



September 2019

FOREIGN MILITARY SALES

DOD Should
Strengthen Oversight
of Its Growing
Transportation
Account Balances

GAO Highlights

Highlights of [GAO-19-678](#), a report to congressional committees

Why GAO Did This Study

The FMS program is one of the primary ways the U.S. government supports its foreign partners, by annually selling them billions of dollars of items and services. According to DOD, the FMS program is intended to operate on a “no profit, no loss” basis, with purchasers not charged excessive fees and fee revenue covering operating costs. Foreign partners can arrange for their own transportation of FMS items or pay DOD a transportation fee to cover the costs of DOD transporting them. The fees are collected into transportation accounts in the FMS Trust Fund.

House Report 114-537 and Senate Report 114-255 included provisions that GAO review DSCA’s management of FMS fees. This report examines (1) the balances of the FMS transportation accounts for fiscal years 2007 through 2018, (2) DSCA’s management oversight of the accounts, and (3) DSCA’s processes for setting transportation fees. GAO analyzed DOD data and documents, and interviewed DOD officials.

What GAO Recommends

GAO is making 10 recommendations to DOD, including six recommendations to strengthen DSCA’s oversight of the transportation accounts—such as by clarifying internal guidance—and four recommendations to improve its transportation fee setting processes. DOD concurred with all of the recommendations and identified actions it plans to take to address them.

View [GAO-19-678](#). For more information, contact Jason Bair at (202) 512-6881 or BairJ@gao.gov.

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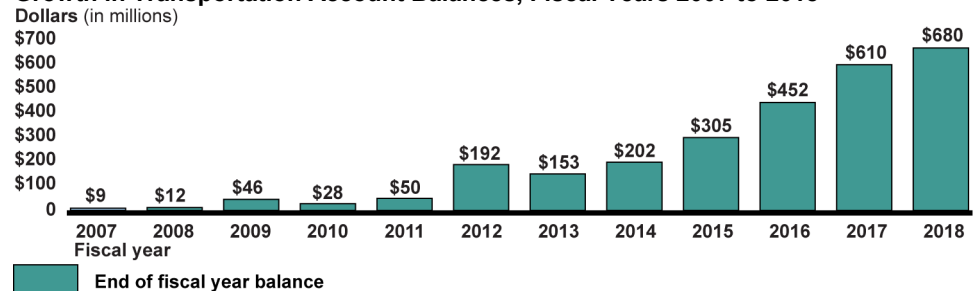
FOREIGN MILITARY SALES

DOD Should Strengthen Oversight of Its Growing Transportation Account Balances

What GAO Found

Fees charged by the Department of Defense (DOD) for the transportation of defense items sold through the Foreign Military Sales (FMS) program are intended to approximate DOD’s transportation costs over time. However, GAO found that the FMS transportation accounts accrued a combined balance of \$680 million by the end of fiscal year 2018. Much of the growth occurred from the end of fiscal year 2011 through fiscal year 2018, when the account grew by approximately \$630 million.

Growth in Transportation Account Balances, Fiscal Years 2007 to 2018



Source: GAO analysis of Department of Defense data. | GAO-19-678

The Defense Security Cooperation Agency (DSCA) has developed limited management oversight guidance for the FMS transportation accounts, which has contributed to the substantial balance growth. DSCA internal guidance requires daily and annual reviews of the accounts to monitor for significant changes in account balances and to ensure the accounts maintain a “healthy” level. However, internal guidance does not define a significant change or “healthy” level, such as a target range for the account balances. This has led to inconsistent reviews and limited oversight of the recent balance growth. DSCA also has no internal guidance on how to perform certain aspects of its annual reviews or what information to include in the resulting reports. As a result, DSCA officials have produced reports with incomplete information, such as on the causes for trends in the account balances, undermining DSCA management’s ability to make informed decisions about the accounts.

DSCA’s processes for setting the FMS transportation fee do not ensure that aggregate fees approximate aggregate costs. For its transportation fee rate reviews, DSCA sends requests to the military departments for historical cost and fee data that lack specificity, such as on timeframes, sampling methodology, and data sources. As a result, DSCA has analyzed data that are not timely or systematically sampled. In addition, military department officials reported difficulty providing the requested data in part because DSCA’s guidance did not specify data sources. Consequently, for the most recent review, Air Force and Navy were unable to find sufficient matching cost and fee data for DSCA to consider them usable. Further, DSCA has established no goals for rate reviews and has no written procedures to follow in performing them. These factors together contributed to recent growth in the FMS transportation account balances and will continue to hinder DSCA’s ability to make appropriate rate-setting decisions moving forward.

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Abbreviations

BPC	Building Partner Capacity
DFAS	Defense Finance and Accounting Service
DIFS	Defense Integrated Financial System
DOD	Department of Defense
DSCA	Defense Security Cooperation Agency
DTS	Defense Transportation System
FMS	Foreign Military Sales
MICP	Managers' Internal Control Program
State	Department of State
TRANSCOM	U.S. Transportation Command

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September 24, 2019

Congressional Committees

The Foreign Military Sales (FMS) program is one of the primary ways the U.S. government supports its foreign partners, by annually selling them billions of dollars of defense items and services. From fiscal year 2007 to 2018, these sales totaled \$472 billion. The Department of State (State) and several components of the Department of Defense (DOD) share responsibility for the program, including the Defense Security Cooperation Agency (DSCA), which administers the program. To cover the costs of operating the FMS program, DOD charges purchasers certain overhead fees, including a transportation fee to cover any costs to DOD of transporting items. Such transportation fees are collected into a series of transportation accounts in the FMS trust fund.¹ According to DOD, the FMS program is intended to operate on a “no profit, no loss” basis, meaning that purchasers should not be charged excessive fees and fee revenue should cover the program’s operating costs.² The fee DOD charges the purchaser for each individual shipment need not equal DOD’s costs for transporting that individual shipment, but DOD aims to set fees such that the total amount of fees paid by all FMS purchasers approximately equals the costs to DOD for all shipments over time, according to DOD officials. Setting fees accordingly should result in relatively low balances in the FMS transportation accounts. Our 2018 review of other FMS overhead fee accounts found that DSCA had allowed those account balances to grow substantially in recent years due in part to weaknesses in DSCA’s management oversight.³

¹The FMS trust fund is used to account for payments received from purchasers and disbursements made to implement the FMS program.

²The Arms Export Control Act authorizes the FMS program and, as delegated, authorizes DOD to sell defense services from DOD and Coast Guard stocks to any eligible country or international organization if such country or international organization agrees to pay, “in the case of the sale of a defense service, the full cost to the United States Government of furnishing such service.” 22 U.S.C. § 2761(a)(1)(C). According to DSCA, DOD’s transportation of FMS goods for purchasers is a service falling under this provision.

³GAO, *Foreign Military Sales: Controls Should Be Strengthened to Address Substantial Growth in Overhead Account Balances*, [GAO-18-401](#) (Washington, D.C.: May 10, 2018).

House Report number 114-537⁴ and Senate Report number 114-255⁵ include provisions for us to, among other things, review DSCA's management and use of fees and to determine whether these fees are generating excess funds.⁶ This report examines (1) the balances maintained in the FMS transportation accounts for fiscal years 2007 through 2018, (2) the extent to which DSCA established and implemented policies and procedures to help ensure management oversight of the transportation accounts, and (3) the extent to which DSCA processes for setting transportation fee rates ensure that the rates are set appropriately.

To examine the balances of the FMS transportation accounts, we analyzed fiscal year 2007 to 2018 account collections, expenditures, and balance data maintained by the Defense Finance and Accounting Service (DFAS) and reviewed related DOD documentation. We did not conduct any independent testing of these data to determine whether these amounts were based on correct payments made toward accurate billings, and instead we reviewed the data in the aggregate and interviewed DFAS and DSCA officials to assess their reliability. We determined these data to be sufficiently reliable for reporting on the overall collections, expenditures, and balances of the individual accounts.

To assess the extent to which DSCA established and implemented policies and procedures to help ensure management oversight of the FMS transportation accounts, we reviewed DSCA procedures and compared those to DSCA documentation of how they implemented those procedures, and to federal internal control standards.⁷ We focused on management oversight processes related to the overall account balances,

⁴H. Rept. No. 114-537 at 240. This House Armed Services Committee report accompanied H.R. 4909, a bill to authorize appropriations for fiscal year 2017 for military activities of the Department of Defense and for other purposes.

⁵S. Rept. No. 114-255 at 228. This Senate Armed Services Committee report accompanied S. 2943, which was enacted as the National Defense Authorization Act for Fiscal Year 2017.

⁶We have an ongoing review that focuses on DSCA's and the Defense Finance and Accounting Service's (DFAS) financial oversight of the collection and use of these fees. We also have issued two prior reports on DSCA's oversight of the FMS administrative fee and contract administration services fee: [GAO-18-401](#) and GAO, *Foreign Military Sales: Financial Oversight of the Use of Overhead Funds Needs Strengthening*, [GAO-18-553](#) (Washington, D.C.: July 30, 2018).

⁷GAO, *Standards for Internal Control in the Federal Government*, [GAO-14-704G](#) (Washington, D.C.: September 2014).

instead of individual transactions that would involve financial oversight. We interviewed DSCA officials on their implementation of the oversight procedures and DFAS officials about some of the reporting that DSCA reviews. We also analyzed trends in the transportation accounts to assess DSCA's conclusions in its annual reports regarding these accounts.

To assess the extent to which DSCA processes for setting transportation fee rates ensure that the rates are set appropriately, we reviewed DOD documentation related to all reviews of the FMS transportation fee rates that DSCA initiated from fiscal year 2007 to 2018. We interviewed DSCA, DFAS, and military department officials about their roles in the rate review processes and related data. We also reviewed internal guidance and interviewed DOD officials regarding the process of determining estimated actual transportation prices to be charged for transporting certain items. We took these steps to compare DSCA's implementation of these processes with DSCA guidance and federal standards, including the Statement of Federal Financial Accounting Standards No. 4 and federal internal control standards.⁸

We conducted this performance audit from May 2018 to September 2019 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

FMS Mission and Benefits

The FMS program is intended to strengthen the security of the United States and partner countries. To accomplish this mission, DOD sells a variety of types of items and services to foreign partners. These sales can range from fighter jets and integrated air and missile defense systems to combat helmets and training on the use of items. (See figure 1.)

⁸[GAO-14-704G](#).

Figure 1: Examples of the Types of Defense Items and Services Sold under the Foreign Military Sales Program



Source: U.S. Air Force photo by Master Sgt. Russ Scalf (top left image); U.S. Navy photo by Chief Mass Communication Specialist Keith W. DeVinney (top right image); U.S. Army photo by Capt. Daniel Parker (bottom left image); New Jersey National Guard photo by Mark C. Olsen (bottom right image). | GAO-19-678

Note: This figure shows examples of the types of defense items and services that may be sold under the Foreign Military Sales (FMS) program, but these exact items and services may not have been sold through the FMS program.

According to DOD and State officials, FMS provides multiple benefits to foreign governments and the U.S. government. Foreign governments that choose to use FMS rather than direct commercial sales receive greater assurances of a reliable product, benefit from DOD's economies of scale, improve interoperability with the U.S. military, and build a stronger relationship with the U.S. government.⁹ From the U.S. perspective, FMS expands the market for U.S. businesses and contributes to foreign policy and national security objectives.

⁹Through direct commercial sales, foreign governments can contract directly with a U.S. firm without the assistance of the U.S. government.

Agency Roles and Responsibilities

While State reviews and approves FMS purchases, DOD is responsible for program implementation. The responsibilities of DOD components vary:

- **DSCA:** DSCA is responsible for administering the FMS program for DOD, including overseeing the FMS transportation accounts' operations and balances. DSCA also sets policies for the FMS process, including for how FMS-purchased items can be transported and how DOD will calculate the fees purchasers will pay to reimburse DOD for any costs of transporting the items.
- **DFAS:** DFAS provides DSCA's accounting services for FMS and is responsible for accounting, billing, disbursing, and collecting funds for the FMS program.
- **Military departments:** The Departments of the Air Force, Army, and Navy are the primary DOD agencies that coordinate with purchasers to prepare and execute FMS agreements, including planning transportation, if necessary.
- **U.S. Transportation Command (TRANSCOM):** TRANSCOM supports transportation planned by the military departments to be conducted through the Defense Transportation System (DTS), which consists of military and commercial resources. Although FMS shipments may receive transportation support through TRANSCOM headquarters, the primary TRANSCOM components providing FMS transportation are the Military Surface Deployment and Distribution Command, which provides defense transportation by sea, rail, or highway, and the Air Mobility Command, which provides defense transportation by air.¹⁰ Contracts between TRANSCOM and private transportation service companies can provide additional commercial resources through DTS. DFAS processes bills to reimburse the TRANSCOM components and private transportation service companies for the costs of performing these transportation services.

FMS Funding, Transportation, and Fee Options

Foreign partners who purchase items and services through the FMS program may use their own funds or, if provided, U.S. funds, such as grants or loans provided through Foreign Military Financing. In addition, some FMS purchases are made using funds appropriated to DOD, State, or other U.S. government agencies for Building Partner Capacity (BPC)

¹⁰The Military Sealift Command within TRANSCOM also provides a subset of FMS transportation via sealift.

programs. These programs purchase items or services for foreign partners through FMS.

Foreign partners and BPC programs have different options available to them for transporting items they purchase through FMS. With the exception of certain hazardous or sensitive items that must be transported via DTS, foreign partners have the option to arrange for their own transportation of FMS items they purchase, such as using a freight forwarder, for all or part of the transportation needed to reach the final destination. On the other hand, BPC programs use DTS to move all their FMS purchases.

