplished with the even handedness necessary to avert a potential drain on the U.S. defense posture.



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

B-165731

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

This is an unclassified version of our report describing the foreign military sales program and the impacts that occur in the U.S. readiness posture. We discuss the long-range implications of a sale made today in the light of future support requirements, and we suggest ways to improve planning and control of the foreign military sales program.

In view of the billions of dollars involved in the foreign military sales program and congressional interest in this area, we reviewed selected military locations to see whether the foreign sales program has had an impact on the readiness of the U.S. Forces and whether the program has been managed effectively.

We made our review pursuant to the Budget and Accounting Act, 1921 (31 U.S.C. 53), and the Accounting and Auditing Act of 1950 (31 U.S.C. 67).

We are sending copies of this report to the Director, Office of Management and Budget, and to the Secretaries of Defense and State.

A handwritten signature in black ink, reading "James B. Atchafalua".

Comptroller General
of the United States

COMPTROLLER GENERAL'S
REPORT TO THE CONGRESS

FOREIGN MILITARY SALES--
A POTENTIAL DRAIN ON
THE U.S. DEFENSE POSTURE
Departments of Defense and State

D I G E S T

Sales of military equipment by the United States to foreign buyers have increased from \$952 million in 1970 to \$8.7 billion in 1976.

Continued congressional concern over the impact of such sales on the U.S. defense posture prompted GAO to review effects of certain weapon systems' sales on U.S. Forces and to examine the considerations given to these effects on the decisionmaking process.

Records of the United States Arms Control and Disarmament Agency indicate that the United States has dominated the world arms market since 1965 and now controls it by almost 50 percent. This domination is attributable to the high technology embodied in the weapon systems sold; the ability to provide follow-on support through systems' life cycles; and, in some cases, a political preference on the part of some countries for buying from the United States rather than from other nations.

Foreign military sales include some of the most advanced weapons and support systems in the U.S. inventory and represent a large percentage of new weapons or equipment. For example, in fiscal year 1975 about 50 percent of the Army's procurement activities were for the support of foreign sales. Similarly, the chief customers have changed from primarily North Atlantic Treaty Organization countries and other allies to Middle East countries not allied with the United States--Iran, Israel, and Saudi Arabia. These countries accounted for over half of the \$8.7 billion foreign sales in 1976.

Foreign military sales are intricately woven throughout the U.S. political, economic, and defense fabric, which makes management of these sales complex and assessment of their effects difficult. However, reasonable assessments from Defense indicate that the armament management and decisionmaking process has, on occasion, allowed foreign deliveries to affect U.S. defense capabilities adversely. GAC believes that, even though some sales are made from a purely political standpoint, there are opportunities to improve the management process for satisfying these and other foreign sales so as to minimize the impact on the U.S. defense posture.

What follows is intended to highlight some of the ways in which foreign sales have had an impact, and may continue to have an impact, on the U.S. defense posture. However, none of the examples, by themselves, create insurmountable problems, and they should not be considered out of context. But when the examples are considered together, their cumulative effect demonstrates how foreign sales aggravate the already difficult task of managing the U.S. defense posture in a peacetime environment. Moreover, the examples provide a valuable insight into the need for improvements today in order to avert potentially greater management complexities in the future.

The report identifies problems that affect the management of the foreign military sales process and attempts to place the potential long-range effects of the sales in perspective. For example:

- Foreign sales agreements provide for future support. At the beginning of fiscal year 1976, undelivered orders totaled about \$24 billion. As more deliveries of such systems are made, problems encountered with production limitations and competing demands for key components will be magnified. (See p. 34.)

--Over 45 percent of support requirements for sales of major end-items from 1970 to 1975 have not been programed. Unless these requirements are definitized and planned for in advance, the United States may not be able to satisfy future foreign support requirements without affecting the U.S. readiness. (See pp. 33 and 34.)

--Management information systems for foreign military sales have data of individual sales satisfied from present production, but the systems do not identify future support requirements for U.S. and foreign customers. (See p. 18.)

--Inadequate consideration has been given to the cumulative effect of foreign military sales on weapon systems with common components. Sales thus made affect not only the system being delivered but also other systems. (See p. 29.)

Many of the problems can be solved at the Department of Defense. The Secretary of Defense should require:

--Inclusion, in all cases, of detailed impact statements in the foreign military sales decisionmaking process so that relevant information is not omitted inadvertently. (See pp. 19 and 20.)

--A supply support agreement or other mechanism to be a part of any sale when it is feasible, so that the Department of Defense can program and fund future support without affecting U.S. defense capabilities adversely. (See p. 38.)

--Development of a forecasting mechanism to identify the probable quantities of future critical support items for U.S. and foreign sales customers, including long leadtime items used on more than one weapon system. Such a mechanism will require a system that will couple existing data on sales and deliveries by country, weapon system, quantities, and delivery dates, with current assets. (See pp. 38 and 39.)

AGENCY COMMENTS

The Department of Defense concurred in GAO's recommendations. It said that it had issued instructions informing the military services of the procedures to be followed when submitting impact statements. The instructions, however, do not specify the criteria to be considered. (See p. 20.)

Explicit criteria should be given to the three services to facilitate the preparation of complete and consistent impact statements.

The Department of Defense said that agreements for supply and support would be made a part of any foreign military sale for major weapons when it was feasible to do so. It did not, however, cite any instructions issued or planned that would emphasize to negotiators that every effort should be made to include such agreements as part of all foreign military sales for major weapon systems. Specific instructions emphasizing this policy are imperative.

The Department of Defense noted that forecasting future foreign military sales for major system requirements was being done by tracking inventories, production, training, and foreign demand on 60 major weapon systems to the extent that the requirements of foreign governments are known to them or to the Department of State. However, the system does not address future support requirements. (See p. 39.)

Defense's system on the 60 major systems is a step in the right direction, but it should be expanded to provide for forecasting requirements in future critical support for those items, whether in the hands of U.S. Forces or foreign customers. Although Defense noted that it planned to issue a directive that would require the services to maintain information on past, present, and forecasted sales of major weapon systems, GAO's

review of the proposed directive disclosed that it did not address the maintenance of such data specifically.

The Department of State had no objection to GAO's recommendations. However, it noted that many foreign military sales that had caused major effects on U.S. capabilities in recent years were the result of political, rather than management, decisions.

C o n t e n t s

		<u>Page</u>
DIGEST		i
CHAPTER		
1	INTRODUCTION	1
	Growth of the foreign military sales program	1
	Foreign military sales market	4
	Previous GAO reports	5
	Scope of review	7
2	BACKGROUND	9
	Foreign military sales organization responsibilities	9
	Types of foreign military sales arrangements	10
	End-item sales	12
	Support sales	12
3	ADMINISTRATIVE COMPLEXITIES OF FOREIGN MILITARY SALES	13
	How a sale is made	13
	Processing a sale	16
	Conclusions	19
	Recommendation	19
	Agency comments and our evaluation	20
4	IMPACT OF FOREIGN MILITARY SALES ON THE U.S. DEFENSE POSTURE	23
	Policy and impact examples	24
	Summary	33
	Follow-on support	33
	Conclusions	35
	Recommendations	38
	Agency comments and our evaluation	39
APPENDIX		
I	Opportunities identified by GAO for improving the management of the foreign military sales program	41
II	Foreign military sales offer and acceptance contract, Du form 1513	44

III	Letter dated February 17, 1976, from the Director, Defense Security Assistance Agency and Deputy Assistant Secretary (ISA), Security Assistance, to the House Committee on Armed Services	47
IV	Letter dated July 28, 1976, from the Director, Defense Security Assistance Agency and Deputy Assistant Secretary (ISA), Security Assistance, to the House Committee on Armed Services	49
V	GAO-suggested subject areas for inclusion in an impact statement	51
VI	Memorandum dated July 9, 1976, from the Director, Defense Security Assistance Agency and Deputy Assistant Secretary (ISA), Security Assistance, to the General Accounting Office	53
VII	Letter dated April 27, 1977, from the Director, Defense Security Assistance Agency and Deputy Assistant Secretary (ISA), Security Assistance, to the General Accounting Office	55
VIII	Letter dated March 15, 1977, from the Deputy Assistant Secretary for Budget and Finance, Department of State	58
IX	Principal officials responsible for administering the activities discussed in this report	61

ABBREVIATIONS

DOD	Department of Defense
DSAA	Defense Security Assistance Agency
FMSO-I	Foreign Military Sales Order I
FMSO-II	Foreign Military Sales Order II
GAO	General Accounting Office
ISA	International Security Affairs

CHAPTER 1

INTRODUCTION

The United States uses foreign military sales to provide military assistance to foreign countries. The principal foreign military sales objective, established by the Foreign Military Sales Act of 1968 (renamed Arms Export Control Act on June 30, 1976), is to:

"* * * facilitate the common defense by entering into international arrangements with friendly countries which further the objective of applying agreed resources of each country to programs and projects of cooperative exchange of data, research, development, production, procurement, and logistics support to achieve specific national defense requirements and objectives of mutual concern."

To this end, the act authorizes the United States to sell defense articles and services to countries that are able to pay to equip their military forces without undue burden to their economies when it will further the security objectives of the United States, and it will be consistent with the objectives of the United Nations.

Many of the nations receiving foreign military sales from the United States have developed, and now control, vast amounts of the world's scarce commodity reserves, for example, Persian Gulf nations that are members of the Organization of Petroleum Exporting Countries. The industrial economies of nations, worldwide, are dependent on these countries for their supply of critical resources. National defense and the stabilization of their governments have therefore become an area of increasing concern for both these nations and the United States. Selling defense items and services has, in many cases, provided the common bond between the United States and these countries. Therefore the foreign military sales programs can play an important role in support of U.S. foreign policy initiatives.

GROWTH OF THE FOREIGN MILITARY SALES PROGRAM

In the past 7 years, foreign sales volume grew from \$952 million to over \$8.7 billion. (See pp. 3 and 4.) The Department of Defense (DOD) has not handled this volume of foreign support since the 1950-54 Korean War period, when grant aid averaged \$8.7 billion and foreign military sales averaged \$350 million (expressed in 1976 dollars).

As shown in the following table, average foreign military sales have continued to escalate throughout the 1950-76 period, whereas total foreign assistance (foreign military sales plus grant aid) dropped during the 1950-69 period and then rose dramatically in the 1970-74 period.

Growth of Foreign Military Sales and Grant Aid

(constant 1976 dollars)

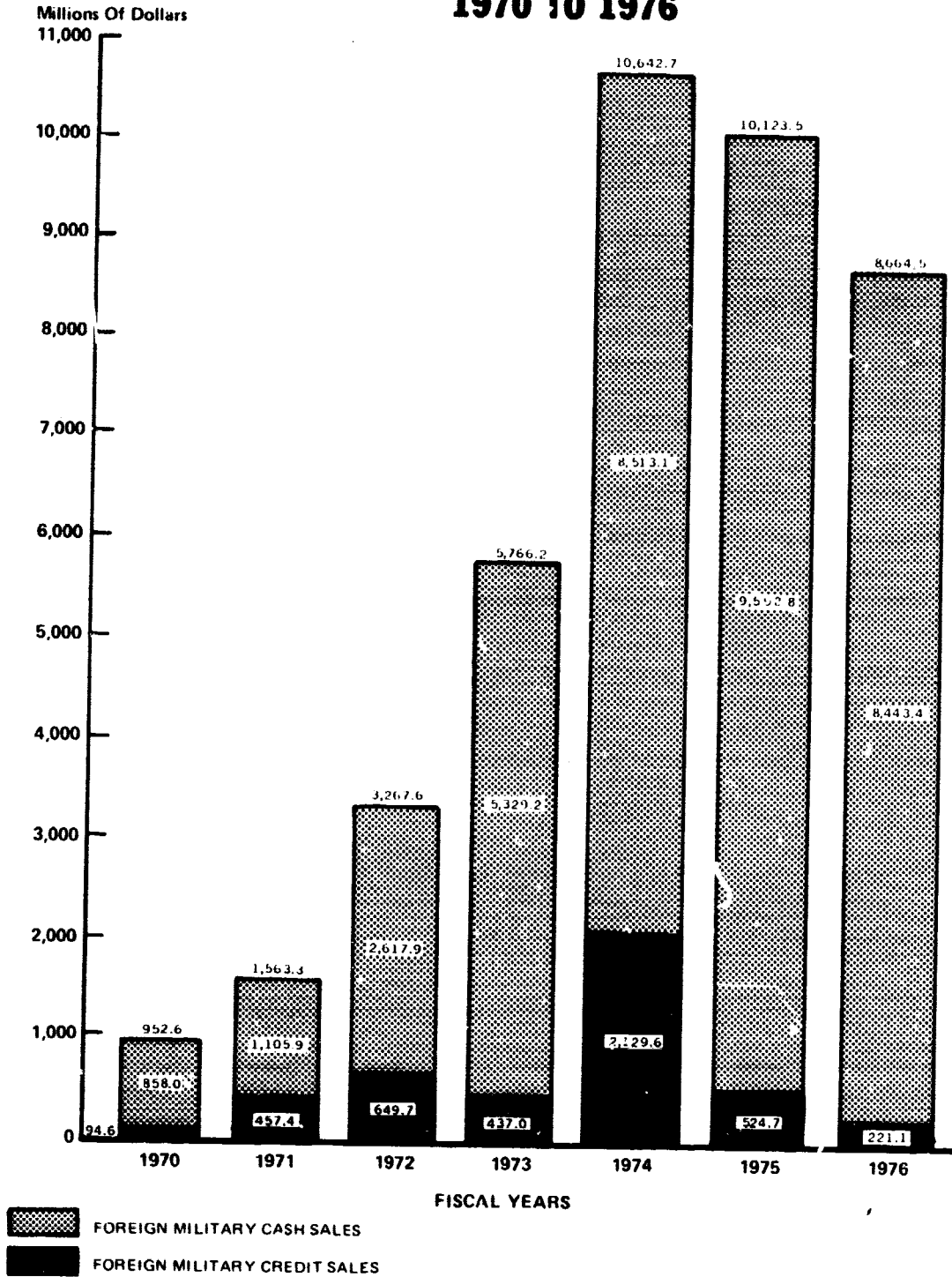
<u>Program</u>	<u>FY 1950-54 average</u>	<u>FY 1955-59 average</u>	<u>FY 1960-64 average</u>	<u>FY 1965-69 average</u>	<u>FY 1970-74 average</u>	<u>FY 1975-76 average (note a)</u>
(000,000 omitted)						
Foreign military sales	\$ 350	\$ 653	\$1,300	\$3,070	\$ 5,820	\$ 9,950
Grant aid	<u>8,720</u>	<u>3,090</u>	<u>2,780</u>	<u>3,100</u>	<u>4,400</u>	<u>1,000</u>
Total	<u>\$9,070</u>	<u>\$3,743</u>	<u>\$4,080</u>	<u>\$6,170</u>	<u>\$10,220</u>	<u>\$10,950</u>

a/Only a 2-year average.

