

FOREIGN MILITARY SALES ACQUISITION POLICY AND PROCESS

INTRODUCTION

The foreign military sales (FMS) process fundamentally is an acquisition process. Under FMS, a foreign government or international organization identifies a need for a military-related item or service and chooses to acquire it from the U.S. government (USG). The government-to-government sales agreement governing the acquisition is the Letter of Offer and Acceptance (LOA). To fulfill the LOA requirements, the USG may supply items or services from on-hand Department of Defense (DOD) resources or the USG may purchase from industry for subsequent delivery to the FMS customer.

This chapter primarily examines acquisition as it relates to the USG's process for purchasing material or services by means of contracts with industry. The goal of the contracting discussion is to highlight where and how FMS procurements fit into the normal DOD procurement process. Additionally, this chapter will discuss the international business agreement referred to as an offset. The offset concept is defined, the USG policy regarding offsets is presented, and the means to address offsets within the FMS process are explained.

Within DOD, the term acquisition is also used to refer to the entire life cycle process DOD uses to develop, test, evaluate, produce, and sustain weapon systems to satisfy formally identified DOD military capability requirements. This formalized acquisition process is referred to as the Defense Acquisition System (DAS). Chapter 13 of this textbook, "Systems Acquisition and International Armaments Cooperation" of this text discusses how issues that may affect future foreign sales of major systems are addressed within the DAS during the system development process.

The DOD uses the term acquisition to encompass multiple functional career field areas. In fact, the Defense Acquisition University (DAU) offers a variety of courses for personnel within fifteen different career fields that support acquisition. These acquisition career fields include the following:

Life cycle logistics	Auditing
Contracting	Cost estimating
Facilities engineering	Industrial and contract property management
Information technology	Production, quality and manufacturing
Program management	Purchasing
Program systems engineer	Science and technology
Systems engineering	Test and evaluation
Financial Management	

All of these various functional acquisition disciplines are utilized in the DAS process. To review the courses offered by the DAU, visit their web site at: <http://icatalog.dau.mil/onlinecatalog/tabnav.aspx>.

GLOBAL MILITARY MARKETPLACE

When an international customer requires a military item or service, it must find a source to fulfill that need. Ideally, from its national perspective, there are many economic and political factors that make acquisition from an indigenous source the preferred choice. However, in today's high technology military environment, a substantial financial investment is required to conduct the research,

development, testing, and to establish production capability for a military system. In addition to the financial investment, considerable time is required to accomplish this process. Given these considerations, many nations fulfill certain military needs by procuring systems from other governments or from foreign commercial firms that have already developed and fielded a capable system rather than developing a new, country unique system.

United States Item Preference

From a security assistance (SA) perspective, the potential foreign customer must first determine whether to acquire a U.S. system rather than developing an indigenous system or purchasing some other country's system. If the foreign customer selects a U.S. system, it must next decide whether to purchase through the government-to-government FMS process or to make the purchase through the government-to-industry Direct Commercial Sales (DCS) process.

The DOD is generally neutral regarding whether a foreign customer chooses to purchase via FMS or DCS. Although officially neutral regarding the procurement method (FMS or DCS), DOD does have a specific preference that friendly nations chose to purchase U.S. systems. The reason for the U.S. preference relates to the political, military and economic benefits resulting from the U.S. and its friends using the same military equipment.

Foreign Military Sales Procurement Rationale

Chapter 15 of this textbook, "A Comparison of Foreign Military Sales and DCS Procurements," compares some of the advantages and disadvantages of FMS and DCS procurements. This chapter will not review all the relative pros and cons; however, the *Security Assistance Management Manual* (SAMM) states that a primary reason that international customers choose the FMS system is because the DOD makes purchases on the customer's behalf using the same USG regulations and procedures that DOD uses to make procurements for itself. As a result, the customer receives the same benefits and protections that are built into the DOD procurement process. This can be a considerable benefit when the customer may be spending hundreds of millions or perhaps billions of dollars to acquire a military system. This chapter examines how the DOD uses its existing acquisition policies and procedures to procure articles and services in fulfillment of LOA agreements.

Foreign Military Sales Content

Typically, FMS system sales consist of weapon systems that DOD has already developed, produced and fielded for its own use. DOD policy states that the USG will only agree to sell systems through FMS that have been approved for full rate production for U.S. forces. The full rate production decision is a key acquisition decision point from the FMS perspective. If a foreign customer requests an LOA for a system that has not yet been approved for full rate production, a policy waiver is required. In this situation, the Defense Security Cooperation Agency (DSCA) will request concurrence from the Under Secretary of Defense for Acquisition, Technology, and Logistics [USD(AT&L)] before offering an LOA for a system that is still under development.

