Foreign Military Sales Financial Management Manual: An Update

By

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Formal Change Number 4, dated 8 September 1989, to the *Foreign Military Sales Financial Management Manual*, DOD 7290.3-M, was recently distributed and contains some significant changes as far as both the FMS customer and the U.S. participants in the FMS program are concerned. The purpose of this article is to emphasize and discuss those points which are believed to be of greatest interest to the reader. [NOTE: The new Fair Pricing Legislation for FY90 (concerning asset use charges, nonrecurring charges, and reimbursement of military salaries and unfunded civilian retirement, as described in the "Legislation and Policy" section of this issue) occurred after Change 4 was published and will be incorporated in subsequent changes to DOD 7290.3-M.]

Paragraph 10102.C.2. reiterates that the President is authorized to enter into agreements with North Atlantic Treaty Organization (NATO) members, Japan, Australia, New Zealand, and other countries which are major non-NATO allies for the cooperative furnishing of training on a bilateral or multilateral basis, if the financial principles are based on reciprocity. These agreements require reimbursement to the U.S. Government for all direct costs, but indirect costs, administrative surcharges, and costs of billeting trainees (except for the amount charged members of the United States Armed Forces occupying comparable accommodations) may be excluded. Previously this authorization had been restricted to agreements with NATO member nations, Japan, Australia, and New Zealand.

Paragraphs 10103.E. and **70103.E.** state that the cost of military pay and entitlements for defense services will be waived for cases funded entirely by MAP or non-repayable FMS credit funds. For cases funded entirely by MAP, the waiver will occur for services provided on or after 1 October 1985. For non-repayable FMS credits, the waiver will be granted for services provided on or after 1 October 1989. However, it should be noted that any subsequent modification or amendment to a case which reduces the source of funding by MAP or non-repayable FMS credits below 100 percent will require the withdrawal of the waiver, and the customer will be charged for any defense services which had been previously waived. Previously, the waiver of military pay and entitlements for defense services had been limited to those FMS cases had been funded exclusively funded by MAP.

Paragraph 20004.B. states that the SAAC issues obligational authority (OA) to the Implementing Agencies (IA) via a DD Form 2060 submitted by the IA when the following three requirements are met: (1) the case is valid; (2) the FMS customer has deposited necessary cash in advance to support the FMS case; and (3) the requested obligational authority does not exceed the dollar value shown on the DD Form 1513, DD Form 1513-1, or DD Form 1513-2. The implication of this paragraph is that if the required amount of OA exceeds the amount shown on the LOA, or subsequent amendment or modification by as little as $1.00, a corresponding DD Form 1513-1 or DD Form 1513-2 must be prepared by the IA prior to the request for the additional OA from the SAAC. Before this change, normal practice had been to request OA up to 110 percent of net case value.

Paragraph 20602. describes exceptions to the requirement for reporting the existence of adverse financial conditions. An adverse financial condition is defined as overobligation at the case level or overexpenditure at the country level. A report of adverse financial condition is not required if any of the following conditions are met:

a. if the overobligation is less than 10 percent of the "estimated cost" shown on the DD Form 1513, and both a DD Form 1513-2 and amended DD Form 2060 were submitted and approved by the SAAC within 60 days of the date of the transaction which resulted in the overobligation. Previously a DD Form 1513-2 was not required to be submitted to and approved by the SAAC for overobligations which were less than 10 percent of the "estimated cost" on the DD Form 1513.

b. if the overobligation is 10 percent or greater of the "estimated cost" shown on the DD Form 1513, and both a DD Form 1513-2 and an amended DD Form 2060 were submitted and approved by the SAAC within 45 days of the date of the transaction which resulted in the overobligation.

c. if the overobligation/overexpenditure was the result of the duplicate posting of an obligation/expenditure transaction and correction is accomplished within 60 days of the transaction date.

Paragraphs 40002.B. and **40002.C.** were added to the manual. Paragraph 40002.B. points out that the FMS trust fund is managed as a single cash entity, but that funds are identified at the country and FMS case level by source of funding (MAP, FMS credit, or customer funds). Paragraph 40002.C. provides a priority for funding FMS cases. DSAA will normally drawdown MAP funds (if available) up to the amount reserved for each case, prior to requesting that an FMS customer drawdown FMS credit funds or provide national funds. Similarly, MAP funds on deposit in the FMS trust fund will be accounted for as expended before FMS credit funds, and FMS credit funds will be accounted for as expended before national funds. In the event that MAP or FMS credit funds become excess to a case's requirements due to case closure or case reduction, they may be applied to another of the customer's cases, if approved by DSAA. However, excess MAP and FMS credit funds may not be refunded to the FMS customer.

