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Procurements Involving Foreign Military Sales. B-65731.
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Decision by Elmer B. Staats, Comptroller General.

Contact: Office of the General Counsel; Procurement Law II.

Organization Concerned: Department of Defense.

Authority: Foreign Military Sales and Assistance Act (P.L. 93-189; 87 Stat. 730). International Security Assistance and Arms Export Control Act of 1976; Foreign Military Sales Act (P.L. 94-329; 90 Stat. 738; 22 U.S.C. 2751). (P.L. 90-629; 82 Stat. 1320). Foreign Assistance and Related Programs Appropriations Act [of] 1978 (P.L. 95-148, title II; 91 Stat. 1235). Armed Services Procurement Act of 1947. P.L. 94-273. P.L. 94-502. 31 U.S.C. 725a. 31 U.S.C. 71. 31 U.S.C. 74. 31 U.S.C. 53. 31 U.S.C. 54. 31 U.S.C. 60. 10 U.S.C. 2301. 55 Comp. Gen. 674. 55 Comp. Gen. 675. 57 Comp. Gen. 311. 4 C.F.R. 20. 43 Fed. Reg. 4010. 40 Fed. Reg. 42406. 42 Fed. Reg. 4311. Executive Order 11958. H. Rept. 93-664. H. Rept. 94-1144. H. Rept. 73-1414. S. Rept. 93-189. S. Rept. 90-1632. B-171067 (1971). B-181469 (1974). B-183686 (1975). B-184911 (1976). B-185174 (1976). B-177450 (1977). B-187765 (1977). B-188332 (1977). Defense Acquisition Regulation 1-102. Defense Acquisition Regulation 6-1300. Defense Acquisition Regulation 3-210.2. Defense Acquisition Regulation 6-1307. DOD Instruction 2140. DOD Instruction 2110.29.

In the past, GAO has declined to consider private party complaints concerning procurements made under the Department of Defense foreign military sales program because it perceived that such procurements did not involve the use of appropriated funds. It will now review the propriety of contract awards under this program because it recognizes that appropriated funds are utilized and that, in view of the significant dollar amounts involved, the area is appropriate for review. (NTW)

DECISION

S. South PL-2
**THE COMPTROLLER GENERAL
OF THE UNITED STATES
WASHINGTON, D. C. 20548**

8302

FILE: B-165731

DATE: November 16, 1978

**MATTER OF: Procurements Involving Foreign
Military Sales**

DIGEST:

General Accounting Office (GAO), despite prior decisions holding otherwise, will undertake bid protest type reviews concerning propriety of contract awards under Department of Defense (DOD) foreign military sales (FMS) program. Change in position is based on recognition that appropriated funds are utilized in FMS procurements and that, in view of significant dollar amounts involved, area is appropriate for review. Prior decisions overruled or modified.

The General Accounting Office during the past two years has declined to consider private party complaints concerning procurements made by Department of Defense (DOD) components pursuant to the Arms Export Control Act, formerly known as the Foreign Military Sales Act, 22 U.S.C. § 2751 *et seq.* (1976). This declination has been grounded in the perception that foreign military sales (FMS) procurements do not involve the use of appropriated funds, and thus are not subject to review under our Bid Protest Procedures, 4 C.F.R. Part 20 (1978).

For some time, however, we have been aware that at least some aspects of FMS procurements have been viewed as involving the use of appropriated funds.

See, e.g., Hughes Aircraft Co. v. United States, 534 F. 2d 889 (Ct. Cl. 1976); Graham, "The General Accounting Office and Foreign Military Sales," 19 A.F.L. Rev. 76, 84-7 (1977); 43 Fed. Reg. 4010 (1978). Moreover, the significant growth of FMS (from fiscal year (FY) 1970 sales of \$953 million to FY 1977 sales of \$11.2 billion and an estimated \$13.2 billion for FY 1978), coupled with continuing requests, despite our declining to consider bid protests in the FMS area, that we review FMS procurements, suggest that such procurements are appropriate for review under our general audit authority, cf. 40 Fed. Reg. 42406-07 (1975), as a concomitant to our ongoing audit reviews in the FMS area. See, e.g., our report entitled The Department of Defense Continues to Improperly Subsidize Foreign Military Sales, FGMSD-78-51, August 25, 1978. Accordingly, we have thoroughly reconsidered our position and, after taking into account the views of DOD, have concluded for the reasons which follow that in the future this Office will consider private party complaints in connection with FMS procurements.

