



August 2017

FOREIGN MILITARY SALES

Expanding Use of Tools to Sufficiently Define Requirements Could Enable More Timely Acquisitions

Accessible Version

GAO Highlights

Highlights of [GAO-17-682](#), a report to congressional committees.

Why GAO Did This Study

The U.S. government procures billions of dollars in goods and services each year on behalf of foreign governments through the FMS program. Multiple federal agencies are involved in the FMS program; however, DOD manages the procurement process. The FMS program is a key component of national security and foreign policy.

House Report 114-537 included a provision for GAO to review certain aspects of DOD's acquisition process such as what effect, if any, certain types of contracts may have on the FMS process. This report addresses (1) how the use of firm-fixed-price contracts compares to other contract types awarded for FMS and the reasons they are used; and (2) the factors that may contribute to delays or potentially increase costs. GAO has other work addressing the FMS process and will issue separate reports.

GAO analyzed FMS procurement data for fiscal years 2007 through 2016, the most current data available to determine trends. GAO also selected a non-generalizable sample of 32 FMS cases from seven program offices, based on use of different contract types to procure the same item; reviewed relevant DOD and federal acquisition regulations and policies; and interviewed DOD officials.

What GAO Recommends

GAO recommends that DOD issue department-wide guidance for program offices to expand the use of tools, such as checklists, to aid FMS customers in specifying their requirements in a way that DOD can act upon in a timely manner. DOD concurred with GAO's recommendation.

View [GAO-17-682](#). For more information, contact Marie A. Makat (202) 512-4841 or MakM@gao.gov.

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What GAO Found

Over the past 10 years, firm-fixed-price contracts—where the contractor is paid a set amount regardless of incurred costs—accounted for 99 percent of contract awards and had the highest obligations for foreign military sales (FMS). But in recent years, there has been an increased use of fixed-price-incentive contracts—where the government and contractor share in cost savings and risks and the contractor's ability to earn a profit is tied to its performance. This trend is consistent with recent Department of Defense (DOD) contracting practices and aligns with department guidance that emphasizes the use of fixed-price-incentive contracts in certain instances where better pricing outcomes might be achieved. Contracting officers generally follow the same acquisition guidance for FMS procurements as they do for DOD and use various contract types based on assessed risks. For example, for decades, the Air Force had awarded firm-fixed-price contracts for FMS customers to procure an air-to-air missile, but in 2015 transitioned to a fixed-price-incentive contract when it realized the contractor could achieve cost savings through production efficiencies. Legislative changes in fiscal year 2017 call for DOD to use firm-fixed-price contracts for FMS unless a waiver is granted. DOD is in the early stages of implementing these revisions and is weighing various factors, such as how waivers will be reviewed.

GAO found several factors may contribute to delays or increased prices in FMS. For example, program officials noted that general acquisition issues, such as delayed contract awards and unforeseen events during production, can similarly affect FMS. Moreover, military department officials stated that the process for defining requirements is a significant challenge that affects expediency of FMS procurements. DOD guidance states that programs may combine FMS and domestic requirements onto a single contract as a way to lower prices and facilitate timely delivery. However, program offices GAO spoke with noted that adequately defining foreign customers' requirements may prevent them from doing so. To expedite requirements definition, the Air Force and Army implemented checklists to aid foreign partners and program offices when specifying requirements. The Navy developed but has not yet disseminated its checklists for use. GAO's analysis of 32 FMS cases showed that checklists were not always available to support procurements but that program offices that used them noted increases in timeliness. Expanding the use of checklists by DOD may better position DOD to obtain information needed to deliver equipment and services to FMS customers when needed.

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Abbreviations

AMRAAM	Advanced Medium-Range Air-to-Air Missile
DOD	Department of Defense
DPAP	Defense Procurement and Acquisition Policy
DSCA	Defense Security Cooperation Agency
FMS	Foreign Military Sales
GMLRS	Guided Multiple Launch Rocket System
JASSM	Joint Air-to-Surface Standoff Missile
NDAA	National Defense Authorization Act
SCIP	Security Cooperation Information Portal

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August 14, 2017

Congressional Committees

Each year, the U.S. government reports billions of dollars in sales of defense articles and services to foreign governments through the Foreign Military Sales (FMS) program. In fiscal year 2016 alone, the program reported sales of \$33.6 billion, representing 1,075 FMS cases for defense articles and services such as weapon systems, spare parts, technical services, and logistics support to 115 countries. The FMS program is considered an integral component of U.S. national security and foreign policy that enhances the capabilities of our allies and supports increased interoperability with the U.S. military, while also helping to sustain the defense industrial base. The Department of State (State) has overall responsibility for the program, including the approval of sales. However, the Department of Defense (DOD) administers the FMS program and manages procurements executed by acquisition programs within the military departments and other DOD components on behalf of foreign governments.¹

The FMS program has been criticized as being slow and cumbersome and not keeping pace with foreign governments' demand for U.S. defense articles needed to train and equip their military forces. In recent years, DOD has undertaken various initiatives intended to make the FMS program more responsive and better able to meet customers' expectations for timeliness and accurate pricing estimates, among other things. For instance, the Defense Security Cooperation Agency (DSCA), which is responsible for overseeing and administering the FMS program within DOD, reported implementation of the Lead Nation Procurement Initiative in July 2016, which is aimed at maximizing purchasing power for North Atlantic Treaty Organization (NATO) members through joint procurement of defense articles and services. At the same time, DSCA also released updated guidance to help expedite the review process to authorize the release of weapon systems for transfer to foreign countries under the FMS program. Further, in the Fiscal Year 2017 National Defense Authorization Act (NDAA), Congress required DOD to revise its

¹In this report, DOD components refer to DOD agencies, offices, activities, and other organizational entities outside of the three military departments.

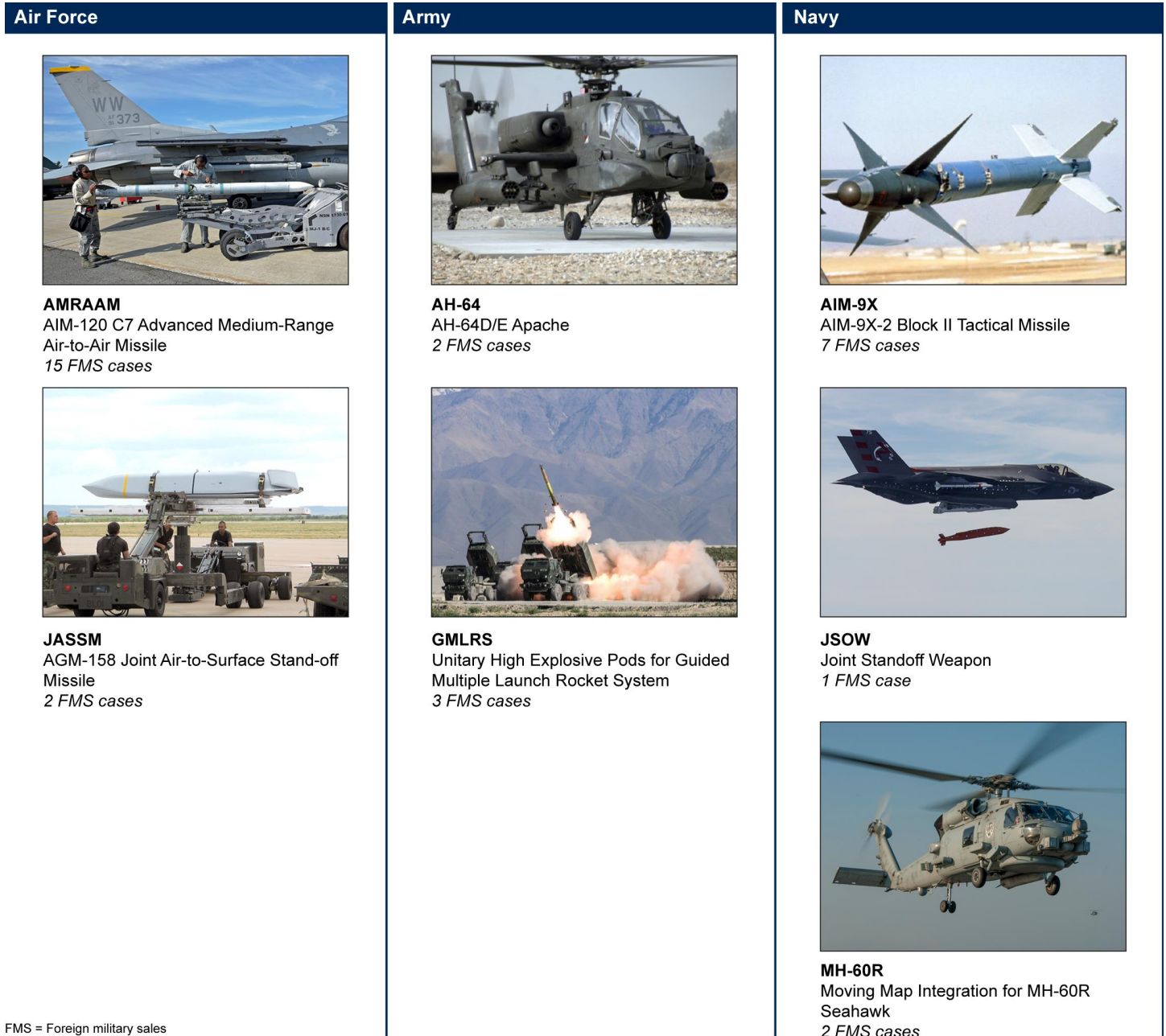
acquisition regulations to place new requirements on FMS contracting and to seek ways to accelerate contracting and pricing for FMS. Generally, the types of contracts that have been used for FMS are firm-fixed-price contracts—where the government pays the contractor a set amount regardless of the contractor’s costs—and fixed-price-incentive contracts—where the government and contractor share in cost savings and risks and the contractor’s ability to earn a profit is tied to performance.

Recognizing that challenges remain with the FMS process, the House Report accompanying the Fiscal Year 2017 NDAA included a provision for us to review certain aspects of DOD’s acquisition process, including contract type selection, to determine their effect, if any, on FMS.² This report addresses 1) how the use of firm-fixed-price contracts compares to other contract types awarded for FMS procurements and the reasons they were used and 2) the factors that may contribute to delays and potentially increase costs for FMS procurements.