There are two ways DOD calculates the fees it charges FMS purchasers to use DTS that lead to collections into the FMS transportation accounts.¹¹

- **Percentage of price.** DOD most commonly calculates the FMS transportation fee using a percentage rate that is applied to the price of the item. The percentage rate varies depending on the extent of the U.S. government's responsibility for transporting the items purchased, such as whether the U.S. government will transport the items to their final destination or to an intermediate destination. As seen in table 1, since fiscal year 2007, DSCA changed the rates in fiscal years 2009 and 2018. Over the full period, the transportation fee has been as high as 22.25 percent of purchase price, or as low as 2.75 percent, depending on where purchasers want to take custody of their items.
- **Price per item.** DOD may instead charge the FMS purchaser an estimated transportation price per item for certain types of items, such as those containing sensitive or hazardous materials.

¹¹FMS purchasers may instead choose to pay for the actual cost of their use of DTS. When this is done, the purchaser's country account within the FMS trust fund reimburses TRANSCOM directly for the costs of transporting the items. We did not review this method of payment for FMS transportation since it does not involve the FMS transportation accounts.

Table 1: Foreign Military Sales Transportation Fee Percentage Ranges, Fiscal Years 2007 to 2019

Date Range	Transportation Fee Percentages
October 2006 ^a -July 2009	3.75-16.25
July 2009-August 2018	3.75-22.25
August 2018-September 2019	2.75-14.75

Source: GAO presentation of Department of Defense information. | GAO-19-678

^aThis percentage range was also in effect prior to October 2006.

Notes: DOD applies the full transportation fee percentage rate for orders to purchase an undefined quantity of an item, called blanket orders. For orders of defined quantities of items, DOD only charges the full transportation fee rate to the first \$10,000 of the item price and multiplies the remaining price by 25 percent of the fee rate to determine the total transportation fee for that item.

Structure and Use of the FMS Transportation Accounts

Eight transportation accounts within the FMS trust fund are used to hold transportation fees collected from FMS purchasers and to pay FMS transportation bills. In aggregate, we refer to these as the combined FMS transportation accounts:

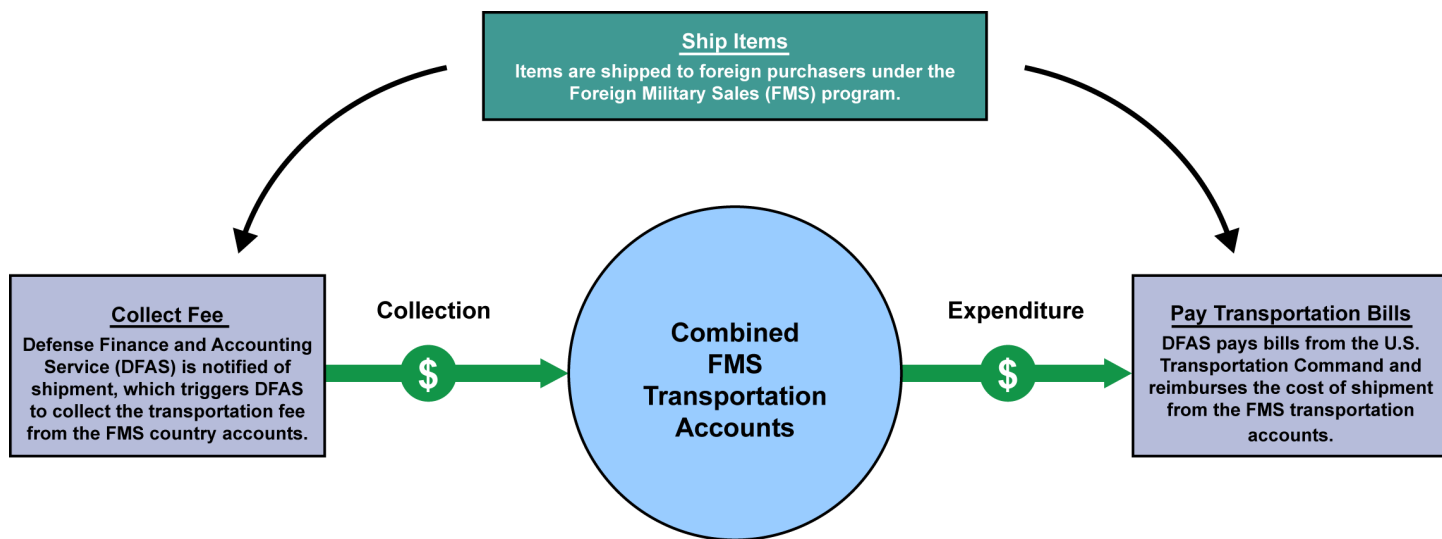
- **Main account.** One main account holds transportation funds for all foreign partner purchasers and smaller BPC programs.
- **BPC accounts.** Seven segregated accounts hold transportation funds for certain larger BPC programs, such as the Afghan Security Forces Fund and the Iraq Security Forces Fund. DSCA created the first four BPC accounts in fiscal year 2012, one in fiscal year 2015, and two more in fiscal year 2018.

Individual shipments trigger collections into and expenditures from the FMS transportation accounts.¹² As shown in figure 2, after DOD ships an item and DFAS is notified of that shipment, DFAS moves the amount of the related transportation fee from the country account or BPC program account into the related transportation account and records the amount as a collection. Once DFAS collects funds into a FMS transportation account, funds are generally no longer segregated or tracked by their

¹²Prior to this, FMS purchasers pay for these fees and other aspects of their FMS cases based on quarterly bills. The purchasers' funds are first held in segregated accounts within the FMS trust fund, which are called either country accounts or BPC program accounts. Each such account pertains either to a foreign partner purchaser or to a specific appropriation authority, appropriation account, or purpose for a BPC program, which allows BPC program funds to be tracked.

originating country or BPC program account.¹³ DFAS receives monthly bills from TRANSCOM that include the costs for FMS transportation, which DFAS pays out of the main transportation account, recording the amount paid as an expenditure. For FMS shipments associated with the seven larger BPC programs, the main account is then reimbursed from the appropriate BPC transportation account.

Figure 2: Process of Collecting Fees into and Expending Funds from the Foreign Military Sales Transportation Accounts



Source: GAO analysis of Department of Defense documents. | GAO-19-678

The FMS Transportation Account Balance Has Grown Substantially

Although aggregate FMS transportation fees are expected to approximate costs over time, we found that the combined FMS transportation account balance grew by over 1,300 percent from fiscal years 2007 to 2018. The ending balance for fiscal year 2018 was \$680 million. Collections and expenditures for the account fluctuated from year to year, but collections have outpaced expenditures since 2014, particularly for the main transportation account, which has grown more quickly than the combined seven BPC accounts.

¹³In fiscal year 2018, the year the most recent two BPC transportation accounts were opened, DFAS began, at DSCA's request, to track funds paid into them by their originating BPC program account.

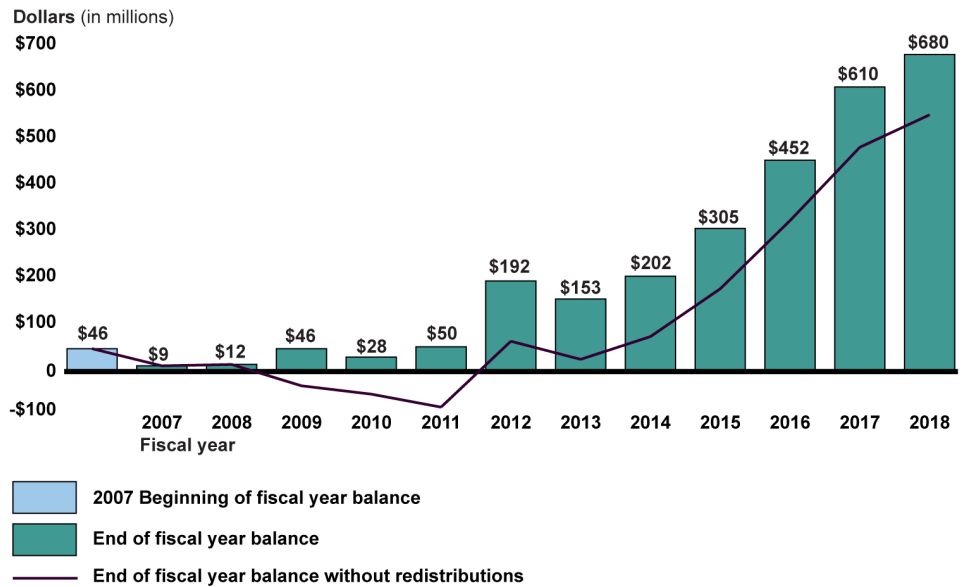
The Combined FMS Transportation Account Balance Grew More Than 1,300 Percent from Fiscal Years 2007 to 2018

The combined balance of the eight FMS transportation accounts grew substantially from the beginning of fiscal year 2007 through the end of fiscal year 2018—from \$46 million to \$680 million, or by 1,378 percent.¹⁴ As shown in figure 3, much of that growth occurred from the end of fiscal year 2011 through fiscal year 2018, during which time the account grew by approximately \$630 million. This substantial recent balance growth was in contrast to balance activity from fiscal years 2007 to 2011, when the collections into the account more closely approximated the expenditures from the account. In fact, the FMS transportation account was at risk of insolvency starting in fiscal year 2009. In response, DSCA redistributed \$80 million in fiscal year 2009 and \$50 million in fiscal year 2011 from the FMS administrative fee account to the main FMS transportation account to ensure it contained sufficient funding to pay transportation bills.¹⁵ If not for the redistributions between accounts, the transportation account may have been unable to disburse payments from the account, for at least some parts of fiscal years 2009, 2010, and 2011.

¹⁴These figures are presented in nominal terms, without adjustment for inflation.

¹⁵The FMS administrative fee account is intended to reimburse overhead costs associated with managing the FMS program, such as the costs of civilian employee salaries, facilities, and information systems.

Figure 3: Combined Balance of the Foreign Military Sales (FMS) Transportation Accounts, With and Without Funds Redistributions, Fiscal Years 2007 to 2018

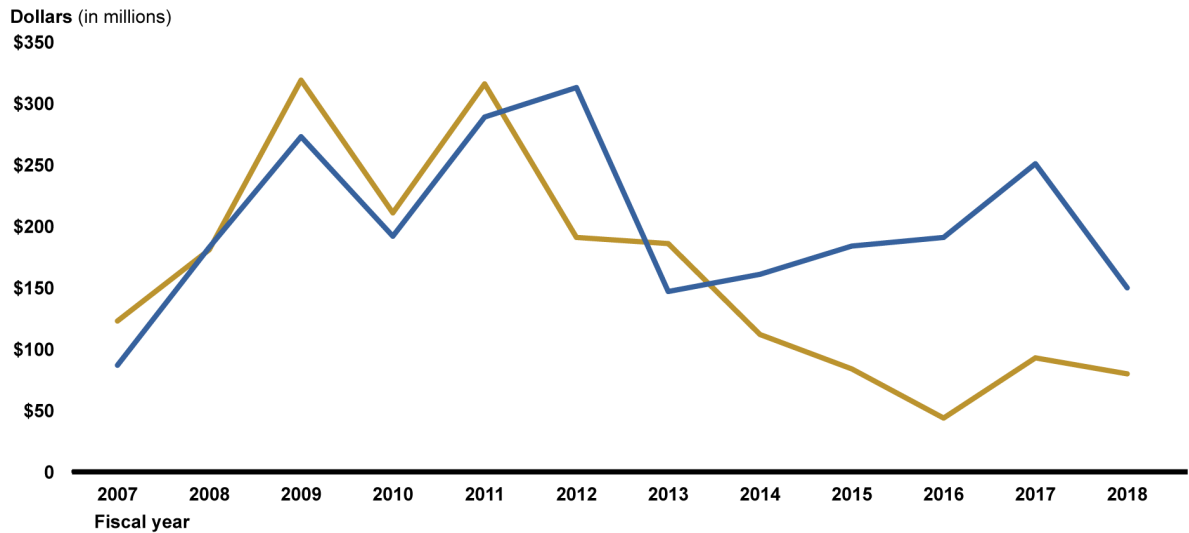


Source: GAO analysis of Defense Finance and Accounting Service data from the Defense Integrated Financial System. | GAO-19-678

Note: The Defense Security Cooperation Agency redistributed \$80 million in fiscal year 2009 and \$50 million in fiscal year 2011 from the FMS administrative fee account to the main FMS transportation account to prevent the account from becoming insolvent.

Collections and expenditures both fluctuated from year to year, as shown in figure 4. Year-to-year changes in collections ranged from decreases of 54 percent to increases of 121 percent, while year-to-year changes in expenditures ranged from decreases of 52 percent to increases of 133 percent. According to DSCA officials, demand for transportation of FMS purchases through DTS is unpredictable, and the accounts' balances may experience volatile swings due to inconsistencies involved in billing the accounts. For example, delays in billing or reporting a particular shipment can result in DOD collecting the fee into the transportation accounts and reimbursing the transportation cost from the accounts at different times. Further, the fees collected and the costs expended for an individual shipment may differ because DOD uses different factors to calculate the transportation fee to charge the purchaser (e.g., the item's value) than it uses to calculate the cost to bill the FMS transportation accounts (e.g., the shipment's origin, destination, and weight, among other factors).