Source: Defense Security Assistance Agency.

The sales include some of the most advanced weapons and support systems in our inventory. Some of these systems are provided to foreign customers before our own forces are fully equipped.

GROWTH IN FOREIGN MILITARY SALES VOLUME 1970 TO 1976



Crowth in Foreign Military Sales by Category

<u>Category</u>	<u>Fiscal year 1970</u>	<u>Fiscal year 1976</u>
Aircraft	\$103,677,000	\$1,519,056,000
Ships	8,460,000	322,568,000
Vehicles and weapons	27,724,000	575,266,000
Ammunition	68,238,000	344,213,000
Missiles	19,810,000	868,541,000
Communication equipment	98,566,000	125,405,000
Other equipment	78,324,000	306,070,000
Total	<u>404,799,000</u>	<u>\$4,061,119,000</u>
Supply support (note a)	368,494,000	1,956,837,000
Training	77,174,000	251,967,000
Construction	30,024,000	808,637,000
Technical assistance	28,093,000	1,227,387,000
Research and development	40,620,000	130,000
Other services	1,479,000	92,471,000
Undefinitized	<u>1,910,000</u>	<u>265,919,000</u>
Total	<u>547,794,000</u>	<u>4,603,348,000</u>
Total	<u>\$952,593,000</u>	<u>\$8,664,467,000</u>

a/Includes concurrent spare parts, repair and rehabilitation, supply operations, and Foreign Military Sales Order I agreements.

Source: Defense Security Assistance Agency.

FOREIGN MILITARY SALES MARKET

Although, according to the United States Arms Control and Disarmament Agency, the United States controls almost one-half of the world arms market, there is keen competition between major industrial powers, which creates somewhat of a buyers' market. (See p. 6.) If one nation will not sell, there are others waiting in the wings with comparable arms that will.

The apparent market advantage for the United States is the current high technology embodied in its arms and the demonstrated capability to provide support. However, other nations, such as the Soviet Union, West Germany, France, and the United Kingdom, are striving to close these technological and support gaps.

Iran, Israel, and Saudi Arabia have been the prime customers for recent U.S. foreign military sales. In fiscal year 1976 these three countries' sales accounted for slightly more than half of the \$8.7 billion sales.

PREVIOUS GAO REPORTS

In addition to this report, we have previously published the following reports on ways to improve the management of the foreign military sales program.

"Department of Defense Stock Piling of War Reserve Materials for Use by United States Allies" (Report to the Senate Committee on Foreign Relations; July 17, 1974; P-74-ID-68)

"Security Assistance to Korea: Accomplishments and Constraints" (Report to the Congress; B-164264; July 1, 1974)

"Status of Emergency Security Assistance to Israel" (Report to Representatives Runnels, Leggett, and Dickinson; B-180356, May 20, 1974 (classified))

"Foreign Military Sales--A Growing Concern" (Report to the Congress; June 1, 1976; ID-76-51)

"Airlift Operations of the Military Airlift Command During the 1973 Middle East War" (Report to the Congress; Apr. 16, 1975; LCD-75-204)

"Military Assistance and Sales to the Persian Gulf States" (Report to the Subcommittee on the Near East and South Asia, House Committee on Foreign Affairs; Dec. 31, 1974; ID-75-37 (classified))

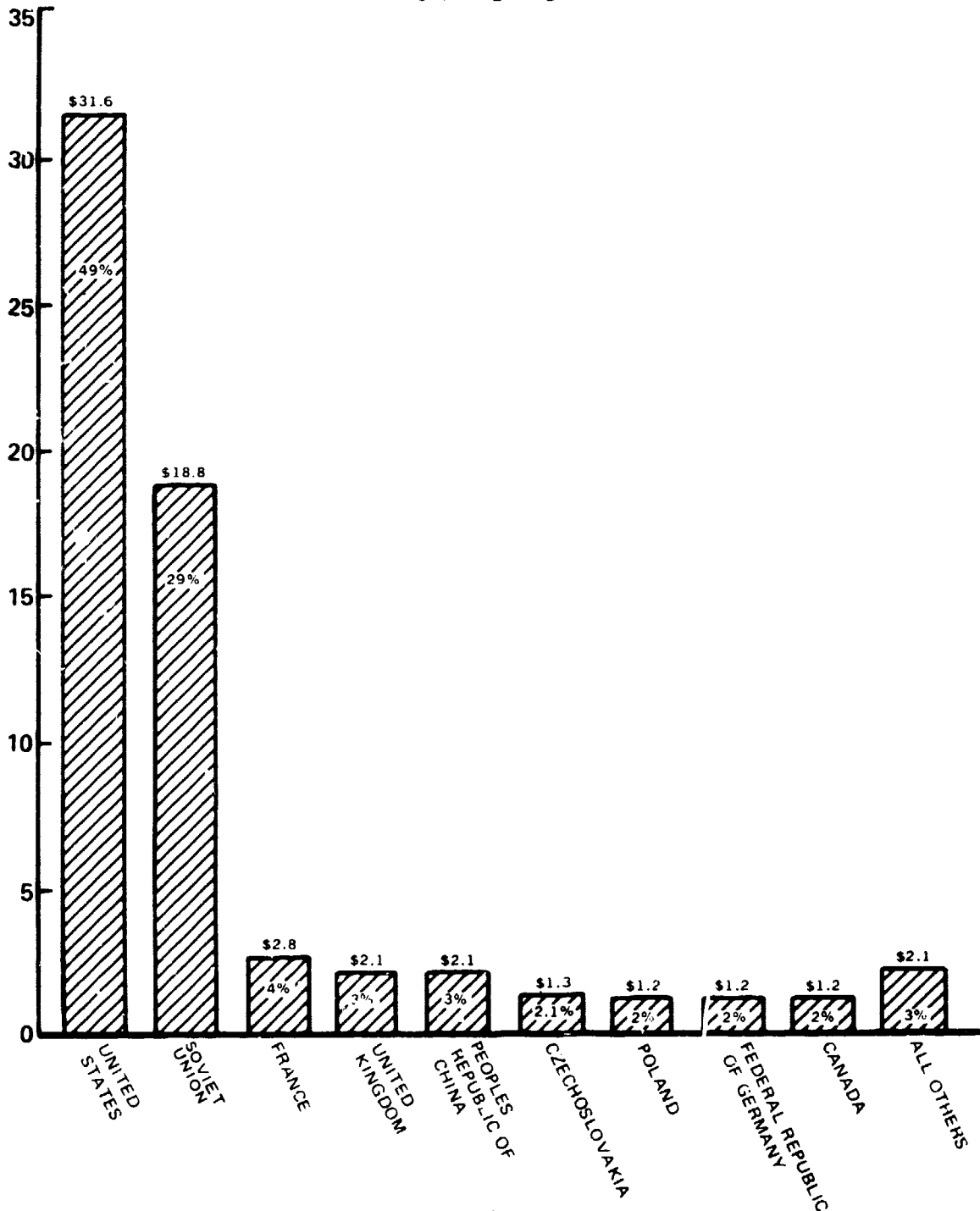
"Issues Related to U.S. Military Sales and Assistance to Iran" (Report to the Congress; Oct. 21, 1974; P-75-ID-15 (classified))

"Reimbursements from Foreign Governments for Military Personnel Services Provided Under the Foreign Military Sales Act" (Report to Representative Les Aspin; Aug. 16, 1974; ID-75-6)

"Equipment Shortages: A Result of Emergency Support of U.S. Allies" (Report to the Congress; Nov. 19, 1975; LCD-75-426)

PERCENTAGE OF \$64.4 BILLION MILITARY ARMS AND SERVICES DELIVERED BY MAJOR SUPPLIERS FROM 1965 TO 1974

Billions Of Dollars



SOURCE: U.S. ARMS CONTROL AND DISARMAMENT AGENCY

"Assessment of Overseas Advisory Efforts of the U.S. Security Assistance Program" (Report to the Congress; Oct. 31, 1975; ID-76-1 (classified))

"Millions of Dollars of Costs Incurred in Training Foreign Military Students Have Not Been Recovered" (Report to the Congress; Dec. 14, 1976; FGMSD-76-91)

"U.S. Logistical Support of Major Military Equipment Provided to Foreign Countries" (Report to the House International Relations Committee; Oct. 21, 1975; ID-76-22)

Short synopses of key reports are included in appendix I.

SCOPE OF REVIEW

Because of continued congressional concern over the impact of foreign sales on the U.S. defense posture, we reviewed the effects of certain weapon systems on the U.S. Forces and examined the considerations given to these effects on the decisionmaking process.

We randomly selected several weapon systems that had experienced a high volume of foreign sales. From these systems, cases were selected and reviewed to determine whether high foreign military sales demand had affected the availability and operational readiness of these systems and whether a forecasting mechanism for follow-on support was available.

We did not review (1) the basis for the foreign policy decisions made pertaining to these sales, (2) the procedures used regarding pricing of the commodities sold, or (3) whether supply support agreements were the best alternative for providing support.

During our review we interviewed and obtained documents from officials of the Department of State; DOD and the military departments; and the United States Arms Control and Disarmament Agency, Washington, D.C. We made our review at:

Office of the Secretary of Defense.
Defense Security Assistance Agency.
Headquarters of the Army and the Air Force.
Air Force Logistics Command, Dayton, Ohio.

Air Force Systems Command, Dayton, Ohio.
Development and Readiness Command, Alexandria, Virginia,
and its subordinate commands.
Army Missile Command, Huntsville, Alabama.
Army Tank Automotive Command, Warren, Michigan.

CHAPTER 2

BACKGROUND

Some background about how the United States makes foreign military sales and about the various types of sale arrangements is essential in order to understand this dynamic and growing activity.

FOREIGN MILITARY SALES ORGANIZATION RESPONSIBILITIES

Numerous departments and agencies within the executive branch (for example, the National Security Council, the Agency for International Development, and the Departments of Commerce and the Treasury) have various responsibilities for foreign military sales. However, aside from the President, who has final determination, the principal responsibilities, established by legislation, have been assigned to the Secretaries of State and Defense.

Department of State

The President has delegated foreign military sales management to the Secretary of State. He, in turn, has delegated it to the Under Secretary for Security Assistance. The action has been assigned to the Bureau of Politico-Military Affairs and its major operating bodies:

1. Office of Security Assistance and Sales, which assesses political, economic, and legal factors associated with foreign sales.
2. Office of Munitions Control, which regulates commercial exports of arms, ammunition, implements of war, and related technical data delineated in the "U.S. Munitions List."

The Under Secretary for Security Assistance also chairs the Security Assistance Program Review Committee, which resolves major policy issues and formulates security assistance programs by country. The Committee includes representatives from DCD; the Office of Management and Budget; the Arms Control and Disarmament Agency; the National Security Council; the Agency for International Development; and the Departments of the Treasury, Commerce, and Labor.

Simply stated, the Department of State decides whether a sale should be made, and DOD determines how to provide the requested article in a timely fashion.

DOD

Although overall responsibility for foreign military sales is vested with the Secretary of State, the offices of the Assistant Secretary of Defense (International Security Affairs (ISA)); the Deputy Assistant Secretary (Security Assistance); and the Defense Security Assistance Agency are the major action offices within the Office of the Secretary of Defense.

The Assistant Secretary (ISA) is responsible for coordinating the activities of DOD components, formulating guidance, and representing the Secretary of Defense in matters concerning security assistance.

The Deputy Assistant Secretary (Security Assistance) is also the Director of the Defense Security Assistance Agency. In the former capacity he supports the Assistant Secretary of Defense (ISA) in formulating policy guidance. In the latter capacity, he directs and supervises the administration and implementation of security assistance programs and maintains management and status information systems on foreign military sales.

The step by step management of foreign military sales is coordinated through the procurement and logistic offices at the Office of the Secretary of Defense level and their counterparts in the individual service headquarters and their subordinate commands.

TYPES OF FOREIGN MILITARY SALES ARRANGEMENTS

There are two basic kinds of foreign military sales, (1) those consisting of an end-item--such as a tank, an aircraft, or a ship--and (2) those consisting of support--such as spare parts, technical assistance, and construction.

Both kinds of sales are handled directly between the U.S. Government and a foreign government, which is the subject of this report, or between a U.S. commercial producer and a foreign government or other foreign organizations. Most requests, however, are handled under government-to-government arrangements. Reasons why foreign nations and international organizations may prefer to deal with the U.S. Government rather than directly with commercial sources are:

--Foreign procurements receive the increased protection of the U.S. procurement regulations.