The reason for this policy concerns future supportability and interoperability issues. Prior to the full rate production decision, there is the risk that the U.S. may decide not to produce the system. This would present an undesirable situation if the U.S. has committed under an LOA to deliver a system to an FMS customer but decided not to deliver this same system to U.S. forces. The FMS customer would be faced with nonstandard support to sustain the system and might lack interoperability with U.S. forces. If the waiver is approved, the LOA for the FMS must include a special note identifying

the risk that the USG may not place this system into production. This waiver policy is often referred to as the Yockey waiver named after a former Under Secretary of Defense.

Although some FMS customers may purchase specific items or services independent of a major DOD end item system, most SA programs are built around the sale of one or more major DOD weapon systems. Under the FMS approach, major weapon system sales are accomplished using the total package approach (TPA). TPA provides the FMS customer the weapon system plus all the necessary support elements to operate and sustain the system for an initial period. Subsequent FMS follow-on support cases continue to sustain the system throughout its operational life.

Because the FMS process is accomplished using existing DOD procurement regulations and policies, the material and services provided under FMS will generally be U.S. origin products. In the SAMM C4.4.1, it states that the DOD will not enter into LOAs that commit to procurement in foreign countries unless DSCA has approved an exception.

CONTRACTING FOR FOREIGN MILITARY SALES

It is important to recognize that the *Arms Export Control Act* (AECA) permits FMS both from DOD stocks and by means of DOD contracting to acquire material or services directly for the FMS customer. Generally, DOD inventory levels are established to support DOD's own level of operations as well as to provide a contingency reserve of material. When an FMS customer submits a requirement under the authority of an LOA, the DOD policy is to use its current inventory for FMS demands if it can do so without negatively impacting its own readiness. As a result, it may be necessary for DOD to procure the required FMS item by contracting with industry rather than to supply it from stock. There is an exception to this policy under a special program called the Cooperative Logistics Supply Support Arrangement (CLSSA). More information on the CLSSA program is contained in Chapter 10 of this textbook, "Logistics Support of International Military Sales."

Buyer and Seller Relationship

When an FMS customer accepts an LOA, it enters a government-to-government agreement to purchase military items or services from the USG. In regard to the LOA, the FMS customer is the buyer and the USG is the seller. The USG may provide the articles or services from stock but often must contract with industry to acquire the items or services for delivery to the FMS customer. In the procurement contract, the USG becomes the buyer and the vendor from industry is the seller. The FMS customer is not a legal participant in the procurement contract with industry. The USG is acting on the FMS customer's behalf. As far as the vendor is concerned, it is under contract and directly obligated to the USG and has no direct contractual relationship with the FMS customer. Also, in the FMS process, the vendor that enters a procurement contract with the USG to produce material or provide services is not exporting their products. The vendor is selling to the USG. It is the USG that is exporting the products under the authority of the LOA.

Letter of Offer and Acceptance and Contract Relationship

The LOA documents the customer's requirement and provides both the authority and funding to initiate contracting actions. In preparing the LOA, the case manager must clearly understand the customer's requirement to ensure the LOA addresses all of the customer's requirements. At the same time, the case manager must also ensure that any special procurement issues from the contracting officer's perspective are adequately discussed with the customer and appropriately documented within the LOA. The goal is to have an LOA that can be implemented by means of a procurement contract that both fulfills the customer's desires and is consistent with all USG contracting regulations. The

key to success in this area is clear communication early in the LOA preparation process between the customer, the case manager and the applicable DOD contracting organization.

Department of Defense Infrastructure for Foreign Military Sales Acquisition

Before discussing the contracting process, an introduction to the DOD's structure for FMS acquisition is required. The DOD does not maintain a separate acquisition infrastructure just for FMS. Instead, the DOD supports FMS by using the same acquisition infrastructure already established to support its own acquisition and logistics needs.

Major System Acquisition

For major weapon systems, the military departments (MILDEPs) establish Program Management Offices (PMO) that are responsible for:

- Developing and acquiring the initial system
- Managing all the technical aspects of the systems delivered to U.S. forces
- Procuring any additional quantities for DOD
- Engineering improved or modified configurations

A PMO team will typically consist of a weapon system program manager supported by personnel from several functional disciplines such as engineering, testing, contracting, logistics, and financial management.