Under the FMS program, the President and DOD enter into agreements with eligible foreign governments and international organizations to sell them defense articles and defense services. Sales can be either from DOD stocks or on a cash sale basis whereby the United States Government, in effect, acts as the agent of the buying customer in dealing with the United States selling company. The United States is also authorized under certain circumstances to finance the sales.

Foreign military sales are transacted under authority of Pub. L. No. 90-629, 82 Stat. 1320, October 22, 1968, as amended by the Foreign Military Sales and Assistance Act, Pub. L. No. 93-189, 87 Stat. 730, December 17, 1973, and the International Security

Assistance and Arms Export Control Act of 1976, Pub. L. No. 94-329, 90 Stat. 738, June 30, 1976, codified at 22 U.S.C. § § 2751 et seq. (1976) (the Act). The pertinent provisions of the Act that bear upon the jurisdictional question concerned are sections 22(a), 22(b), and 23 of the Act, which respectively provide:

"§2762. [§22(a)]. Procurement for cash sales
"(a) Except as otherwise provided in this section, the President may, without requirement for charge to any appropriation or contract authorization otherwise provided, enter into contracts for the procurement of defense articles or defense services for sale for United States dollars to any foreign country or international organization if such country or international organization provides the United States Government with a dependable undertaking (1) to pay the full amount of such contract which will assure the United States Government against any loss on the contract, and (2) to make funds available in such amounts and at such times as may be required to meet the payments required by the contract, and any damages and costs that may accrue from the cancellation of such contract, in advance of the time such payments, damages, or costs are due. Interest shall be charged on any net amount by which any such country or international organization is in arrears under all of its outstanding unliquidated dependable undertakings, considered collectively. The rate of interest charged shall be a rate not less than a rate determined by the Secretary of the Treasury taking into consideration the current average market yield on outstanding short-term obligations of the United States as of the last day of the month preceding the net arrearage and shall be computed from the date of net arrearage.

"(b). [§22(b)]. The President may, if he determines it to be in the national interest, issue letters of offer under this section which provide for billing upon delivery of the defense article or rendering of the defense service and for payment within one hundred and twenty days after the date of billing. This authority may be exercised, however, only if the President also determines that the emergency requirements of the purchaser for acquisition of such defense articles and services exceed the ready availability to the purchaser of funds sufficient to make payments on a dependable undertaking basis and submits both determinations to the Congress together with a special emergency request for authorization and appropriation of additional funds to finance such purchases under this Act. Appropriations available to the Department of Defense may be used to meet the payments required by the contracts for the procurement of defense articles and defense services and shall be reimbursed by the amounts subsequently received from the country or international organization to whom articles or services are sold.

"§2763. [§23]. Credit Sales

The President is authorized to finance procurements of defense articles and defense services by friendly foreign countries and international organizations on terms requiring the payment to the United States Government in United States dollars of-

- (1) the value of such articles or services within a period not to exceed twelve years after the delivery of such articles or the rendering of such services; and

(2) interest on the unpaid balance of that obligation for payment of the value of such articles or services, at a rate equivalent to the current average interest rate, as of the last day of the month preceding the financing of such procurement, that the United States Government pays on outstanding marketable obligations of comparable maturity, unless the President certifies to Congress that the national interest requires a lesser rate of interest and states in the certification the lesser rate so required and the justification therefor."

In order to carry out these provisions, the President, by Executive Order No. 11958, January 18, 1977, 42 Fed. Reg. 4311, delegated the responsibility of administering all of section 22(a) and all the functions of section 23, except the certifying of a rate of interest to the Congress as provided for by paragraph (2) of that section, to the Secretary of Defense. Under this grant of authority, the Secretary has established the Foreign Military Sales Trust Fund to manage funds received from foreign customers. See U.S. Department of Defense, Military Assistance and Sales Manual, Pt. III, para. 2b and 3, Change 17, February 1, 1978, and DOD Instructions 2140.1, 2140.3 and 2110.29. Funds deposited into the FMS Trust Fund are required by the terms of 31 U.S.C. § 725s (1970) to " * * * be deposited into the Treasury as trust funds with appropriate title * * *." Section 725s further provides that " * * * all amounts credited to such trust fund accounts are appropriated and shall be disbursed in compliance with the terms of the trust * * *." Pursuant to this section, funds received from foreign customers are deposited in Treasury account 97-11X8242, "Advances, Foreign Military Sales." Funds are then either disbursed directly from the Fund, for contracts that directly cite the Fund as a source of funding, or are transferred from the Trust Fund to a DOD appropriation account and then disbursed.