Figure 4: Collections into and Expenditures from the Combined Foreign Military Sales Transportation Accounts, Fiscal Years 2007 to 2018



Ratio of collections to expenditures	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Ratio of collections to expenditures	0.69	1.01	0.85	0.91	0.91	1.66	0.78	1.46	2.30	4.97	2.84	1.95

Source: GAO analysis of Defense Finance and Accounting Service data from the Defense Integrated Financial System and Department of Defense documents. | GAO-19-678

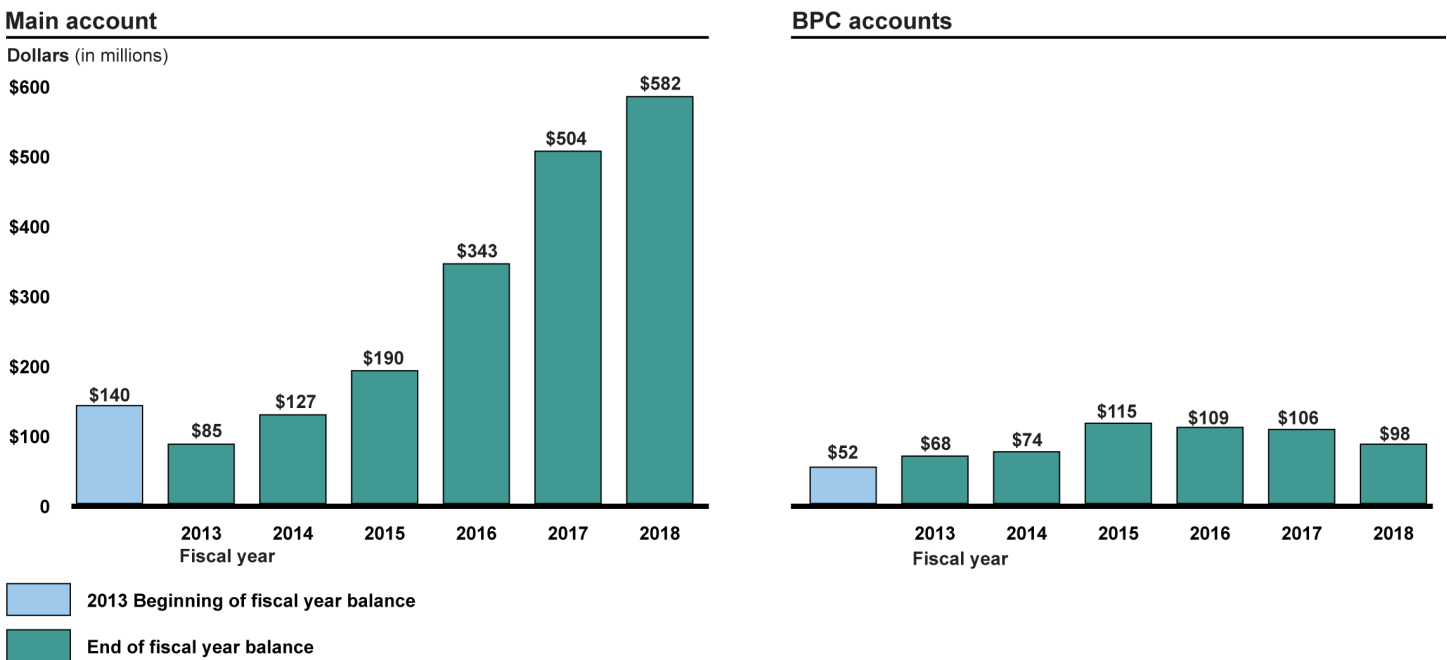
Notes: Collections and expenditures reflect the amount of funds in the aggregate moved into and out of the FMS transportation accounts. To reflect only transportation-related data, we adjusted certain amounts to remove funds that were moved from other accounts. In particular, we increased the expenditures in fiscal years 2009 and 2011 by \$80 million and \$50 million, respectively, to account for two redistributions from the FMS administrative account into the transportation accounts, which the Defense Finance and Accounting Service (DFAS) had recorded as negative expenditures. Additionally, we reduced the collections in fiscal year 2012 by \$19.4 million to remove the initial funding of new transportation accounts DFAS had recorded as collections, and we increased the expenditures in fiscal year 2015 by \$3.3 million to remove the initial funding of a new transportation account, which was recorded as a negative expenditure.

Despite this volatility over time, from fiscal years 2014 to 2018, collections consistently exceeded expenditures, which drove the substantial balance growth. In figure 4, we show this relationship in a collections-to-expenditures ratio, for which a value of 1.0 would indicate collections equaled expenditures for the fiscal year. A ratio greater than 1.0 indicates an increasing account balance that fiscal year. The average collections-to-expenditures ratio for fiscal years 2007 to 2018 was 1.26; from fiscal year 2014 to 2018, this ratio ranged from 1.46 to 4.97. At the end of each fiscal year, any collections that exceed expenditures remain in the account and are carried over to the next fiscal year’s beginning balance, which contributes to balance growth from year to year.

The Main Account Balance Has Grown More Quickly than the Balances of the Combined BPC Accounts

Much of the recent combined balance growth has been driven by growth in the main account's balance, as shown in figure 5. The main account grew more quickly than the combined balance of the BPC accounts from fiscal year 2013—the first full year of operation for the BPC accounts—to fiscal year 2018. The main account grew by 316 percent, from \$140 million at the beginning of fiscal year 2013 to \$582 million at the end of fiscal year 2018, while the combined BPC accounts grew by 88 percent, from \$52 million to \$98 million, during the same time period.

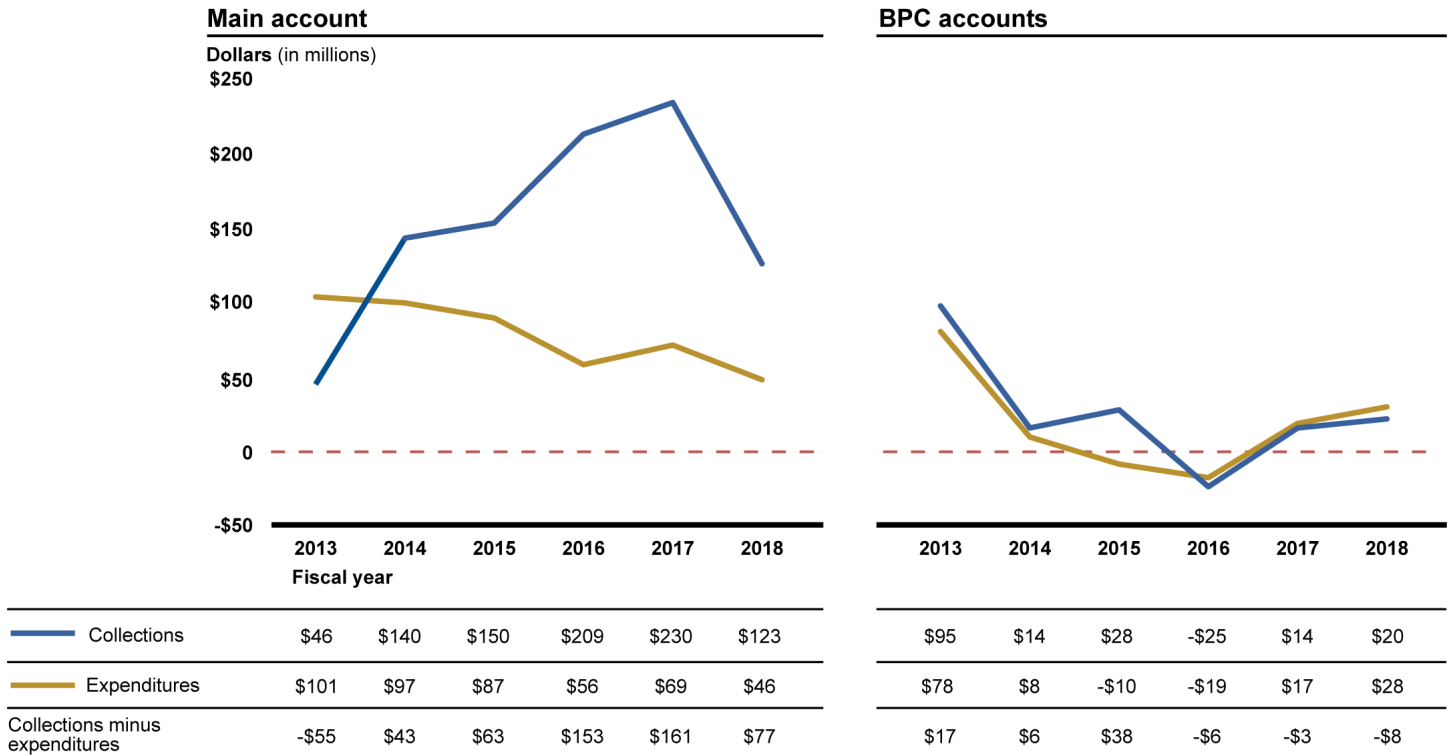
Figure 5: Balances of the Main Foreign Military Sales Transportation Account and the Combined Building Partner Capacity (BPC) Transportation Accounts, Fiscal Years 2013 to 2018



Source: GAO analysis of Defense Finance and Accounting Service data from the Defense Integrated Financial System and Department of Defense documents. | GAO-19-678

As seen in figure 6, our analysis shows that, for fiscal years 2013 to 2018, collections exceeded expenditures more frequently and by a greater extent in the main account than in the BPC accounts, which has driven balance growth. On average during this period, collections exceeded expenditures for the main account by \$74 million per year, as compared to \$7 million per year for the BPC accounts.

Figure 6: Collections into and Expenditures from the Main Foreign Military Sales Transportation Account and the Combined Building Partner Capacity (BPC) Transportation Accounts, Fiscal Years 2013 to 2018



Source: GAO analysis of Defense Finance and Accounting Service data from the Defense Integrated Financial System and Department of Defense documents. | GAO-19-678

Notes: Collections and expenditures reflect the amount of funds in the aggregate moved into and out of the FMS transportation accounts. To reflect only transportation-related data, we adjusted certain amounts to remove funds that were moved from other accounts. In particular, we increased the combined BPC account expenditures in fiscal year 2015 by \$3.3 million to remove the initial funding of a new transportation account, which was recorded as a negative expenditure.

The combined BPC account expenditures were negative in fiscal year 2015 and the combined BPC account expenditures and collections were negative in fiscal year 2016 due largely to activity for the Afghan Security Forces Fund transportation account. According to a DSCA account assessment, this occurred at least in part because this BPC program was transitioning to paying for its transportation based on actual costs directly from its BPC program account instead of based on the transportation fee that involves use of the transportation account. According to DFAS officials, negative collections and expenditures can be caused by adjustments and corrections to shipping charges and by realignments of funds between transportation accounts.

DSCA officials speculated that BPC programs may use more air transportation for shipments to areas without regular TRANSCOM shipment routes, which may result in higher expenditures. DSCA officials could not provide any further explanation for why the main account's balance has grown more quickly than the balances of the BPC accounts.

DSCA's Limited Management Oversight Guidance Contributed to Substantial Growth in the FMS Transportation Account Balances

DSCA has limited management oversight guidance for the FMS transportation accounts, which has contributed to their substantial balance growth. DSCA has established internal guidance for its two main management oversight processes to monitor for significant changes in the FMS transportation account balance—a daily review and annual review—but this guidance is unclear and lacks key details. As a result, DSCA's implementation of these processes lacks rigor and DSCA's reporting to its management has not included complete information about the causes for recent balance growth. In addition, DSCA has no internal guidance to ensure that funds remaining in BPC-specific transportation accounts after the related programs close are transferred to the miscellaneous receipts of the Treasury, which risks these funds not being transferred as DOD officials told us DOD intends to do.

DSCA Established Management Oversight Procedures

In fiscal year 2016, DSCA established a Managers' Internal Control Program (MICP) for overseeing the FMS transportation accounts, according to DSCA officials. These procedures formalized two management oversight processes for the FMS transportation accounts that DSCA officials had performed previously: daily and annual reviews. These reviews both serve the purpose of ensuring the accounts have sufficient funds to pay expenses. MICP documentation to help guide these processes includes

- flow charts that explain certain steps that should be included in each of these reviews,
- a risk assessment that explains how each of the MICP processes mitigates risks for the FMS transportation accounts, and
- test procedures that lay out expectations for how each MICP process should be conducted so that DSCA can periodically test to ensure the processes were carried out as intended.

Daily review. MICP procedures indicate that DSCA staff should review a report from DFAS daily that includes the previous day's balances for each of the transportation accounts to ensure that the FMS transportation accounts do not drop below a "healthy level." If DSCA staff identify a large decrease or "significant" level of change in the accounts, the procedures direct them to ask DFAS to explain what caused the change and to take corrective action, such as to ask for billing corrections, if necessary. According to the MICP risk assessment, the FMS transportation accounts experience volatile swings due to inconsistencies involved in billing the account, and reviewing the account balances on a daily basis helps to

address this risk. The MICP procedures state that, if DSCA allows the FMS transportation accounts to drop below this “healthy level,” the accounts could become insolvent and be delinquent in disbursing transportation expenses.

Annual review. MICP procedures indicate that DSCA should annually assess the financial health of the transportation accounts, which DSCA staff have stated they implement by preparing an annual report for DSCA leadership.¹⁶ To test whether the annual review has occurred, certain DSCA staff are to examine the annual report to confirm that DSCA assessed the FMS transportation account with the purpose of ensuring that the overall financial health of the accounts is strong and collections are sufficient to pay expenditures.

DSCA Inconsistently Implemented Daily Reviews Due to Unclear Internal Guidance

DSCA has inconsistently implemented its daily reviews due to unclear internal guidance on these reviews. Specifically, the guidance does not specify the level of change that warrants further examination or what DSCA staff should consider as a healthy level, or target range, for the accounts.

DSCA’s Internal Guidance Does Not Define What Changes in Daily Transportation Account Balances Warrant Examination

DSCA’s daily review procedures are meant to monitor for significant changes in the FMS transportation accounts so that such changes can be further examined and, if needed, corrected; however, MICP internal guidance does not establish criteria for determining what constitutes a significant change in these accounts’ balances. According to federal internal control standards, management should define the acceptable level of variation in performance, or risk tolerance, in specific and measurable terms.¹⁷ However, the MICP procedures use different and undefined terms when referencing the types of balance changes DSCA should look for in their daily review procedure. These terms include:

¹⁶The MICP annual review procedures also describe three other processes that DSCA officials responsible for the accounts do not consider part of the annual review process. First, the MICP procedures indicate DSCA should annually update, as needed, the estimated prices DOD charges for the transportation of certain items based on data calls to the military departments. Second, the procedures indicate in certain places that a review of the FMS transportation fee rates should be conducted annually. We discuss these processes later in the report when we evaluate DSCA processes for ensuring transportation fee rates are set appropriately. Third, the procedures indicate DSCA should annually issue an updated list of BPC country codes, which DSCA officials stated they do as needed instead of annually.

¹⁷[GAO-14-704G](#).