To address both objectives, we selected a non-generalizable sample of contracts awarded for FMS procurements between fiscal years 2011 through 2015, which represented the most current data available at the time of our sample selection. To select this sample, we used procurement data from the Federal Procurement Data System–Next Generation (FPDS-NG) and FMS case data from the Security Cooperation Information Portal (SCIP), which is managed by DSCA, to identify acquisition programs from the Air Force, Army, and Navy that used a mix of contract types to procure the same item for FMS. For example, we selected the Advanced Medium-Range Air-to-Air Missile (AMRAAM) program because it awarded both firm-fixed-price and fixed-price-incentive production contracts that included FMS procurements. Taking this approach allowed us to gain insight into the reasons why programs would use a different type of contract to procure the same item. Based on this criterion, we selected a sample of 14 contracts from seven acquisition programs. These contracts were used to procure goods or services for 32 individual FMS cases for various countries. Figure 1 below lists the selected acquisition programs within our sample.

²GAO has additional work addressing other aspects of the FMS process including forthcoming reports on DOD’s management of the FMS program and the FMS Trust Fund.

Figure 1: Selected Acquisition Programs by Military Department



FMS = Foreign military sales

Source: GAO analysis of Department of Defense contract information (data); Army, Air Force, Navy, and Defense Video & Imagery Distribution System (images). | GAO-17-682

To determine trends in the contracts used by DOD to support FMS procurements over the past 10 years, we analyzed contracting data from FPDS-NG for fiscal years 2007 through 2016, which represented the

most current and complete data available to analyze trends over time. We compared total obligations and the contract type used for FMS procurements to those for DOD's requirements for the same items and services outside of the FMS program to determine the extent to which there were similar trends in contracting. Based on our discussions with officials about the data available as well as our review of contract documents and electronic testing for obvious errors and missing values, we determined that the data were sufficiently reliable for the purposes of our reporting objectives. We interviewed program officials and contracting officers with knowledge of the selected acquisitions to obtain information on the factors that are considered when determining which contract type is appropriate for FMS procurements. We reviewed defense acquisition regulations and FMS guidance, such as the Security Assistance Management Manual, to identify contracting requirements in place to guide procurement of goods and services on behalf of foreign governments. We interviewed officials from the Defense Procurement and Acquisition Policy (DPAP) office to obtain their insights about trends in contract types used for DOD and FMS procurements and to discuss the resulting impact, if any, of DOD guidance, such as the Better Buying Power memorandums, on contract type selection for DOD procurements. In our discussions with DOD officials, we also discussed the implications of recent legislative requirements that directed DOD to use firm-fixed-price contracts for FMS procurements and the status of DOD's efforts to implement this requirement and associated waiver process.

To gain insights about the factors that contributed to delays in the FMS process or potential increased costs, we first obtained FMS case development data reported in SCIP to determine how long it took for our selected programs and their FMS customers to define FMS requirements and develop government-to-government agreements for FMS. We interviewed DSCA officials about their process for ensuring the accuracy of the data reported in SCIP and determined that these data were sufficiently reliable for the purposes of our reporting objectives. For each of the seven acquisition programs and 32 FMS cases in our sample, we reviewed contracts and other related documentation, FMS case documentation such as letters of request from foreign governments and letters of offer and acceptance provided by military departments, and interviewed contracting and acquisition program officials to discuss the challenges that programs may have faced when procuring items for FMS customers. We also interviewed officials from DSCA, acquisition program offices, and security cooperation offices within the military departments to discuss the facts and circumstances regarding the letter of request

received from the FMS customer and the development of the letter of offer and acceptance.

We conducted this performance audit from June 2016 to August 2017 in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

Background

At its core, the FMS program is an acquisition process through which the U.S. government procures military equipment, training, and other services on behalf of foreign governments.³ Under the FMS program, foreign governments pay the U.S. government to administer the acquisition of defense articles and services on their behalf. Typically, weapon systems made available for transfer or sale to foreign governments are systems that have completed operational testing and are entering full rate production. Multiple organizations have a role in the FMS program, including DOD and State. Within DOD, DSCA and the military departments play an extensive role in administering the program and managing FMS acquisitions. DSCA carries out key administrative functions, such as coordinating the formulation and execution of FMS cases and conducting negotiations with foreign governments. The military departments carry out the day-to-day implementation of procurements to fulfill FMS agreements between the U.S. and foreign government.

³The Arms Export Control Act authorizes the sale of defense articles and services to eligible foreign customers under the FMS program, which is one of multiple security cooperation programs that provide for the transfer of defense articles and services to foreign governments. Other security cooperation programs permit foreign governments to procure items directly from industry through a direct commercial sale without the assistance of the U.S. government. In addition, the Foreign Military Financing program provides funding to eligible partner nations to purchase defense articles, services, and training through FMS or, for a limited number of countries, through direct commercial contracts. Further, the Excess Defense Articles program allows partner nations to purchase equipment no longer required by the U.S. government at a reduced price.

Key Phases of the FMS Process

The FMS process is complex and involves multiple interactions between foreign and U.S. governments and defense contractors. The FMS process has five phases, as described in the *DSCA Security Assistance Management Manual* and summarized below.

- 1) **Assistance request.** The FMS process begins when a foreign government submits a letter of request to State or DOD to purchase defense articles or services. In the letter of request, the foreign government may express interest in (1) obtaining a preliminary cost estimate for the capabilities it needs, or (2) requesting a letter of offer and acceptance that details the specific items, quantities, cost, and schedule for the sale of military articles and services. Defining the requirements to meet the desired capability can be an iterative process that requires multiple interactions between the foreign government and the military department. For example, to sufficiently define the requirement, DOD consults with the foreign government to identify not only the weapon system but also support needed to achieve the desired capability. Specifically, if a foreign government seeks to acquire an aircraft, DOD will also ensure the customer considers factors such as the operational environment in which the aircraft will be used, the capacity of its forces to operate and maintain the aircraft, and spare parts needed, among other things. According to DOD, this approach helps ensure the foreign government is adequately equipped to operate and sustain the defense items obtained under the FMS program.

- 2) **Agreement development.** The request is forwarded to the military department responsible for the particular defense article, which then provides preliminary pricing data or develops a sales agreement between the United States and the foreign government called a letter of offer and acceptance. A single DOD entity may not have full responsibility for all aspects of the FMS agreement and thus coordination within and across military departments may be needed to obtain complete information on pricing and availability to include in the letter of offer and acceptance. When developing the agreement, DOD takes into account the specific system and related support such as training, logistics, warranties, and spare parts. Once the agreement has been drafted by the military department, State and DSCA officials review and approve






the agreement and Congress is notified if the proposed sale meets certain dollar thresholds and other requirements.⁴ The military department then sends the agreement to the foreign government for its acceptance and signature.

- 3) **Acquisition.** In this phase, the responsible military departments fulfill the FMS request from existing supply or procure defense items and services. Once the letter of offer and acceptance has been signed and funding has been received, DOD contracting officers may solicit requests for proposals from industry and negotiate prices, as necessary, to award contracts. During this phase contracting officers make a determination about the best acquisition strategy, including the appropriate contracting vehicle to fulfill the FMS requirement, as articulated in the agreement. For example, the contracting officer may determine the best approach is to combine FMS and U.S. requirements on a single contract or to place them on separate contracts depending on which approach is deemed to be more cost effective and best meets production schedules that align with the foreign customer's timeframes.
- 4) **Delivery.** Upon the contractor's delivery of items included in the letter of offer and acceptance, the FMS customer will take custody and make arrangements for their transport. The foreign customer may pay the U.S. government to deliver these items or arrange for a freight forwarder authorized to manage these deliveries.
- 5) **Case Closure.** An FMS case is a candidate for closure when all materiel and services have been delivered and the FMS customer has not requested for the case to be kept open. Any remaining funds may be made available to the foreign country.

⁴Congress must be notified about FMS sales of major defense equipment that total \$14 million or more, other defense articles or services that total \$50 million or more, or design and construction services that total \$200 million or more. For FMS sales to NATO countries, Japan, Australia, the Republic of Korea, and New Zealand, those dollar thresholds increase to \$25 million, \$100 million, and \$300 million. The proposed sale can only proceed if Congress does not enact a joint resolution prohibiting the agreement within specific time frames. Major defense equipment is equipment that is identified on the U.S. Munitions List as requiring special export controls and for which the U.S. government incurred more than \$50 million in non-recurring research and development costs or more than \$200 million in total production costs.

Figure 2 summarizes the role of selected entities in the FMS process.

Figure 2: Selected Entities and Their Role in the Foreign Military Sales (FMS) Process

Organization	Assistance request	Agreement development	Acquisition	Delivery	Case closure
 <p>Foreign Military Sales Customer</p>	<ul style="list-style-type: none"> Identifies defense capabilities and refines requirements to be purchased. Submits letter of request (LOR). 	<ul style="list-style-type: none"> Sends signed letter of offer and acceptance (LOA) to implementing agency and provides funds that will be used for payment, or rejects offered LOA. 	<ul style="list-style-type: none"> Receives updates on progress from implementing agency. 	<ul style="list-style-type: none"> Receives manufactured products or services completed. Coordinates transportation of items to destination. Performs export requirements and secures authorizations to transport items. 	<ul style="list-style-type: none"> Participates in financial management reviews, meets with U.S. government entities to resolve closeout issues. After contract and case closeout, receives final bill and excess funds.
 <p>Security Cooperation Organization (SCO)</p>	<ul style="list-style-type: none"> Assists FMS customer in defining and refining requirements prior to LOR. Evaluates LOR. Coordinates the development of the LOR. 	<ul style="list-style-type: none"> Transmits offered LOA to FMS customer. 	<ul style="list-style-type: none"> Maintains case files and responds to FMS customer requests. 	<ul style="list-style-type: none"> May have responsibilities for coordinating certain methods of delivery. 	
 <p>Defense Security Cooperation Agency (DSCA)</p>	<ul style="list-style-type: none"> Reviews, evaluates, and approves or disapproves LOR. 	<ul style="list-style-type: none"> Assembles LOA documents using implementing agency-provided data. Reviews and approves LOA to be offered. Notifies Congress of potential sale; Congress can enact a joint resolution to reject a sale during the 15 to 45 day review period. 	<ul style="list-style-type: none"> Reviews and approves all LOA modifications. 	<ul style="list-style-type: none"> Reviews and approves all LOA modifications. 	<ul style="list-style-type: none"> Publishes and updates policies for case closure. Final arbiter of case closure issues. Leads various case closure meetings.
 <p>Military Department</p>	<ul style="list-style-type: none"> Evaluates LOR. Ensures LOR includes sufficient information for LOA. Assigns a case manager to coordinate case development and execution. 	<ul style="list-style-type: none"> Prepares and processes price and availability or LOA data, including price, schedule, and line items. Reviews and approves LOA to be offered after DSCA assembles it. Sends LOA to FMS customer directly or to SCO to offer to FMS customer after DSCA approval. 	<ul style="list-style-type: none"> Seeks proposals from industry. Negotiates and awards a contract. Oversees progress of contractor and provides program management reviews to FMS customer. 	<ul style="list-style-type: none"> Coordinates with FMS customer on transportation plans. 	<ul style="list-style-type: none"> Manages and facilitates record reconciliation with FMS customer and Department of Defense stakeholders.
 <p>State Department</p>	<ul style="list-style-type: none"> Evaluates LOR to ensure consistency with U.S. foreign policy and national security objectives, and either approves or disapproves the LOR. 	<ul style="list-style-type: none"> Reviews and approves LOA to be offered. Clears sale documentation for Congressional notification. 			