We first considered the question of our bid protest jurisdiction over FMS procurements under section 22(a), 22 U.S.C. § 2762(a), in Teledynamics Division of AMBAC Industries (Teledynamics), 55 Comp. Gen. 674 (1976), 76-1 CPD 60. The protest concerned the award of a non-competitive contract by the Department of the Navy. The Navy challenged our jurisdiction to render an authoritative decision on the merits of the protest because the contract costs were charged against the Navy's FMS Trust Fund that consisted of payments made by foreign governments. We agreed that we had no jurisdiction in the matter because the contract did not involve payments from appropriated funds:

"From the foregoing record it is sufficiently clear that this contract will not involve payments from appropriated funds. It is well established that this office is without authority to render authoritative decisions with respect to procurements which do not involve expenditure of appropriated funds. B-171067, March 18, 1971. Our bid protest jurisdiction is based upon our authority to adjust and settle accounts and to certify balances in the accounts of accountable officers under 31 U.S.C. 71, 74 (1970). Where we do not have such settlement authority over the account concerned, we have declined to consider protests on the grounds that we could not render an authoritative decision on the matter. See Equitable Trust Bank, B-181469, July 9, 1974, 74-2 CPD 14 and Ralco, Inc., B-183686, May 5, 1975, 75-1 CPD 276." 55 Comp. Gen. at 675.

In Keco Industries, Inc., B-184911, B-185174, June 1, 1976, 76-1 CPD 352, we extended this rationale by refusing to take exception to the award of a contract involving payments from nonappropriated funds merely because appropriated funds may be used by the procuring agency for processing and administering the contract.

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In Consolidated Diesel Electric Company, B-177450, January 6, 1977, 77-1 CPD 7, we further extended our holding in Teledynamics by expressing the view that, even though payments to a contractor under a section 22(a) sales contract were initially made from a United States Army appropriation that later was reimbursed by funds furnished by the foreign customer, this was an insufficient use of appropriated funds to provide us with jurisdiction given the mere incidental and temporary charging of the Army appropriation pending reimbursement.

We reached a similar result in Aerosonic Corporation, B-187765, June 13, 1977, 77-1 CPD 424, where we declined jurisdiction over a protest involving a transaction under section 22(b) of the Act on the ground that " * * * the use of appropriated funds serves merely as a temporary convenience for what is essentially a purchase ultimately paid for from non-appropriated funds * * *."

In Verne Corporation, B-188332, June 2, 1977, 77-1 CPD 386, we declined jurisdiction over a protest involving a sale of defense articles financed pursuant to section 23 of the Act. We stated:

"While in the instant case the United States Government is the nominal contractor, * * * the funds for this procurement are borrowed by the Government of Gabon and will be repaid to the United States Government."

Section 22(b) of the Act authorizes the President (and, by his delegation to the Secretary of Defense, DOD) to use "appropriations available" to DOD to meet payments required by the contracts for the procurement of certain qualifying defense articles and services. The foreign customer is given up to 120 days after the date of billing upon delivery of the article or

rendering of the defense service to reimburse the DOD appropriation account fully. The Act's language clearly makes DOD appropriations available for meeting contract payments; those appropriations represent accounts which are subject to our settlement authority under 31 U.S.C. §71 (1970) and our authority to certify balances in the accounts under 31 U.S.C. §74. Even though there is an eventual reimbursement of those funds by the foreign government, "there can be no question that * * * regular DOD/ * * * appropriated funds were intended to be used, and were so used, in the first instance." Hughes Aircraft Co. v. United States, supra at 909. In Hughes, the Court of Claims expressly held a section 22(b) transaction as one financed with appropriated funds and assumed jurisdiction on that basis. We now believe that the court's position is the better one, and that the temporary use of the appropriated funds should not defeat our jurisdiction.