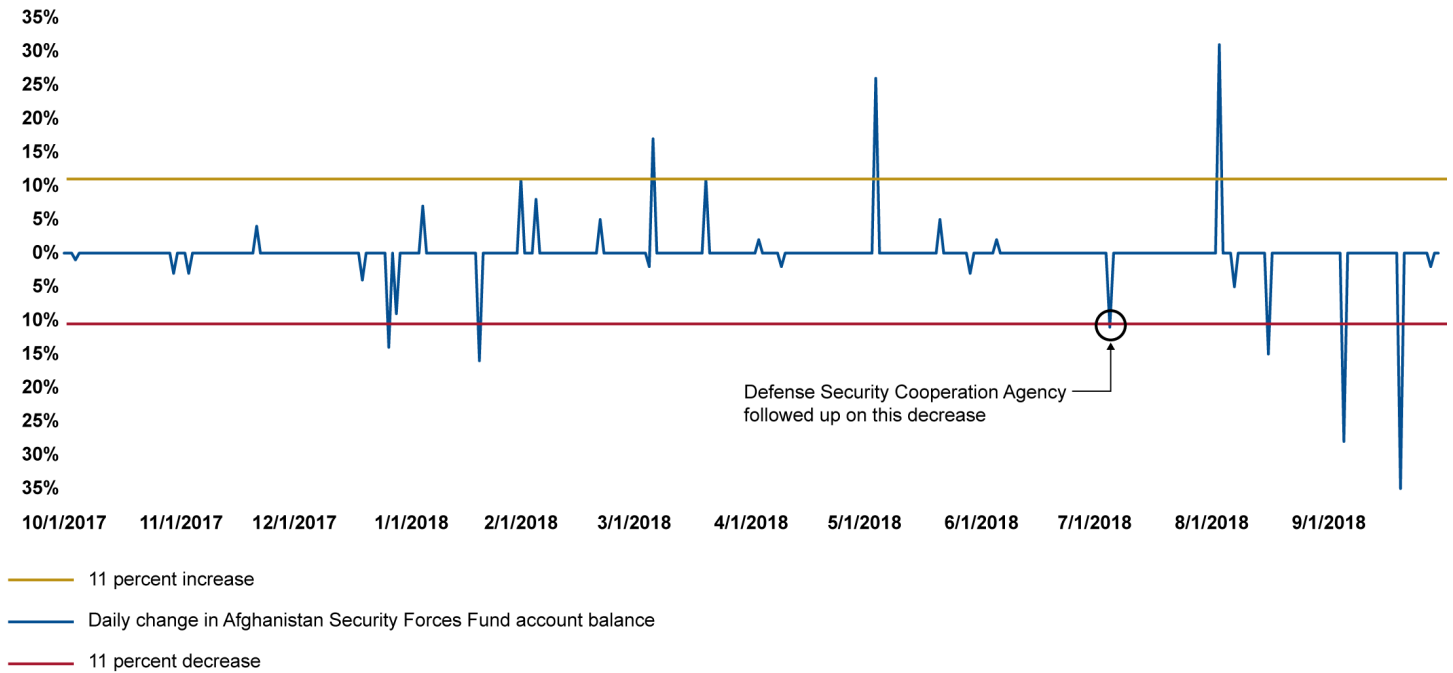
“change,” “significant change,” and “significant reduction.” Although some of these terms could be interpreted as DSCA needing to monitor for any significant changes—whether increases or decreases in the accounts—DSCA staff have chosen to focus these reviews on decreases.

As a result of DSCA’s unclear internal guidance, DSCA staff have inconsistently determined which changes warrant examination and should trigger them to contact DFAS to examine the reasons for the change. This makes it less likely that DSCA will be alerted to and take corrective action to address significant changes in the account balances. From fiscal year 2018, DFAS was able to provide one documented instance of DSCA staff contacting DFAS as a result of the daily review.¹⁸ The contact was regarding an 11 percent balance decrease of approximately \$6 million in the Afghan Security Forces Fund’s transportation account that occurred on July 5, 2018.¹⁹ However, we identified a total of 30 instances of balance changes greater than 11 percent (12 decreases and 18 increases) in fiscal year 2018 across the eight FMS transportation accounts. For example, figure 7 shows the fiscal year 2018 daily balance changes for the Afghan Security Forces Fund. This figure includes the July 2018 balance decrease that resulted in DSCA contacting DFAS to examine the change, as well as nine other instances of balance changes greater than 11 percent that did not result in any documented contact between DSCA and DFAS.

¹⁸Although neither DSCA nor DFAS officials were able to provide documentation of any other such contacts in fiscal year 2018, the responsible DSCA official said that they typically contact DFAS to inquire about changes in the accounts approximately eight to 12 times per year.

¹⁹When DSCA requested that DFAS provide information about the cases and amounts that caused this balance decrease, DFAS responded that the requested information was unavailable and instead explained that the decrease was consistent with typical end-of-quarter fund movements in the account. However, DSCA officials found that the decreases continued in fiscal year 2019, and worked with DFAS officials to further research the issue. They identified the cause as incorrect reporting of certain types of costs. According to DFAS officials, as of July 2019, they are working with DSCA to resolve this issue.

Figure 7: Daily Balance Changes in the Afghan Security Forces Fund's Foreign Military Sales Transportation Account in Fiscal Year 2018



Source: GAO analysis of Defense Finance and Accounting Service data from the Defense Integrated Financial System and Department of Defense documents. | GAO-19-678

Note: In fiscal year 2018, the Defense Finance and Accounting Service (DFAS) was able to provide one documented instance of the Defense Security Cooperation Agency (DSCA) contacting DFAS as a result of the daily review and DSCA was not able to provide any such documentation. However, the responsible DSCA official said that they typically contact DFAS to inquire about changes across the eight FMS transportation accounts approximately eight to 12 times per year. This figure shows the changes in the daily balance for one of those eight accounts.

By inconsistently conducting daily reviews, DSCA weakens the effectiveness of this oversight mechanism to identify potential errors, which risks allowing either insufficient or excessive funds in the accounts. In particular, in recent years, the lack of clarity on what these reviews should monitor for has weakened DSCA's oversight and contributed to the substantial balance growth.

DSCA's Internal Guidance Does Not Establish a Target Range for the Transportation Account Balances

DSCA has not defined what it considers an acceptable target range for these accounts despite the unpredictability of transportation account balances and the MICP daily review procedures requiring DSCA officials to monitor account balances to ensure they remain at or above a "healthy level." According to DSCA officials, DSCA has not determined an acceptable target range for the transportation accounts because future collections and expenditures are difficult to predict, making it difficult to

know how much money DSCA needs in the accounts. However, this unpredictability makes it all the more important for DSCA officials to establish a target range for what is “healthy” account activity to enhance their oversight of the accounts. As we previously reported, to ensure the accountability of fee-funded programs and the ability to manage a program with sufficient reserves, federal agencies are advised to use a risk-based strategy to establish desired upper and lower bounds for account balances.²⁰

DSCA has already established upper and lower bounds for two other FMS overhead fee accounts, the FMS administrative fee and contract administration services fee accounts.²¹ DSCA calculates these bounds based on the amounts of planned expenses from the accounts, which automatically adjusts the bounds over time to reflect the size and needs of the FMS program. DSCA’s internal guidance states that setting upper and lower bounds of acceptable levels provides the agency with a “control box” to alert it to a dramatic change in the FMS operating environment that may require an agency response such as a fee rate review.

Similarly, establishing a target range, with an upper and lower bound, for the FMS transportation account balances could strengthen DSCA’s ability to use its daily reviews to manage the accounts’ volatility by identifying when the account balances are growing excessively high or falling excessively low. Such an upper bound could better inform DSCA leadership and help prevent excessive growth in the transportation accounts while a lower bound could help to ensure that the accounts have sufficient funds to pay for transportation bills.

DSCA Prepared Annual Reports Missing Key Details Due to Lack of Internal Guidance

DSCA has no internal guidance for its staff to follow when preparing annual reports on the health of the FMS transportation accounts, which has led the reports DSCA produced for fiscal years 2015 to 2018 to contain incomplete information on the underlying causes for the trends in

²⁰GAO, *Federal User Fees: Fee Design Options and Implications for Managing Revenue Instability*, GAO-13-820 (Washington, D.C.: Sept. 30, 2013).

²¹In GAO-18-401, we reported on DSCA’s use of lower bounds for these accounts and recommended that DSCA also define a method for calculating an upper bound of a target range for each of these two fee accounts. DSCA has since taken steps to implement these recommendations by creating related internal guidance and calculating such an upper bound for the accounts.

Lack of Internal Guidance
Regarding Annual Reports Has
Contributed to Incomplete
Reporting

the accounts and for the reports to lack key details about the source of some of the funds in the main FMS transportation account.

For fiscal years 2015 to 2018, DSCA produced annual reports assessing the financial health of FMS transportation accounts that contained incomplete information because DSCA did not use rigorous methods to determine the underlying causes for trends in the accounts. As a result, DSCA had a limited ability to make informed decisions about the accounts at a time when the balances were experiencing substantial growth. According to the DSCA staff who produce the annual reports, they distribute the reports within DSCA up to the agency's Director to provide information about the health of the FMS transportation accounts.

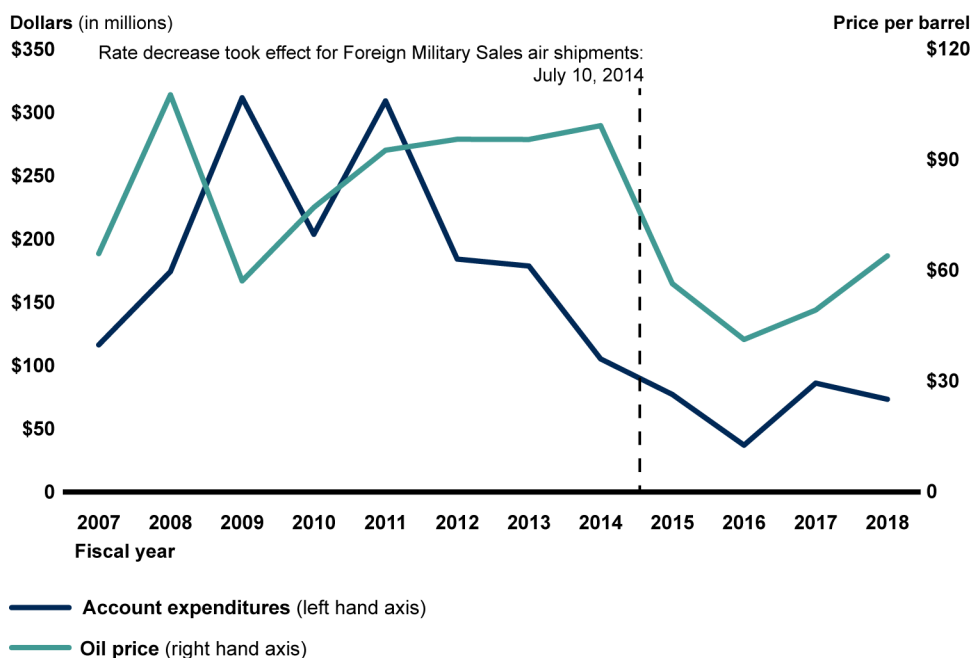
DSCA's annual reports on the FMS transportation accounts for fiscal years 2015 to 2018 followed a consistent format. These reports contained information on the net change in balances for each of the transportation accounts during the fiscal year. The reports also included a summary of any major activity in each of the accounts. For example, the fiscal year 2018 assessment stated that the main FMS transportation account grew by \$77.8 million during that fiscal year due to several large collections significantly greater than billings. All of the reports end with a conclusion regarding the health of the accounts, which for fiscal years 2015 to 2018, was that the accounts were healthy and should remain financially solvent.

All of these annual reports also include statements regarding the underlying causes of account trends, which we found to be incomplete and unsupported by rigorous data analysis. When discussing reasons for year-to-year account balance increases, DSCA's reports stated they were mainly due to a decline in oil prices and a legal change that DOD implemented in July 2014 that allowed TRANSCOM to charge lower DOD rates for FMS air shipments, both of which could likely affect expenditures from the account.²² However, DSCA officials said that they conducted no specific analysis to support the extent to which these two factors affected

²²10 U.S.C. § 2642 (as amended by National Defense Authorization Act for Fiscal Year 2014, Pub. L. No. 113-66, Div. A, Title X, § 1073(a), (b) (Dec. 26, 2013)). Following this legal change, a July 2014 DOD memorandum delegated to TRANSCOM the authority to approve the use of the DOD transportation rates for FMS shipments based on certain criteria, including that the total transportation costs for each FMS case not exceed a certain amount. According to TRANSCOM officials, in practice, this change broadened an exception to certain types of air shipments that had already been available for other types of transportation services, although FMS purchasers must apply for a waiver from TRANSCOM to use the DOD transportation rates.

the account balance increases. As seen in figure 8, our analysis shows that these reasons could not fully explain the account balance increases in each of the annual reports from fiscal year 2015 to 2018. In particular, while FMS transportation expenditures began to decrease in fiscal year 2012, the price of oil did not begin to significantly decline and the legal change did not come into effect until 2014. Further, the annual reports did not discuss underlying reasons for trends in collection activity, which also affect the account balance.

Figure 8: Foreign Military Sales Transportation Account Expenditures and Oil Price, Fiscal Years 2007 to 2018



Source: GAO analysis of account data from the Defense Finance and Accounting Service and oil price data from the Energy Information Agency. | GAO-19-678

Note: The oil price data used in the figure is for Cushing, Oklahoma, West Texas Intermediate oil, which is used commonly as a global benchmark for oil prices.

DSCA’s analysis for its annual reports is limited by the lack of internal guidance for completing these reports. Specifically, the MICP guidance for the annual review process does not specify how to prepare the annual report. Without such guidance, according to DSCA officials, DSCA’s analysis for the annual reports has involved re-reviewing the documentation related to the daily reviews as well as monthly reviews that DSCA performs for financial oversight purposes. DSCA officials completed no additional analysis to inform the annual reports, such as

DSCA Has Not Reported Redistributions between Accounts or Assessed Whether to Return Funds Due to Lack of Internal Guidance

any quantitative analysis to understand annual changes or trends over time. Federal internal control standards state that effective internal guidance communicates the who, what, when, where, and why of what needs to be accomplished, and that management should obtain relevant data from reliable sources and process that data into quality information to aid decision making.²³ Without clear internal guidance, the annual account reviews lack the rigor necessary to ensure DSCA management is provided reliable information for decision making.