--Foreign nations are assured that the items supplied will meet standard U.S. Government configurations.

--Many foreign nations are inexperienced in procurement procedures but have had longstanding diplomatic experience.

Under government-to-government arrangements, the United States manages the actual procurement, and the foreign country relies on its diplomatic experience to obtain favorable delivery dates, should the need arise.

Payment for foreign military sales is either on a credit or a cash basis. Foreign military credit sales are, in some cases, an intermediate step for countries making the transition from grant aid.

Repayment periods are up to 12 years. Foreign military cash sales are made in the following manner.

1. Cash in advance--The full amount of the sale is paid when the customer signs the contract.
2. 60-day payment--The full amount is paid within 60 days after delivery.
3. 120-day payment--The payment plus interest may be deferred with congressional approval from 60 to 120 days after delivery.
4. Dependable undertaking--The customer makes a firm commitment to pay all costs for new production or services and insures the U.S. Government against any loss in the venture. For example, under the dependable undertaking provisions of the supply support agreement, wherein the customer accepts the financial obligation for the materiel on order, the U.S. Army is authorized to purchase and stock materiel based on demand experience in anticipation of the customer's needs and thereby provide dependable and timely service to the customer.

Foreign military sales credit is extended to eligible countries on the basis of credit agreements, which make specified amounts of credit available for use by such

countries to finance foreign orders. The terms of the loan agreements require that purchase be placed against the available credit funds before a specified date, usually 2 years after the date that the loan agreement was signed.

END-ITEM SALES

Other than arranging for payments, the sale of an end-item is a relatively simple contractual agreement. It is very similar to buying an automobile. The contract specifies the items and the accessories, such as radios, engines, guns, and paint color. (See app. II for a specimen contract, DD form 1513.)

SUPPORT SALES

Foreign military sales specifically for support are called cooperative logistics support agreements and fall into two main categories: Foreign Military Sales Order I (FMSO I) and Foreign Military Sales Order II (FMSO II). These are far more complex than an end-item sale, in both the items called for and the means of payment.

FMSO I has two parts. The first part is normally a cash arrangement and specifies the items to be stocked to meet the 120-day consumption requirement for the customer. Part two lists the quantity of items to be placed on procurement for the 360-day consumption requirement and is normally a dependable undertaking.

FMSO II is an open-ended sales order for the continued consumption of the items stipulated in FMSO I. (A customer must have an FMSO I arrangement before negotiating an FMSO II.) When the FMSO II is accepted and the necessary funds deposited in the United States, the customer is then allowed to submit requisitions which will be filled from U.S. stocks. However, no provisions are made to hold the customer's requisition until its stocks have been procured. Thus, to the degree that a foreign country's requisitions exceed the funded amount of its FMSO II agreement, the stocks will be funded by U.S. stock funds until a new quarterly payment is made by the foreign country.

The mechanisms for administering foreign military sales and the impact on the U.S. defense posture are discussed in the following chapters.

CHAPTER 3

ADMINISTRATIVE COMPLEXITIES OF FOREIGN MILITARY SALES

The growth of foreign military sales has strained DOD's ability to routinely administer both foreign customers' and U.S. Active Forces' needs for weapon systems and support. However, this growth has allowed U.S. manufacturers to operate plants at higher levels of production and, in some cases, to continue operating plants which otherwise might have been closed down. Additionally, foreign military sales can play an important role in support of foreign policy initiatives.

Functioning as a political, economic, and defense tool has made the administration of foreign military sales a complex assignment. The rapid rise in volume of foreign military sales has taxed the ability of DOD to manage the program, and there are indications that some deliveries to foreign customers have had an adverse impact on the U.S. Forces' inventories. Since, at the beginning of fiscal year 1976, undelivered orders totaled about \$24 billion, there are opportunities to improve the existing method of administration to insure that future sales and deliveries will not detract from the U.S. defense efforts.

HOW A SALE IS MADE

The mechanism for making a foreign sale varies within DOD, depending on the article sold, the kind of support required, and the service responsible for their management. But, in general, they follow the sequence outlined in the following sections.

Origin of a sale

Foreign countries continually review the defense articles offered by the major industrial nations. Their activities are somewhat similar to an individual's, when the individual shops and purchases a major household item.

If a country wants a U.S. article, it normally requests a quote on current prices and delivery dates through the Department of State. If the Department determines the request is in our best interests, it will notify DOD. DOD will then determine the price and the delivery date and forward a letter of offer with a contract (DD form 1513).

If the country accepts, it signs the contract and provides the necessary funding. If not, the country may renegotiate or buy its defense needs elsewhere.

Forecasting

The purpose of forecasting for both end-items and support requirements is to arrange for the orderly, timely, effective, and efficient procurement and delivery of goods and services for a customer. It is widely recognized as a prudent business practice. However, because the Arms Export Control Act precludes DOD from making advanced procurements based on foreign military sales forecasts, DOD's forecasting abilities have not been fully exploited. Consequently, when an order is received and the requested article is not in a surplus position, DOD must

- procure the article from ongoing production;
- divert the article from production intended for either U.S. or other foreign customers, including items undergoing depot level overhauls;
- withdraw articles from war reserve stocks; or
- withdraw articles from Active Forces inventories.

Most foreign military sales are provided from ongoing production sources within normal leadtimes even though the weapon may not have been fully deployed. In some instances, foreign policy and national security considerations dictate sales with such a short leadtime that the first alternative above is not satisfactory. Consequently, when there are insufficient stocks on hand to simultaneously supply both U.S. and foreign needs, the sales may result in withdrawals or diversions from our own forces' inventories. Since the October 1973 Israeli war, the dollar value of foreign military sales in weapons and ammunitions which resulted in either withdrawal or diversion has dropped from a high of 17 percent in fiscal year 1973 to a level of only 1 percent in fiscal year 1976.

Although considerable improvements have been made in reducing withdrawals and diversions, the growth of foreign sales is creating a potential for future impact on U.S. Forces needs. There is a large and growing inventory of weapons in foreign hands for which the United States

will have to provide support, and currently there is no adequate mechanism for forecasting how the support requirements will affect the U.S. Forces in the out years.

To some degree these potential problems have been recognized. Recent changes to the Arms Export Control Act established the need for credible forecasts and require the President of the United States to submit to the Congress an "Annual Estimate and Justification for Sales Program," a quarterly report on the status of all military exports and, specifically, to identify for congressional approval all sales for \$25 million or any major defense equipment for \$7 million or more. Further the changes require that:

"Sales of defense articles and defense services which could have significant adverse effects on combat readiness of the armed forces of the United States shall be kept to an absolute minimum."

In addition, at the request of certain committees, the President must, among other things, provide: "* * * an analysis * * * of the impact of the proposed sale on military stocks and the military preparedness of the United States * * *."

Taken together, these changes clearly mandate that DOD have a credible sales forecasting mechanism. At present, DOD has not specified the minimum essential criteria for assessing the impacts of both end-item and follow-on support sales. Moreover, the basis for determining impacts vary on a case-by-case basis. The use of criteria to determine the impacts are the heart of effective sales forecasts. Consequently, the basis for developing credible forecasts that can be used for determining alternative sales actions has been open to wide interpretation.

Moreover, available statements of impact were developed solely for cases where there were withdrawals and/or diversions. Even these, however, are not uniform in criteria or content. Further, the remaining cases, which constitute the majority of sales satisfied from production, did not require a statement of impact. Consequently, it is not known whether, in fact, these cases had an adverse impact on our forces.

Appendixes III and IV show the type of impact statement submitted before and after the changes to the Arms Export

Control Act. In comparing the two statements, there appears to be little difference in the information or content, and in neither case is the follow-on support addressed. In contrast, a distillation of the information gleaned from personnel experienced in foreign military sales suggests that the criteria set forth in appendix V would reasonably reflect minimum essential information needed to adequately evaluate the impact of a foreign sale and thus support credible forecasts and provide a basis for satisfying congressional needs.

It is doubtful that any private sector manufacturing organization controlling a dominant market position could effectively maintain this position without producing and stocking sufficient inventory to meet its projected sales forecasts. Nor could it develop useful sales alternatives without good information about the impact of the proposed sale on the organization itself. Assuming that DOD will continue to be a major factor in the foreign military sales market, it is equally doubtful that it can continue to sell and support its advanced weapon systems in an orderly manner without the benefit of good sales forecasts.

In reality DOD is the manager of foreign military sales and should be in a better position to forecast both the sales of major articles and follow-on support. Although we did not evaluate the private sector forecasts, it seems probable that they try to anticipate the impact of such sales on their own production base. Moreover, to the extent this information is exchanged with DOD, it will be in a better position to manage the total foreign military sales environment. The flow of information between DOD and the private sector--in both directions--is necessary to insure accurate forecasts which contribute to smooth production runs.

PROCESSING A SALE

The processing of a sale is a complex interaction between the Department of State, DOD, and the Departments of the Army, Navy, and Air Force and their numerous subordinate commands, plus a multitude of system and item managers and contractors. As the processes within each service differ slightly to accommodate differing environments, for simplicity, we will discuss a typical process.

The State Department has divided all countries eligible for military sales into two groups, category A and category B. Category A countries are those to which DOD may sell

defense articles and services without referral to the State Department for policy guidance; countries in this group are the Western industrialized countries, for example, most North Atlantic Treaty Organization countries and Japan and Australia. Category B countries are those countries whose requests for purchase of defense articles and services must be cleared by the State Department. Some countries, depending on the weapon system, may be categorized as A for some and B for others. If the Department of State has assigned an eligibility of category A to a country, that country's request for U.S. arms, support, or services is made directly to DOD. Category B countries, however, must submit their requests to the Department of State which decides if the projected sale is in the best interests of the United States. This analysis is almost exclusively in a political context. If it is in our best interests, the request is forwarded to DOD along with category A country requests. Otherwise it is returned to the originating country.

The approved country's request is then forwarded to the appropriate military department for processing. After some analysis the request is forwarded to the International Logistics Office of the appropriate subcommand and subsequently to that command's comptroller for price information and item manager for availability information.

The item manager then determines how the requested item can be provided within the given period. His determination along with pricing data is then returned to the International Logistics Office. At this point a key decision is made. If the item can be supplied within the time constraints from either surpluses or ongoing production without diversion, the International Logistics Office formulates a letter of offer with a sales contract and sends them to the service headquarters for transmittal to the country. However, if the requested delivery time is so urgent that the item must be either diverted or withdrawn, an impact statement outlining these concerns is drawn up and forwarded with the letter of offer and the sales contract to the service headquarters.

The content and form of the impact statement are not prescribed, nor is the mechanism for including the statement in the decisionmaking process formalized. However, if the service headquarters agrees that there is no other viable alternative to diversion or withdrawal, the proposed sale is forwarded to the Secretary of Defense. At this point the exact procedure becomes unclear. There are

no standard practices promulgated by either the Department of State or DOD for handling these exceptional cases, and, consequently, there is no clear audit trail. However, as a result of extensive interviews with State and DOD officials, the following sequence of events has emerged. The alternatives to either withdraw or divert articles for the sale are reviewed within the Office of the Secretary of Defense. If analyses support the service position, the Secretary of Defense advises the Department of State that, in the light of the overall defense impact, State should reevaluate the propriety of the sale.

Management system

The Defense Security Assistance Agency (DSAA) is responsible for reporting on the status of foreign military sales. In so far as the sales relate to end-items that are in production or for which production capacity can be made available, DSAA has developed a system encompassing about 60 major weapon systems and their key long leadtime components on an individual basis. This system is dependent on information from the services. To the extent that information is timely and accurate, DSAA can readily determine the available production capacity at any point in time as well as the impact of diverting production from one customer to another, including the United States. But what this system does not portray is the consequence of withdrawing articles from inventory or the cumulative effect of both diversions from production and withdrawals from inventory. Consequently, DSAA cannot readily determine whether a foreign sale, to be satisfied from other than production, will adversely affect existing or projected inventories.

For example, we contacted DSAA to determine how it tracked the cumulative effect of withdrawals and diversions of end-items on existing inventories; we were told there were no effects. Moreover, to its knowledge, there had only been a few isolated instances where the effect resulted in withdrawals or diversions other than emergency assistance to Israel during the October 1973 war. In March 1976 we requested DSAA to prepare a list of all foreign military sales for fiscal years 1975 and 1976 which authorized either withdrawal or diversion of stocks.

On July 9, 1976, DSAA sent us a letter which stated that:

"The DOD does not keep cumulative records by type transactions and, therefore, our reply has been delayed pending completion of a survey of various country files."

The letter listed 43 instances in which decisions were made to provide DOD equipment, such as M-60A1 tanks, M-113A1 armored personnel carriers, and the Dragon and TOW missiles in less than normal leadtime from new production (diversion) or from DOD inventory (withdrawal). The detailed listing included 15 instances for [redacted] and the remaining 28 instances for [redacted] deleted Oman, [redacted] Ethiopia, Morocco, Korea, Cambodia, and Indonesia. (See app. VI.)

We attempted to compare the data included in the DSAA July 9, 1976, letter with information we had received from the Coordinator for Army Security Assistance regarding withdrawals and diversions for the same period of time. This comparison showed inconsistencies in the lists obtained from the two sources. The DSAA letter did not include fifty-four M-48A5 tanks withdrawn from U.S. stocks and twenty-two M-113A1 armored personnel carriers, which were withdrawn and diverted.

CONCLUSIONS

There is no indication that the United States will reduce its active role in the foreign military sales market. The fact that these sales are made with political, economic, and defense overtones makes their administration complex and the opportunity for error great. Therefore, to effectively balance mutual political, economic, and defense needs, it is critical that the information used to make these far-reaching decisions be credible and timely.