Source: GAO analysis of Defense Security Cooperation Agency guidance and regulations. | GAO-17-682

Contract Types Used for FMS

Each year, federal agencies procure a variety of products and services in support of their respective missions and activities. Agencies acquire products and services through contracts that specify the government's requirements, the price and payment arrangements agreed upon by the government and the vendor, and other terms and conditions. There are several different contract types and selection is the principal means that DOD has for allocating cost risk between the government and the contractor.

To fulfill FMS requirements, DOD generally follows the same acquisition process it uses to meet its own military needs. In this regard, DOD follows federal and defense acquisition regulations, which provide uniform policies and procedures to guide the acquisition of goods and services. At times, DOD may combine FMS purchases with its own procurements. Similar to contracting approaches used for DOD's requirements, DOD contracting officers have, prior to recent legislation described below, selected from among multiple types of contracts to acquire goods and services on behalf of foreign governments as specified in the letter of offer and acceptance.

Contract types generally fall under categories such as fixed-price and cost-reimbursement.⁵ The Federal Acquisition Regulation (FAR) notes that contract type selection should be based on the type, complexity, and urgency of the requirement, the contractor's technical capability, and the extent of subcontracting and acquisition history.⁶ Further, consideration should be given to the degree to which analysis can provide insight into prices, the cost impact of uncertainties, and the reasonable allocation of cost responsibility to the contractor. Each contract type comes with a different level of cost or performance risk for the government and contractor. The following is a brief description of fixed-price and cost-reimbursement contract types:

⁵Time and materials is another category of contract types. Under these contracts, payments are made based on the number of labor hours billed at hourly rates and, if applicable, materials.

⁶FAR 16.104

- Fixed-price contracts provide for a firm price or, in appropriate cases, an adjustable price.⁷ Examples of fixed-price contracts include:
 - Firm-fixed-price contracts which provide a price for the good or service that is not subject to any adjustment on the basis of the contractor's costs during performance of the contract. This contract type places upon the contractor maximum risk and full responsibility for all costs and resulting profit or loss. It provides maximum incentive for the contractor to control costs and perform effectively and imposes a minimum administrative burden upon the contracting parties.
 - Fixed-price-incentive contracts which provide for an adjustable profit and establish the final contract price by a formula based on the relationship of the final negotiated total cost to the total target cost. A fixed-price-incentive contract allows the government to share in contractor cost savings if the contractor underruns its target cost although it must also share in contractor cost overruns up to the contract's ceiling price. According to acquisition guidance, fixed-price-incentive contracts may be appropriate in situations where there is more cost uncertainty, such as for acquisition programs in the early production phase following critical design review where significant developmental testing remains. Incentive arrangements can be designed to achieve specific objectives by motivating contractor efforts that might not otherwise be emphasized and discouraging contractor inefficiency and waste.
- Cost-reimbursement contracts, such as cost-plus-fixed-fee contracts, are used when requirements are not well defined or a lack of knowledge does not permit costs to be sufficiently estimated to use a fixed-price contract. These contracts establish an estimate of total costs and a ceiling that the contract may not exceed without the approval of the government. Under cost-reimbursement contracts, the contractor is reimbursed for its reasonable costs of performance, regardless of whether the work is completed. The government pays the contractor's allowable incurred costs to the extent specified in the contract and may include an additional fee, or profit. By way of example, cost-plus-fixed-fee contracts provide for payment to the contractor of a negotiated fee that is fixed at the inception of the

⁷Adjustably-priced contracts, such as fixed-price-incentive contracts, are subject to adjustment only by operation of contract clauses, unless otherwise provided in the contract.

contract. Additionally, incentive or award fees may be used to motivate contractor performance.

Since 2010, DOD has issued guidance and updated regulations that have emphasized the benefits of using fixed-price-incentive contracts, which would also apply to FMS procurements. In June 2010, DOD issued the first of its Better Buying Power memorandums that, among other things, called on acquisition officials and contracting officers to use proper contract types for development and procurement. The guidance emphasized use of incentive contracts, in which the government shares equally in cost increases or savings. Then in 2012, subsequent guidance called for further consideration of fixed-price-incentive contracts, particularly when moving from system development to production. In addition to using fixed-price-incentive contracts during early production efforts, DOD has also emphasized that these contracts may be useful during the mature production phase of an acquisition program, especially when programs have reason to conclude that there is a poor correlation between the negotiated price and actual cost outcomes. Finally, defense acquisition regulations articulate that, in instances where actual costs on a firm-fixed-price production contract have varied by more than 4 percent from negotiated costs, contracting officers should consider using fixed-price-incentive contracts for future procurements of the same system.

Recent Legislation Modified Contracting Requirements for FMS

The Fiscal Year 2017 NDAA called for DOD to revise its regulations by June 2017 to require the use of firm-fixed-price contracts for FMS procurements unless a waiver is granted or the foreign government states a preference for an alternate contract type. In addition, DOD must establish a pilot program to examine ways to accelerate the contracting and pricing process for full rate production of major weapon systems for FMS. The pilot program is to expire on January 1, 2020. Lastly, the NDAA called for DOD to revise its acquisition regulations on the use of undefinitized contract actions—actions that authorize contractors to begin work and incur costs prior to reaching final agreement on contract terms, specifications, or price. DOD has the authority to award undefinitized contractual actions for its own procurements as well as for FMS. However, these contractual actions, when used for FMS, were previously exempt from a requirement in the Defense Federal Acquisition Regulation Supplement to be definitized—that is, finalize the terms of the contract—within 180 days or before obligating 50 percent of the estimated contract

price, whichever occurs earlier.⁸ Pursuant to the NDAA, undefinitized contractual actions for FMS acquisitions will now be subject to the same definitization timeframe and obligation requirements as other procurements.

Firm-Fixed-Price Contracts Are Widely Used for FMS but Use of Fixed-Price-Incentive Contracts Is Increasing

Between fiscal years 2007 and 2016, DOD primarily used firm-fixed-price contracts to support FMS requirements. However, in recent years, there has been an increase in the use of fixed-price-incentive contracts for FMS procurements, which is consistent with DOD guidance that has emphasized the use of these contracts. For the 32 FMS cases across the seven acquisition programs that we reviewed, contracting officials used various types of contracts to procure the same item in order to influence better cost outcomes. DOD is in the early stages of implementing the Fiscal Year 2017 NDAA requirement to use firm-fixed-price contracts and is weighing various factors such as how waivers will be reviewed and approved.

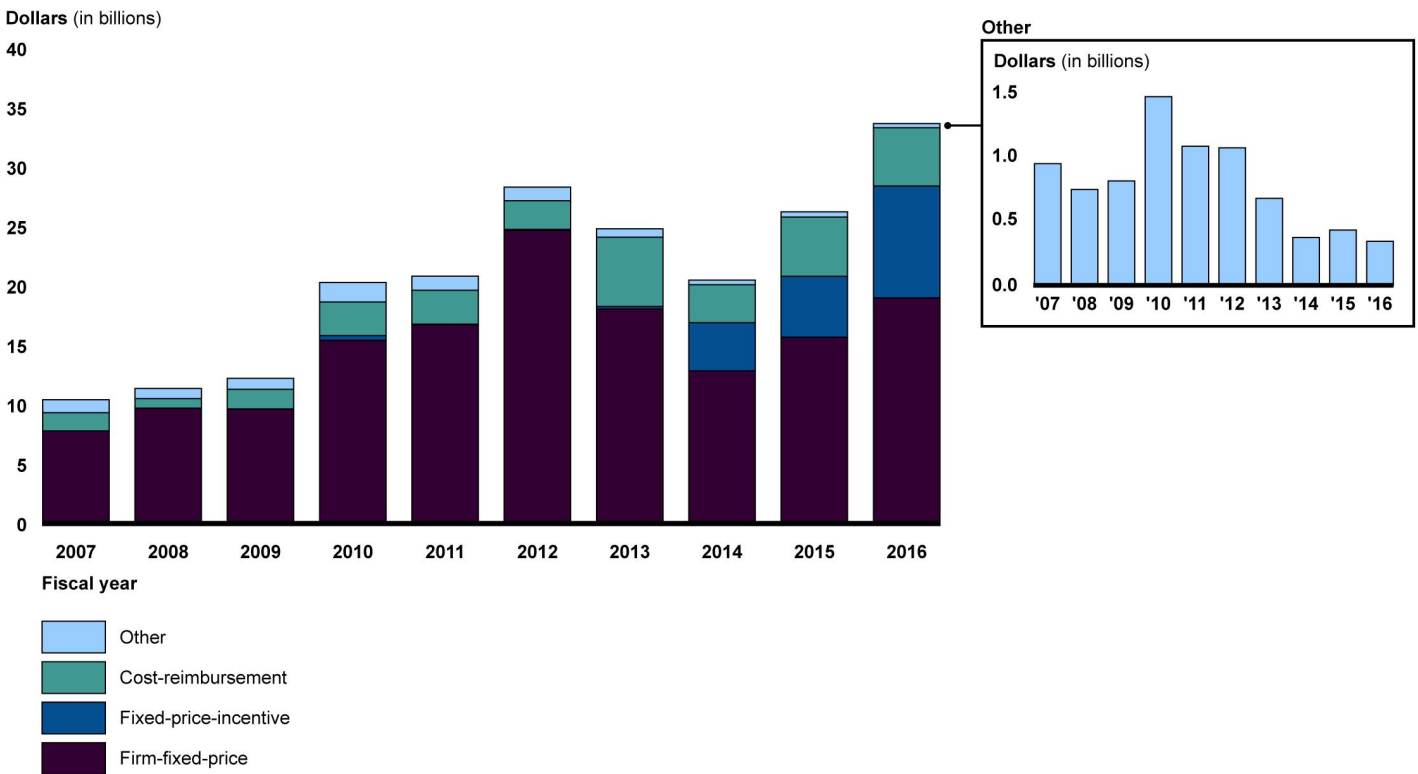
Firm-Fixed-Price Contracts Accounted for Nearly All FMS Procurements but Use of Fixed-Price-Incentive Contracts Has Increased