Paragraph 40003.B. emphasizes that in the event payment schedules do not require sufficient payments to meet the cash requirements of a case, the implementing agency must notify SAAC to accelerate billings and cash collections and follow up this notification by issuing a revised payment schedule by means of a DD Form 1513-2. Of course, implementing agencies must also review the payment schedules to ensure that payment schedules do not improperly accelerate cash requirements. In the event that payment schedules call for payments which accelerate the cash requirements of a case, the payment schedule may be revised to decelerate the payments.

Paragraph 50303.G. provides guidance regarding billings after case closure. If the implementing agency identifies a charge (or credit) against a closed case, a reimbursable DD COMP(M) 1517 report is processed against the closed case. No self-reimbursable transactions are allowed.

a. If the charge is within the minor reconciliatory amounts allowed for closed cases (less than one percent of the net FMS case value up to a maximum of $10,000) the charge is reported to the FMS customer through an omnibus quarterly billing statement. The charges are normally funded from the FMS customer country level holding account. If there are insufficient credits available in the FMS customer's country level holding account, the omnibus billing statement will request additional funds. If, on the other hand, the charge exceeds the minor reconciliatory amount, the case must be reopened to process the charge and a new case closure certificate must be prepared by the implementing agency.

b. Credits for closed cases, regardless of whether the minor reconciliatory amount is exceeded or not, are reported to the FMS customer by an omnibus quarterly billing statement and the credit is transferred to the country level holding account. Implementation procedures are still being reviewed by the implementing agencies.

Table 503-1 requires that the FMS case closure certificate include a statement that DD COMP (M) 1517 Delivery Performance Reporting and the FMS trust fund account 1020 (Cash Disbursements) have been reconciled with the implementing agency records and that there are no known unreconcilable differences.

Paragraph 70002.J. provides clarification concerning the situation in which the United States Government "buys back" items which were initially sold under the FMS program. Such transactions are considered to be outside the FMS program and must be conducted in accordance with the normal DOD procurement rules which consider all sources of supply. However, monies due an FMS customer may be credited to the customer's trust fund in accordance with the customer's instructions.

Paragraph 70202.E. restates the requirement that if a principal or major item is sold from inventory, without replacement, the percentage of useful life remaining on the item is applied to the most recent actual procurement cost, plus the cost of any modifications or improvements. This amount constitutes the base cost of the item. It also clarifies the policy that if the item is being replaced "in kind" (with the same model and series) or with an improved item, the base cost of the item is calculated by applying the percentage of remaining useful life against the acquisition cost of the new item. If the item is being replaced with an improved item, the base cost is increased by 10 percent for a force rearrangement factor. Regardless of whether the principal or major item is being replaced or not, the cost of major overhauls and outfittings accomplished within 24 months prior to the sale date is added to the base cost of the item.

Table 702-4B shows an alternate method for calculating remaining useful value of a principal or major item being sold from inventory. This method, known as the constant percentage method, calculates annual depreciation by applying the percentage of annual depreciation against the remaining value of the item, as opposed to the straight line method, which calculates annual depreciation by applying the percentage of annual depreciation against the original (undepreciated value) of the item. For example, assume there is a principal item being sold from inventory. The most recent actual procurement cost of the item was $10,000.00. The item has a total useful life of 10 years, and the item has been in service for 3 years. The percentage of annual depreciation is 10 percent (10 percent per year for 10 years = 100 percent). Under the constant percentage method, depreciation would be calculated as follows:

The basic formula is
annual depreciation = (remaining value) * (annual depreciation rate)

for year 1,
annual depreciation = ($10,000) * (.1) = $1,000.00

for year 2,
annual depreciation = ($9,000) * (.1) = $900.00

for year 3,
annual depreciation = ($8,100) * (.1) = $810.00

at the end of year 3,
total depreciation = $1,000.00 + $900.00 + $810.00 = $2,710.00

remaining useful value= original value – total depreciation
= $10,000.00 – $2,710.00
= $7,290.00

The remaining useful value can also be calculated under the constant percentage method by using the formula

remaining useful value = R_n * original value

where R_n is the remaining useful like factor after n years, and R_n is defined by the formula:

$$R_n = (1 - d)^n$$

in which n is the age in years of the item and d is the percentage of useful life lost after each year.