The State Department and DOD have attempted to closely coordinate the complex administration of foreign military sales. But the separation of political and economic interests from defense needs, coupled with incomplete information, has created continuing management problems. Many, we believe, can be solved at the DOD level.

RECOMMENDATION

To reduce the possibility that future foreign sales and deliveries may hinder the U.S. defense effort, we recommend that the Secretary of Defense require in all cases the

inclusion of detailed impact statements in the foreign military sales decisionmaking process so that relevant information is not inadvertently omitted.

AGENCY COMMENTS AND OUR EVALUATION

Our preliminary report was submitted to the Department of State and DOD for comment. In response, DOD concurred in our recommendations and the Department of State said that it had no objections to them. State noted, however, that many foreign military sales that had caused major impacts on U.S. capabilities in recent years were the result of political, rather than management, decisions. These comments are included as appendixes VII and VIII.

DOD agreed with our recommendations that impact statements be required in the foreign military sales decisionmaking process. They cited a December 14, 1976, memorandum from the Deputy Secretary of Defense to the service secretaries apprising them of the procedures to be followed when submitting such statements.

The cited memorandum, however, does not address the specific matters to be considered by the services in determining whether a proposed foreign military sale will have an adverse impact on the U.S. military capability. It merely requires a "full description of the effect the proposed sale will have on combat readiness of the Armed Forces of the United States." Nor does a proposed DOD directive that will supersede the December 14, 1976, memorandum include any specific criteria for impact statements.

We believe that the services should be given specific guidance on the factors to be considered in determining the impact and that these factors should be clearly addressed in all impact statements. This would insure consistency in impact statements, both within and between the services, and would provide DOD with a better basis for determining whether the adverse impact of a proposed sale was of such significance as to require Presidential reporting to the Congress under the provisions of the Arms Export Control Act. Appendix V identifies specific areas that, we believe, should be addressed in impact statements.

DOD concluded that the main thrust of our report was that foreign military sales had had an adverse impact on U.S. defense capabilities. Although DOD concurred in all

of our recommendations for improvement, it did not believe that the examples in the report supported such a conclusion.

In addition, DOD said that only about one-half of 1 percent of the total dollar value of fiscal year 1976 foreign military sales had an impact on U.S. Forces. DOD believed we ignored the total force policy under which a foreign sale may enhance allied defense capabilities and ease the U.S. defense burden.

It was not our intent to try to demonstrate an overall adverse impact on U.S. defense capabilities as the result of foreign military sales. We have shown, however, that such sales have impaired the availability of certain items to U.S. Forces and, we believe, have demonstrated the potential drain on the U.S. posture that such sales can have if their impact on U.S. needs is not adequately considered.

We are mindful of the fact that enhancement of allied defense capabilities may ease U.S. defense burdens. We believe, however, that such enhancement to the detriment of the capability of U.S. Forces is a decision that should be reached only after the most careful and complete consideration of all the ramifications of the impact on U.S. Forces and the benefits to be gained. Moreover, although only a small percentage of foreign military sales may have an adverse impact on U.S. Forces, as we have shown in chapter 4, many of the items in this category are the most advanced weapons and support systems in our inventory.

DOD also said that our statement that

"diversion and withdrawal of end items and spare and repair parts have been made to the point where minimum essential quantities have been denied to our own forces"

implied that this was a serious problem when it was not. Again, as we commented earlier, we did not attempt to evaluate the overall adverse impact on U.S. Forces resulting from foreign military sales. Obviously, however, for the examples cited in our report--important current weapons, such as the TOW and Dragon missiles--the U.S. military capability was seriously affected.

DOD said that our report was not objective and well balanced because it had a number of inaccurate and unsupported statements. However, it cited only one example--our

comment that DSAA had not identified fifty-four M48A5 tanks withdrawn from stocks after we asked them to identify all foreign military sales during fiscal year 1975 and fiscal year 1976 which authorized withdrawal or diversion of stocks. (See pp. 18 and 19.) DOD said that DSAA did not identify these items to us because the Army had concluded there was no adverse impact on U.S. Forces as a result of this withdrawal.

Our request, however, asked not only for withdrawals that had an impact on U.S. Forces but also for all sales that authorized withdrawals from stocks during the above-mentioned period. Moreover, as pointed out previously, the Army Coordinator for Security Assistance had identified these items as being withdrawn from stocks. Although DOD in its comments had cited this example as portraying an inaccuracy in our report, its final comments on this matter concluded that the situation indicated that perceptions varied at different levels of an organization because of information available--in other words, that the Army Coordinator and LSAA personnel viewed this matter differently as to whether it should be considered a withdrawal from stocks.

CHAPTER 4

IMPACT OF FOREIGN MILITARY SALES

ON THE U.S. DEFENSE POSTURE

The adequacy of the U.S. defense posture can be expressed as a measure of a number of factors, such as the capability, quantity and quality of manpower, equipment, and support. However, when any one or a combination of these factors is adversely affected by actions, such as foreign military sales, to the point where the required quantity, quality, or capability is reduced below the established minimum essential levels or deployment of critical articles is significantly postponed, then logic dictates that there is an undesirable impact on the U.S. defense posture.

Two possible indicators of an adverse impact are:

--Shortfalls and delays in achieving either authorized acquisition objectives, which is the required level necessary to support the U.S. Forces and allied forces in a wartime situation, or initial issue quantities, which is the minimum level a unit must have on hand to carry out its mission responsibilities.

--Delayed deployments of critical weapon systems.

In addition to these factors that have an impact on foreign sales, there are other factors, such as funding constraints and production limitations, which have an impact on the achievement of inventory objectives and the timely deployment of weapon systems. For example, the year-to-year phasing of procurement funds frequently stretches the achievement of authorized acquisition objectives, initial issue quantities, and deployments over a number of years. In this situation, if the available production capacity is greater than the scheduled U.S. procurements, foreign sales usually can be readily accommodated. In contrast, if scheduled U.S. production uses all of the available production capacity, foreign sales are not easily accommodated unless they can be added to the end of the U.S. production run. Otherwise, the foreign sales must be either diverted from U.S. production or withdrawn from other sources of stocks, at the expense of the U.S. defense posture.

What follows is intended to highlight some of the ways in which foreign sales have had an impact and may continue to have an impact, on the U.S. defense posture. However, none of the examples, by themselves, create insurmountable problems, and they should not be considered out of context. But when the examples are considered together, their cumulative effect demonstrates how foreign sales aggravate the already difficult task of managing the U.S. defense posture in a peacetime environment. Moreover, the examples provide a valuable insight into the need for improvements today in order to avert potentially greater management complexities in the future.

The Army has recognized a potential problem in providing future follow-on support for foreign sales and has initiated a study to determine whether the United States has the capability to supply spare and repair parts to satisfy both future U.S. and foreign requirements. The basis for the Army's concern is that, in the next 5 to 6 years, the delivery schedule will steadily increase.

We have discussed the contents of the Army study with responsible officials and have been told that the study's initial findings are that the foreign military sales agreements we sign commit us to a support role for many years into the future. In addition, while we are contractually committed to future support there is no fully satisfactory means currently available for forecasting future foreign support requirements. The information developed by the Army on future support is similar to the observations we present later in this chapter.

POLICY AND IMPACT EXAMPLES

DOD's policy is to satisfy foreign military sales in a manner which will not adversely affect the U.S. defense posture. However, emergency sales of defense articles have continued to be satisfied through diversions and withdrawals. While the volume of these types of sales has now dropped to about 1 percent of total weapon and ammunition sales, a world or localized crisis could quickly reverse this trend. Therefore, a brief examination of how these types of sales have resulted in both favorable and unfavorable impacts will illustrate their risks and provide a background for a better understanding of commitments for follow-on support.

M-113A1 armored personnel carrier

The armored personnel carrier is a very popular item under both military assistance programs and foreign military sales programs. At present, about 34,000 of these vehicles have been produced and about 23,000, or 68 percent, have been distributed to foreign countries.

The foreign military sales program has had many beneficial effects on the armored personnel carrier. For example, during a recent period when the Army was not procuring any of these vehicles, foreign sales

- allowed the contractor to remain in operation;
- postponed costs of closing down the production line;
- provided employment during the U.S economic downturn;
- established a peacetime production base, which could generate vehicles immediately if the United States became involved in a crisis; and
- retained key suppliers of unique components in the defense business.

On the other hand, total commitment of peacetime production for foreign sales has postponed the Army's replacement of [deleted] armored personnel carriers withdrawn earlier from Army inventories to support [deleted] [deleted] during the October 1973 war. After the war the Army was to get paid back [deleted] vehicles from new production. It was to get the first [deleted] vehicles; [deleted] the next [deleted] the Army, the next [deleted] and [deleted] [deleted] the final [deleted] However, because [deleted] wanted more vehicles even sooner than production rates could provide, its delivery schedule was advanced. Consequently, the Army was paid back only the first [deleted] vehicles. The next [deleted] vehicles were diverted to [deleted] After that, the Army was to have received its [deleted] vehicles, to complete its payback quantity. However, Morocco urgently needed [deleted] so [deleted] of the Army's next [deleted] were also diverted, and these were not scheduled for payback until 1977, 4 years after the war.



The impact of these actions, particularly as they relate to Europe, has been highlighted in a previous GAO report 1/ on prepositioned equipment, where we stated:

"The major problem facing the prepositioned equipment program is the important shortage of combat-essential major end items. Some of these shortages will likely exist for some time due to production base limitations in producing sufficient assets to satisfy all outstanding requirements."

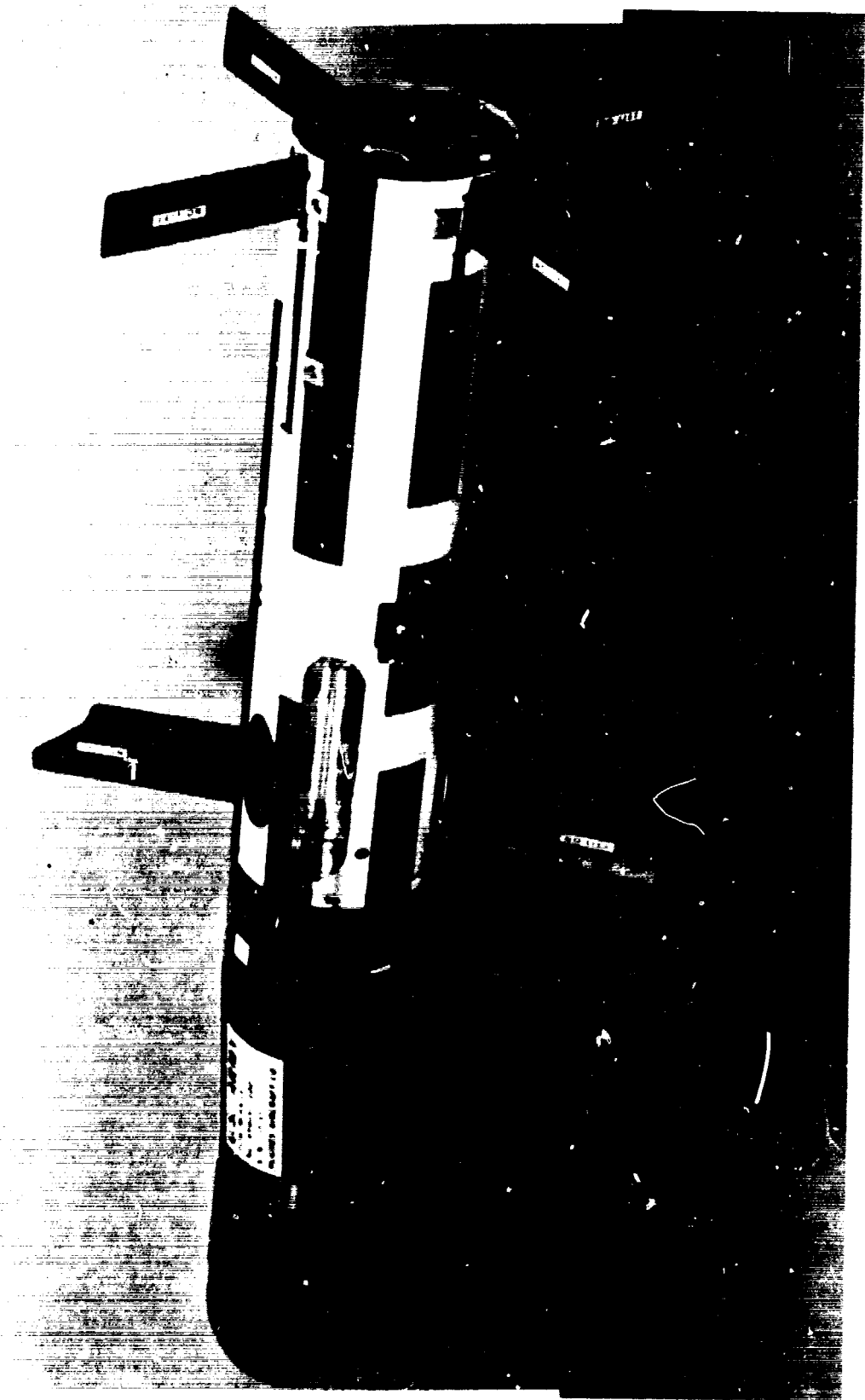
TOW missile

By creating a larger procurement quantity in fiscal year 1976, foreign military sales of the TOW missile have been beneficial in lowering the cost of the missiles' launchers by as much as 15 percent. However, diversions of production of the TOW missile for foreign sales have perpetuated the shortage of spare and repair parts and have delayed scheduled U.S. deployments.