According to DSCA officials, DSCA's annual review process should also involve an assessment of whether funds should be redistributed between the FMS overhead fee accounts; however, DSCA does not have specific internal guidance on when and how to perform such assessments or on what to include about this portion of the annual review in its resulting annual reports. This lack of guidance has led DSCA to produce annual reports without information related to redistributed funds and to not conduct assessments related to redistributed funds. According to DOD's financial management regulations, DSCA and DFAS should periodically review activity in the FMS overhead fee accounts to serve as a basis for decisions by DSCA management to, among other purposes, redistribute account balances between these accounts.²⁴ According to DSCA officials, if they were to perform these periodic assessments, they would perform them as part of their annual account reviews.²⁵ However, the MICP guidance for the annual reviews does not describe how to assess whether or how much to redistribute funds between the fee accounts, or how or when to assess returning previously redistributed funds.

The annual FMS transportation account and administrative account assessments for fiscal years 2015 to 2018 do not report that \$130 million in the main FMS transportation account came from funds redistributed from the FMS administrative account between fiscal years 2009 and 2011

²³[GAO-14-704G](#).

²⁴DOD, *Financial Management Regulation, Volume 15: "Security Cooperation Policy,"* Section 030408.G (May 2017).

²⁵DSCA also performs annual reviews culminating in annual reports about the other main FMS overhead fees: the FMS administrative fee and the contract administration services fee.

that have not been returned.²⁶ According to DSCA officials, they only report redistributions in the year that they occur.

In addition to not including this information in its annual reports, DSCA has not assessed the need for other redistributions of funds between the FMS fee accounts since it last redistributed funds from the FMS administrative account to the main FMS transportation account in fiscal year 2011. DSCA officials indicated they intend to return the funds to the administrative account but have not done so because they have no urgency, given that the FMS administrative account balance has been consistently above its lower bound in recent years. As of the end of fiscal year 2018, the FMS administrative account balance was approximately \$4.7 billion, which was approximately \$3.1 billion more than the account's lower bound that DSCA determined was necessary to support FMS operations.

The lack of specific internal guidance on how to assess and report redistributions has resulted in incomplete reports to DSCA management, which inhibits DSCA management's ability to make informed decisions in overseeing the FMS fees. In particular, without reports that clearly state the amount of redistributed funds and their source(s), and assess their continued need, DSCA management is less informed when determining whether and when to redistribute funds, including whether to return previously redistributed funds.

According to our User Fee Design Guide, assigning costs to identifiable users can promote equity and more informed rate-setting; however, redistributing fees from the FMS administrative account to the main FMS transportation account has intermingled funds that have different sources.²⁷ DOD charges the FMS administrative fee to all FMS purchasers while DOD charges the FMS transportation fee to only certain purchasers for the portion of the transportation of their FMS items that

²⁶The FMS administrative account reports for fiscal years 2015 and 2016 included table notes stating that amounts had been transferred to the FMS transportation account in fiscal year 2011, but did not specify the amount. These reports did not mention the fiscal year 2009 redistributions. Moreover, the fiscal years 2017 and 2018 FMS administrative account reports and the fiscal years 2015 to 2018 FMS transportation account reports did not mention any of the redistributions.

²⁷We have previously reported that fee design should balance, among other factors, ways to encourage greater equity, signifying that all beneficiaries should pay their fair share. See GAO, *Federal User Fees: A Design Guide*, [GAO-08-386SP](#) (Washington, D.C.: May 2008).

uses DTS. Distributing funds from the FMS administrative account to the main FMS transportation account intermingled these fees, which has two main effects. First, not returning redistributed funds if the transportation account no longer needs them raises concerns regarding the fees' equity in ensuring only the beneficiaries of a service pay for the cost of providing it. Second, the appropriateness of DSCA management's rate-setting decisions for both fees is limited by incomplete information about the full expected balance of the fee accounts from which future expenditures could be paid.

DSCA Has No Internal Guidance to Ensure Proper Disposition of Unused Funds in BPC Transportation Accounts

DSCA has no internal guidance to ensure proper disposition of any funds remaining in the BPC-specific transportation accounts after the related programs close and those remaining funds are no longer needed. In fiscal year 2020, DSCA expects the first BPC-specific transportation account to close, which had a balance of approximately \$42 million at the end of fiscal year 2018. DSCA officials have said that funds remaining in the BPC-specific transportation accounts after the related programs close should be transferred to the miscellaneous receipts of the U.S. Treasury. According to DSCA officials, this process was agreed to with DOD's Office of the Under Secretary of Defense (Comptroller) in November 2011 when DSCA met with that office to discuss how DSCA would handle creating the BPC-specific transportation accounts. DSCA officials also said that following this process would be in line with a requirement in DOD's financial management regulations for any collections that are authorized or required to be credited to an account after that account's closure to be deposited in the Treasury as miscellaneous receipts.²⁸

However, DOD officials could not provide a documented agreement from the November 2011 meeting, and we do not consider the referenced regulation specific enough to this circumstance to alone serve as internal guidance that would ensure the funds are transferred. In particular, this regulation applies broadly to DOD collections received after an account's closure, and does not specifically address the disposition of funds that had already been collected into an account upon the closure of that account .

Officials from relevant DOD components have different understandings of how this process should occur, which could risk the process not being

²⁸DOD, *Financial Management Regulation, Volume 3: "Budget Execution – Availability and Use of Budgetary Resources,"* Section 100311.B (March 2015).

completed as intended without related specific internal guidance. According to DSCA officials, DFAS will be responsible for moving any remaining funds in these transportation accounts to the miscellaneous receipts of the Treasury, but the pertinent DFAS officials have stated they are unaware of what should be done in such circumstances. According to DSCA officials, they intend to write a memo to DFAS related to each instance of a BPC-specific transportation account closure instead of providing DFAS written guidance to follow in any such instance because DSCA officials prefer providing specific directions to DFAS regarding moving such funds. DSCA officials said they do not need specific internal guidance to ensure they direct DFAS to complete such fund transfers because DOD's Office of the Under Secretary of Defense (Comptroller) would ensure that DSCA does so when that office reviews all DOD accounts. However, Comptroller's Office officials stated that, as part of DSCA's program oversight responsibilities for FMS, DSCA is responsible for ensuring any funds are identified and transferred to the miscellaneous receipts of the Treasury.

Without clear internal guidance, DOD may not have accurate information on or sufficient oversight of its budgetary resources and account balances, and funds that could be put to other uses may remain in the BPC transportation accounts. Federal internal control standards state that effective internal guidance communicates the who, what, when, where, and why of what needs to be accomplished, thereby providing a means to retain organizational knowledge and mitigate the risk of having that knowledge limited to a few personnel.²⁹ According to DSCA officials, the first BPC-specific transportation account likely to close is dedicated to the Iraq Security Forces Fund, which had a balance of approximately \$42 million at the end of fiscal year 2018. According to DSCA records, this program's appropriations were canceled at the end of fiscal year 2017 and, according to DSCA officials, by sometime in fiscal year 2020, the program's FMS cases should go through their final reconciliation process. Through this process, DOD may pay outstanding bills or correct accounting errors and the related cases will close. According to DSCA officials, the BPC-specific transportation account would then be ready for closure.

²⁹[GAO-14-704G](#).

DSCA's Processes for Setting Transportation Fees Have Not Ensured Fees Approximate Costs over Time and Contributed to Account Balance Growth

DSCA's processes for setting the FMS transportation fee do not ensure that aggregate fees DOD collects approximate aggregate transportation costs over time, thus contributing to recent growth in the FMS transportation account balances. DSCA's ability to set appropriate transportation fee rates is undermined by DSCA's unclear guidance to the military departments on what data they should provide DSCA to analyze in its transportation fee rate reviews, leading DSCA to review data that is not timely or systematically sampled. Further, the lack of clarity in its internal guidance for these reviews has led DSCA to complete these reviews infrequently, perform limited analysis, and burden the military departments with compiling data DSCA did not use. In addition, our analysis raises concerns about negative effects of the current transportation fee rate structure, including that the structure makes it more difficult for DSCA to determine appropriate transportation fee rates. Finally, DSCA's internal guidance to the military departments for estimating transportation prices, instead of rates, for certain items lacks key specific details. As a result, the military departments follow varying procedures for estimating these prices, and are unsure of the prices' accuracy.

DSCA's Transportation Fee Rate Reviews Used Unsuitable Data, Were Completed Infrequently, and Involved Limited Analysis

DSCA's ability to set appropriate transportation fee rates is undermined by unclear guidance for its reviews of these rates. The lack of clear guidance has led the military departments to provide DSCA data that is not suitable for rate-setting decisions because, while the individual data points DSCA analyzed were accurate, they may not accurately predict future rates because they were not timely or systematically sampled. Unclear guidance also led DSCA to perform infrequent and limited analysis of these data.

DSCA's Rate Reviews Do Not Use Timely and Systematically Sampled Data

DSCA's ability to determine the appropriate FMS transportation fee rates is limited by the data analyzed in its rate reviews that are not timely or systematically sampled. According to its MICP documentation, DSCA is to review its FMS transportation fee rates to ensure the resulting transportation fees collected from FMS purchasers in aggregate cover the amount needed to pay for transportation expenses. DSCA requests the military departments provide historical data on transportation fees charged and transportation costs paid so that DSCA can analyze these data to determine appropriate fee rates. However, DSCA's data requests to the military departments are unclear in multiple key respects, which leads the military departments to provide data to DSCA that—though it contains accurate cost and fee data—are unsuitable to use for DSCA's resulting rate-setting decisions because it is not timely or systematically

sampled. The combined effects of these deficiencies could skew DSCA's rate review process.

When DSCA requests data from the military departments for the rate reviews, DSCA does not specify key elements about which data to provide or which information sources to use to obtain each data element. As a result, the departments have followed different processes and provided data that was not timely. As shown in table 2, the data submitted by the military departments varied significantly.

Table 2: Characteristics of Data the Military Departments Provided to the Defense Security Cooperation Agency for Its Fiscal Year 2018 Foreign Military Sales Transportation Fee Rate Review

Military department	Level of data	Data sources for fee amounts charged to FMS purchasers	Data sources for related costs paid from FMS transportation accounts	Time period data covers
Air Force	Shipment order ^a	Air Force system	3 separate TRANSCOM systems for air, surface, and commercial shipments	December 2014 to July 2017
Army	Case (which could include numerous shipments)	Defense Finance and Accounting Service (DFAS) system	4 separate TRANSCOM systems for air, military sealift, surface, and commercial shipments	Approximately 2011 to 2018 ^b
Navy	Shipment	DFAS system	1 TRANSCOM system for air shipments	January 2012 to June 2017

Legend: FMS = Foreign Military Sales TRANSCOM = U.S. Transportation Command

Sources: GAO presentation of information from DOD documents and officials. | GAO-19-678

^aShipment orders, also known as requisitions, can be completed through one or more shipments.

^bArmy officials estimated that the cases should mostly have been up to 5 to 7 years old although some may have been older. As a result, shipments related to these cases may have occurred at any point since the cases began, although DSCA officials stated that it is common for shipments not to occur until multiple years into a case.

Because DSCA's data requests did not specify where the data should be sourced, the military departments have had difficulty responding to these requests and the amount of data they have produced has been limited. Military department officials explained difficulties finding the necessary data in other DOD agencies' systems, understanding those data's reliability, and accurately matching the data across multiple systems. In particular, transportation cost data is stored in multiple TRANSCOM billing systems, which military department officials responsible for

responding to DSCA's data requests said they do not regularly access.³⁰ In addition, DFAS has copies of transportation cost data in the monthly bills that it pays from the FMS transportation accounts. The bills include the individual costs of each shipment made during that month, but are stored in individual documents and are not accessible to the military departments. Transportation fee data is available in a DFAS system used to process the FMS transportation fee, but, according to DFAS documents and officials, this system is not built to easily extract such data and therefore neither DFAS nor the military departments can reliably pull fee data from this system specific to particular shipments or cases.

According to DSCA officials, ultimately DSCA only used Army data for setting rates in 2018 because Navy and Air Force provided relatively small samples.

- **Navy.** Navy officials reported having particular difficulty finding data on transportation costs for the most recent rate review. After unsuccessfully requesting more specific guidance or assistance from DSCA and DFAS, according to Navy officials, Navy found a spreadsheet DSCA had provided Navy for an unrelated purpose that contained the costs for Navy FMS shipments moved by TRANSCOM's Air Mobility Command. According to Navy officials, because researching the individual transportation fees for each FMS shipment was time-consuming and they lacked clear guidance about how much data DSCA needed for its rate review, they decided to provide related fee data on 103, or 3 percent, of the 3,536 air shipments for which Navy had cost data.
- **Air Force.** The U.S. Air Force Security Assistance and Cooperation Directorate has developed a detailed process, described in a 280-page internal guidance document, to respond to DSCA's requests, but following this process does not yield much data. For the most recent review, Air Force provided DSCA with data for 639, or 2 percent, of 28,886 shipment orders for which they reviewed data because of the

³⁰Officials from the U.S. Army Security Assistance Command stated that they are further hampered in their ability to access cost data for FMS air shipments because the Department of the Army stopped paying for their access to the Financial and Air Clearance Transportation System a few years ago.

difficulty of finding relevant matching cost and fee data across the different systems used, as shown in table 3.³¹

Table 3: Steps Followed by Air Force to Provide Shipment Order Data to the Defense Security Cooperation Agency for its Fiscal Year 2018 Foreign Military Sales Transportation Fee Rate Review

Step in Air Force data collection process	Number of shipment orders remaining	Percent of total	Reasons why Air Force dropped shipment orders from full population
Air Force pulls transportation cost data from three TRANSCOM billing systems.	28,886	—	—
Air Force reviews cost data to remove any that are invalid or incomplete.	6,110	21	Cost data had included shipments that were not for Air Force, not paid out of the FMS transportation accounts, or were missing data in key fields.
Air Force used identifying information within data from DFAS's Defense Integrated Financial System to associate cost and fee data from disparate systems.	About 4,000	About 14	Cost data had included duplicates, canceled deliveries, and returns for item discrepancies for which the purchaser does not pay a transportation fee.
Air Force individually looked up fee data on each of the about 4,000 shipments in Air Force's Security Assistance Management Information System.	639	2	The shipment identifiers in the cost data were not found in the Air Force system for reasons such as the bills using a nonstandard identifier or the fee amount not yet charged to the purchaser.