Over the past 10 years DOD used a mix of contract types to procure defense articles and services on behalf of foreign customers through the FMS program; however, firm-fixed-price contracts were most frequently used, both in terms of number of contracts awarded and dollars obligated. Specifically, of the more than 78,000 FMS contracts awarded to procure a range of products and services, firm-fixed-price contracts accounted for 99 percent of contracts during fiscal years 2007 through 2016. Similarly, when compared to other contract types, firm-fixed-price contracts had the

⁸DFARS 217.7402, 217.7403, and 217.7404-3(a).

highest obligations, ranging from \$7.8 billion to as high as \$24.7 billion during the 10-year period, as shown in figure 3.⁹

Figure 3: Foreign Military Sales Obligations by Contract Types, Fiscal Years 2007 through 2016



Source: GAO analysis of Federal Procurement Data System-Next Generation data for fiscal years 2007 to 2016. | GAO-17-682

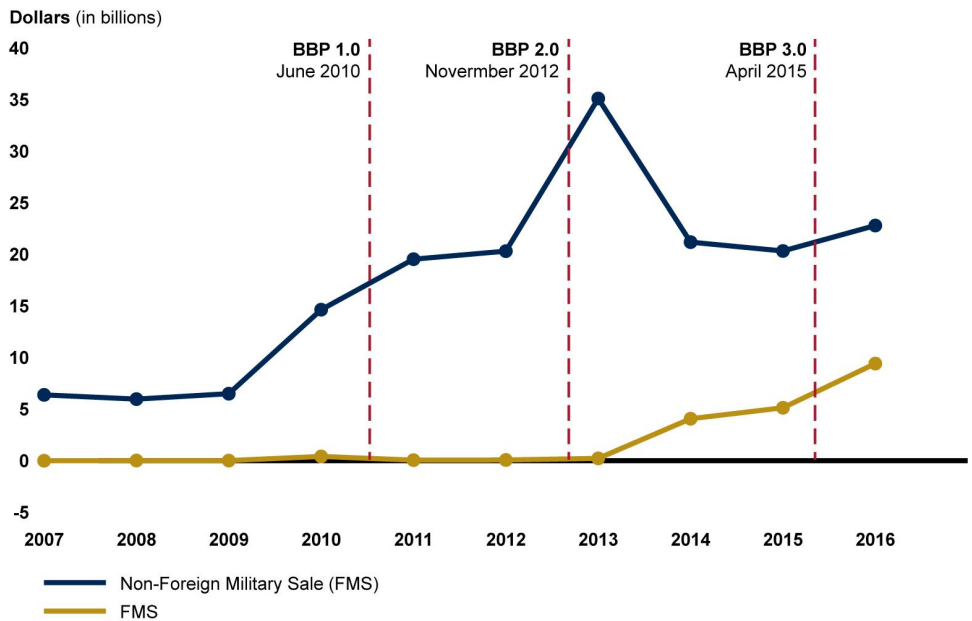
Note: Obligation amounts obtained from FPDS-NG were adjusted for inflation using the Fiscal Year Gross Domestic Product price index.

While fixed-price-incentive contracts accounted for less than 1 percent of overall FMS procurements over the 10-year period, these contract types were among the fastest growing based on obligations. For example, obligations grew from \$0 to \$9.4 billion and the number of fixed-price-incentive contracts grew from none in fiscal year 2007 to 12 contracts in fiscal year 2016. We found that DOD’s increased use of fixed-price-incentive contracts for FMS procurements was similar to that of the department’s increased use of these contracts to meet its own

⁹All FPDS-NG data have been adjusted to represent fiscal year 2016 dollars, and thus include the effects of inflation or escalation. We adjusted for inflation using the Fiscal Year Gross Domestic Product price index.

requirements. We observed the increased use generally followed the issuance of DOD guidance that emphasized the use of fixed-price-incentive contracts. Since 2010, DOD has issued various guidance which pertain to FMS contracts, such as Better Buying Power memorandums, that highlighted the benefits of using fixed-price-incentive contracts as a means to achieve better pricing outcomes. Our analysis showed that since the first issuance of Better Buying Power in 2010, obligations on fixed-price-incentive contracts have been on the rise for contracts awarded to meet FMS and DOD requirements, as illustrated in figure 4 below. While there was a decrease in obligations on fixed-price-incentive contracts awarded for DOD's requirements from fiscal year 2013 to 2014, obligations on these contracts for DOD and FMS have generally increased and consistently stayed above the levels prior to when guidance emphasizing use of fixed-price-incentive contracts, where appropriate, was issued in 2010.

Figure 4: Obligations on Foreign Military Sales (FMS) and Non-Foreign Military Sales Fixed-Price-Incentive Contracts, Fiscal Years 2007-2016



BBP = Better buying power

Source: GAO analysis of Federal Procurement Data System-Next Generation data for fiscal years 2007 to 2016. | GAO-17-682

Note: For a direct comparison of contract type, the analysis is limited to non-foreign military sales obligations on the same products and services categories associated with FMS procurements, such as fixed wing aircraft, guided missiles, and support services. DOD's Office of Defense Pricing and Acquisition Policy issued its Better Buying Power guidance in June 2010 and updated it twice in separate memorandums referred to as Better Buying Power 2.0 and 3.0. All updates address the

appropriate use of fixed-price-incentive contracts. Obligation amounts obtained from FPDS-NG were adjusted for inflation using the Fiscal Year Gross Domestic Product price index.

Selected Programs Used a Mix of Contract Types for FMS to Influence Better Cost Outcomes

For the seven acquisition programs that we reviewed, contracting officers used a mix of contract types to procure various defense articles and services, such as missiles and aircraft, along with related components and engineering services. In each of these programs, a combination of different contract types was used for FMS development or production requirements. For example, three of the seven acquisition programs we reviewed initially awarded a cost-reimbursement contract for development activities and then awarded a fixed-price contract as the procurement transitioned to production. In two of these instances, the items being procured for the foreign country were missiles that had been developed for DOD but required some hardware and software customization to be operational with the foreign customer's aircraft fleet rather than U.S. aircraft.

For example, on an individual FMS case to acquire the Joint Air-to-Surface Standoff Missile (JASSM), the program office first awarded a cost-plus-fixed-fee contract because the scope of work to customize the missile with new hardware and software to meet the foreign customer's needs was broad and requirements could not be sufficiently defined for a firm-fixed-price contract. Despite the customization of the missile in the development phase, production of the missile was largely the same as that for DOD and relied on existing manufacturing processes. Realizing this, contracting officials awarded a fixed-price-incentive contract in the production phase, as the requirement was well-defined and leveraged prior knowledge. On a subsequent FMS case to procure JASSM for a different country that also required similar hardware and software customization, a firm-fixed-price contract was awarded because the program office and contracting officials had gained insight about the costs from the prior FMS case that used a cost-plus-fixed-fee contract. While cost-reimbursement contracts generally pose greater risk to the U.S. government relative to fixed-price contracts, the government only reimburses contractors for reported allowable costs.

In other instances, we found that programs transitioned from firm-fixed-price contracts to fixed-price-incentive contracts for FMS cases procuring systems in the production phase. Consistent with DOD guidance, programs used fixed-price-incentive contracts to incentivize contractor

performance and reduce costs for the U.S. and foreign governments. The following two examples provide some insight into programs' rationale for transitioning to fixed-price-incentive contracts.

- During contract negotiations for a production contract to acquire rocket pods under the Guided Multiple Launch Rocket System (GMLRS) for U.S. and foreign governments, the Army determined, through its analysis of cost data provided by the contractor from a previous contract, that the negotiated prices were substantially higher than actual costs incurred. The Army had previously awarded firm-fixed-price contracts for GMLRS and subsequently discovered the contractor had earned profits ranging up to 42 percent. Under firm-fixed-price contracts, the contractor bears full responsibility for all costs and for the resulting profit or loss, providing maximum incentive for the contractor to control costs. According to program officials, because of this, contractors may factor in additional costs and thus present higher offers to account for potential cost risks. Once Army officials discovered the high profit rates, they switched to a fixed-price-incentive contract for subsequent awards to position the U.S. government and FMS customers to share in any subsequent cost savings.
- Similarly, program officials for the AMRAAM had a history of using firm-fixed-price contracts for decades, but in 2015 converted to fixed-price-incentive contracts because officials believed the contractor would gain efficiency savings as more units were produced and that both U.S. and foreign governments should share in those savings. According to AMRAAM officials, this change in contracting strategy was driven, in part, by their realization that the contractor was able to reduce its production costs during previous firm-fixed-price contracts by bundling purchases of common parts required to manufacture AMRAAM and other types of missiles. Therefore, officials estimated that savings could be gained to reduce the overall AMRAAM unit costs. We found that the ceiling price of AMRAAM missiles was reduced by 40 percent when the program awarded the fixed-price-incentive contract.

DOD Is Weighing Various Factors as It Takes Steps to Implement Legislative Contracting Requirements for FMS

The Fiscal Year 2017 NDAA called for DOD to revise its acquisition regulations to require the use of firm-fixed-price contracts for items procured under the FMS program, unless a waiver is granted or the foreign customer states a preference for an alternate contract type. DOD

is in the early stages of implementing these changes. Officials stated that in doing so it will be desirable for the department's policy changes to retain some flexibilities that allow contracting officers to consider the unique circumstances of FMS cases when selecting a contracting strategy. DOD's revisions to its defense acquisition regulation are subject to its rule-making process and may not be finalized until fiscal year 2018, according to DPAP officials.

In revising its regulations, DOD is considering various factors, including the impact on the FMS acquisition processes, potential adverse effects on pricing, and the process to review and approve waivers. Officials from DPAP and the program offices included in our review told us that restricting contracting strategies to require firm-fixed-price contracts could result in higher costs for the U.S. and foreign governments because it may limit their ability to combine U.S. and foreign requirements onto the same contract. DOD is also weighing whether programs will be required to award separate firm-fixed-price contracts or use a single contract that incorporates different line items and corresponding contract types for the U.S. versus foreign portions. Combining requirements on the same contract can allow the U.S. government and FMS customer to benefit from economies of scale, which materialize in the form of cost savings when additional units are procured. However, a decrease in the number of units procured may have the opposite effect as it reduces economies of scale, thus potentially leading to increased prices. For example, when the Army significantly reduced the number of units it planned to procure of a variant of the GMLRS rocket pods there was a resultant price increase of about 64 percent for the FMS customer because the costs could not be spread over as large a quantity as had been previously estimated. In addition to cost savings, combining U.S. and foreign procurements on the same contract can result in schedule benefits that may not be possible when awarding separate contracts. According to DOD officials, using separate contracts may result in additional administrative burdens to negotiate, definitize, and award FMS contracts separately.