The impact of withdrawing and diverting secondary items on the U.S. defense posture is clearly stated in a March 8, 1976, Army document on the TOW missile, prepared shortly after a drawdown of stocks to support a foreign military sales case for deleted. The document states that:

"Secondary item operational readiness support posture on a worldwide basis will be jeopardized on many critical long leadtime items, because assets must be drawdown from other programs, i.e., War Reserves, SSA, and initial issues. This type of high priority (take out of your hide) requirements have a drastic degrading effect on materiel readiness posture, and further increases zero balance, out of stock, and potential zero balance stock position."

1/"Continuing Problems with U.S. Military Equipment Prepositioned in Europe," LCD-76-456, July 27, 1976.



TOW MISSILE

The Army document also states that the expedited sale of the TOW missile for [deleted] increased existing shortages in repair parts that were required for imminent U.S. deployment to the 13 Army activities listed below:

Ft. Hood, Texas	Ft. Ord, California
Ft. Carson, Colorado	Ft. Stewart, Georgia
Ft. Riley, Kansas	Ft. Polk, Louisiana
Ft. Bliss, Texas	Ft. Knox, Kentucky
Ft. Campbell, Kentucky	Panama
Ft. Lewis, Washington	Alaska (172d Infantry Brigade)
Ft. Benning, Georgia	

[deleted]

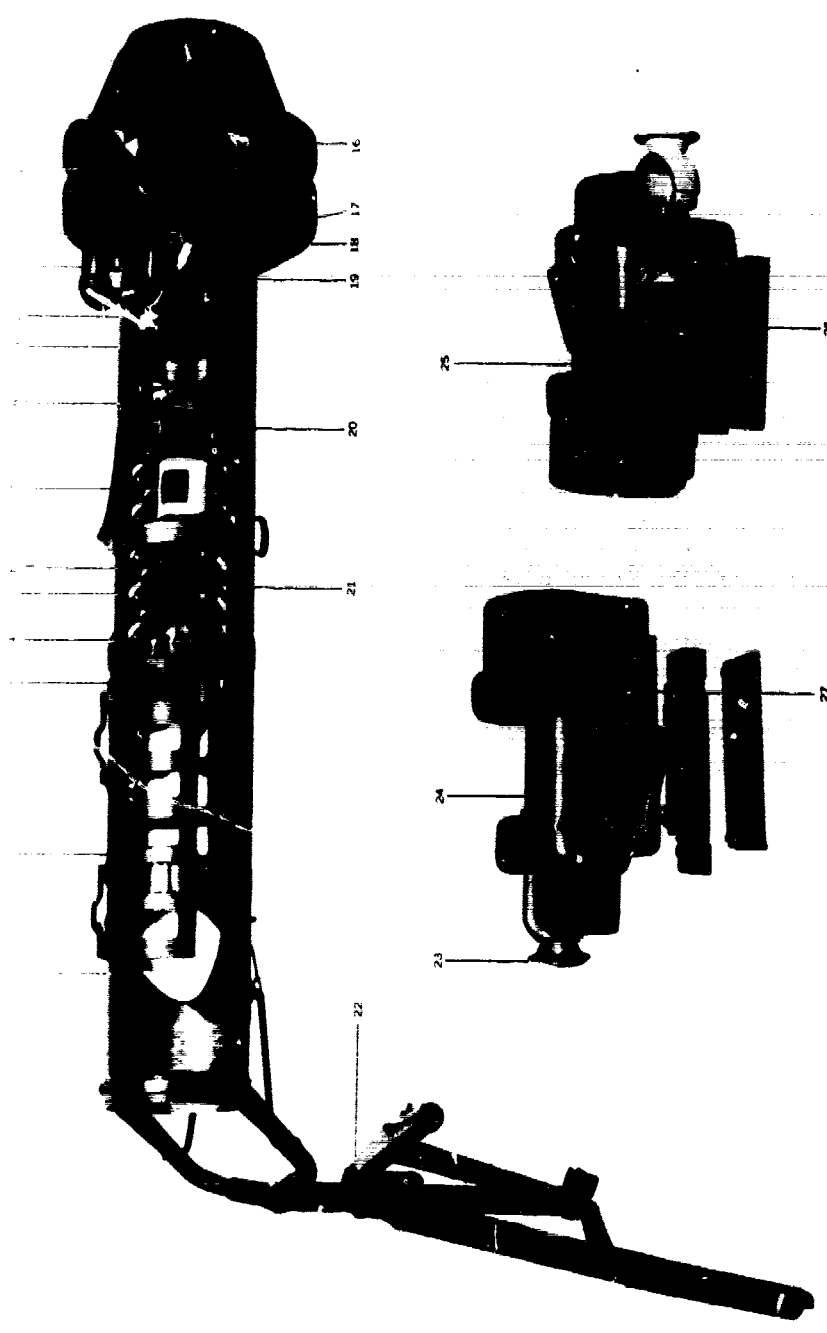
Although there are many factors which affect operational readiness, such as funding and production constraints, previously mentioned foreign military sales also have been a factor in keeping equipment in an inoperable condition due to spare parts shortages. Some of these items are common to both the TOW and the Dragon missile systems, for example, the power supply modulators, cable assembly, and power supply.

Dragon missile

The Dragon missile is the Army's newest antiarmor system and is in the early stages of deployment. At present the Army has [deleted] [deleted] yet sales of the Dragon missile continue. For example, a foreign military sales case in early 1976 called for advance delivery of [deleted] [deleted] which had to be met by diverting programmed U.S. production. The Army impact statement sent to the Secretary of Defense stated that [deleted]

[deleted]

[deleted] which is the minimum level a unit must have on hand to carry out its mission responsibilities.



DRAGON
 XIM47 SURFACE ATTACK
 GUIDED MISSILE SYSTEM

- | | | | |
|---------------------------------------|--------------------------|-------------------------|-------------------------|
| 1. WARHEAD SECTION | 19. FOLDING FINS | 25. TRACKER BATTERY | 19. INITIATOR SQUARE |
| 2. TRACKER SUPPORT | 20. TRACKER BATTERY | 26. MISSILE | 20. MISSILE |
| 3. TRACKER CONNECTOR | 21. LAUNCHER TUBE | 27. LAUNCHER TUBE | 21. LAUNCHER TUBE |
| 4. SAFETY AND ARMING DEVICE | 22. SUPPORT STRAND | 28. SUPPORT STRAND | 22. SUPPORT STRAND |
| 5. ROCKET MOTOR | 23. PROPELLANT STICKS | 29. MONOCULAR EYEPIECE | 23. MONOCULAR EYEPIECE |
| 6. ROCKET MOTOR FIRING CIRCUIT BOARDS | 24. LAUNCHER AFT END CAP | 30. TRIGGER ASSEMBLY | 24. TRIGGER ASSEMBLY |
| 7. BATTERY | 31. BREICH | 31. ERROR SENSOR | 25. ERROR SENSOR |
| 8. GYRO | 32. WIRE SPOOL | 32. TELESCOPIC SIGHT | 26. TELESCOPIC SIGHT |
| 9. CONTROL SYSTEM ELECTRONICS | 33. FLAME ASSEMBLY | 33. ELECTRONIC ASSEMBLY | 27. ELECTRONIC ASSEMBLY |

deleted

Although the Army voiced its concern, DOD approved the diversion.

In addition, this expedited sales case had an adverse impact on critical long leadtime secondary items common to both the TOW and the Dragon weapon systems. The effect on the Dragon system are categorized as follows:

deleted

It appears that the impacts on the defense posture of those U.S. units which have not attained their initial issue quantities severely counter suggested benefits of foreign sales for the Dragon missile.

Maverick missile

The Maverick missile, however, has not been adversely affected by foreign military sales. Moreover, the increased foreign sales demand has kept existing production lines open and maintained employment during the recent economic downturn, and the costs for inventory modernization have been reduced through recoupment of \$5.6 million in research and development costs.

Additionally, the Air Force efforts to introduce the Maverick missile, model C, into its inventory are another example of the positive side of foreign military sales. Currently the Air Force is selling the Maverick missile, model A, to foreign customers from inventory and is replacing it with new production of the improved model B. If the Air Force is successful in maintaining the sales levels for another 22 months, the model C will be ready for production and the Air Force expects to avoid about \$97.6 million in closedown and startup costs.



MAVERICK MISSILE

SUMMARY

The examples briefly discussed previously portray situations when foreign military sales have had mixed benefits. But, on balance, when these benefits are coupled with impacts on the U.S. defense posture, both become difficult to quantify. The impacts of foreign sales, which include diversions from fully committed production capacity, delays in replenishment of withdraw war reserve stocks, increased shortages of critical support items, and delays in deployment and increasing rates of not operationally ready for repair, make it clear that more definitive information must be developed before making a sale. These immediate impacts, when coupled with the long-term agreements for follow-on support, clearly indicate that, when we assess the benefits of a foreign sale, we must consider the potential long-range impacts on the U.S. defense posture.

FOLLOW-ON SUPPORT

When the United States sells defense articles to a foreign customer, it also agrees to provide follow-on support after the initial spare and repair parts have been consumed; when it plans to retire the articles from its inventory, it also notifies the customer within 2 years of the anticipated retirement and allows the customer to make a life-time buy. In the interim the United States encourages the customer to enter into a cooperative logistics support agreement so that the needed follow-on support can be provided in an orderly fashion--the FMSO I and II arrangements, discussed in chapter 2.

Because, at the beginning of fiscal year 1976, undelivered orders totaled about \$24 billion and were for increasingly sophisticated equipment, our experience with follow-on support is still very much in an evolving stage. Nonetheless, it is in this evolving state that symptoms of future problems can often be identified before they become critical. That is the major thrust of this section; namely, timely identification of potential support problems is essential so they can be avoided in future sales.

Forecasting

By entering into a cooperative logistics support agreement, the foreign customer is assured of a reliable supply of spare and repair parts. Moreover, DOD can reasonably forecast foreign requirements along with U.S. requirements and thereby make orderly arrangements for deliveries.

In fiscal year 1975 DOD provided 26 cents' worth of support, including initial spare parts, for every dollar of end-items sold. However, only 55 percent of the support was provided under cooperative logistics support agreements. The remaining 45 percent represent spare and repair parts support for which DOD has not forecasted.

The history of life-cycle costing for most U.S. defense articles shows that operation and maintenance costs far exceed the original acquisition costs. As foreign sales of end-items grow, they create a long-term requirement for support. Based on current difficulties in simultaneously fulfilling support needs of both the United States and foreign customers, it is probable that DOD will face even greater complexities in providing future support unless it can reasonably forecast for more than just 55 percent of foreign customer demands.

Production limitations

Limited production availability, like insufficient inventories, also has created problems in satisfying both foreign military sales customers' and U.S. Forces' competing demands for similar items.

For example, the infrared potted tube is a key item used to produce both the M-19 and the M-24 night vision periscopes. The M-19 periscope is used in the armored personnel carrier and in 11 other major Army end-items and is also used by the Navy and the Air Force. The M-24 periscope is used in the M-60A1 tank and the M-88 recovery vehicle. Additionally, both periscopes are produced for replacement inventories for foreign sales customers and U.S. active and reserve components.

Production of the infrared potted tube is inadequate to meet all current requirements. Because the M-60A1 tank has the highest peacetime production priority, most of the available production is used for the M-24 periscope. Also much of the existing inventory has been reduced in support of tank production. Concurrently, foreign military sales demand for the armored personnel carrier and the M-19 periscope have increased. To avoid penalty charges resulting from production disruption, the Army has had to withdraw deleted M-19s. Of these, deleted were actually removed from vehicles, rendering them ineffective for their night combat missions.

Another example is the transfer gear assembly for the armored personnel carrier. This secondary item has been in short supply because there is insufficient available production for the gears to satisfy both new armored personnel carrier production and secondary support inventories. Moreover, the demand for armored personnel carriers has resulted in diverting production destined for support inventories and has aggravated existing shortages.

Currently, 68 percent of the armored personnel carriers being supported are in foreign inventories. As of March 1976, 95 percent of the 1,638 backorders for the assembly were from foreign countries. In this case the adverse impact is on the ability of the United States to provide secondary follow-on support to foreign customers. As mentioned earlier, this ability to provide secondary support for the weapon systems is one of the U.S. advantages and conversely the inability to provide it reduces the long-term attractiveness of U.S. defense articles.

CONCLUSIONS

DOD's policy is to provide foreign military sales in a manner which will not adversely affect the U.S. defense posture. However, discounting the Viet Nam and Israel conflicts, DOD has satisfied foreign sales of end-items at the expense of the U.S. Forces.