When an FMS customer purchases a major weapon system, the same PMO that oversees the acquisition of that system for the DOD will also manage the acquisition for the FMS customer. The system PMO may acquire the FMS quantities either as individual procurements or by merging the FMS requirements with DOD's requirements on the same U.S. contract. The contracting officer within the overall PMO is the only individual with the authority to enter into contracts on the behalf of the USG. In this role, the contracting officer will be supported by the functional expertise of the members of the program office team in establishing source selection criteria, evaluating offers, and negotiating the terms and pricing of the contract.

In order to accomplish successful program execution, major FMS system sales may require PMO services beyond those provided by the standard level of service discussed in the SAMM C.5. Additional management services will be funded by a well-defined services line on the LOA. The SAMM requires each service line to include a LOA line item note to describe the details of the services provided and to identify the length of the service performance period.

Follow-on Support Acquisition

In regard to standard follow-on support, FMS requirements from the LOA will be routed to the DOD inventory control point (ICP) that manages the item for the DOD. ICPs assign item managers the responsibility for managing the inventory levels for a range of specific standard items. The ICP item manager responsible for the requisitioned item will decide whether the FMS order should be supported from on-hand stock, held on back order for support from materiel due into stock, or placed on a purchase request for procurement. If procurement is required, the item manager will generate a purchase request identifying the items to be procured and the funding source to finance the procurement. The purchase request, containing a fund cite from the applicable FMS LOA, will be routed to the ICP's contracting activity. A contracting officer will follow the normal DOD procurement process to select a vendor, and award a contract to fulfill the FMS requirement. Based on the volume of FMS activity, the ICP's manpower may be augmented with additional positions funded by the overall FMS

administrative fund. For standard follow-on support, the same DOD functional organizations that purchase the respective item for the DOD will also be responsible for FMS purchases.

Nonstandard Acquisition

DOD policy is to support all systems sold through FMS for as long as the FMS customer chooses to operate the system. For the FMS customer, the DOD decision to curtail or end operations of a given system may impact support. Many examples exist where DOD currently supports systems operated by FMS customers that the DOD no longer actively retains in its inventory, such as the F-5 and the F-4 aircraft. In these situations, components of the system may transition from being standard to nonstandard items. SAMM chapter 6 states that the MILDEPs should notify foreign users of weapon systems that will soon become obsolete to the USG. Foreign users should then have a minimum of two years to place a final order for secondary support items to sustain the system for the additional period that the foreign purchaser plans to continue to operate the system.

Nonstandard requirements are, by definition, items that are not actively managed in the DOD supply system for U.S. forces. Nonstandard FMS requirements have historically been difficult to support because there is no existing management or acquisition infrastructure within the DOD to support them. Because no ICP activity manages or buys these items for DOD, the MILDEPs have contracted with commercial buying services (CBS) to procure most nonstandard items in lieu of DOD directly contracting for nonstandard items. More information on CBS is presented in Chapter 10 of this textbook, “Logistics Support of International Military Sales.”

Contracting Regulations

The *Federal Acquisition Regulation* (FAR) system establishes a set of uniform acquisition policies and procedures to be used by all federal agencies of the USG. The FAR is the primary document governing contracting actions undertaken by the USG. Many of the FAR requirements originate in various laws passed by Congress. One of the best known legislated requirements is the *Competition in Contracting Act* (CICA). Like other federal regulations, the FAR is considered to have the force and effect of law. The current version of the FAR is publicly available online. See references to this chapter for the web site address.

In the LOA, standard term and condition 1.2 states that the USG will follow the same regulations and policies when procuring for FMS as it does when procuring for itself. This condition in the LOA is referring to the FAR. The SAMM (which provides overall policy for the conduct of FMS) states that the FAR provisions applicable to DOD will apply to FMS procurements.

Given that the DOD procures many unique items, the *Defense Federal Acquisition Regulation Supplement* (DFARS) was created to supplement the FAR. Each of the MILDEPs and their subordinate commands have, in turn, issued further supplements to the DFARS to aid contracting personnel in implementing FAR and DFARS. It is important to recognize the hierarchy in the contracting regulations. The FAR remains the over arching authority. Each subordinate supplement may amplify and expand on the principles of the FAR but cannot contradict. Accordingly, each supplement issued by the MILDEP can only amplify on the principles in the DFARS. It is interesting to note that DFARS, Subpart 201.104, states that the DFARS applies to contracts issued by the DOD in support of FMS. The current version of the DFARS is available online. See References to this chapter for the web site address.