Further, when using firm-fixed-price contracts, the contractor bears the risk if costs exceed the price of the contract. According to DOD officials, contractors may estimate higher costs when negotiating contract price in order to minimize their potential burden should costs increase. Officials added that the increased prices that would be quoted in letters of offer and acceptance may deter foreign customers from pursuing FMS transactions. Recognizing this, DOD is taking steps to explore options to ensure accurate price forecasting; however, these efforts are in the early stages.

Pursuant to the Fiscal Year 2017 NDAA, DOD acquisition programs will be able to request a waiver that permits them to award contracts other than firm-fixed-price for FMS; however, the specifics of the waiver process, including who will review and approve the waivers along with the required documentation, if any, is not yet known. DPAP and program officials told us that the waiver process could also result in additional administrative burden that has the potential to add time to the FMS process, which is a factor they will consider when revising the defense acquisition regulations.

Variety of Factors Can Extend FMS Timeframes and Increase Costs, but Some DOD Programs Use a Checklist to Expedite Requirements Definition

A variety of factors can prolong various phases of the FMS acquisition process, but program officials we spoke to most commonly cited the challenge in defining FMS customer's requirements as a major contributing factor. DSCA has established two performance goals to better manage timeliness in the requirements definition process. The military departments and programs have developed some checklists to facilitate more timely completion of activities in the requirements definition process but one-quarter of the FMS cases we reviewed were managed by programs that do not have a checklist. DOD officials also cited additional factors such as lengthy reviews of letters of offer and acceptance to approve and finalize a sale, unanticipated events in the production phase, and U.S. budget uncertainties.

Challenges in Defining Requirements Can Slow the FMS Process, but Some Programs Use a Checklist to Minimize Delays

Officials from DSCA and the military departments noted that timely definition of the FMS customer's requirement is a common challenge in the FMS acquisition process. Defining the requirement—that is, the materiel and services needed—occurs in the first phases of the FMS process and is the linchpin to enable DOD to deliver the goods and services to FMS customers by the time they need them and at a price they can afford. Consistent with prior GAO findings, officials we spoke

with reiterated that the acquisition acumen of FMS customers varies and some may not have the expertise or experience to identify requirements and present a well-informed letter of request.¹⁰ Without properly defined requirements in the FMS customer's letter of request, DOD does not have the information it needs to develop a letter of offer and acceptance that can be presented to the FMS customer for signature. DOD considers a letter of request actionable when it specifies, among other things, the materiel or service needed, including the hardware, training, and support services applicable to the operational environment in which the military equipment will be used. This level of detail about the FMS customer's requirements enables the military departments to coordinate with the respective program offices or other DOD components at the outset. In addition, specifying these details enables the contracting officer to obtain more accurate pricing data from the contractor and better estimate delivery timeframes. When the circumstances are appropriate, DOD will seek to synchronize FMS purchases with its own purchases of the same item, which, as noted above, can result in cost savings and shorter timeframes to award and execute the contract.

Program officials from six of the seven programs we reviewed noted that letters of request from FMS customers can vary in detail and lack the information needed to draft the letter of offer and acceptance. For example, a request may include the number of missiles desired by the FMS customer but lack information about the training and support services to ensure the foreign government is able to use and maintain the missiles. Delays in responding to the program office's requests for additional information can prolong the overall FMS acquisition for an individual case. Further, program officials noted that, at times, an FMS customer may end up modifying its FMS requirements because of changes in its defense budgets and priorities, which, in turn, may lengthen the FMS process.

DSCA has implemented performance goals for program offices to sufficiently define requirements within specified timeframes with the goal of developing and providing the letter of offer and acceptance as quickly as possible. First, DSCA has instituted a goal for programs to define requirements identified in the letter of request within 20 days so that

¹⁰GAO, *Security Assistance: DOD's Ongoing Reforms Address Some Challenges, but Additional Information Is Needed to Further Enhance Program Management*, [GAO-13-84](#) (Washington, D.C.: Nov. 16, 2012).

programs can begin constructing the letter of offer and acceptance.¹¹ We reviewed 32 FMS cases from across the seven programs in our sample and found that program offices missed the 20-day goal in 14 cases. We found there was wide variation in how long it took programs to achieve a sufficiently defined letter of request, with some being sufficiently defined the same day of receipt and others requiring additional time, up to 476 days. On average, it took all of the programs we reviewed nearly four times longer than the DSCA goal, or about 78 days. DOD officials said that a range of factors explains the causes for the wide variation in the timeframes to define the requirement including (1) the complexity of the acquisition, (2) foreign policy implications, (3) the degree of coordination needed between the program offices and contractor, and (4) changing customer requirements.

Second, DSCA has implemented a broader performance goal that seeks to provide the FMS customer with a letter of offer and acceptance within established timeframes. For this performance goal, referred to as the anticipated offer date, military departments assign a deadline according to DSCA policy for how long it should take for the department to provide the letter of offer and acceptance that ranges from 45 to 150 days after receipt of the letter of request. The amount of time for each case depends on the complexity of the requirement outlined in the request.¹² Of the 32 FMS cases that we reviewed, we found that anticipated offer dates were available for only 28 cases.¹³ Of these 28 cases, we found that most had not presented a letter of offer and acceptance by the goal dates that were assigned when requests were received. Only 5 of the 28 cases we reviewed sent a letter of offer and acceptance to the FMS customer on or before the anticipated offer date. On average, the letter of offer and

¹¹Department of Defense, Defense Security Cooperation Agency, *Security Assistance Management Manual*, C5.1.7.1.2.

¹²Department of Defense, Defense Security Cooperation Agency, *Security Assistance Management Manual*, C5.4.2.1. and C.5.4.2.2. Anticipated offer dates can be amended by the military department if there are extenuating factors in the case development such as funding issues, changing requirements, or first-time purchase of a defense article or service by an FMS customer.

¹³Among the 32 FMS cases that were a part of our sample, only 28 FMS cases had anticipated offer date data available in the Security Cooperation Information Portal. According to program officials, one of the FMS cases did not have an anticipated offer date because that figure did not exist when the case was being developed. In two other cases, the program offices said that an anticipated offer date was not entered in DSCA's system to track FMS cases. For an additional case, GAO was not able reconcile inconsistencies between DSCA and program office data.

acceptance was presented about 68 days after the anticipated offer date. In one instance, the letter of offer and acceptance was presented to the FMS customer as late as 329 days after the target date. According to program officials, a letter of offer and acceptance may be delayed if an FMS customer makes requests that result in changes to a letter of offer and acceptance, such as changes in quantities to be procured or in the payment schedule.

Table 1: Summary of Selected Foreign Military Sales (FMS) Cases Meeting Defense Security Cooperation Agency (DSCA) Goals

FMS case that sufficiently defined requirement within 20 days ^a	Provide a Letter of Offer and Acceptance to FMS Customer by Anticipated Offer Date ^{b,c}
18 of 32 (56.3 percent)	5 of 28 (17.9 percent)

Source: GAO analysis Defense Security Cooperation Agency data. | GAO-17-682

^aDSCA has instituted a goal for acquisition programs to sufficiently define requirements identified in a letter of request within 20 days of receipt of that request.

^bDSCA has instituted a goal for programs to provide a letter of offer and acceptance to the FMS customer by a deadline, known as the anticipated offer date, that ranges from 45 to 150 days from receipt of a letter of request depending on the complexity of the requirement outlined in the request.

^cFour of the 32 FMS cases in our sample did not have available data regarding anticipated offer dates in the Defense Security Assistance Management System or Security Cooperation Information Portal, which are DOD systems used to track FMS case data.

DSCA and the military departments have developed checklists or templates to help facilitate a more efficient requirements definition process. For example, DSCA has developed a generic checklist that outlines the basic information that is required in the letter of request. According to DSCA guidance, other checklists that are unique to individual acquisition programs may be needed to ensure the requirement is fully defined to account for not only the weapon system but also the logistics and support services needed to deliver a complete and sustainable capability to the FMS customer. Accordingly, the military departments have developed a range of checklists, with some from the Air Force and Army available to the public on the Internet.

- The Air Force has developed checklists for specific weapon systems such as missiles, global positioning systems, and various types of aircraft. For example, the AMRAAM program developed a checklist in 2006 that is specific to the program, as illustrated in figure 5.

Figure 5: Notional Foreign Military Sales (FMS) Checklist for Developing Letter of Request to Purchase the Advanced Medium -Range Air-to-Air Missile (AMRAAM)

Foreign Military Sales (FMS) Checklist for Advanced Medium Range Air-to-Air Missile

I. General Information

a. Request for: Acquisition Price and Availability Sole source procurement Amendment

b. Timeframe to accept letter of offer and acceptance mm/dd/yyyy Projected Delivery Date: mm/dd/yyyy

c. Is missile being procured as part of an aircraft case? Yes No

d. Projected flying hours per aircraft per year _____

e. Is missile being procured as part of a multi-weapons case? Yes No

II. Procurement Requirements

a. Does the letter of request include the total number of missiles required? Yes No

b. Have you identified supporting equipment available on-site to support the missile? Yes No

c. Are you requesting a missile warranty? Yes No

d. Have you identified the number of captive air training missiles to be procured? Yes No

e. Have you identified the number of out-year spares? Yes No

f. Will you require additional spares for support equipment? Yes No

g. Have you addressed whether launchers will be needed as part of the FMS case? Yes No

h. Does the letter of request address the number and format of technical manuals? Yes No

III. Integration and Flight Testing

a. Do you plan on conducting weapons integration testing? Yes No

b. If yes, have you addressed the number of tests to be conducted, the test schedule, and location of the test? Yes No

c. Have you addressed the transportation of the test assets? Yes No

d. Do you plan to purchase or lease target drones for any planned testing? Yes No

IV. Training Requirements

a. Does the letter of request contain training requirements? Yes No

b. Specify what training is desired Yes No

- Explosive Ordnance Disposal – Phase I is 9 weeks, Phase II is 15 weeks Yes No
- English language training – total of 10 weeks Yes No
- Pilot training – 5 days Yes No
- General maintenance – 6 days Yes No

c. Is in-country training required? Yes No

d. Is training being requested under a separate letter of request? Yes No

V. Freight Forwarder Requirements

a. Does the letter of request identify any special transportation instructions? Yes No

b. Does your freight forwarder have the required import/export licenses? Yes No

c. Is your freight forwarder registered with the US Department of State? Yes No

Source: GAO adaptation of information from the Air Force Security Assistance Command. | GAO-17-682

- Similarly, the Army has developed generic and 25 system-specific checklists for, among other things, artillery, aviation and missiles, and satellite systems. For example, the Apache program developed a template in 2014 that is used to guide discussions with foreign

governments that are interested in purchasing the helicopter.¹⁴ The template captures items such as maintenance and support services, potential software configurations, and unique country requirements that ensure the procured helicopter provides a complete and sustainable capability. According to officials, the Army is considering the development of training for its security cooperation organization workforce on the use of requirement checklists.