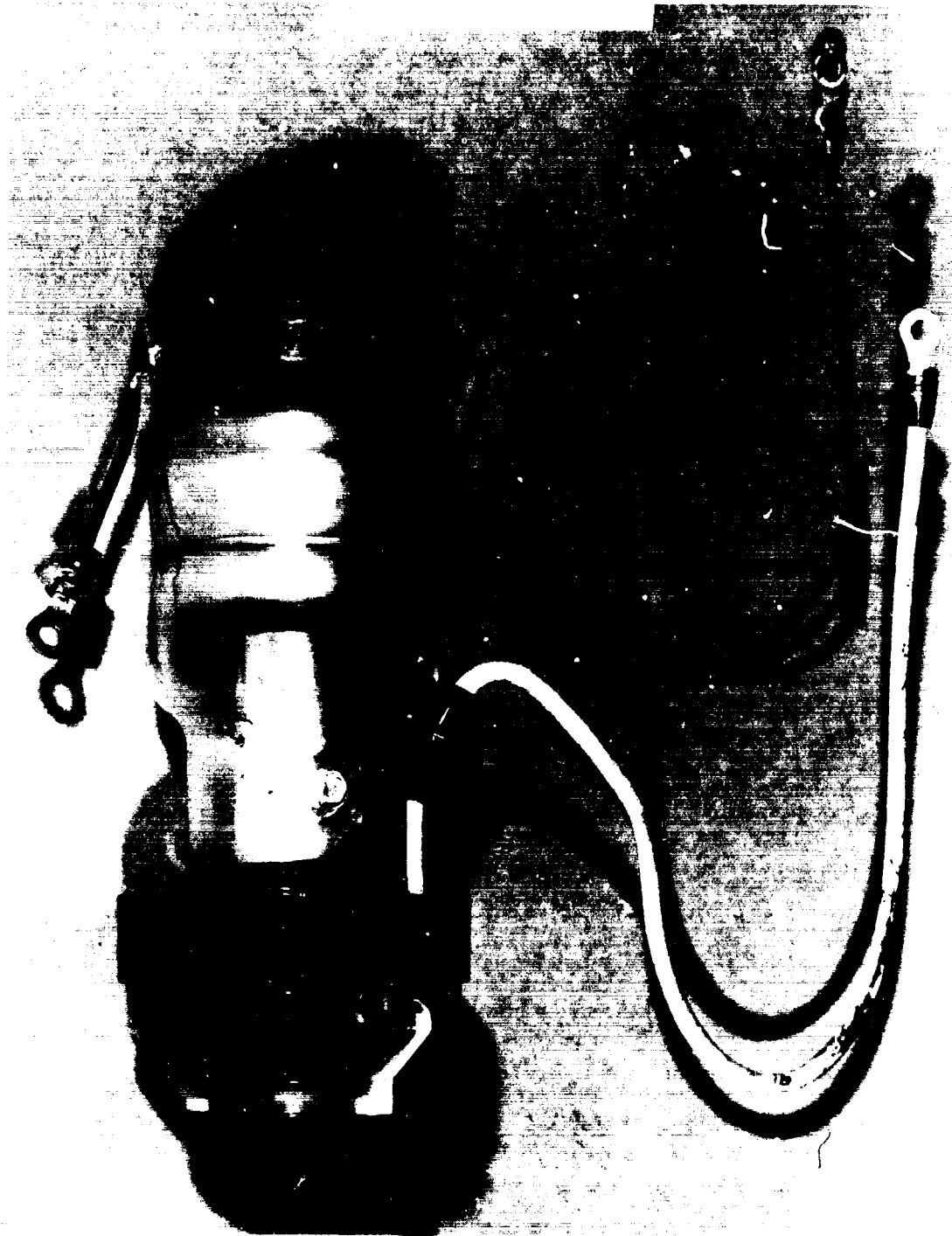
Problems associated with providing foreign sales cut across the entire logistics spectrum. But they are most dramatically highlighted by the fact that diversion and withdrawal of end-items and spare and repair parts have been made to the point where minimum essential quantities have been denied to the U.S. Forces. Moreover, as foreign sales of end-items continue to grow, so does the U.S. requirement to provide the follow-on support. Each end-item sale creates an implied obligation to provide support for the life of the end-item. With about \$24 billion in undelivered orders at the beginning of fiscal year 1976, the futurity of the follow-on support impact has been masked by the emphasis to satisfy today's sales.

Diversion and withdrawals of stocks to support foreign sales have aggravated our ability to provide an orderly flow of secondary items to satisfy competing demands from both U.S. and foreign customers. Moreover, as mentioned previously, over 45 percent of the U.S. support is unprogrammed, that is, support not covered by a logistic support agreement. This has strained secondary item management



CAUTION
DO NOT EXPOSE
THIS INSTRUMENT TO
DIRECT SUNLIGHT

M-19 NIGHT VISION PERISCOPE



INFRARED POTTED TUBE--KEY COMPONENT FOR PERISCOPES

systems as well as the foreign sales covered by cooperative logistics support agreements. Consequently, shortages of combat-essential equipment have been created and in some cases perpetuated. Further, available production capacity has been diverted from its prime mission of satisfying U.S. defense needs.

Many key long leadtime secondary items are used throughout several families of major end-items, for example, the M-60A1 tank and the armored personnel carrier. Frequently subcomponents for the secondary items are limited by existing production capacity. Therefore, when foreign sales demands require the reallocation of end-items between U.S. and foreign customers, the existing production base often cannot make the necessary adjustment in a timely fashion and further withdrawals of stocks are required. This complicates the already difficult task of managing the U.S. defense in a peacetime environment.

In contrast, the coordinated sales of the Maverick missile demonstrate that, with careful planning and the customer's cooperation, foreign sales can provide a positive impact. The phased sales of existing model A stocks which have coincided with the replenishment of technically superior model B stocks have provided a warm production base and needed employment during the recent economic contraction. Additionally, if the phased sales continue as planned, the Air Force expects to avoid \$97.6 million in closedown and start-up costs and has already recouped about \$5.6 million in research and development costs.

RECOMMENDATIONS

If we are to continue as a major supplier of defense articles, then the mechanisms for providing these articles and their support must be configured to prevent the degradation of the U.S. defense posture. We therefore recommend that, while the state of foreign sales is still evolving, the Secretary of Defense:

- Require that a supply support agreement or other mechanisms be a part of any sale when it is feasible to do so, so that DOD can program and fund future support with out adversely affecting the U.S. defense capabilities.
- Develop a forecasting mechanism which will identify the probable quantities of future critical support

items for U.S and foreign sales customers, including long leadtime secondary items used in more than one weapon system. Such a mechanism will require a system that will couple existing foreign military sales data on sales and deliveries by country, weapon system, quantities, and delivery dates with current assets.

AGENCY COMMENTS AND OUR EVALUATION

DOD concurred in our recommendations that a support agreement be part of any sale, so it can forecast and fund future support without affecting U.S defense capabilities. It said that such agreements would be part of any sale when it was feasible to do so. DOD did not, however, cite any planned or issued instructions that would emphasize to negotiating personnel that every effort should be made to include support agreements as part of all foreign military sales for major weapon systems.

With respect to our proposal to develop a forecasting mechanism, DOD commented that this was already being done to the extent that the requirements of foreign governments were known by the State Department and/or DOD. According to DOD, when future requirements are known, they are incorporated in a Master Planning Book maintained by DSAA with inputs provided by the services. The book contains 60 major systems and includes up-to-date information on inventories, production, training, and foreign demands (current and forecast). Information on weapons other than the 60 major systems is maintained internally within the services. DOD said that in those cases where future or forecast sales were firm and authorized by the U.S. Government, it was planning its production and inventories to meet such demands. DOD also commented that accurate usage and consumption data might not be obtained from some foreign military sales customers due to their own security requirements.

Such a system is a step in the right direction in developing a data base for use in forecasting future support requirements. It does not, however, identify the specific future support requirements for U.S. and foreign customers that can be expected as the result of past, present, and forecasted sales of major weapon systems. If this system included data on future support requirements on the basis of such factors as known usage and fatigue rates, it would go a long way in becoming a better forecasting document. We

recognize that precise data may not always be available or easily obtainable. This does not preclude using the best available data, whether based on information furnished by customers or on our own estimates of a customer's usage and consumption.

DOD stated that it was in the process of writing a directive that would require the military services to gather and maintain the data addressed in our second recommendation. However, our review of the proposed directive disclosed that it did not specifically address the accumulation of such data at all.

OPPORTUNITIES IDENTIFIED BY GAO FOR
IMPROVING THE MANAGEMENT OF
THE FOREIGN MILITARY SALES PROGRAM

"Foreign Military Sales--A Growing Concern"
(Report to the Congress; June 1, 1976;
ID-76-51)

The increased congressional and public attention focused on the dramatic growth in the volume of the U.S. foreign sales program led us to place into perspective a number of arms-transfer issues related to areas of concern in the program.

The report did not make any recommendations and is an overview of the major issues surrounding the program's operation and growth and discusses issues which include:

- Closely controlled foreign military sales, which are an important foreign policy tool.
- Economic impact of transfer to foreign manufacturers of U.S. technology.
- Extent U.S. military capabilities and readiness suffer from increased sales.
- Implication of providing logistical support for defense articles sold to foreign countries.

"Equipment Shortages--A Result of Emergency Support of U.S. Allies"
(Report to the Congress; Nov. 19, 1975;
(LCD-75-426)

The readiness position of the United States has been adversely affected by the accelerated emergency support to South Vietnam and Israel over the past several years because:

- Equipment was taken from Active Forces.
- Equipment stocks in U.S. depots and prepositioned in Europe were reduced below desired levels.
- Equipment in the possession of, or earmarked for delivery to, Reserve components was diverted or withdrawn and transferred to these countries.

We recommended that the Secretary of Defense improve DOD's logistics management structure to manage emergency logistics support to allies and improve contingency planning for emergency logistics support to allies. Plans should include at least

- an inventory of major weapons systems in the country's armed services,
- the quantity and serviceable number of equipment items in inventory,
- the level of inventory stocks normally maintained to support the equipment,
- loss rates projected to occur under various combat conditions, and
- the maintenance capability and expertise within the ally's military services.

We also recommended that the Secretary

- establish criteria to limit the extent of degradation that will be accepted by U.S. Forces in support of contingency plans for allies, particularly for items in an existing critical stock position at the time of the emergency and
- Apprise appropriate congressional committees of DOD's contingency plans, including the effect such potential support could have on U.S. Forces (both Active and Reserve components).

"Military Assistance and Sales to the Persian Gulf States" (Report to the House Subcommittee on the Near East and South Asia; Dec. 31, 1974; ID-75-37)

Sales agreements under the foreign military sales program to the Persian Gulf States from fiscal years 1967 through 1974 totaled \$8.5 billion. This classified report addresses U.S. military programs and third-country military assistance in the Persian Gulf.

"Issues Related to U.S. Military Sales and Assistance to Iran" (Report to the Congress (unclassified digest of a classified report); Oct. 21, 1974; P-75-ID-15)

Iran agreed to purchase more arms from the United States in 1974 than did the rest of the entire world combined in any other preceding year.

Despite the law requiring recovery of all costs to the maximum extent possible, the United States is conducting these sales at considerable cost.

Even though we found no firm contradictions with the requirement of the Foreign Military Sales Act, it questions the impact of such sales on the arms race, the extent and character of the military requirements, and the legitimate self-defense needs of the purchasing country. The Congress does not receive timely information on the volume and makeup of cash sales or on the nature of the military capability they provide.

We suggested that the Congress may want to require the executive branch to periodically furnish information on the volume and nature of major cash sales that could materially increase the military capability of the purchasing nation.

"Status of Emergency Security Assistance to Israel" (Report to Representatives Runnels, Leggett, and Dickinson; B-180356; May 20, 1974)

As a result of the 1973 Arab-Israeli War, the Emergency Security Assistance Act of 1973 was passed to provide Israel with \$2.2 billion in assistance to maintain a balance of power in the Middle East.

In a classified report, we presented the status of the funding and equipment deliveries under this act and of other U.S. assistance provided to Israel.

UNITED STATES DEPARTMENT OF DEFENSE OFFER AND ACCEPTANCE				(1) PURCHASER (Name and Address) (Include ZIP Code) Government of XXXXXX		
(2) PURCHASER'S REFERENCE		(3) CASE DESIGNATOR				
		FMS DA XXXXX				
OFFER						
The Government of the United States hereby offers to sell to the above purchaser the defense article(s) and defense service(s) listed below, subject to the terms contained herein and conditions cited on the reverse.						
(4) THIS OFFER EXPIRES Oct. 1977.				(5) SIGNATURE, TYPED NAME AND TITLE OF US REPRESENTATIVE		
				(7) US DEPARTMENT OF		
				(6) DATE		
(8) ITEM OR REF. NO.	(9) ITEM DESCRIPTION (Including stock number, if applicable)	(10) QUANTITY	(11) UNIT OF ISSUE	ESTIMATED		(14) AVAILABILITY AND REMARKS
				(12) UNIT COST	(13) TOTAL COST	
DRAGON SYSTEM						
1	6920-00-175-6327 Trainer launch effects, Guided Missile XMSA (B1K/L/K)	5	Ea	7,000.00	35,000.00	See note 1
2	6920-00-017-4482 Transmitting set, infrared (B1k/L/K)	2	Ea	9,000.00	18,000.00	See note 1
3	Concurrent spare parts organization, maintenance, plus one year RO (B9A/9/L/K)		Do		165,000.00	See note 2
(15) ESTIMATED COST					\$218,000.00	
(16) ESTIMATED PACKING, CRATING, AND HANDLING COSTS					10,000.00	
(17) ESTIMATED ADMINISTRATIVE CHARGE					10,000.00	
(18) ESTIMATED CHARGES FOR SUPPLY SUPPORT ARRANGEMENTS						
(19) OTHER ESTIMATED COSTS (Specify)						
(20) ESTIMATED TOTAL COSTS					\$238,000.00	
(21) TERMS						
Dependable undertaking. Deposit \$70,000.00 with acceptance.						
ACCEPTANCE						
(22) I am a duly authorized representative of the Government of _____ _____ and upon behalf of _____				(24) OFFER/RELEASE CODE _____		
said Government, accept this offer under the terms and conditions contained here-				(25) FREIGHT FORWARDER CODE: _____		
in, this (23) _____ day of _____ 19 _____.				(26) MARK FOR CODE _____		
				(27) POINT OF DELIVERY: _____		
(28) TYPED NAME AND TITLE				(29) SIGNATURE		

CONDITIONS

Pursuant to the US Foreign Military Sales Act, as amended, the Government of the United States (hereinafter referred to as "USG") hereby offers to sell to the Purchaser the defense articles and defense services listed hereinafter or referred to collectively as "Items" and individually as "Defense articles" or "Defense services" subject to the conditions set forth below:

A. THE GOVERNMENT OF THE UNITED STATES:

1. Agree to furnish such items from its Department of Defense (hereinafter referred to as "DOD") stocks and resources, or to procure them under the most advantageous terms and conditions available consistent with DOD regulations and procedures. When procuring for the Purchaser, the DOD shall, to the extent possible employ the same contract clauses, the same contract administration, and the same inspection procedures as would be used in procuring for itself, except as otherwise requested by the Purchaser and as agreed to by the DOD.