Legend: FMS = Foreign Military Sales TRANSCOM = U.S. Transportation Command DFAS = Defense Finance and Accounting Service

Sources: GAO analysis of U.S. Air Force Security Assistance and Cooperation Directorate documents and interviews with officials. | GAO-19-678

Not only were the data DSCA reviewed not indicative of all FMS shipments since they included no Navy or Air Force data, the data were also not indicative of Army's shipments and included older data because the DSCA data requests were unclear. In particular, DSCA's data requests stated that each military department should provide at least 20 cost and fee comparisons for each fee rate for each of the FMS transportation accounts, and requested that these data include as many different foreign partners or FMS cases as possible. As a result, according to Army officials, the data Army provided to DSCA included a mix of different partners and cases of different dollar values; however, no systematic sampling methods were used that would have ensured that

³¹Of the shipment orders for which Air Force was able to provide matching cost and fee data, two-thirds were for shipment orders charged to two of the seven potential FMS transportation fee rates. Air Force was able to provide minimal data for the other rates. For example, Air Force could only provide data on four shipment orders that were charged the rate to move shipments to inland destinations in Newfoundland, Labrador, Thule, Iceland, South America, Asia, Africa, or the Middle East.

the resulting data were indicative of overall Army shipments during the time period covered. Also, DSCA's request did not specify a time period the data should cover. Army provided data for cases that likely were at least 5 to 7 years old. According to DSCA officials, if the rate review is to analyze case-level data, such as Army provided, it is necessary to analyze data on cases for which the FMS agreements were signed multiple years prior, because shipments may not take place until multiple years into cases. However, the Army officials we spoke to about the data Army provided were unaware how long ago the shipments occurred for the related cases, and stated that some may have occurred years before. TRANSCOM pricing changes annually, so cost information that is multiple years old and not adjusted to reflect such changes would be unlikely to predict future costs. As a result, DSCA set rates to cover future costs based on a sample of cases that was not systematically sampled and may have included shipments over the past 5 or more years.

DSCA officials stated that their data requests are not more specific because they thought the military departments had direct access to these data and that more specificity would hinder the military departments' ability to respond to the requests. However, related data are available in TRANSCOM and DFAS, instead of military departments' systems. Further, the current processes produce data that are not timely or systematically sampled, making it unsuitable to use to determine future costs and rates. In setting user fees, agencies should analyze timely and reliable data, consistent with applicable accounting standards,³² to avoid the risk of making skewed fee-setting decisions.³³ DSCA's use of data that are not timely or systematically sampled for its rate reviews could skew its rate-setting decisions, ultimately affecting transportation account balances.

³²According to Statement of Federal Financial Accounting Standards No. 4, reliable information on the costs of federal programs and activities is crucial for effective management of government operations, which includes setting user fees.

³³[GAO-08-386SP](#). Because generating and maintaining reliable cost data can be expensive, agencies must consider the costs of implementing, maintaining, and using financial management systems when determining the level of cost detail they need. Recognizing this, OMB Circular No. A-25 notes that program cost should be determined or estimated from the best available records of the agency and that new cost accounting systems need not be established solely for this purpose.

DSCA's Unclear Internal Guidance Has Contributed to Rate Reviews Completed Infrequently and with Limited Analysis

DSCA's internal guidance for its rate reviews is unclear regarding the timing of the reviews and lacks key details, which has limited DSCA's ability to use the rate review to set appropriate rates.

- **Timing.** DSCA's internal guidance for overseeing the FMS transportation accounts is unclear. In one part the guidance indicates that DSCA should conduct a rate review every 5 years, which is in line with the expectations explained by DSCA officials who oversee these accounts. However, other parts of DSCA's internal guidance indicate that DSCA should conduct such a review annually.
- **How reviews should be conducted.** DSCA's internal guidance states that the rate reviews should allow DSCA to determine whether current transportation fee rates are sufficient, based on predetermined criteria, to cover the related costs. However, this internal guidance does not specify how these criteria should be determined or contain any procedures regarding how DSCA should analyze the data collected for its rate review.

DSCA has not completed its transportation fee rate reviews in a timely manner, which allowed the FMS transportation account balances to grow over recent years as collections consistently exceeded expenditures but fee rates remained constant. Since fiscal year 2007, DSCA has completed two reviews more than 9 years apart: in March 2009 and May 2018.

For these reviews, DSCA officials did not predetermine criteria for the level of alignment between cost and fee that each review should achieve and DSCA's analysis considered few factors and involved a limited analysis of only Army data, which hindered DSCA's ability to set appropriate fee rates. In particular:

- **Fiscal year 2009:** For this review, DSCA compared the transportation cost to the transportation fee charged across seven transportation fee rates for 144 of the thousands of Army's FMS cases. In this sample, the transportation costs exceeded the fees paid by 19 percent overall. When briefing DSCA management on the review, DSCA officials reported a concentration of undercharges in two of the rates. As a result, DSCA decided to increase these two rates such that, if the new rates had applied to the full sample DSCA analyzed, fees on the

cases in the full sample would have exceeded costs by 14 percent.³⁴ Our analysis of the sample showed that while these two rates had the largest difference in value between the costs and fees, other rates also had large differences within this sample. Specifically, one other rate had a larger percentage of undercharges and three of the other rates had percentages of overcharges exceeding 1,000 percent. However, DSCA made no changes to these other rates.

- **Fiscal year 2018:** For this review, DSCA compared the transportation cost to the transportation fee charged across the seven transportation fee rates for a sample that contained data on 993 Army cases. For this sample, on average transportation fees charged to purchasers exceeded transportation costs by 158 percent, with all rates except one overcharging on average. However, when briefing DSCA management on the review, DSCA officials reported incorrect data to serve as the basis for decision making. In particular, according to the DSCA official responsible for the analysis, likely due to an oversight, DSCA included data on only 878 of these cases in the briefing to DSCA management. Total fees for this portion of the sample were 90 percent higher than the related total costs. Based on this limited data, DSCA decided to decrease all of its transportation fee rates such that, if the new rates had applied to the full sample DSCA analyzed, fees would still have exceeded costs by 77 percent, with five of the seven fee rates still exceeding the cost by more than 100 percent for that sample. DSCA officials stated that their intent in this rate review was to lower the rates modestly to see their effect on the account balances; however, their ability to accurately meet this goal is reduced by its lack of specificity and the limited analysis DSCA performed.

Given that the data DSCA analyzed for both these reviews was not generalizable to all shipments, the above percentages do not indicate that the rates overall would have affected fees in these exact ways. Instead, DSCA's decision making may have been further skewed by its method of analysis.

In addition to completing these two reviews, DSCA also initiated rate reviews by sending requests to the military departments three additional

³⁴Effective July 2009, DSCA increased two of the seven transportation fee rates. Specifically, the rate for DOD movement to a foreign inland location in Newfoundland, Labrador, Thule, Iceland, South America, Asia, Africa, and the Middle East was increased from 16.25 percent to 22.25 percent, a 37 percent increase. The rate for DOD movement to a foreign port in the same countries was increased from 13.25 percent to 19.25 percent, a 45 percent increase.

times for data DSCA did not use, thereby placing an unnecessary burden on the military departments. Specifically, DSCA requested data from the military departments in November 2011, September 2013, and November 2014. After obtaining the data from the military departments, DSCA officials said that management decided DSCA would not analyze the data due to competing priorities, and DSCA did not use these data for any other purpose. Air Force officials said that the months of work put into responding to each of DSCA's rate review requests seemed like a waste of resources because their data has consistently shown that the transportation fees collected were drastically higher than the related costs and yet the fee remained unchanged for years. To respond to DSCA's request for data for the fiscal year 2018 rate review, each military department spent between 2 to 4 months of staff time to collect and prepare the data, according to military department officials. Asking for and then not using such data put an unnecessary burden on the military departments and wasted DOD staff resources.

Without clearer internal guidance for its rate reviews regarding their timing and the analysis needed, it will be difficult for DSCA management to make appropriate fee-setting decisions based on future rate reviews. Federal internal control standards state that effective internal guidance communicates the who, what, when, where, and why of what needs to be accomplished.³⁵ According to DSCA officials, DSCA is considering conducting its next transportation fee rate review in fiscal year 2020, with a goal of lowering the FMS transportation account balances. DSCA officials' ability to meet this goal could be hindered without more clarity about the timing of the reviews and more rigorous analysis that involves explicit goals, such as for the level of alignment between cost and fee or of the account balances.

DSCA's Rate Structure Hinders Its Ability to Set Appropriate Transportation Fee Rates

The structure of the FMS transportation fee rate further hinders DSCA's ability to set appropriate rates. According to DSCA officials, the current rate structure was developed to use data that are easily available, which limits DOD's administrative burden in calculating the fee. However, our analysis raises concerns about the extent to which the current rate structure may have negative implications for the transportation fee's equity, efficiency, and revenue adequacy. We have previously reported that fee design should balance ways to encourage greater efficiency,

³⁵[GAO-14-704G](#).

equity, and revenue adequacy while reducing administrative burden on the agency and payers of the fees, as shown in Table 4.³⁶ These factors interact and often conflict with each other so that tradeoffs among these factors should be considered when designing a fee's structure.³⁷

Table 4: Factors to Consider When Designing the Structure of Fees

Factor	Explanation of Factor
Administrative burden	<ul style="list-style-type: none"> The cost of administering the fee, including the cost to the agency of collection and enforcement. Any administrative costs imposed on the payers of the fee.
Efficiency	<ul style="list-style-type: none"> User fees can simultaneously constrain demand and reveal the value that beneficiaries place on the service when identifiable beneficiaries pay for the costs of services.
Equity	<ul style="list-style-type: none"> All beneficiaries of a service pay their fair share. This can have multiple facets: under the beneficiary-pays principle, the beneficiaries of a service pay for the cost of providing it; under the ability-to-pay principle, beneficiaries who are more capable of bearing the burden of fees should pay more for the service than those with less ability to pay.
Revenue adequacy	<ul style="list-style-type: none"> The extent to which the fee collections cover the intended share of costs. This also incorporates the concept of revenue stability, or the degree to which short-term factors influencing the program may affect the level of fee collections.

Source: GAO analysis. | GAO-19-678

The current transportation fee rate structure limits DSCA's administrative burden because it relies on only a few factors, which involve easily accessible data, but these factors vary considerably from those TRANSCOM uses to price its transportation. The FMS transportation fee amount charged to purchasers is generally based on three factors, which should be identified in FMS agreements: (1) the price of the item; (2) the foreign destination rate area,³⁸ and (3) the extent of U.S. government responsibility for transporting the item (e.g., to an inland destination in the

³⁶GAO-08-386SP. The concept of revenue adequacy also incorporates the concept of revenue stability.

³⁷For example, a fee closely aligned with the cost of the services provided to a particular user may promote efficiency and the beneficiary-pays aspect of equity, but could impose a higher administrative burden and conflict with the ability-to-pay aspect of equity.

³⁸For the rate areas, DSCA divides the world such that it charges one rate for all transportation to Europe, Hawaii, Central America, the Caribbean Basin, and Mediterranean ports, and another rate for all transportation to Newfoundland, Labrador, Thule, Iceland, South America, Asia, Africa (other than Mediterranean ports), and the Middle East. As of August 2018, the second rate was 1.75 percentage points higher than the first rate.

continental United States or to a foreign inland or port destination).³⁹ At the time of the FMS agreement, DSCA and the military departments lack information about other factors that would make it easier for DOD to set fee rates such that fees would approximate the actual cost of the transportation. For example:

- **Mode.** DOD may not know how it will move the items at the time of the FMS agreement, and costs vary depending on the mode of transportation, such as by air or a surface vessel.
- **Route.** Although DOD should be aware of the final destination for items, DOD may be unaware of where the shipment will originate or the specific route the items will take, and transportation costs can vary depending on the specific route. For example, to transport goods in a 20-foot container on a surface vessel door-to-door from a location on the East Coast of the United States to Afghanistan in fiscal year 2018, TRANSCOM rates ranged from \$548.85 to \$1,077.03 per measurement ton shipped, depending on the specific route, whereas DSCA's fee rates would be constant and applied to the price of the items.

Also, even if DOD knew the exact mode and route, approximating the exact cost for each shipment would be difficult because TRANSCOM updates its rates annually, and shipments often occur years after signing the FMS agreement.