CONTRACT SOURCE SELECTION

The CICA requires USG agencies to promote the use of full and open competition in procurements. This legislated requirement is detailed in Part 6 of the FAR, which discusses contract competition. In a competitive procurement, the USG makes public notification of its intent to purchase. This public notification used to be accomplished via a publication, the *Commerce Business Daily*. The USG currently electronically posts these notifications on its Federal Business Opportunities (FEDBIZOPPS) web site: <http://www.fedbizopps.gov>. These public notifications are commonly referred to as solicitations. The FEDBIZOPPS web site provides interested vendors an opportunity to submit a bid or proposal to the USG in accordance with the solicitation instructions. Submitting a bid or proposal enables the vendor to be considered in the contract source selection process. Per the FAR, all federal agencies are required to use competitive procurement procedures as the normal method of acquisition.

As an exception under certain conditions, the FAR does permit procurement on a noncompetitive basis. In a noncompetitive procurement, the USG negotiates with a single source at the exclusion of all other potential sources. In order to use this exception to normal procurement procedures, a justification must be prepared to document the reasons why a noncompetitive procurement is required rather than conducting a competitive procurement. According to the FAR, noncompetitive procurements are permitted only when justified based on one or more of the following seven conditions.

- Property or services required are available from only one responsible source and no other type of supply or services will satisfy agency requirements
- Need for the supply or services is of an unusual and compelling urgency
- Award the contract to a particular source or sources in order to:
 - Maintain a facility, producer, manufacturer, or other supplier available for furnishing supplies or services in case of a national emergency or to achieve industrial mobilization
 - Establish or maintain an essential engineering, research, or development capability to be provided by an education or other nonprofit institution or a federally funded research and development center
 - Procure the services of an expert for use in any litigation or dispute involving the federal government
- International agreement or a treaty between the U.S. and a foreign government or international organization (specifies a source)
- Statute expressly authorizes or requires that the procurement be made from a specified source
- Disclosure of the agency's needs would compromise the national security
- Head of the agency determines that it is necessary in the public interest to use procedures other than competitive procedures

Foreign Military Sales Competitive Source Selection

The LOA standard terms and conditions reflect the FAR preference for competition in contract awards as mandated by the CICA. LOA condition 1.2 states that the USG is responsible for selecting the contractor to fulfill the LOA requirements. Additionally, condition 1.2 states that the U.S. will select the contractor on the same basis as it makes contractor selections to fulfill its own requirements. In other words, the norm for FMS contract awards is for the U.S. to use its competitive contract award

process to select the contractor to fill the FMS customer's requirement. The SAMM C6.3.4 states that competitive source selection will be utilized to the maximum extent possible in support of FMS.

Foreign Military Sales Sole Source by Customer Request

Section 1.2 of the LOA standard terms and conditions does permit the FMS customer to formally request a noncompetitive procurement be conducted on its behalf. Within the FMS community, a customer's request for a noncompetitive contract award is commonly referred to as a sole source request. A customer's sole source request must comply with the criteria in the SAMM, Section C6.3.4 and should be submitted with the Letter of Request (LOR). The sole source request must have sufficient justification to demonstrate that sole source procurement is necessary to meet the objective needs of the customer. The SAMM, Table C6.T2, identifies the following situations where sole source procurement may be considered appropriate to meet objective customer needs. The SAMM does not limit the customer to these five reasons but most customer sole source requests will fall into one of these areas.

- Urgent Requirement - One of the numerous suppliers can deliver faster, and the situation is urgent enough to forego the benefits of the competitive process.
- Nonstandard Item - Procurement is for a nonstandard item which is not active in the DOD supply system, and the customer country knows of a specific source for the item.
- History - A country has an established history of procurement for articles or services from a particular source and to change would adversely affect an ongoing program. For example, this could include an ongoing maintenance program where a particular contractor is providing technical services and the customer country desires to continue with this same contractor for the next contract period.
- Customer Source Selection - The foreign purchaser has conducted its own source selection competition but desires to procure using the FMS process. In using this sole source justification, the customer country must provide the following:
 - A copy of the country's request for proposal, invitation for bid, or request for tender
 - A description of the method used to advertise the requirement and any restrictions placed thereon
 - A narrative summary of the country's source selection criteria and method of evaluation. If price is not the sole selection criterion, the country must identify the weight that was given to each criterion.
- Standardization - When a country has established a history of procurement for articles or services from a particular source and needs to continue procurement from that source to continue standardization of equipment with consequent benefits of standardized logistics support.

Sole source requests are received by the implementing agency (IA) responsible for preparing the LOA. The IA determines whether the sole source request meets the requirements of the SAMM. Sole source requests determined to be patently arbitrary or a discriminatory exclusion are disapproved. All responses to the foreign purchaser informing of a sole source disapproval must be coordinated with DSCA.