Accordingly, Aerosonics Corporation, supra, and other decisions relying on the rationale of that case are overruled.

It is less clear that Congress envisioned that United States appropriations would be expended in connection with section 22(a) cash sales. While the section 22(b) delayed payment method authorizes initial outlays from DOD appropriations, section 22(a) requires the foreign customer to provide initial and advance funding. The intent of Congress is that all expenses related to section 22(a) procurements be charged to the foreign customer, U.S. P.L. No. 93-664, 93d Cong., 1st Sess., 46 (1973). Section 22(a), on its face, authorizes the President (and, by his delegation to the Secretary of Defense, DOD) "without requirement for charge to any appropriation or contract authority or otherwise provided" in effect to act as a procurement agent for eligible foreign customers once the foreign customer promises, by means of providing the United States Government with a "dependable undertaking" (1) to pay the full amount of FMS contracts

the buyer assuring the United States Government against any loss on the contract and (2) to make sufficient funds available in advance to meet payments required by the contract and damages and costs that may accrue from the cancellation of the contract.

The first sentence of the present version of Section 22(a) was originally enacted under the Foreign Military Sales and Assistance Act, Pub. L. No. 93-187, § 25(3), 87 Stat. 730, December 17, 1973. The Senate report accompanying the measure explained how the section is to operate:

"Under this authority the U.S. Government, in effect, acts as the agent of the buying country in dealing with the U.S. selling company.

* * * * *

"The principal changes from existing law [section 22 of the Foreign Military Sales Act] are a specific requirement that the arrangements provide for payment by the foreign country of a pro rata base of the administrative expense for the sales program * * *." S. Rep. No. 93-189, 93d Cong., 1st Sess. 15 (1973).

Pub. L. No. 94-329, supra, added the second sentence to section 22(a) providing for charging interest "on any net amount by which any purchasing country or international organization is in arrears under all of its outstanding unliquidated dependable undertakings to finance its procurements, considered collectively." H.R. Rep. No. 94-1144, 94th Cong., 2d Sess 26 (1976) reprinted in [1976] U.S. Code Cong. & Ad. News 1402.

From the foregoing, it is clear Congress envisioned the section 22(a) program to be self-sufficient and to exist without benefit of United States fiscal participation. To assure the fiscal integrity of the

section 22(a) program, moreover, Congress provided in 22 U.S.C. § 2777(a) that cash payments received from foreign customers be available solely for payments to suppliers and refunds to purchases and not for financing credits and guarantees. See S. Rep. No. 90-1632, 90th Cong., 2d Sess. (1968) reprinted in [1968] U.S. Code Cong. & Ad. News 4478.

DOD maintains that we should not exercise bid protest jurisdiction over procurements involving section 22(a) accounts because there is no requirement that DOD use its appropriation accounts as bookkeeping vehicles for collecting funds and making disbursements. DOD states:

"Hence, payments under contracts entered into under authority of section 22(a) legally could be accomplished without the use of either United States appropriation accounts or a United States disbursing officer, i.e., payments could be made directly from a foreign country to a contractor or by use of an intermediary financial institution, by way of letters of credit or otherwise."

However, as indicated above, under DOD procedures funds received from foreign customers under section 22(a) are normally deposited into the FMS Trust Fund, a fund initially established pursuant to 31 U.S.C. § 725s (1970) as amended by Pub. L. No. 94-273 and Pub. L. No. 94-502, 31 U.S.C.A. 725s (1978 Supp.). That section provides, in pertinent part:

"The funds appearing on the books of the Government and listed in subsections (b) [sic] and (c) of this section shall be classified on the books of the Treasury as trust funds. All moneys accruing to these funds are hereby appropriated, and shall be disbursed in compliance with the terms of the trust. Hereafter moneys received by the Government as trustee analogous to the funds named in * * * this section, not otherwise herein provided for, * * * shall likewise be deposited into the Treasury as trust funds with appropriate title and all amounts credited to such

trust-fund accounts are hereby appropriated and shall be disbursed in compliance with the terms of the trust * * *."