- The Navy has developed a generic checklist and some system-specific checklists, using the Army’s checklists as a template. However, a senior official from the Navy’s International Programs Office said that the checklists have not been widely used yet as the Navy is still determining the best way to disseminate these tools to program offices and other appropriate Navy staff.

In our review of selected FMS cases, we found that more than half of the 32 cases had checklists available for use during requirements definition, but for some cases such tools had not yet been developed. Specifically, 17 of 32 cases had checklists available for use while 15 did not at the time requirements definition began, as seen in table 2. However, programs for 7 of the 15 cases that did not have checklists have since developed such tools.

Table 2: Summary of Checklist Availability for Selected Foreign Military Sales (FMS) Cases

Number of FMS cases where a checklist was available	Number of FMS cases where a checklist was not available but was subsequently developed	Number of FMS cases where no checklist is available
17	7	8

Source: GAO analysis Defense Security Cooperation Agency data. | GAO-17-682

Officials from multiple programs noted that using checklists helped to facilitate quicker requirements development. According to AMRAAM program officials, the use of the checklist developed by the program has helped to reduce the time necessary to define requirements by as much as 60 percent though formal analysis has not been completed. Similarly, GMLRS program officials said that a checklist developed to facilitate procurement of GMLRS rockets and the system that launches them has reduced the time it takes to define requirements by about 30 to 60 days.

¹⁴The Apache tool was developed after the two Apache FMS cases that were part of our review. While the tool was not used for the two FMS cases we reviewed, Apache program officials said that the tool has been used for at least seven later FMS cases.

While Apache program officials did not identify how much time is saved by using a checklist, they said that the tool is designed to capture the unique configuration, production, and other requirements that are not captured by DSCA's generic checklist.

DSCA and the military departments continue to develop initiatives that are in varying stages of implementation to help facilitate the timely definition of FMS requirements. Among its initiatives, DSCA will update the guidance it provides to foreign partners to promote more complete letters of request at the outset of FMS cases. The Air Force has examined FMS requirements changes, among other factors affecting FMS timeframes, and established a goal to reduce the time between when the letter of request is received and when the letter of offer and acceptance is provided to the foreign customer for certain cases. Army officials said they are studying the metrics regarding FMS process timeframes to identify leading indicators for successful outcomes. As part of DOD's reform initiatives, expanding the use of checklists could supplement its overall efforts to improve the timeliness of requirements definition in the FMS process. Existing DOD guidance suggests, but does not require, that program offices use checklists to help facilitate requirements definition. Federal standards for internal controls call for agencies to design responses that reduce the likelihood or magnitude of risks that can impede agency objectives.¹⁵ Program officials noted that various extenuating factors can hinder timely FMS acquisitions; however, they also acknowledged there are benefits to using checklists to expedite requirements definition, which is a key first step in the FMS process. As such, programs may be missing opportunities to realize efficiencies in the FMS process by not using readily available checklists that can help facilitate timely requirements definition.

Delays during FMS Case Reviews May Prevent Synchronization of DOD and FMS Requirements

According to DOD program officials, the reviews conducted by the U.S. and foreign governments after a program office develops a letter of offer and acceptance can be lengthy and may affect a program's ability to synchronize FMS and U.S. procurements. A letter of offer and acceptance that has been prepared by a program office requires review

¹⁵GAO, *Standards for Internal Control in the Federal Government*, [GAO-14-704G](#) (Washington, D.C.: Sept. 10, 2014).

from the relevant military department, State, Congress (known as Congressional notification), and DSCA before being offered to the foreign government for signature.¹⁶ Program officials said that delays in completing DOD's review of the letter of offer and acceptance and in initiating Congressional notification may cause an FMS case to miss program deadlines for placing FMS requirements on an upcoming production contract, potentially resulting in increased unit costs due to reduced economies of scale. In particular, officials said that DSCA delays in notifying Congress of impending sales to FMS customers can delay the overall process to approve the letter of offer and acceptance and places proposed contracting timelines in jeopardy. Based on our analysis of schedule data available for the FMS cases included in our sample, we found that letter of offer and acceptance reviews by the State Department and DSCA for our selected FMS cases took an average of about 18 days once they were submitted by the military department, but in one case took up to 221 days. DSCA officials stated that case complexity may contribute to variation in how long reviews take. Our analysis of schedule data available for complex FMS cases throughout DOD for fiscal years 2011 through 2016 found that it took about 10 days on average for letters of offer and acceptance to be reviewed. DSCA has identified multiple initiatives aimed at improving the efficiency of its FMS case review processes, such as improved data sharing between DSCA and military departments, minimizing the number of reviews that are necessary for FMS cases, and reviewing quality assurance and coordination requirements for processing letters of request and letters of offer and acceptance.

Though officials report that long review periods by FMS customers can result in delays, DSCA has identified an initiative to address this issue. Program officials said that lengthy response times by foreign governments to sign the letter of offer and acceptance may push FMS purchases to the next available production contract, which could result in a different price and schedule. Letters of offer and acceptance are provided to foreign governments with an offer expiration date after which the offer is no longer valid, as the pricing and schedule may change and therefore need to be adjusted. FMS customers accepted letters of offer

¹⁶According to DSCA's, *Security Assistance Management Manual* C5.5.3, Congressional notification is required for FMS letters of offers and acceptance—including any related amendments—if it meets certain dollar thresholds that are set for different procurement categories. Congress has between 15 and 45 calendar days to review submitted documentation prior to when the offer is presented or delivery of defense articles.

and acceptance an average of about 104 days after they were provided. Apache and AMRAAM program officials said that FMS customer delays in signing a letter of offer and acceptance could result in an FMS purchase being pushed to a different production contract because of limited space on planned production lines. FMS requirements for these programs are contracted as letters of offer and acceptance are agreed to and signed by FMS customers. Because of high demand from multiple FMS customers, production capacity may be reached before a particular offer is accepted. In its October 2016 Vision 2020 report, DSCA described an initiative aimed at finding ways to streamline foreign customers' review and acceptance of letters of offer and acceptance in order to prevent delays and cost increases.

Contract Award Delays and Unforeseen Production Issues Are Not Unique to FMS Acquisitions

Program officials from all three military departments said delays in awarding contracts could extend FMS schedules and increase costs and that the use of undefinitized contract actions may reduce schedule risk to FMS cases because they allow for work to start more quickly. Under the DFARS, DOD is authorized to use undefinitized contract actions to permit contractors to begin work immediately when time constraints do not allow for negotiating a contract and defining its terms and conditions.¹⁷ Our analysis of DOD-wide contracting data shows that all three military departments used undefinitized contract actions to support FMS procurements. Two Army programs we reviewed used these contract actions to begin work on contracts that supported FMS and domestic procurements. For example, GMLRS contracting officials said that uncertainty surrounding the fiscal year 2013 and 2014 budgets for U.S. procurements caused delays in defining domestic requirements and prevented the timely award of the production contract that would also support FMS cases. Further, contract awards for both FMS and domestic procurements at Army Material Command may take as long as 700 days, which GMLRS officials stated could result in even longer timeframes for FMS cases. As a result of these circumstances, the GMLRS officials stated the decision was made to use an undefinitized contract action to help them adhere to FMS schedules. Similarly, Apache program officials said that using an undefinitized contract action for production reduced the time to procure helicopters by nearly a year—thereby meeting delivery

¹⁷DFARS Subpart 217.74

dates stated in letters of offer and acceptance—and also helped synchronize purchases by different FMS customers, which in turn resulted in lower prices.

While program offices may find schedule benefits from using undefinitized contract actions, we have previously found that undefinitized contract actions are not a desirable form of contracting, as the government bears the majority of the cost and risk during the undefinitized period.¹⁸ In the FMS cases we reviewed for the Apache and GMLRS programs, contract definitization took between 516 and 1,296 days with as much as 75 percent of the estimated contract price obligated. Though FMS procurements were exempt from requirements to definitize within 180 days or before 50 percent of the estimated contract price has been obligated, the Fiscal Year 2017 NDAA now requires DOD to revise its acquisition regulations to apply these requirements to FMS undefinitized contract actions.¹⁹

Similar to domestic acquisitions of defense systems, FMS acquisitions may experience issues during production that can impact cost and schedule. As our prior work has found, unforeseen performance and management issues during the execution of an acquisition affect cost and schedule for DOD procurements.²⁰ Schedule delays or cost growth for acquisitions may be a result of an unsound business case or honest mistakes and unforeseen obstacles. We found that similar challenges were experienced by programs during the procurement for the FMS cases we reviewed. For example, the initial operating capability for a FMS variant of the JASSM missile was late as a result of testing delays and failures during live fire testing, which collectively has held up delivery. For the AMRAAM program, rocket motor defects identified during production

¹⁸*Defense Contracting: Use of Undefinitized Contract Actions Understated and Definitization Time Frames Often Not Met*, [GAO-07-559](#) (Washington, D.C.: June 19, 2007)

¹⁹DFARS 217.7404-3(a)(1) and (2). Definitization schedules for undefinitized contract actions may be extended past 180 days, but not after the contractor submits a qualifying proposal. The DFARS currently exempts undefinitized contract actions for FMS from these requirements, but the FY2017 NDAA requires undefinitized contract action schedules for FMS to provide for definitization within 180 days. Under DFARS 217.7404-4, undefinitized contract actions may obligate up to 75 percent of the estimated contract price following the submission of a qualifying proposal by the contractor.

²⁰*Defense Acquisitions: Assessments of Selected Weapon Programs*, [GAO-17-333SP](#) (Washington, D.C.: Mar. 30, 2017) has found production issues for multiple programs.

caused FMS delivery dates to be revised. Finally, the Joint Standoff Weapon program reported that FMS deliveries will be missed because of delays in providing government furnished equipment resulting from export controls issues that arose in a separate procurement for warheads. In each of these instances, programs reported that steps were taken to mitigate cost and schedule impacts.

Conclusions

The FMS program is a central component of the U.S. government's efforts to assist foreign governments by providing U.S. military equipment and related services. Over the past decade, DOD and Congress have established various reform efforts designed to expedite the FMS process, yet there is continued concern that the process remains slow. The FMS acquisition process continues to be hindered by insufficiently defined requirements that do not fully articulate the desired equipment, training, and other services and can, from the outset, impede timely delivery to FMS customers. Although checklists, when developed and available for use, help FMS customers and military departments define requirements more efficiently, they have not been developed for all systems that are procured under the FMS program. Using such tools, especially for complex FMS requirements, may increase the potential for DOD to obtain the full complement of information. More importantly, these tools can help ensure DOD is well-positioned, at the outset, to deliver equipment and services to the foreign government within agreed-upon timeframes.