2. Admits that when the DOD procures for itself, its contracts include warranty clauses only on an exceptional basis. However, the USG shall, with respect to items being procured, and upon timely notice, attempt to obtain any particular or special contract provisions and warranties desired by the Purchaser (including those arising under any amendments) the USG may have under any contract connected with the procurement of any items. Any additional cost resulting from obtaining special contract provisions or warranties, or the exercise of rights under any contract connected with the procurement of Items, shall be charged to the Purchaser.

3. Shall, unless the condition is otherwise specified herein (e.g., "As Is"), repair or replace free of charge defense articles which are damaged or found to be defective in respect of material or workmanship and which are supplied from DOD stocks, when it is established that these defense articles were procured from the source specified in the purchase order. With respect to items procured from sources other than DOD stocks, the USG shall, upon request, attempt to obtain and issue a warranty on behalf of the Purchaser pursuant to AS above to assure, to the extent possible, that the warranty, replacement or correction of such items found to be defective. In addition, the USG shall make no warranties other than those specifically set forth herein. In particular the USG disclaims any liability resulting from patent infringement committed by the use or manufacture by or for Purchaser outside the United States of items supplied hereunder.

4. Agree to deliver and pass title to the items to the Purchaser at the initial point of shipment unless otherwise specified herein. With respect to the defense articles procured for sale to the Purchaser, this will normally be at the manufacturer's loading facilities, with respect to defense articles furnished from DOD stocks, this will normally be at the US depot. Items will be packed, crated or otherwise prepared for shipment prior to the time this offer is "Point of Delivery" designated on the invoice. It is specified otherwise than the initial point of shipment, the supplying Military Service will arrange movement of the items to the authorized delivery point at reimbursable service. Custody must not be construed to mean retention of title.

5. Admits that unless otherwise specified, USG standard items will be furnished without regard to make or model.

6. The price of items to be procured shall be at their total cost to the USG. Unless otherwise specified, the cost estimates of items to be procured based on current available data. The USG will use its best efforts to advise the Purchaser or its authorized representative.

(1) of any identifiable cost increase that might result in an increase in the "Estimated Total Costs" in excess of 10 percent but its failure to do so shall not affect the Purchaser's obligation under paragraph B above.

(2) of any delays which might significantly affect the estimated delivery dates.

7. The USG will, however, use its best efforts to deliver items or render services for the amount and at the times quoted.

8. Under unusual and compelling circumstances when the best interests of the United States require it, the USG may reserve the right to cancel all or part of its order at any time prior to the delivery of defense articles in performance of services. The USG shall be responsible for all termination costs or expenses resulting from cancellations under this paragraph.

9. Shall refund to the Purchaser any payments received hereunder which prove to be in excess of the final total cost of delivery and performance of the order.

B. THE PURCHASER:

1. In payment for the items shall forward with its acceptance of this offer a check payable in United States dollars to the Treasurer of the United States in the amount shown on the estimated total cost, unless different arrangements are specified under "Terms".

2. Agree, if "Terms" specify payment by "dependable undertaking" to pay the USG such amount at such times as may be specified by the USG in order to cover shipments from stock or services rendered or to meet any claims incurred by contracts under which items are being procured, and any claims and costs that may accrue from cancellation of contracts resulting from Purchaser's action under paragraph B4 hereof. Requests for funds may be issued upon requirements for advance and progress payments to suppliers or delivery of items and bills of lading and invoices. Requests for funds or bills of lading, as the case may be, are due in full on presentation. Documentation not already on deposit, are due in full on presentation. Documentation not already on deposit, are due in full on presentation. Documentation not already on deposit, are due in full on presentation. Documentation not already on deposit, are due in full on presentation. Documentation not already on deposit, are due in full on presentation.

3. Agree, if "Terms" specify payment on evidence of constructive delivery, to make payment in full amount of any request for funds or billing within the month following the month of the request, or as otherwise required in accordance with the "Terms" herein.

4. Agree, if "Terms" specify payment under a Credit Agreement between the Purchaser and DOD, to pay to the USG on a "dependable undertaking" basis, in accordance with B 1b above, such costs as may be in excess of the amounts funded by the Credit Agreement.

5. Shall furnish shipping instructions for the items with its acceptance of this offer. Such instructions shall include (a) Office/Release Code, (b) Freight Forwarder Code and (c) the Mark for Code, as applicable.

6. Shall be responsible for obtaining the appropriate insurance coverage, and, except for items exported by the USG, appropriate export licenses.

4. Shall accept title to the defense articles at the initial point of shipment (see A 4 above) unless otherwise specified herein. Purchaser shall be responsible to defense articles transported by Parcel Post shall pass to the Purchaser on date of parcel post shipment. Standard Form 348 shall be used in submitting claims item deficiency, improper identification or improper documentation and shall be submitted by Purchaser promptly. Claims of \$25.00 or less will not be reported for average shipments, or damage. Claims received after one year from date of passage of title or billing, whichever is later, will be disallowed by the USG.

5. Shall reimburse the USG if the final cost to the USG exceeds the amount estimated in this sales agreement.

6. May cancel the order with respect to any or all of the items listed in the sales agreement at any time prior to the delivery of defense articles or performance under this paragraph. It shall be responsible for all costs resulting from cancellations under this paragraph.

7. Shall, except as may otherwise be mutually agreed, use the items sold hereunder only:

a. For the purposes specified in the Mutual Defense Assistance Agreement, if any, between the USG and the Purchaser.

b. For the purposes specified in any bilateral or regional defense treaty to which the USG and the Purchaser are both parties, if subparagraph a of the paragraph is inapplicable, or

c. For internal security, self-defense, and/or civil action, if subparagraph a and b of the paragraph are inapplicable.

8. Shall not transfer title to, or possession of, the defense articles, components and/or accessories, or other material furnished under this sales agreement to any person, or organization (including reexportation agencies), or other government, class, division of, or permit of, any class, division of, or information furnished to the USG. To the extent that any items, plans, specifications, or information furnished by the USG in connection with this transaction may be classified by the USG for security purposes, the Purchaser shall maintain a similar classification and employ all necessary security to preserve such security equivalent to those employed by the USG. The USG will notify the Purchaser if the classification is changed. The Purchaser will not disclose, by all means, the information, or information furnished, whether patented or not.

C. INDEMNIFICATION AND ASSUMPTION OF RISKS

1. It is understood by the Purchaser that the USG in procuring and furnishing the items specified in this agreement does so on a non-profit basis for the benefit of the Purchaser. The Purchaser therefore undertakes, subject to AS above, to indemnify and hold the USG, its agents, officers, and employees harmless from any and all loss or liability (whether in tort or in contract) which might arise in connection with this agreement because of: (i) injury to or death of personnel of the USG; (ii) damage to or destruction of (A) property of the USG; (B) property of the Purchaser; (C) property of third parties; or (D) patent infringement.

2. Subject to any express special contractual warranties obtained for the purchase in accordance with AS above, the Purchaser agrees to release the USG from the risk of loss damage to or destruction of the USG's property (including the items procured hereunder) to the extent that the USG would assume for its property if it were procuring for itself the same items or items procured pursuant to this agreement.

D. ACCEPTANCE:

To accept this offer, the Purchaser will return the original and three copies properly signed, to the US Military Department making the offer not later than the expiration date of the offer set forth herein. When properly accepted and returned as specified herein, the provisions of the offer shall be binding upon the Government. Unless written extension is obtained from an authorized representative of such US Military Department, the offer shall terminate at the end of such expiration date.

E. ENCLOSURES

Enclosures attached hereto are, by this reference, incorporated herein and are made a part hereof as though set forth in full.

EXPLANATORY NOTES

1. The item or reference numbers appearing in the "ITEM OR REFERENCE" column may not correspond with reference used in your original request. However, the number, together with the case designation shown should always be used as a reference in future correspondence.

2. Availability lead time quoted in the "AVAILABILITY AND REMARKS" column is the number of months required to deliver items after receipt of acceptances of the offer pursuant to Section D above and the conclusion of appropriate financial arrangements. The planned source of supply for each item is expressed in the following codes:

- S (*) Service Stocks
P (*) Procurement
R (*) Repair/Modification
X (*) Stock and procurement, e.g. initial repair parts
*Availability is stated in months.

3. Condition of the defense articles shown in the "AVAILABILITY AND REMARKS" column is expressed in the following codes:

AJ Items to be provided in existing condition without repair, restoration or rehabilitation which may be required. Condition indicated in item description.

M Article of mixed condition (new, repaired and rebuilt) and may be assembled when used. Example: repair parts, ammunition, assemblies, kits, tool sets and shop sets.

N Serviceable defense articles.

O Obsolete or non-standard item in an "AS IS" condition for which repair parts support may not be available from DOD.

S Substitute. Suitable substitutions may be shipped for an unavailable defense article unless otherwise advised by the Purchaser.

U Reworked or rehabilitated defense articles possessing original specifications insofar as practicable, including all Modifications Work Center and Engineering Change Orders as applied to such defense articles when issued but defense articles should not be considered as having had total replacement of worn parts and/or assemblies. Only parts and components not meeting US Armed Forces serviceability standards and standards will have been replaced in all instances such defense articles will meet US Armed Forces standards of serviceability.

Note 1 -

Items cited on this case are programmed for availability as follows:

	March 1977	April 1977	May 1977
Line Item: 1	2	2	1
Line Item: 2	1	-	1

Note 2 -

Supply support of the Dragon System will be available for a period of 8 to 10 years. A reevaluation of support period will be made 2 years prior to termination date and you will be offered either an extension of the support period or a life-of-type buy with termination of normal supply occurring as originally specified.



OFFICE OF THE DIRECTOR DEFENSE SECURITY ASSISTANCE AGENCY
AND
DEPUTY ASSISTANT SECRETARY (SECURITY ASSISTANCE), DASD/ISA
WASHINGTON, D.C. 20301

17 FEB 1976

In reply refer to:
I-12585/75

Mr. Frank M. Slatinshek:
Chief Counsel, Armed Services Committee
House of Representatives
Washington, D.C. 20515

Dear Mr. Slatinshek:

Enclosed is additional information to Transmittal No. 76-27,
which concerns the Department of the Army's proposed Letter
of Offer to Saudi Arabia estimated to cost \$26.1 million.

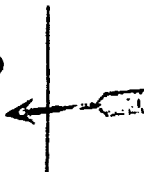
Sincerely,

H. M. FISH
Lieutenant General, USAF
Director, Defense Security Assistance Agency
and
Deputy Assistant Secretary (ISA), Security Assistance

Same Letter to:
Senate Committee on Appropriations

Distr:
Gen Fish
R&C
TC RF (2)
PR CHRON
PR Orig
Cong Rel

PREP: LTC Martin/c1/DSAA/TC/X79304



Additional information Related to Transmittal No. 76-27

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Classified by ~~USAA Comptroller~~
SUBJECT TO CENTRAL INTELLIGENCE AGENCY SCHEDULE OF
EXECUTIVE ORDER 11652. ADMINISTRATIVELY DOWNGRADED
AT TWO YEAR INTERVALS. DECLASSIFIED ON 31 Dec 82

GAO note: See pp. 29 to 31 for description of how the case was actually affected.



OFFICE OF THE DIRECTOR DEFENSE SECURITY ASSISTANCE AGENCY
AND
DEPUTY ASSISTANT SECRETARY (SECURITY ASSISTANCE), OASD/ISA
WASHINGTON, D.C. 20301

28 JUL 1976

In reply refer to:
I-3133/76

Mr. Frank M. Slatinshek
Chief Counsel, Armed Services Committee
House of Representatives
Washington, D. C. 20515

Dear Mr. Slatinshek:

Enclosed is additional information to Transmittal No. 7T-2, which concerns the Department of the Army's proposed Letter of Offer to Israel estimated to cost in excess of \$25 million.

Sincerely,

R. M. FISH
Lieutenant General, USAF
Director, Defense Security Assistance Agency
Deputy Assistant Secretary (ISA), Security Assistance

Attachment

Same Ltr to:
Senate Committee on Appropriations

DISTR: PREP: LTC Martin/cl/DSAA/TC/x79303
Gen Fish
ASD/ISA File
R&C
TC RF (2)
PR Chron
PR Orig
Cong Rel
State

(U) Additional Information Related to Transmittal No. 7T-2

(C)

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- (U) This proposed case involving major defense equipment in the amount of \$25 million or more is being handled as a foreign military sale in accordance with Section 38 of the Arms Export Control Act.
- (U) The acquisition of these missiles will improve Israel's defensive capability.
- (U) The purchaser will pay all costs for items provided plus an administrative charge for handling this case as a foreign military sale. This proposed sale would have a positive impact on the U.S. balance of payment.

Classified by 651A COMPTON/ALX
SUBJECT TO GENERAL DECLASSIFICATION SCHEDULE
EXECUTIVE ORDER 11652. AUTOMATICALLY DECLASSIFIED
AT TWO YEAR INTERVALS. DECLASSIFIED ON 2 Dec 82

GAO-SUGGESTED SUBJECT AREAS FOR INCLUSIONIN AN IMPACT STATEMENTSECTION IShort-term impact

1. Identify the authorized acquisition objective and the initial issue quantity status and the position after the proposed sale.
2. Identify assets that might be substituted--U.S., allies, or other.
3. What would be the source of assets and how much would come from each?
 - a. Ongoing production.
 - (1) leadtime away.
 - (2) Diversion of production.
 - b. Depot stocks.
 - c. Reserve component inventory.
 - d. Active forces' inventory.
 - e. Other (identify).
4. How long will it take to replace the articles sold?
5. What units will be affected and in what way?
6. What percent of the worldwide inventory of assets are in foreign hands?
7. Will the sale require U.S. citizens or Government employees?
 - a. How many?
 - b. For what duration?
 - c. Where will they come from?
8. If a sale is made, what is the projected difference between the sale price and the replacement cost?
9. Will replacement articles differ from those being sold? (explain)
10. Will the article sold represent or introduce a level of technology currently not available in the customer's inventory?