In addition to reviewing the customer's sole source justification, the SAMM also recommends that the sole source request be forwarded to the applicable contracting office for information and advice. Typically, the contracting officer will have previous experience procuring this same or similar item or

service for DOD. DOD maintains data on past procurements and the performance of various vendors in fulfilling previously awarded DOD contracts. Based upon the contracting officer's experience and access to procurement data, the USG may possess additional information that indicates the customer's sole source selection may not be a prudent procurement choice. In these instances, the contracting officer can inform the case manager, who would, in turn, provide this additional information to the FMS customer for further consideration.

Sole source requests typically specify a particular prime contractor. A sole source request may also request that specific subcontractors be utilized by the prime contractor. Specifying sole source subcontractors limits the ability of DOD to hold prime contractors to specific performance and cost parameters. Normally, the prime contractor would be responsible for selecting and overseeing subcontractor work to ensure all contract targets are achieved. When a sole source subcontractor is specified, the prime contractor will be required to use certain subcontractors. This removes the prime contractor's ability to shift work away from under-performing subcontractors and could relieve the prime contractor from certain contract liabilities. If the FMS customer chooses to request specific subcontractors, the purchaser should be advised of the additional risk as stated in the SAMM C6.3.4.2.

Per SAMM, Section C6.3.4.6, approved sole source requests must be documented in an LOA sole source note. The reason for documenting the sole source approval in the LOA is to comply with the FAR. The fourth FAR exception for noncompetitive procurement permits noncompetitive procurement based on an international agreement. For FAR purposes, the LOA is considered to be within the international agreement category. An LOA containing an approved sole source permits the USG contracting officer to initiate a noncompetitive procurement at the FMS customer's request and still be in compliance with the FAR. A copy of the accepted LOA containing the sole source note should be forwarded to the applicable contracting officer to permit compliance with the FAR 6.3 requirements for noncompetitive procurements.

As an exception to policy, a sole source request may be considered after LOA acceptance. The same sole source review and decision process would occur. If approved, the accepted LOA would require an amendment to be issued to incorporate the sole source note. LOA amendments require customer acceptance before the changes can be implemented. However, if the request for sole source is submitted by a customer official known to have equivalent or greater authority than the official who signed the LOA, then the sole source note can be added to the LOA by a modification. [SAMM, Section C6.3.4.1] LOA modifications are unilateral documents that can be immediately implemented upon issuance.

Foreign Military Sales Sole Source without Customer Request

Although most FMS sole source procurements originate with the foreign customer, noncompetitive procurements can originate unilaterally with the USG. In this situation, although the FMS customer did not have any specific desires for a particular sole source, the USG managers conducting the procurement may determine that the FMS procurement needs to be conducted on a noncompetitive basis. In this case, the USG managers must generate a written justification for the noncompetitive procurement based on one of the other FAR noncompetitive procurement exceptions (i.e., other than international agreement).

An example of a sole source procurement that was not requested by the FMS customer would be a major system acquisition. If the customer wanted to purchase F-16 aircraft through FMS, the customer would not need to submit a sole source request that the F-16s be purchased from Lockheed-Martin.

Under the FAR, after initial source selection, major weapon systems are considered to be single source items. The USG will not conduct a competitive procurement for these type items. The USG would unilaterally justify a noncompetitive procurement based on the item being a single source item.

Competitive Source Selection

Unless the LOA reflects an approved customer sole source request or the contracting officer has justified a noncompetitive award in accordance with another of the FAR noncompetitive exceptions, a competitive source selection process will be conducted. It is important for the FMS customer to recognize that the competitive process requires time to accomplish. Foreign customers often wonder why it may take so long to deliver an item under FMS. Part of the item lead time concerns the time necessary to plan and conduct the competitive source selection process.

Per the FAR, competitive source selection can be accomplished using one of three methods: simplified acquisition procedures (SAP), sealed bids, or by negotiation. This represents a hierarchy of preferred use. For any given procurement, the first option should be to consider whether the procurement qualifies to be accomplished under simplified acquisition procedures. If it does not meet the criteria for SAP, the next option is to evaluate whether sealed bidding criteria can be met. The final option, when the first two types cannot be applied, is to use negotiation. This hierarchy reflects the degree of difficulty and cost invested by the USG in the procurement. The SAP are the easiest and least costly type whereas negotiation requires the most government resources and incurs the highest cost.