Recommendation for Executive Action

To help increase efficiency when defining FMS requirements to be placed on contract, we recommend that the Secretary of Defense issue department-wide guidance for the military departments and DOD components to expand the use of requirements checklists to develop more comprehensive letters of request for FMS cases.

Agency Comments

We provided a draft of this report to the Department of Defense (DOD) for comment. In its comments, reproduced in appendix II, DOD concurred with our recommendation. DOD also provided technical comments, which we incorporated, as appropriate.

We are sending copies of this report to the appropriate congressional committees and the Secretary of Defense. In addition, the report is available at no charge on the GAO website at <http://www.gao.gov>.

If you or your staff have any questions about this report, please contact me at (202) 512-4841 or makm@gao.gov. Contact points for our Offices of Congressional Relations and Public Affairs may be found on the last page of this report. GAO staff who made key contributions to this report are listed in appendix III.



Marie A. Mak
Director, Acquisition and Sourcing Management

List of Committees

The Honorable John McCain
Chairman

The Honorable Jack Reed
Ranking Member
Committee on Armed Services
United States Senate

The Honorable Bob Corker
Chairman

The Honorable Ben Cardin
Ranking Member
Committee on Foreign Relations
United States Senate

The Honorable Thad Cochran
Chairman

The Honorable Richard Durbin
Ranking Member
Subcommittee on Defense
Committee on Appropriations
United States Senate

The Honorable Lindsey Graham
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The Honorable Patrick Leahy
Ranking Member
Subcommittee on State, Foreign Operations, and Related Programs
Committee on Appropriations
United States Senate

The Honorable Mac Thornberry
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The Honorable Adam Smith
Ranking Member
Committee on Armed Services
House of Representatives

The Honorable Ed Royce
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The Honorable Eliot Engel
Ranking Member
Committee on Foreign Affairs
House of Representatives

The Honorable Kay Granger
Chairwoman

The Honorable Pete Visclosky
Ranking Member
Subcommittee on Defense
Committee on Appropriations
House of Representatives

The Honorable Hal Rogers
Chairman
The Honorable Nita Lowey
Ranking Member
Subcommittee on State, Foreign Operations, and Related Programs
Committee on Appropriations
House of Representatives

Appendix I: Objectives, Scope, and Methodology

The House Report 114-537 that accompanied the National Defense Authorization Act of Fiscal Year 2017 included a provision for GAO to review certain aspects of Department of Defense's (DOD) acquisition process, including contract type selection, to determine their effect, if any, on foreign military sales (FMS).¹ We assessed 1) how the use of firm-fixed-price contracts compares to other contract types awarded for FMS procurements and the reasons they were used and 2) the factors that may contribute to delays and potentially increase costs for FMS procurements.

To address both objectives, we selected a non-generalizable sample of seven FMS programs that used more than one contract type for FMS procurements between fiscal years 2011 and 2015, which represented the most current data available at the time of our analysis, to procure similar items or services. We used procurement data from Federal Procurement Data System-Next Generation (FPDS-NG) and FMS case data from the Defense Security Cooperation Agency's Security Cooperation Information Portal (SCIP) to identify examples from the Air Force, Army, and Navy. Across the seven selected programs, we reviewed 14 contracts that supported 32 individual FMS cases for various countries. We used SCIP data to select pairs of contracts used to procure the similar item or services. In some instances, each contract supported multiple FMS cases. For example, we selected the Advanced Medium Range Air-to-Air Missile (AMRAAM) program because it awarded both firm-fixed-price and fixed-price-incentive production contracts that included procurements for 15 FMS cases. Table 1 below lists the selected acquisition programs that we reviewed.

¹GAO has additional work addressing other aspects of the FMS process including forthcoming reports on DOD's management of the FMS program and the FMS Trust Fund.

Table 3: Sample of Selected Acquisition Programs by Military Department

Military department	Weapon system	Number of contracts and related foreign military sales (FMS) cases
Air Force	AIM-120 C7 Advanced Medium-Range Air-to-Air Missile (AMRAAM)	Two contracts that supported a total of 15 FMS cases
	AGM-158 Joint Air-to-Surface Stand-off Missile (JASSM)	Two contracts that supported two FMS cases
Army	AH-64D/E Apache (AH-64)	Two contracts that supported two FMS cases
	Unitary High Explosive Pods for Guided Multiple Launch Rocket System (GMLRS)	Two contracts that supported three FMS cases
Navy	Joint Standoff Weapon (JSOW)	Two contracts that supported one FMS case
	AIM-9X-2 Block II Tactical Missile (AIM-9X)	Two contracts that supported seven FMS cases
	Moving Map Integration for MH-60R Seahawk (MH-60R)	Two contracts that supported two FMS cases

Source: GAO analysis of Security Cooperation Information Portal and Federal Procurement Data System – Next Generation data | GAO-17-682

For the Navy and Army, we combined SCIP and FPDS-NG data by matching contract numbers contained in both systems to determine the contract types used to purchase specific products and services for FMS. To identify the specific programs for our review, we limited the universe based on complexity of procurements as defined in guidance from the Defense Security Cooperation Agency and determined the specific services and products procured, as defined by the Military Article and Service List identifiers. Using these data points, we looked for instances where fixed-price-incentive contracts and at least one other contract type, such as firm-fixed-price, was used. We limited our selection to contracts between fiscal years 2011 and 2015, which represented the most current and complete data available at the time we selected our sample. Using the contracting office identifications, we determined the Army and Navy commands where multiple contract types for the same item or services were used most frequently and selected programs from these commands. Based on these criteria, we selected the Joint Standoff Weapon and AIM-9X missile programs from the Naval Air Systems Command at Patuxent River, MD and the AH-64 Apache helicopter and Guided Multiple Launch Missile System programs from the Army’s Aviation and Missile Command at Redstone Arsenal, AL.

Because Air Force contract data are not available in the SCIP database, we used a separate methodology to select our sample for this military department. Air Force officials told us that there are no common data points among its financial and contracting systems to link the contract type with FMS case data reported in SCIP. We analyzed FMS obligations data reported in FPDS-NG for fiscal years 2011 through 2015 to determine which Air Force command obligated the most funding on fixed-

price-incentive contracts. From within this command, we narrowed our focus to the contracting locations that obligated more than \$6 million against fixed-price-incentive contracts and that had the most instances of where at least one additional type of contract was used to purchase the same product for FMS customers. We then analyzed all FMS contracts at this contracting location to determine what items, as described in FPDS-NG, were procured for FMS using any combination of at least two types of contract. We used the Electronic Document Access system—an online system that provides access, storage, and retrieval of DOD contract documents—to review the content of all FMS contracts used to purchase these products and services to ensure that items were the same. Based on this selection methodology, we identified AMRAAM and JASSM missile systems from the Air Force Materiel Command’s offices at Eglin Air Force Base as case studies.

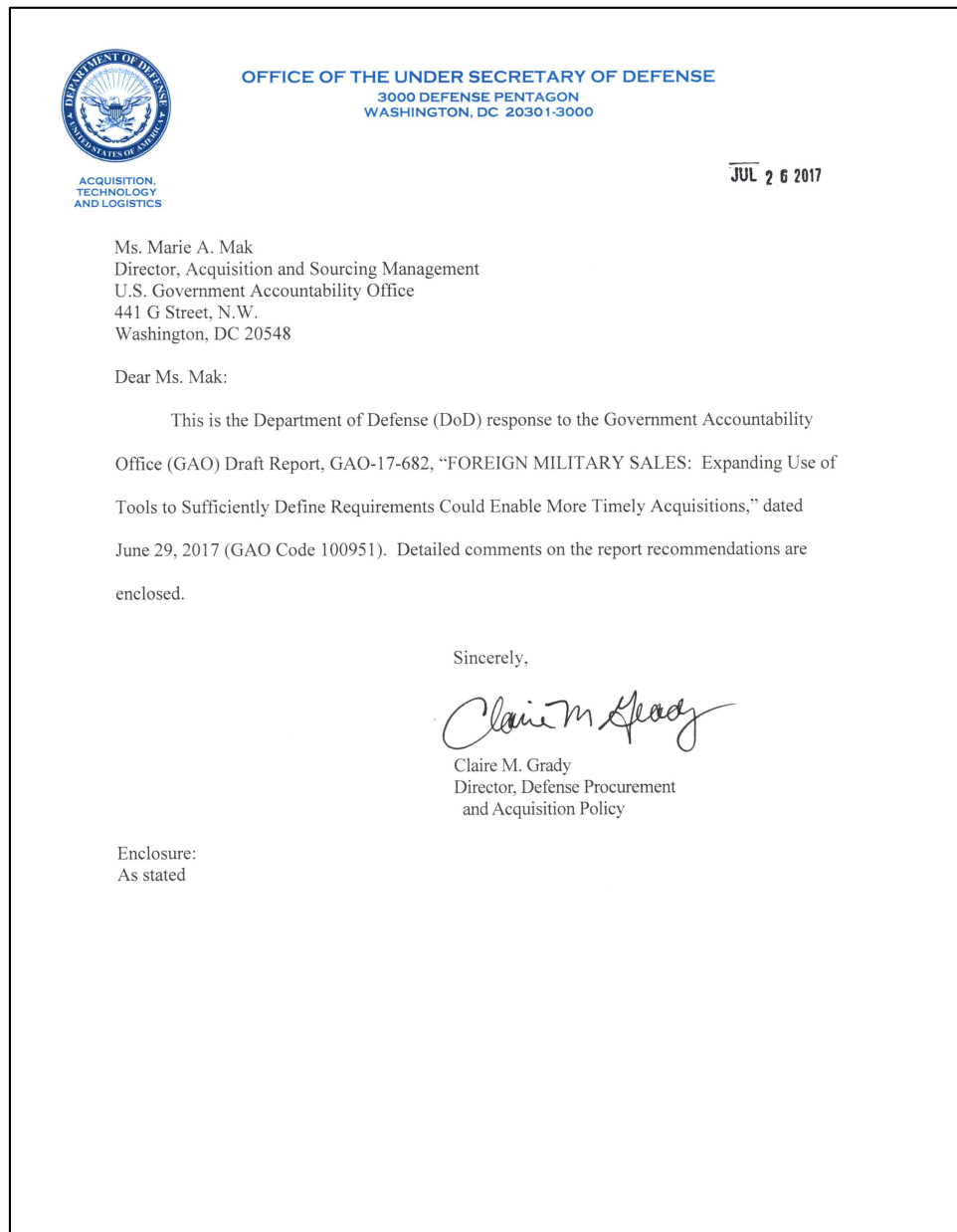
To determine how DOD’s use of fixed price contracts compares to other types of contracts for FMS procurements over the past 10 years, we analyzed FPDS-NG data for fiscal years 2007 through 2016, which represents the most current data available to analyze trends over time. Based on our discussions with officials about the data available as well as our review of contracting documentation and electronic testing for obvious errors and missing values, we determined that the data were sufficiently reliable for the purposes of our reporting objectives. We compared DOD and FMS obligations for various contract types and interviewed officials from the Defense Procurement and Acquisition Policy office to understand the effects of certain DOD guidance, such as the Better Buying Power memorandums, on FMS procurements. We reviewed federal and defense acquisition regulations, DOD-wide and military departments’ acquisition policies, and FMS guidance to identify contracting requirements in place for the procurement of goods and services on behalf of foreign governments. For the programs we selected, we reviewed contract documentation, such as acquisition strategies and determination and finding memorandums, and interviewed cognizant program and contracting officials to determine the reasons why programs use specific types of contracts for FMS procurements. In our discussions with DOD officials, we also discussed the implications of recent legislative requirements to use firm-fixed-price contracts for FMS procurements and the status of DOD’s efforts to implement this requirement.