The distinct factors used to determine the fee and cost for FMS transportation make it difficult for the cost and fee to align, which has potential implications for the fee's equity. Although the data DSCA obtained from the military departments for its fiscal year 2018 rate review was unsuitable for that purpose because it was not timely or statistically sampled, we performed extensive data reliability procedures to determine that the individual cost and fee data points are reliable and as a result analyzed these data to obtain insights into the extent to which the cost

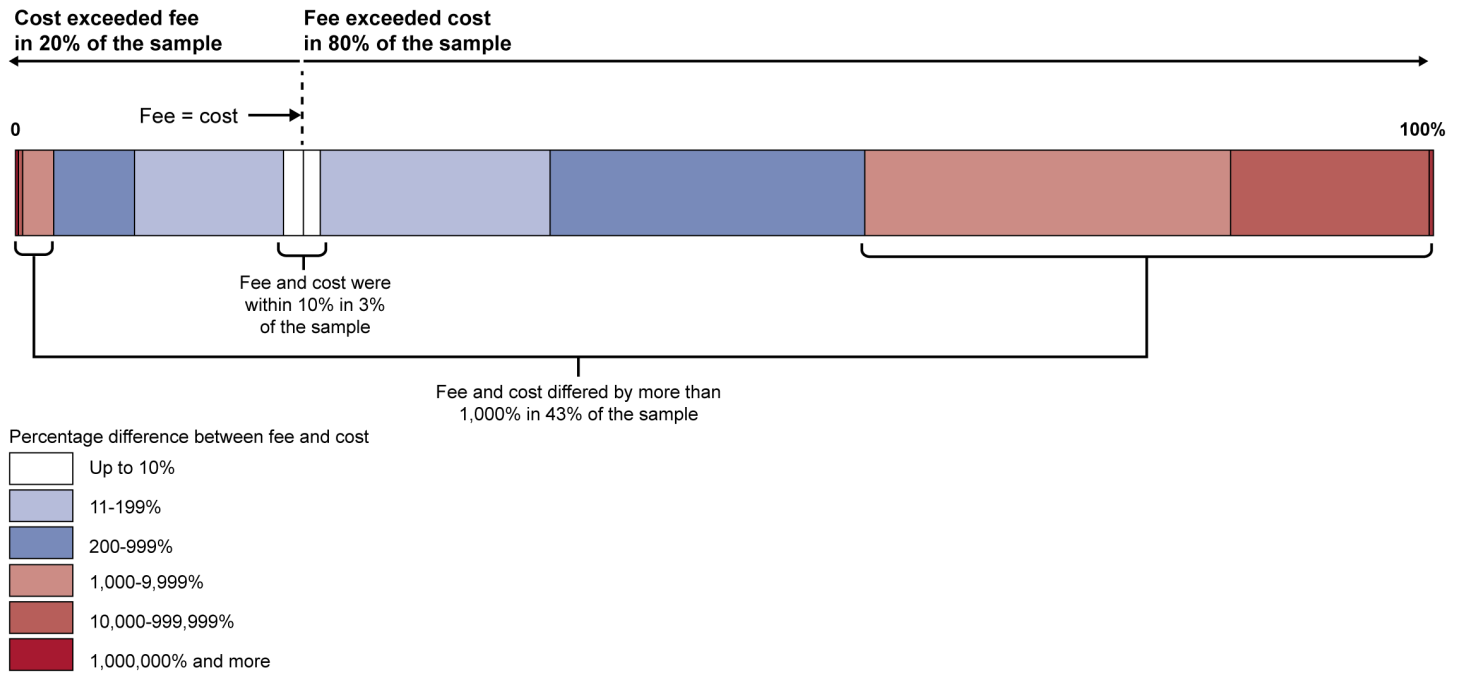
³⁹Certain exceptions exist to this base rate structure. For orders of defined quantities of goods, DOD only charges the full transportation fee rate to the first \$10,000 of the item price and multiplies the remaining price by 25 percent of the fee rate to determine the total transportation fee for that item. Also, for stock items that the Defense Logistics Agency ships from its warehouses, DOD reduces the transportation fee rate by 2.75 percentage points to avoid double-charging the purchaser because the Defense Logistics Agency builds an equivalent amount into its items' prices to compensate the agency for its related work.

and fee were aligned within that sample.⁴⁰ As shown in figure 9, we found extreme differences between the transportation cost billed to the FMS transportation accounts and the fee the purchaser paid. Within this nongeneralizable sample, costs and fees were within 10 percent of each other for only 30 of the 1,152 cases or shipments (3 percent), whereas the difference was more than 1,000 percent higher or lower for 492 of the cases or shipments (43 percent). In addition, we identified five instances of the difference between the cost and the fee exceeding 1,000,000 percent.⁴¹ Although these data were not systematically sampled to ensure they would be indicative of the full population of shipments, the high incidence of such large differences is concerning. Within this sample, we also found that certain countries were either always over-charged or always under-charged. Since the rate review data are not generalizable, this pattern may or may not be consistent across FMS shipments. However, such a pattern could plausibly occur due to the differences between TRANSCOM's and DSCA's rate areas.

⁴⁰For a detailed description of our data reliability procedures, see appendix I.

⁴¹In aggregate for this nongeneralizable sample, we found that the average fees exceeded the average costs by 143 percent while the percentage difference between the median fee and cost was 857 percent.

Figure 9: Comparison of Foreign Military Sales Costs and Fees in the Data the Military Departments Submitted for the Defense Security Cooperation Agency Fiscal Year 2018 Transportation Fee Rate Review



Source: GAO analysis of Department of Defense data. | GAO-19-678

Note: The sample of data shown here include data provided to DSCA by the Army, Air Force, and Navy, which were provided, respectively, at the case; shipment order (i.e., requisition); and shipment level to compare historical costs and fees. Due to the structure of DSCA's requests for these data, these data are not generalizable to all FMS shipments for the related time period, which spanned over 5 or more years preceding the rate review.

Potential concerns about the fee structure's efficiency and revenue adequacy also stem from the difficulty in aligning the current fee structure with related costs.

Efficiency. The large disparities between cost and fee in the current FMS transportation fee rate structure may be leading some FMS purchasers to choose not to use DTS. According to Army officials, some FMS purchasers choose to use their own freight forwarders instead of DTS because of a perception that the FMS transportation fee is too high. These decisions could have broader effects on DTS. According to TRANSCOM, the additional demand from FMS purchasers allows TRANSCOM to better leverage DTS, such as by filling excess capacity with paying cargo and supporting training needs to maintain combat readiness.

Revenue adequacy and stability. The potentially large differences between the transportation cost and fee resulting from the current FMS transportation fee rate structure has led to large fluctuations in collections and expenditures over time. For example, in fiscal years 2009 and 2011, DSCA had to redistribute a combined \$130 million into the main FMS transportation account from the FMS administrative fee account to cover costs and avoid insolvency.

Around the time of the fiscal year 2009 rate review, DSCA began reviewing the fee rate's structure as part of an overall attempt to address issues related to the transportation account nearing insolvency. As part of that review, DSCA worked with the military departments and TRANSCOM to assess factors such as administrative burden, data availability, and ability to more accurately charge transportation costs to FMS purchasers, which would have enhanced the fee's equity and efficiency. Specifically, they considered the benefits and costs of six alternative rate structures:

- Three of the six options would have involved replacing the rate-based fee for some or all shipments, by charging actual transportation costs or estimating likely actual costs per type of item. According to documentation from this review, the DOD agencies said these three options would have placed high administrative burdens on the military departments and required changes to military department or TRANSCOM information systems.
- The other three options the DOD agencies considered would have modified the structure of the current rate-based fee to take into account additional factors, such as transportation method (e.g., air) and item weight, or creating additional rate areas to target specific locations where costs of transportation were higher. The agencies determined that some of these options would have a lower administrative burden than the first three options.

However, DSCA decided to maintain its current fee rate structure and address the potential insolvency through other approaches such as by redistributing funds from the FMS administrative fee account to the transportation account. According to DSCA officials, DSCA made this decision because it could not obtain agreement with the military departments and TRANSCOM on any of the other options. DSCA has not since reviewed the rate structure.

DSCA Internal Guidance to the Military Departments Does Not Specify Key Details on How to Estimate Transportation Prices for Certain Items

DSCA provides internal guidance to the military departments on how to estimate the transportation prices to be charged for certain items, but the internal guidance does not specify key details about how to calculate the estimates. As a result, the military departments follow different procedures for estimating these prices, and individual military department procedures may differ over time depending on staff turnover. Federal internal control standards state that management should use quality financial information that is complete and reasonably free from error, and that effective internal guidance informs users of the who, what, when, where, and why of what needs to be accomplished, thereby helping to retain organizational knowledge.⁴²

Estimated Transportation Prices for Certain Items

For certain items that need to be shipped via the Defense Transportation System, such as goods with sensitive or hazardous materials, and for which charging the transportation fee rate would significantly differ from transportation costs, DOD may instead charge a set transportation price per item. The fees collected from these estimated prices and the costs to transport these items are paid in and out of the FMS transportation accounts.

These prices are not location-specific because DOD charges each purchaser of this item the same estimated price. According to DOD officials, such items are often low-weight, high-cost items, such as missiles, for which the usual transportation fee rate could greatly overcharge the FMS purchaser.



Source: DOD documents and officials (text); U.S. Navy photo by Lt. Mike Wilcox (image). | GAO-19-678

DSCA's internal guidance for how to estimate these transportation prices includes limited information and does not take into account key information for accurately estimating transportation costs. Specifically, the guidance lists certain types of transportation cost elements to include and not to include in these price estimates. For example, estimated port handling costs should be included while security costs should be charged to the FMS purchaser separately. The guidance also indicates the estimates should be on a per-item basis with two potential prices to transport each item, one for any transportation within the United States and one for transportation to any foreign destination. Other key factors in transportation costs, such as the transportation mode or specific origin or destination, are not considered. Also, DOD charges these prices per item, although economies of scale can be gained by transporting batches of the same item together.

The lack of specificity in DSCA's internal guidance has led the military departments to adopt inconsistent estimation processes that may not lead prices to approximate actual costs. These inconsistent processes could lead DOD to charge FMS purchasers more or less than DSCA intends and ultimately affect account balances. For example:

Origin and destination. The three military departments take different approaches to compensate for having to estimate the cost of transporting an item without knowing its specific origin and destination. Although all military departments follow the same general process of estimating potential transportation costs for commonly used origin and destination ports and averaging these to attempt to estimate these prices, they all

⁴²[GAO-14-704G](#).

use different locations to create their estimates, which leads to different pricing. For example, one command within Army uses a central location within the United States as the origin for its estimates to simulate an average of potential costs for transportation from any continental United States location. However, according to Army officials, another command within Army attempts to ensure that the transportation price estimated will cover costs by simulating a “worst case scenario” by basing its estimates on locations distant from each other.

Batch shipments. The military departments also vary in terms of how they estimate per item costs for items that could often be transported in batches. Air Force and Navy calculate how many of an item can fit in a container, and then divide the average price estimated to transport such a container by this batch size to determine final pricing, but Army does not.⁴³ When Air Force and Navy estimate prices this way, they do not require shipments to be transported in a container of this size or for purchasers to buy or receive these items only in batches of this size, which could lead the price charged to vary greatly from the actual costs. For example, for one type of missile, Air Force determined that 20 of them could fit in a container and therefore divided the average price it had estimated to transport a container by 20 before submitting the price to DSCA. Therefore, if only one of the item were purchased, instead of the 20 built into the estimate, the transportation cost could be about 20 times the fee.

The lack of specificity of DSCA’s guidance has also led to large changes in one of the military departments’ estimated prices after staff turnover. According to the Air Force official who prepared Air Force’s 2018 updates to these prices, that was the first year that official estimated these prices after another Air Force official had done so through 2015. The new Air Force official said that Air Force had not updated its prices during the previous 3 years because it lacked rates to estimate the costs of transporting explosive materials by ocean vessel. After receiving guidance from DSCA to exclude these rates from their estimates, the new Air Force official updated the prices for 2018. When doing so, this Air Force official found that some of the updated price estimates were much higher than the prior prices due to increased port handling rates, whereas

⁴³According to Army officials, one part of Army will sometimes use the number of items that could fit in a 20-foot container to divide the port handling rate but not to estimate the cost for transporting the item itself, while another part of Army will instead divide by the average quantity sold to determine the unit price estimate.

the prices to transport items to foreign destinations were at times lower due to lower air rates used in the estimates. For example, the price to transport a certain item within the continental U.S. had been set at \$278.00 per item for 2015 through 2017, and the 2018 price estimate was \$8,447.00. DSCA initially accepted the updated prices, but Air Force later rescinded them after foreign partner countries voiced concerns about the increased prices affecting existing contracts and Air Force was unable to prove that the new estimates better approximated actual costs without the ability to compare actual bills with the price estimates. According to the responsible Air Force official, the calculation process from 2015 was used to recalculate the 2018 prices and was again used for 2019, albeit with current fiscal year rate information, due to continued uncertainty regarding this process.

Since late 2016, the military departments have voiced concerns to DSCA regarding the difficulty of following DSCA's internal guidance to estimate these transportation prices. In particular, in late 2016, Army officials developed a white paper for DSCA that described challenges developing these estimated prices posed by updates to how TRANSCOM calculates its transportation pricing. In September 2018, Air Force officials also raised various concerns regarding the accuracy of the prices, such as concerns about how the batch size of a shipment affects per item costs and the lack of key details affecting transportation costs. Military department officials said they would prefer more specific guidance from DSCA that could help them to more uniformly calculate these prices. In January 2019, DSCA officials stated they were at an early stage of exploring possible changes to the information required to calculate these types of transportation prices. In May 2019, DSCA officials stated that they were still working to define the problem and how it could be addressed. Further research into the military departments' difficulties in establishing these price estimates and the costs and benefits of the methodologies they use would better inform DSCA on what pricing process could most accurately reflect costs moving forward.

Conclusions

FMS is one of the primary ways the U.S. government engages in security cooperation with its foreign partners, by annually selling them billions of dollars in defense items and services. When transporting FMS items on their behalf, DOD charges purchasers a transportation fee such that, according to DOD, it should involve "no profit, no loss"—foreign partners should not be charged excessive fees and fee revenue should cover the program's operating costs. However, from fiscal year 2007 to 2018, the FMS transportation accounts experienced substantial balance growth of

over 1300 percent. To address risks such as the historical unpredictability of collections and expenditures prior to recent dramatic account growth, DSCA implemented processes to conduct daily and annual management oversight of the accounts. However, the effectiveness of these processes is limited by a lack of specific internal guidance. In particular, although the daily reviews are meant to keep DSCA aware of significant changes in the accounts and ensure that they maintain healthy balances, DSCA has not specified what should be considered as significant changes or how to calculate healthy target levels for the accounts. Lack of rigorous annual review processes has also led the annual reports provided to DSCA management to be missing key details. In particular, they have contained incomplete information on the causes for account trends and have omitted information on the source of \$130 million that had been redistributed into this fee account from the FMS administrative fee account in fiscal years 2009 to 2011 to address a danger of insolvency that the FMS transportation accounts no longer face. The resulting reports inhibit DSCA management's ability to oversee the accounts at a time when they have grown so quickly. In addition, a lack of clear internal guidance explaining how to assess when redistributions are needed and when to return unused BPC-specific transportation funds may lead to a surplus of funds in the FMS transportation accounts that could be used for other purposes.