SECTION IILong-term impact

1. Has the customer entered into a cooperative logistic support agreement?
2. What is our production capability to support the sale in the out years?
3. Are key components of the article sold common to other articles? If so, what are they, and is there sufficient capacity available to satisfy both U.S. and foreign requirements?
4. Are there production limitations associated with either the article itself or key components? If so, how will they be overcome?

SECTION IIIAction

Based on the information contained to sections I and II, explain why the sale should or should not be made. (This section might be signed by the same person who signs the letter of offer.)



OFFICE OF THE DIRECTOR DEFENSE SECURITY ASSISTANCE AGENCY
AND
DEPUTY ASSISTANT SECRETARY (SECURITY ASSISTANCE), DASD/ISA
WASHINGTON, D.C. 20301

9 JUL 1976

In reply refer to:
I-22180/76

MEMORANDUM FOR MR. CANTER, GAO

SUBJECT: GAO Inquiry - Decisions to Provide DOD Equipment at Less than Normal FMS Leadtime.

The attached information is provided in response to your informal inquiry regarding Executive Branch decisions to provide equipment to foreign governments via FMS at less than normal FMS leadtimes during the period 1 July 1974 through 31 March 1976. As my staff indicated to you, the DOD does not keep cumulative records by type transaction and, therefore, our reply has been delayed pending completion of a survey of various country files.

It is DOD policy that equipment will be offered with normal FMS leadtimes for sale to foreign purchasers. Occasionally, for broader foreign policy reasons, the Executive Branch decides that it is in the best interests of the United States to provide such equipment at less than normal FMS leadtimes. Within DOD such a decision requires OSD approval, usually at the Deputy Secretary level, if such action would impact unfavorably on one or more of the military services. Normal FMS leadtime is defined as that period of time from the date of complete purchaser acceptance of a Letter of Offer, including satisfaction of financial terms, to availability of the item(s) to the foreign purchaser. It includes FMS administrative leadtime (to implement the accepted case to the appropriate contracting officer), contracting leadtime (to negotiate and let the contract) and production leadtime (following contract placement, the period to actually produce the item and accomplish those other actions necessary prior to availability to the customer).

The normal FMS availability for the items listed in the attachment was in excess of 24 months. These items were provided in less than normal FMS leadtime either from new production or from DOD inventory.

Signed

Attachment

H. M. FICH
Lieutenant General, USAF
Director, Defense Security Assistance Agency
Security Assistance

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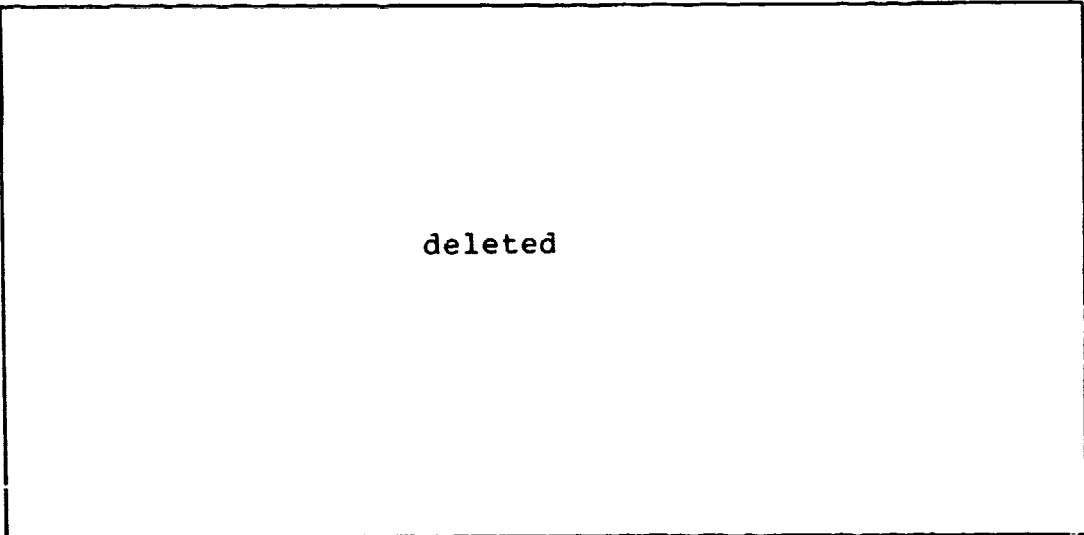
DEFENSE SECURITY ASSISTANCE AGENCY
AND
DEPUTY ASSISTANT SECRETARY (SECURITY ASSISTANCE), OASD/ISA
WASHINGTON, D.C. 20301

In reply
refer to: 1-20555/76

Mr. Fred J. Shafer
Director, Logistics & Communications
Division
U.S. General Accounting Office
Washington, D.C. 20548

Dear Mr. Shafer:

(U) This is in reply to your letter to the Secretary of Defense regarding GAO's draft report of January 1977, "Foreign Military Sales - A Potential Drain on U.S. Defense Posture" (OSD Case #4535), (LCD 76-455)



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(U) Attached for your consideration are the DOD's detailed comments and recommendations. We would welcome a meeting with you to discuss these comments after you have had an opportunity to review them.

(U) DOD is conducting the requested security classification review of the draft report and the results will be furnished separately.

Sincerely,

Classified by Director, DSAA
.....
SUBJECT TO GENERAL DECLASSIFICATION SCHEDULE OF
EXECUTIVE ORDER 11652. AUTOMATICALLY DOWNGRADED
AT TWO YEAR INTERVALS. DECLASSIFIED ON 31 Dec 1991.

H. M. FISH
Lieutenant General, USAF
Director, Defense Security Assistance Agency
and
Deputy Assistant Secretary (ISA), Security Assistance

Attachment
a/s

DOD COMMENTS

GAO DRAFT REPORT "FOREIGN MILITARY SALES - A POTENTIAL DRAIN ON U.S. DEFENSE POSTURE" (OSD CASE #4535), (LCD 76-455)

GENERAL

1. The main thrust of the report is that FMS has had an adverse impact on our defense capabilities. However, only a few examples are cited in the report to "support" this conclusion. Far better documentation is required for such a far-reaching conclusion as this.

(See GAO note, p. 57.)

2. The statement on page i that FMS dollar growth from \$952 million in 1970 to \$10 billion in 1974 has taxed DOD's ability to maintain U.S. defense posture is not supported by examples. In fact, it is our belief that the U.S. defense industrial base is not being fully utilized and our foreign military sales have been very beneficial.

(See GAO note, p. 57.)

3. On page 44, the report states that DOD has continued to satisfy foreign sales of end items at the expense of our own forces. The conclusion suggests a finite either/or relationship which is demonstrable neither in the report nor in fact. Only about one half of one percent of the total DOD dollar value of FY 76 sales impacted on our own forces. The conclusion also ignores the total force policy, under which a foreign sale may enhance allied defense capabilities and ease U.S. defense burdens in the process.

4. On page 44, the report states: ". . . diversion and withdrawal of end items and spare and repair parts have been made to the point where minimum essential quantities have been denied to our own forces." As presently written, the implication is that this is a serious problem when in reality it is not.

5. The draft report correctly notes that advanced FMS procurement based upon forecasting is specifically prohibited by the Arms Export Control Act. However, the report fails to note, that prohibition notwithstanding, that accurate usage and consumption data may not be obtained from some FMS customers due to their own security considerations.

Recommendations (Page 25) (See GAO note, p. 57.)

#1. Concur. This is already being done to the extent that the requirements of foreign governments are known by the State Department and/or DOD. When future requirements are known they are incorporated in a "Master Planning Book" maintained by DSAA with inputs provided by the Services. The book contains 60 major systems and includes up-to-date information on inventories, production, training and foreign demands (current and forecast). Information on weapons over and above the major systems noted above are maintained internally within the Services. In those cases where future or forecast sales are firm and authorized by the U.S. Government, DOD does plan its production and inventories to meet such demands.

#2. Concur. Per Deputy Secretary of Defense Memorandum of 14 December 1976, a DOD Directive is being staffed which requires the Military Services to maintain the data addressed in the recommendation.

#3. Concur. Per Deputy Secretary of Defense memorandum of 14 December 1976, the Military Departments were apprised of the procedures to be followed when submitting impact statements.

Recommendations (Page 46) (See GAO note below.)

#1. Concur.

#2. Concur. A support agreement, when it is feasible to do so, will be a part of any sale, to enable DOD to forecast and fund downstream support without affecting our defense capabilities.

#3. Concur.

Accuracy/Clarity/Completeness

(See GAO note, p. 60.)

GAO note: Page references in this appendix refer to the draft report and do not necessarily agree with page numbers in the final report.



DEPARTMENT OF STATE

Washington, D. C. 20520

March 15, 1977

Mr. J. K. Fasick
Director
International Division
U.S. General Accounting Office
Washington, D. C. 20548

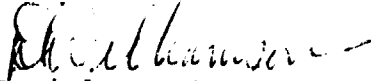
Dear Mr. Fasick:

I am replying to your letter of February 1, 1977, which forwarded copies of the draft report: "Foreign Military Sales - A Potential Drain on U.S. Defense Posture."

The enclosed comments were prepared by the Deputy Director for the Bureau of Politico-Military Affairs.

We appreciate having had the opportunity to review and comment on the draft report. If I may be of further assistance, I trust you will let me know.

Sincerely,


Daniel L. Williamson, Jr.
Deputy Assistant Secretary
for Budget and Finance

Enclosure: As stated

GAO DRAFT REPORT: FOREIGN MILITARY SALES - A POTENTIAL
DRAIN ON US DEFENSE POSTURE

Thank you for the opportunity of commenting on the subject report. Our suggested emendations follow:

Various Categories of Sales

The term "foreign military sales" is used throughout the study to refer both to the sum of arms transfers and to sales under the Foreign Military Sales Program. On the first page of Digest section, the term seems to refer to the FMS program, although the numbers are confusing and not borne out by the tables in the body of the text (see page 2). This confusion could be overcome by using the term "arms transfer" as a description of our overall arms export activities (including grant assistance and commercial sales as well as FMS cash and credit sales), and the term "Foreign Military Sales Program" to refer to arms sales on FMS cash or credit basis administered by the Department of Defense.

Management vs. Political Decisions

There is also a failure throughout the study to distinguish adequately between the impact on defense capabilities of management decisions made by DOD and political decisions made by the President. The decisions which have had major impact on capabilities in recent years (viz. Israeli resupply) have been manifestly political; the management process at DOD has often been devoted minimizing the effects of such political decisions on capabilities. In the nature of things, of course political decisions which impact on capabilities are difficult to anticipate in the management process. These comments apply particularly to the discussion in the first paragraph of page ii.

The Role of Private Manufacturers

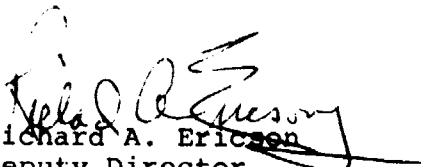
The paper implies (page 18, page ii) that the responsibility for production planning for defense articles rests entirely with DOD. While DOD obviously plays an important role in this area, arms manufacturers can and do make production and inventory decisions based on their own projections of foreign orders. The flow of information between Defense and the arms industry is thus crucial to ensuring smooth production runs.

Further comments on specific points in the text follow:

(See GAO note below.)

Proposals

The Department does not object to any of the proposals advanced by the report. It is our understanding, however, that Defense has already taken extensive steps to improve forecasting techniques, to assess cumulative impact of sales on capabilities, and to include supply support arrangements as part of FMS sales agreements.



Richard A. Ericson
Deputy Director
Bureau of Politico-Military
Affairs

GAO note: The comments which have been deleted have been considered in the report.

PRINCIPAL OFFICIALS RESPONSIBLE FOR
ADMINISTERING THE ACTIVITIES DISCUSSED IN THIS REPORT

	<u>Tenure of office</u>	
	<u>From</u>	<u>To</u>
<u>DEPARTMENT OF DEFENSE</u>		
SECRETARY OF DEFENSE:		
Dr. Harold Brown	Jan. 1977	Present
Donald H. Rumsfeld	Nov. 1975	Jan. 1977
James R. Schlesinger	July 1973	Nov. 1975
William P. Clements, Jr. (acting)	Apr. 1973	July 1973
DEPUTY SECRETARY OF DEFENSE:		
Charles W. Duncan, Jr.	Jan. 1977	Present
William P. Clements, Jr.	Jan. 1973	Jan. 1977
ASSISTANT SECRETARY OF DEFENSE (INSTALLATIONS AND LOGISTICS):		
Dale R. Babione (acting)	Jan. 1977	Present
Frank A. Shrontz	Feb. 1976	Jan. 1977
John J. Bennett (acting)	Mar. 1975	Feb. 1976
Arthur I. Mendolia	June 1973	Mar. 1975
DEFENSE SECURITY ASSISTANCE AGENCY:		
Lt. Gen. Howard M. Fish	Aug. 1974	Present
Rear Adm. Raymond E. Peet	June 1972	Aug. 1974
<u>DEPARTMENT OF STATE</u>		
SECRETARY OF STATE:		
Cyrus Vance	Jan. 1977	Present
Henry A. Kissinger	Sept. 1973	Jan. 1977
William P. Rodgers	Jan. 1969	Sept. 1973