To identify the factors that may contribute to delays and potentially increase costs for FMS procurements, we analyzed FMS case data reported in SCIP to determine how long it took for selected programs in our sample to define FMS requirements and develop government-to-

government agreements. We interviewed DSCA officials responsible for managing the system and reviewed system documentation to determine that these data were sufficiently reliable for the purposes of our reporting objectives. For each acquisition program and FMS case in our sample, we reviewed contracts, other related procurement documentation, and FMS case data such as letters of request and letters of offer and acceptance, and conducted interviews with program and contracting officials to discuss the challenges that programs faced when procuring items for FMS customers.

We conducted this performance audit from June 2016 to August 2017 in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

Appendix II: Comments from the Department of Defense



**GAO Draft Report Dated June 29, 2017
GAO-17-682 (GAO CODE 100951)**

**“FOREIGN MILITARY SALES: EXPANDING USE OF TOOLS TO SUFFICIENTLY
DEFINE REQUIREMENTS COULD ENABLE MORE TIMELY ACQUISITIONS”**

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

RECOMMENDATION: To help increase efficiency when defining Foreign Military Sales (FMS) requirements to be placed on contract, the Government Accountability Office (GAO) recommends that the Secretary of Defense issue department-wide guidance for the military departments and the Department of Defense (DoD) components to expand the use of requirements checklists to develop more comprehensive letters of request for FMS cases.

DoD RESPONSE: Concur. The Department intends to issue department-wide guidance to request the military departments and DoD components review the Security Assistance Management Manual (SAMM) evaluation criteria in preparing FMS letters of request and to consider developing and implementing tools and resources, including checklists, to assist in the development of more comprehensive FMS requirements.

Appendix III: GAO Contact and Staff Acknowledgments

GAO Contact

Marie A. Mak, (202) 512-4841 or MakM@gao.gov

Staff Acknowledgments

In addition to the contact named above, Candice Wright (Assistant Director), Tom Twambly (Analyst-in-Charge), Emily Bond, Kurt Gurka, Julia Kennon, Zachary Sivo, Leslie Stubbs, and Roxanna Sun made key contributions to this report.

Appendix IV: Accessible Data

Data Tables

Accessible Data for Figure 2: Selected Entities and Their Role in the Foreign Military Sales (FMS) Process

Organization	Assistance request	Agreement development	Acquisition	Delivery	Case closure
Foreign Military Sales Customer	Identifies defense capabilities and refines requirements to be purchased. Submits letter of request (LOR).	Sends signed letter of offer and acceptance (LOA) to implementing agency and provides funds that will be used for payment, or rejects offered LOA.	Receives updates on progress from implementing agency.	Receives manufactured products or services completed. Coordinates transportation of items to destination. Performs export requirements and secures authorizations to transport items.	Participates in financial management reviews, meets with U.S. government entities to resolve closeout issues. After contract and case closeout, receives final bill and excess funds.
Security Cooperation Organization (SCO)	Assists FMS customer in defining and refining requirements prior to LOR. Evaluates LOR. Coordinates the development of the LOR.	Transmits offered LOA to FMS customer.	Maintains case files and responds to FMS customer requests.	May have responsibilities for coordinating certain methods of delivery.	
Defense Security Cooperation Agency (DSCA)	Reviews, evaluates, and approves or disapproves LOR.	Assembles LOA documents using implementing agency provided data. Reviews and approves LOA to be offered. Notifies Congress of potential sale; Congress can enact a joint resolution to reject a sale during the 15 to 45 day review period.	Reviews and approves all LOA modifications.	Reviews and approves all LOA modifications.	Publishes and updates policies for case closure. Final arbiter of case closure issues. Leads various case closure meetings.

Appendix IV: Accessible Data

Organization	Assistance request	Agreement development	Acquisition	Delivery	Case closure
Military Department	Evaluates LOR. Ensures LOR includes sufficient information for LOA. Assigns a case manager to coordinate case development and execution.	Prepares and processes price and availability or LOA data, including price, schedule, and line items. Reviews and approves LOA to be offered after DSCA assembles it. Sends LOA to FMS customer directly or to SCO to offer to FMS customer after DSCA approval.	Seeks proposals from industry. Negotiates and awards a contract. Oversees progress of contractor and provides program management reviews to FMS customer.	Coordinates with FMS customer on transportation plans.	Manages and facilitates record reconciliation with FMS customer and Department of Defense stakeholders.
State Department	Manages and facilitates record reconciliation with FMS customer and Department of Defense stakeholders.	Reviews and approves LOA to be offered. Clears sale documentation for Congressional notification.			

Accessible Data for Figure 3: Foreign Military Sales Obligations by Contract Types, Fiscal Years 2007 through 2016

	Firm-fixed-price	Fixed-price-incentive	Cost-reimbursement	Other
2007	7.786	0	1.534	1.103
2008	9.703	0.011	0.801	0.851
2009	9.637	0.007	1.658	0.917
2010	15.416	0.408	2.821	1.641
2011	16.731	0.049	2.847	1.186
2012	24.686	0.066	2.409	1.151
2013	18.055	0.22	5.816	0.716
2014	12.841	4.062	3.193	0.387
2015	15.683	5.125	4.978	0.442
2016	18.997	9.407	4.901	0.349

Accessible Data for Figure 4: Obligations on Foreign Military Sales (FMS) and Non-Foreign Military Sales Fixed-Price-Incentive Contracts, Fiscal Years 2007-2016

	Non-FMS	FMS
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	Non-FMS	FMS
2007	6.376	-0.008
2008	5.966	0.011
2009	6.49	0.007
2010	14.634	0.408
2011	19.528	0.048
2012	20.308	0.0661
2013	35.103	0.22
2014	21.18	4.062
2015	20.325	5.125
2016	22.791	9.407

Accessible Data for Figure 5: Notional Foreign Military Sales (FMS) Checklist for Developing Letter of Request to Purchase the Advanced Medium-Range Air-to-Air Missile (AMRAAM)

Foreign Military Sales (FMS) Checklist for Advanced Medium Range Air-to-Air Missile

I General Information

Request for: Acquisition Price and Availability Sole source procurement Amendment

Timeframe to accept letter of offer and acceptance mm/dd/yyyy Projected Delivery Date: mm/dd/yyyy

Is missile being procured as part of an aircraft case? Yes No

Projected flying hours per aircraft per year _____

Is missile being procured as part of a multi-weapons case? Yes No

II Procurement Requirements

Does the letter of request include the total number of missiles required? Yes No

Have you identified supporting equipment available on-site to support the missile? Yes No

Are you requesting a missile warranty? Yes No

Have you identified the number of captive air training missiles to be procured? Yes No

Have you identified the number of out-year spares? Yes No

Will you require additional spares for support equipment? Yes No

Have you addressed whether launchers will be needed as part of the FMS case? Yes No

Does the letter of request address the number and format of technical manuals? Yes No

III Integration and Flight Testing

Do you plan on conducting weapons integration testing?

If yes, have you addressed the number of tests to be conducted, the test schedule, and location of the test? Yes No

Have you addressed the transportation of the test assets? Yes No

Do you plan to purchase or lease target drones for any planned testing? Yes No

IV Training Requirements

Does the letter of request contain training requirements?	<input type="checkbox"/> Yes <input type="checkbox"/> No
<i>Specify what training is desired</i>	
Explosive Ordnance Disposal – Phase I is 9 weeks, Phase II is 15 w weeks	<input type="checkbox"/> Yes <input type="checkbox"/> No
English language training – total of 10 weeks	<input type="checkbox"/> Yes <input type="checkbox"/> No
Pilot training – 5 days	<input type="checkbox"/> Yes <input type="checkbox"/> No
General maintenance – 6 days	<input type="checkbox"/> Yes <input type="checkbox"/> No
Is in-country training required?	<input type="checkbox"/> Yes <input type="checkbox"/> No
Is training being requested under a separate letter of request?	<input type="checkbox"/> Yes <input type="checkbox"/> No
V Freight Forwarder Requirements	
Does the letter of request identify any special transportation instructions?	<input type="checkbox"/> Yes <input type="checkbox"/> No
Does your freight forwarder have the required import/export licenses?	<input type="checkbox"/> Yes <input type="checkbox"/> No
Is your freight forwarder registered with the US Department of State?	<input type="checkbox"/> Yes <input type="checkbox"/> No

Agency Comment Letter

Accessible Text for Appendix II: Comments from the Department of Defense

Page 1

OFFICE OF THE UNDER SECRETARY OF DEFENSE

ACQUISITION, TECHNOLOGY AND LOGISTICS

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WASHINGTON, DC 20301-3000

Jul 26 2017

Ms. Marie A. Mak

Director, Acquisition and Sourcing Management

U.S. Government Accountability Office

441 G Street, N.W.

Washington, DC 20548

Dear Ms. Mak:

This is the Department of Defense (DoD) response to the Government Accountability Office (GAO) Draft Report, GA0- 17-682, "FOREIGN MILITARY SALES: Expanding Use of Tools to Sufficiently Define Requirements Could Enable More Timely Acquisitions," dated June 29, 2017 (GAO Code 100951). Detailed comments on the report recommendations are enclosed.

Sincerely,

Claire M. Grady

Director, Defense Procurement and Acquisition Policy

Enclosure : As stated

Page 2

GAO Draft Report Dated June 29, 2017 GA0-17-682 (GAO CODE 100951)

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