- Simplified acquisition procedures are aimed at streamlining government procurement. Price quotes are solicited from vendors, and the government then issues an order to the vendor determined to provide the best value. Given the reduced bureaucratic approach, dollar value limitations have been placed on the situations in which this method can be used. Purchases up to \$100,000 in noncommercial items are permitted. Because of the price regulating influences of the commercial marketplace, this method can be used for purchases of commercial items up to \$5.5 million. FAR Part 13 describes this process.
- Sealed bids are used if time permits the solicitation, submission, and evaluation; if the award can be made on the basis of price and other price-related factors; if it is not necessary to conduct discussions with the prospective vendors; and if there is a reasonable expectation of receiving more than one sealed bid. Under sealed bidding, the government advertises its requirements and invites interested firms to submit a bid. Vendors interested in competing for this business submit their respective bids in accordance with the invitation for bid instructions. Generally, there will be a deadline date for bid submission and a date established when the government will open the bids. On the bid opening day, the USG will open and review all the bids submitted. The contract will most likely be awarded to the firm that submitted the lowest price bid that was responsive to the requirements. Responsive means that the bidder offered what the government requested and not something else. FAR Part 14 describes this process.
- Negotiation is used if any of the above conditions for simplified acquisition or sealed bidding cannot be met, and when it is necessary to conduct discussions with prospective contractors. The main steps in this process as described in FAR Part 15 are:
 - USG solicits competitive proposals
 - Offerors prepare and submit proposals

- Competitive range determination is made by the USG to decide with which offerors to conduct written or oral discussions
- USG technical and price evaluation of proposals. In this process, the USG typically has two evaluation teams separately consider the merits of each proposal. One team will be comprised of subject matter experts capable of distinguishing between the relative technical and qualitative benefits presented by each proposal. The other team, comprised primarily of financial and business type individuals, will review the price related factors of each proposal.
- USG selects and awards a contract to the vendor whose offer is most advantageous to the government. The most advantageous or best value offer is the one determined to provide the best combination of performance and price. It is not necessarily the lowest price offer or the best performing product/service.

Advertising for Competition

The federal government has entered the electronic age and now officially advertises all federal contracting opportunities valued over \$25,000 from a single web site at: <http://fedbizopps.gov>. FMS requirements will also be advertised on this web site for interested vendors.

Set-aside Procurements

As previously stated, all procurements for FMS will be conducted in compliance with FAR and DFARS policy and procedures. As such, the potential does exist for certain FMS procurements to be set-aside for special classifications of businesses to exclusively compete. This is another example of the USG conducting FMS procurements in the same manner as it conducts procurements for itself. The FAR Part 19 describes this process.

Although procurements may be set-aside, the FAR also requires that contract awards be made to responsible contractors. A responsible contractor is one that the government believes to possess the ethics, resources, capability, and capacity to successfully deliver the contract requirements in a timely manner.

Contract Types

The decision concerning the type contract to use in a FMS procurement is an internal USG decision. The USG will select the contract type for FMS in the same manner that it selects contract types for itself. Often, the USG will combine its own requirements with FMS requirements on a single contract. Although the USG will select the type of contract used to procure for FMS, the contract type may impact the customer when it comes to timely case closure. Under FMS, the financial policy is for the USG to recover the total cost of performance against the FMS case. The type of contract used in making FMS procurements can impact how long it will take to determine the total cost. As a result, the type contract can ultimately impact how long it will take to close the FMS case. More information on FMS case closure is contained in Chapter 12 of this textbook, "Foreign Military Sales Financial Management."

There are two fundamental categories of contracts used in DOD procurement: fixed-price and cost-reimbursement. Within these two broad categories, a wide variation of contract types is available to the government and contractors.

- Fixed-price contracts establish a price that is generally not subject to any adjustment, regardless of the contractor's costs experienced in performing the contract. This contract type makes the contractor responsible for cost risk and the resulting profit or

loss with little or no cost risk to the government. When a contractor delivers materiel or services under a fixed-price contract and the USG accepts the product, no significant further action is required by either party. The government will pay the predetermined fixed price and the contract can be closed. The FAR standard for closing fixed price contracts is within six months following final delivery.

- Cost-reimbursement contracts pay the contractor all incurred costs determined to be allowable per the provisions of the contract. These types of contracts are suitable for use only when uncertainties involved in contract performance do not permit costs to be estimated with sufficient accuracy to use a fixed-price type of contract. Under cost-reimbursement contracts, the contractor has less cost risk, whereas the cost risk to the government is higher. Under a cost-reimbursable contract, the contractor will submit contract performance cost data to the USG. The USG must then review this cost data to validate that the costs claimed by the contractor are allowable, allocable, and reasonable.
 - Allowable means the cost category being claimed is considered to be a legitimate expense category by FAR cost standards.
 - Allocable means the proportion of the overall cost being claimed under the respective contract is an appropriate share of the resources actually applied to the respective contract.
 - Reasonable means that the amount claimed by the contractor for an allowable and allocable share does not exceed that which would be incurred by a prudent person in the conduct of competitive business.
- Due to the time necessary for the contractor to gather and report cost data and for the USG to perform any necessary review and audits of the cost data, it may take a lengthy amount of time to close out a cost reimbursable contract. The FAR standard for closing cost contracts, following final delivery, is within 20 months for contracts without indirect rates and within 36 months for contracts with indirect rates.