In the previous example, where n = 3 years and d = 10%, we could calculate R_n by the formula:

$$R_n = (1 - .1)^3 = .729$$

and calculate remaining useful value by the formula:
remaining useful life = R_n * original value
= .729 * $10,000.00
= $7,290.00

Under the straight line method, depreciation would be calculated as follows:

for year 1,
annual depreciation = ($10,000) * (.1) = $1,000.00

for year 2,
annual depreciation = ($10,000) * (.1) = $1,000.00

for year 3,
annual depreciation = ($10,000) * (.1) = $1,000.00

at the end of year 3,
total depreciation = $1,000.00 + $1,000.00 + $1,000.00 = $3,000.00

remaining useful value = original value – total depreciation
= $10,000.00 – $3,000.00
= $7,000.00

The remaining useful value could also be calculated under the straight line method by using the formula remaining useful value = R_n * original value where R_n is the remaining useful life factor after n years

where R_n is defined by the formula $R_n = 1 - d * n$

where d is the percentage of useful life lost after each year

In the previous example, where n = 3 years and d = 10 percent, we could calculate R_n by the formula:

$$R_n = 1 - .1 * 3 = .70$$

and calculate the remaining useful life by the formula

$$\begin{aligned} \text{remaining useful life} &= R_n * \text{original value} \\ &= .70 * \$10{,}000.00 \\ &= \$7{,}000.00 \end{aligned}$$

Paragraphs 70308. and **70501.** revise the policy regarding reimbursement for DOD expenses related to procurement for FMS cases. Under current policy, this expense is charged to the FMS Administrative Fund. Previously, it had been included in the above-the-line cost off a new procurement item.

Paragraph 70403. includes Canada as well as CONUS locations for delivery term codes 2, 3, and 5.

Paragraph 71704.C. states that logistic support charge (LSC) will be credited by the SAAC at the time that an approved report of discrepancy (ROD) is being processed. Implementing agencies are urged in this paragraph to ensure that the original shipping date of the article being credited is contained in positions 61-64 of the DD COMP (M) 1517. Since LSC was effective 1 April 1987, only those honored RODs with an original ship date of 7091, and later, will be credited with LSC.

Paragraph 80103. reformats the DD Form 645, "Foreign Military Sales Billing Statement." When implemented by the SAAC, Column 10, Cumulative Delivery Costs & Work in Process" will represent all deliveries which have been reported on DD COMP (M) 1517 and SAAC charges applied to these deliveries. However, amounts applicable to contractor holdbacks, unearned advances, and potential termination liabilities will appear in Column 11, "Forecasted Financial Requirements." Previously, amounts applicable to contractor holdbacks, unearned advances, and potential termination liabilities had been included in the amount shown in Column 10. Implementation of this change is not anticipated before late 1990.

Paragraph 80302.R. includes Canada as well as CONUS destination for Transportation Bill Codes (TBC) A and B. Previously, TBCs "A" and "B" had applied only to CONUS destinations. When implemented by the SAAC, Canada will be charged transportation at the rate of 3.75 percent for deliveries to destinations in Canada rather than the previous practice of considering Canada as an overseas location in rate area "1."

- This same paragraph also introduced a new TBC of "W." Under procedures already implemented by the SAAC, when deliveries are reported with a TBC of "W," the Transportation Look-Up Table is checked to determine the rate for the National Stock Number (NSN) of the item which was delivered. If the NSN is not listed in the table, the report of delivery is considered invalid and is rejected. If the delivery is reported with a TBC of other than "W"" or a TBC is not included, the SAAC will check to see if a Delivery Term Code (DTC) of "6," "8," or "9" was reported. If this is the situation, the Transportation Look-Up table will be checked to verify that its NSN is listed and that the date shipped is on or after the effective date of the entry in the table. If this is true, then transportation charges are applied per the entry in the table. If this is not the case, then transportation charges are computed using the applicable percentage based on the TBC or DTC.

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