The House Report on the measure that became 31 U.S.C. § 725a explained that even though "the moneys are not Government moneys, and in no way enter into the fiscal program of the Government, * * *" the provision was constitutionally necessary because "[o]nce moneys are covered into the Treasury, regardless of the nomenclature that may be applied to the account in which they are deposited, they are bound by the constitutional inhibition that 'no money shall be drawn from the Treasury but in consequence of appropriations made by law.'" H.R. Rep. No. 1414, 73d Cong., 2d Sess. 11 (1934).

Thus, in a technical sense, amounts in the FMS Trust Fund are appropriated funds, even though they are not annually appropriated by Congress and not subject to direct Congressional control. Cf. Fortec Constructors, 57 Comp. Gen. 311 (1978), 78-1 CPD 153. 1/

1/ It should be noted that we do not consider the FMS Trust Fund analogous to the commissary surcharge funds discussed in Fortec. In Fortec, we considered the surcharge to be a continuing appropriation established for the purpose of generating funds for commissary construction. The funds involved in Fortec are properly characterized as a kind of Federal Fund Account in which the Government credits receipts which it collects, owns, and uses solely for its purposes. Comptroller General, Terms Used in the Budgetary Process, 15 (PAD-77-9 July 1977). In contrast, amounts deposited in trust funds are collected and used by the Federal Government for carrying out specific purposes and programs according to the terms of a trust agreement or statute. Id., at 15. Amounts deposited into the FMS Trust Fund are, in reality, foreign customers' funds that are administered by the United States Government only in a fiduciary capacity.

Moreover, given the current high dollar level of annual FMS procurements, we believe this is an area which should be reviewed under the authority of 31 U.S.C. §§ 53(a), 53(c), 54 and 60 (1970). The importance of review in this area is pointed up by our recent efforts which have resulted in significant findings. See, for example, our reports Loss of Accounting Integrity in Air Force Procurement Appropriations, FGMSD-77-81, November 1, 1977 and The Department of Defense Continues to Improperly Subsidize Foreign Military Sales, supra.

Therefore, our Office in the future will review, upon request of prospective contractors and other interested parties, the propriety of awards and proposed awards made by DOD personnel acting under authority of section 22(a) of the Act. Teledynamics and the line of cases resulting from it are modified accordingly.


We find little impediment to reviewing section 23 transactions. Section 23 of the Act is used to provide credit financing of the procurement of military items by foreign countries on credit terms of up to 12 years. According to DOD, there is no such thing as a section 23 "sale":

"Contrary to popular misconception, we do not make credit sales under section 23. A credit 'transaction' under section 23 is in fact a separate agreement involving a credit or loan agreement substantially identical in form to those used by commercial banks. This agreement is separate and apart from the purchase arrangement which may be an FMS sale under section 21 [purchase from DOD stock] or section 22 or a direct sales contract between the borrowing country and the United States supplier. When the borrowing country is billed for payments due as a result of such sales, it is that country's option

either to request a disbursement from the section 23 credit agreement or to provide its own funds or a mix of both."

It is clear that a section 23 credit agreement involves use of funds, specifically appropriated by Congress to finance credit sales. See Foreign Assistance and Related Programs Appropriations Act, 1978, Pub. L. No. 95-148, Title II, 91 Stat. 1235. Thus, just as section 22(b) transactions are subject to review because appropriated funds are involved in short-term financing, sales financed under section 23 also are subject to review. Moreover, given our decision to review both 22(a) and 22(b) procurements, it is of no relevance, insofar as our review authority is concerned, that it may not be known during the contract formation stage if the contract is to be funded by moneys made available pursuant to the section 23 credit arrangement. Verne Corporation, supra, is overruled.

Finally, we point out that one question concerning our reviews of FMS procurements has been the applicability of the Armed Services Procurement Act of 1947, 10 U.S.C. 2301 et seq. (1976) and the Armed Services Procurement Regulation/Defense Acquisition Regulation (ASPR/DAR) to those procurements. The ASPR/DAR, however, now explicitly provides that it is applicable to FMS procurements. See ASPR/DAR 1-102, 6-1300 et seq., particularly 6-1302. Although the regulation provides a specific exemption for FMS procurements from the general requirement for competition, see ASPR/DAR 3-210.2 (xviii) and 6-1307, allowing sole source contracting at the request of the foreign government, the overall applicability of the regulatory provisions governing DOD's appropriated fund procurements provides uniform standards for our reviews.


Comptroller General
of the United States