SPECIAL FOREIGN MILITARY SALES CONTRACTING CONSIDERATIONS

Throughout this chapter, it has been emphasized that contracting for FMS will be in accordance with normal FAR and DFARS policies and procedures. As a result, contracting for FMS essentially mirrors the process DOD uses in contracting for itself. As may be expected, there are a few peculiarities associated with FMS contracts. The DFARS contains a special subpart that addresses these peculiarities. This subpart is DFARS 225.7300, “Acquisitions for Foreign Military Sales.”

Foreign Military Sales Solicitation and Contract Marking

DFARS states that all solicitations to industry for FMS requirements should separately identify the requirement as being for FMS and also indicate the specific FMS customer. It is important for industry to know this information because special rules concerning cost allowability for FMS may apply as discussed later in this chapter. Additionally, all awarded contracts containing FMS requirements are to be marked “FMS Requirement” and are to include the FMS case identifier code.

Contracting Officer Involvement in Letter of Offer and Acceptance

The only person legally authorized to commit the USG in a procurement contract is a warranted contracting officer. A warrant is a specific certification provided to a federal employee or military officer which authorizes that person to commit the USG in contracts. The contracting officer along with other procurement professionals on the team will take the requirement identified on the LOA along with the LOA funding to ultimately award a contract with industry that is compliant with the FAR and DFAR requirements.

Potential problems that may arise when the LOA is implemented for procurement can be identified and minimized through close coordination between the case manager and the contracting officer. The DFARS states that the role of the contracting officer is to assist the FMS case manager by:

- Assisting in preparing the price and availability (P&A) data
- Identifying and explaining all unusual contractual requirements or requests for deviations
- Reviewing sales commissions and other unique fees
- Communicating with potential contractors
- Identifying any logistics support necessary to perform the contract

Contract Pricing for Foreign Military Sales

The FAR and DFARS provisions are intended to ensure procurement at fair and reasonable prices. In addition to protecting the USG interests, the FAR and DFARS also attempt to treat contractors fairly. The provisions of DFARS Subpart 225.7303-2 recognize that, in working to fulfill FMS contract requirements, contractors may incur legitimate additional business expenses that they normally do not incur in DOD only contracts. As a result, DFARS Subpart 225.7303-2 permits certain types of costs to be allowable for FMS contracts. Although the same pricing principles are used, FMS contract prices are not always identical to the DOD contract prices. This situation is due to slightly different rules regarding cost allowability for FMS requirements than for DOD requirements. Examples of such allowable FMS contract costs include:

- Selling expenses
- Maintaining international sales and service organizations
- Sales commissions and fees in accordance with FAR, Subpart 3.4
- Sales promotions, demonstrations, and related travel for sales to foreign governments
- Configuration studies and related technical services undertaken as a direct selling effort
- Product support and post-delivery service expenses
- Operations or maintenance training, training or tactics films, manuals, or other related data
- Technical field services provided in a foreign country related to accident investigations, weapon system problems, operations/tactics enhancement, and related travel to foreign countries
- Offset costs which are further defined later in this chapter

Although DFARS 225.7303-2 does permit certain costs for FMS to be allowable, the amount claimed by the contractors must also be determined to be both an amount appropriately allocable to

the respective contract and reasonable in the rate charged. DFARS 225.7303-5 limits this special cost allowability provision to only apply to procurements originating from LOAs financed with either customer funds or repayable credits. If the LOA is financed by USG grant funds such as Foreign Military Financing Program (FMFP) funds or Military Assistance Program (MAP), then the cost allowability rules default back to the standard DOD criteria.

Sales Commissions

Sales commissions, referred to in the FAR as contingent fees, are generally allowable if the commission or fee is paid an employee or a selling agency engaged by the prospective contractor for the purpose of legitimately securing business.

DFARS, 225.7303-4 permits contingent fees to exceed \$50,000 only if the customer agrees to the fees in writing before contract award. The following countries must approve all contingent fees regardless of value before they can be considered allowable FMS contract costs:

Australia	Egypt	Greece	Israel
Japan	Jordan	Republic of Korea	Kuwait
Pakistan	Philippines	Saudi Arabia	Taiwan
Thailand	Turkey	Venezuelan Air Force	

SAMM, Section C6.3.7.1, states that if sales commissions are part of a contract proposal, the inclusion should be made known to the purchasing government prior to, or in conjunction with, the submission of the LOA to that government. The notification should include the name and address of the agent; the estimated amount of the proposed fee, and the percentage of the sale price; and a statement that appropriate officials of DOD consider the fee to be fair and reasonable or that the USG cannot determine the reasonableness of the proposed fee. This statement is normally included as an LOA note.

SAMM C6.3.7.4 states that all LOAs which include contingent fees (regardless of value of the case) and all correspondence with a purchaser on the subject of contingent fees relative to P&A data or an LOA, as well as all post-LOA notifications about contingent fees, must be coordinated with DSCA.

Foreign Military Sales Customer Involvement in Contracting

The FMS process primarily involves the foreign customer in LOA related issues. After the LOA is accepted, internal USG processes are undertaken to fulfill the LOA requirements. Generally, these internal processes are accomplished without direct foreign purchaser involvement. The SAMM, Section C6.3.5, states that sufficient details should be included in the LOA to allow the U.S. contracting officer to negotiate and award a contract without requiring foreign country representation or direct involvement in the formal negotiation process.

Although the norm has been no or very limited FMS customer involvement in the DOD contracting process, policy in both the SAMM and the DFARS does permit FMS customers to participate in certain elements of the contracting process. This policy supports the overarching intent for the FMS process to provide transparency to international customers. Unfortunately, there can be confusion on the part of workers within the DOD acquisition infrastructure, as well as by international purchasers, regarding the extent of FMS customer participation permitted in the DOD contracting process. To highlight this issue, the DSCA Director issued a policy memorandum 09-60 “Foreign Military Sales (FMS) Customer Participation in the DOD Contracting Process,” that elaborates on the DFARS provisions

for customer participation. This memorandum states that some FMS customers with an interest in participation believe they are being summarily shut out of the contracting process. The DSCA Director encourages the DOD acquisition community to follow the provisions of DFARS 225.7304 and actively seek opportunities for customer participation. Attachment 9-1 of this chapter, provides the text of this memorandum.

The following sections outline the areas, per the SAMM and DFARS, that the customer may choose to have greater participation and other areas where customer participation is not permitted.

Source Selection

Competitive contract awards are the default procurement method for FMS. As discussed above, the FMS process does provide a process whereby the customer can request the USG contract on a non-competitive basis with a specific vendor in support of an LOA requirement. This process is referred to as a sole source request. Unless the customer submitted a sole source request, the customer cannot provide direction regarding source selection decisions. LOA standard term and condition 1.2 states the following:

. . . the Purchaser understands that selection of the contractor source to fill requirements is the responsibility of the USG, which will select the contractor on the same basis used to select contractors for USG requirements.

The FMS purchaser is not permitted to interfere with a prime contractor's placement of subcontracts or to direct the USG to exclude certain vendors from participating in a respective FMS competitive source selection. Customers may suggest that certain additional firms be considered because this has the effect of increasing competition. [SAMM, Section C6.3.5.1 and DFARS, 225.7304(a), (f), and (g)]

Contract Negotiations

Under FMS, the foreign purchaser has authorized the USG to solely negotiate the procurement contracts that originate from the LOA requirements. LOA standard term and condition 1.2 states:

. . . the Purchaser agrees that the U.S. DOD is solely responsible for negotiating the terms and conditions of contracts necessary to fulfill the requirements of this LOA.

Although the USG should be able to accomplish contracting actions without FMS purchaser involvement, the SAMM C6.3.5.2 states that contracting officers should consult with the FMS purchaser on any matter that could be perceived as inconsistent with or significantly different from the LOA. Per DFARS 225.7304, FMS purchasers may participate with USG acquisition personnel in discussions with industry to develop technical specifications, establish delivery schedules, and identify any special warranty provisions or other requirements unique to the FMS purchaser. Additionally, customers may participate in reviewing varying alternatives, quantities, and options needed to make price-performance trade-offs. The degree of participation of the FMS purchaser during contract negotiations is left to the discretion of the contracting officer after consultation with the contractor. USG personnel are not permitted to release any contractor proprietary data unless approved by the contractor. FMS customer participation may be limited in situations where:

- The contract includes requirements for more than one FMS customer
- The contract includes unique U.S. requirements
- Negotiations involve contractor proprietary data