Similarly, DSCA has established a process to review FMS transportation fee rates but this process has several weaknesses that may skew DSCA's rate setting decisions. DSCA's rate review process involves analysis of historical cost and fee data provided by the military departments, but due to unclear requests to the military departments, the process is burdensome and leads to data that are untimely and unsystematically sampled. Although DSCA requested such data from the military departments five times between fiscal years 2007 to 2018, DSCA only conducted rate reviews using these data twice because DSCA did not prioritize use of its resources for the other reviews. In addition, for the two reviews it did conduct, DSCA never used Air Force or Navy data because unclear guidance from DSCA and difficulties finding sufficient data across disparate DOD information systems limited the data Air Force and Navy could provide. Further, DSCA based their reviews on minimal internal guidance and used limited analysis and unclear criteria upon which to set new rates.

The current rate review process and the overall fee rate structure reduce DSCA's administrative burden, but raise various concerns regarding the fee's equity, efficiency, and revenue stability. DSCA also has similarly

unclear internal guidance for the military departments for situations when the FMS purchaser is charged a set transportation price per item instead of a transportation fee rate. By strengthening these rate setting processes, DSCA would enhance its ability to manage account balances and to make timely decisions to ensure the FMS transportation fee rate is set to cover related transportation costs but not overcharge FMS purchasers.

Recommendations for Executive Action

We are making the following 10 recommendations to DOD:

The Secretary of Defense should ensure that the Director of DSCA clarify internal guidance for daily account reviews by specifying criteria for the level (such as percentage or dollar amount) of change in transportation account balances that would require DSCA to contact DFAS for further examination. (Recommendation 1)

The Secretary of Defense should ensure that the Director of DSCA establish a methodology to calculate a target range, with desired upper and lower bounds, for FMS transportation account balances that could be used to better inform DSCA's account reviews. (Recommendation 2)

The Secretary of Defense should ensure that the Director of DSCA modify the internal guidance for the annual review process to include the specific steps DSCA officials should take in preparing the annual report, including ensuring that they incorporate rigorous analysis into the annual reports. (Recommendation 3)

The Secretary of Defense should ensure that the Director of DSCA develop internal guidance related to the redistribution of funds between the FMS trust fund fee accounts. Such internal guidance could include criteria for when to consider redistributing funds between accounts and for when to return those funds, how to analyze the amount of any redistributions needed, and how to clearly report any redistributions to DSCA management. (Recommendation 4)

The Secretary of Defense should ensure that the Director of DSCA assess whether funds redistributed from the administrative account to the transportation account should be moved back to the FMS administrative account and document this decision. If the Director of DSCA determines that the funds should be moved back to the FMS administrative account, the Director should ensure the movement of funds in accordance with this decision. (Recommendation 5)

The Secretary of Defense should ensure that the Director of DSCA develop internal guidance for the steps that DSCA, in combination with DFAS, should undertake when a BPC-specific transportation account closes to help ensure that any remaining unused funds are transferred to the miscellaneous receipts of the U.S. Treasury in accordance with DOD officials' stated intention to do so. (Recommendation 6)

The Secretary of Defense should ensure that the Director of DSCA create specific internal guidance for how and from where data should be obtained to be used for its transportation fee rate reviews and the timeframes the data should cover to ensure DSCA has a systematic sample upon which to base its rate setting decisions. This updated internal guidance should be based on consultations with the military departments, DFAS, and TRANSCOM on which sources of transportation cost and fee data are the most reliable and comparable for use in its FMS transportation fee rate reviews. (Recommendation 7)

The Secretary of Defense should ensure that the Director of DSCA develop specific internal guidance to follow when performing transportation fee rate reviews. Such internal guidance could specify when these reviews should occur; a process to obtain management commitment to complete a review before DSCA requests that the military departments compile data for it; and a process for performing the reviews that includes developing clear, documented goals and an appropriate level of analysis to best ensure that DSCA's analysis meets those goals. (Recommendation 8)

The Secretary of Defense should ensure that the Director of DSCA conduct a review of the current structure of the FMS transportation fee rate, in consultation with other relevant DOD agencies, to determine if other rate structures could better balance considerations related to administrative burden, equity, efficiency, and revenue adequacy. (Recommendation 9)

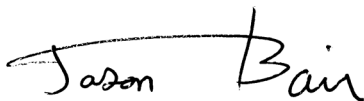
The Secretary of Defense should ensure that the Director of DSCA clarify internal guidance for the military departments on how to calculate the estimated actual transportation prices to charge FMS purchasers for certain items, such as by specifying a calculation methodology. This updated internal guidance should be based on consultations with the military departments, TRANSCOM, and any other relevant DOD components on which sources of data and which calculation methodologies would be most accurate. (Recommendation 10)

Agency Comments

We provided a draft of this report to DOD and State for review and comment. DSCA provided written comments on behalf of DOD, which are reprinted in appendix II. DSCA concurred with all of our recommendations, and identified actions it plans to take to address them and initial steps it has begun to take toward addressing some of them. We also received technical comments from DOD, which we incorporated in our report as appropriate. State did not provide any written or technical comments.

We are sending copies of this report to the appropriate congressional committees, the Secretary of Defense, the Secretary of State, and other interested parties. In addition, this 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) 512-6881 or BairJ@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.



Jason Bair
Director, International Affairs and Trade

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House of Representatives

Appendix I: Objectives, Scope & Methodology

This report examines (1) the balances maintained in the Foreign Military Sales (FMS) transportation accounts for fiscal years 2007 through 2018, (2) the extent to which the Defense Security Cooperation Agency (DSCA) established and implemented policies and procedures to help ensure management oversight of the transportation accounts, and (3) the extent to which DSCA processes for setting transportation fee rates ensure that these rates are set appropriately.

To examine the balances of the FMS transportation accounts, we analyzed fiscal year 2007 to 2018 overall collections, expenditures, and balance data for each of the individual FMS transportation accounts maintained by the Defense Finance and Accounting Service (DFAS) in the Defense Integrated Financial System (DIFS). We chose to review data from these fiscal years based on data availability. To determine the reliability of these data, we reviewed the data for internal consistency by reviewing for duplicate entries, gaps, and obvious errors, and we compared the data to similar data obtained for a prior review of two other FMS fees.¹ We also reviewed relevant documentation, including annual account assessments conducted by DSCA and the internal control procedures for conducting such reviews. Lastly, we interviewed DFAS and DSCA officials to clarify questions about how to interpret the data. We did not conduct any independent testing of the data obtained from DFAS to determine whether the amounts reflected correct payments made toward accurate billings. As such, when presenting collections and expenditures, we note that they reflect the amount of funds in the aggregate moved into and out of the FMS transportation accounts. We determined the collections, expenditures, and balance data to be reliable for the purpose of showing the movement of funds in and out of the FMS transportation accounts and the accounts' balances over time.

To analyze trends in collections into and expenditures from the FMS transportation accounts, such as in figures 4 and 6, we adjusted the data to remove the effects of two redistributions from the FMS administrative fee account that took place in fiscal years 2009 and 2011, as well as amounts that were moved into certain new Building Partner Capacity (BPC) transportation accounts to initially fund them in fiscal years 2012 and 2015. We reviewed documentation related to the two redistributions of funds from the FMS administrative fee account to the transportation

¹GAO, *Foreign Military Sales: Controls Should Be Strengthened to Address Substantial Growth in Overhead Account Balances*, [GAO-18-401](#) (Washington, D.C.: May 10, 2018).

account and the initial funding amounts allocated to new BPC transportation accounts, and interviewed DFAS and DSCA officials to understand how they accounted for these fund movements.

To assess the extent to which DSCA established and implemented policies and procedures to help ensure management oversight of the FMS transportation accounts, we reviewed DSCA internal guidance included in DSCA's Managers' Internal Control Program (MICP) procedures for daily and annual FMS transportation account reviews, federal internal control standards, our prior report on federal user fees,² and documentation showing how DSCA officials implemented those procedures. We also interviewed DSCA officials responsible for these reviews.

- **Daily reviews.** We reviewed a DSCA spreadsheet in which DSCA officials documented the daily reviews they conducted in fiscal year 2018. We chose to review this one fiscal year of data because it was the most recent complete fiscal year and would thereby be most relevant to current implementation. We also analyzed these data against the related MICP procedures, interviewed relevant DSCA and DFAS officials, and requested documentation of related correspondence to determine the extent to which DSCA consistently took any actions in response to these reviews. Because the data in these daily reviews is sourced from the same balance data in DIFS as we analyzed for our first objective, we compared the data between the two sources to ensure its consistency, and interviewed DFAS and DSCA officials about how these data were pulled for the daily reports. Based on these steps, we determined these data to be sufficiently reliable for assessing DSCA's implementation of the daily review process.
- **Annual reviews.** We reviewed the annual reports DSCA created for fiscal years 2015 to 2018—all of the years for which DSCA created such reports—and interviewed DSCA officials about their process for creating these reports and other aspects of the MICP procedures for the annual review. To determine the extent to which the annual reports accurately convey information about the causes of trends in the accounts, we compared account expenditures data to oil price

²GAO, *Standards for Internal Control in the Federal Government*, [GAO-14-704G](#) (Washington, D.C.: September 2014), and GAO, *Federal User Fees: Fee Design Options and Implications for Managing Revenue Instability*, [GAO-13-820](#) (Washington, D.C.: Sept. 30, 2013).

data for fiscal years 2007 to 2018. We performed this analysis because DSCA's annual reports cite declining oil prices as a factor contributing to the increasing account balances in the FMS transportation accounts. For data on oil prices, we analyzed data from the U.S. Energy Information Agency on Cushing, Oklahoma, West Texas Intermediate oil prices by month, which is an established source for these data that is used commonly as a global benchmark for oil prices. As such, we determined these data to be reliable to use for this purpose. We also reviewed legislation that changed the rates the Department of Defense (DOD) can charge for FMS air shipments, and interviewed DSCA and U.S. Transportation Command officials about the effect and timing of this legislative change. We also reviewed the fiscal year 2015 to 2018 annual reports for the FMS transportation and administrative accounts to determine whether the redistributions that had been made from the FMS administrative account to the FMS transportation accounts were clearly reported, and reviewed related internal guidance in DOD's Financial Management Regulations.

For BPC-specific transportation accounts, we reviewed DOD's Financial Management Regulations and related DSCA documentation against federal internal control standards regarding the clarity of internal control guidance.³ We also interviewed DSCA officials and received written responses to questions from DOD's Office of the Under Secretary of Defense (Comptroller) regarding the process DSCA should follow when any of the BPC-specific transportation accounts close.

To review the extent to which DSCA processes ensure that transportation fee rates are set appropriately, we reviewed DSCA guidance and interviewed DSCA and military department officials about the different processes DSCA uses to set transportation fees. For the transportation fee rate review, we reviewed DSCA's MICP procedures and the requests DSCA sent to the military departments for data to analyze in its rate reviews against the Statement of Federal Financial Accounting Standards No. 4, our prior report on federal user fees,⁴ and federal internal control

³[GAO-14-704G](#).

⁴GAO, *Federal User Fees: A Design Guide*, [GAO-08-386SP](#) (Washington, D.C.: May 2008). In particular, this report stated that fee design should balance ways to encourage greater efficiency, equity, and revenue adequacy while reducing administrative burden on the agency and payers of the fees.

standards.⁵ To understand the reliability of the data the military departments submitted to DSCA and what these data showed in terms of the alignment between transportation costs and fees, we reviewed the data, including by performing internal consistency checks on the data, such as by reviewing it for duplicate entries, gaps, or obvious errors. We also reviewed any military department procedures for compiling these data and interviewed or received written responses from military department officials responsible for compiling the data. Based on these steps, we determined that these data were reliable for our purposes of making some comparisons between costs and fees for the sample provided. However, as noted earlier in this report, the departments could only provide partial data, which they did not select using systematic sampling techniques to ensure the data were indicative of the full population of shipments. Therefore, we determined that these data were unsuitable for DSCA's purpose of making fee-setting decisions.

We also reviewed DSCA documentation of the analysis it performed for its 2009 and 2018 transportation fee rate reviews, including analysis spreadsheets and briefings to DSCA management on the reviews' results. Regarding instances when DOD charges FMS purchasers estimated transportation prices instead of a transportation fee rate, we reviewed DSCA guidance on this process in the Security Assistance Management Manual against related federal internal control standards. We also reviewed any internal guidance the military departments have developed to further guide these estimation processes, examples of the military department estimation processes, and other documents that showed concerns regarding these processes that the military departments had previously raised to DSCA. We interviewed and sent questions for written responses to DSCA and military department officials regarding these processes and the military departments' concerns.

We conducted this performance audit from May 2018 to September 2019 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.

⁵[GAO-14-704G](#).

Appendix II: Comments from the Department of Defense



DEFENSE SECURITY COOPERATION AGENCY
201 12TH STREET SOUTH, SUITE 101
ARLINGTON, VA 22202-5408

11 SEP 2019

Mr. Jason Bair
Acting Director, International Affairs & Trade
U.S. Government Accountability Office
441 G Street, NW
Washington, DC 20548

Dear Mr. Bair:

Enclosed is the Department of Defense (DoD)'s response to the Government Accountability Office (GAO) Draft Report, GAO-19-678 "FOREIGN MILITARY SALES (FMS): DoD Should Strengthen Oversight of Its Growing Transportation Account Balances," dated August 13, 2019 (GAO Code 102811).

Thank you for the opportunity to respond to this report. We appreciate any opportunity to learn how we can improve our processes for the effective management of the FMS Transportation Surcharge Account, which will benefit the entire security cooperation community. I concur with the 10 identified recommendations. DSCA has proactively developed Corrective Action Plans to insure timely compliance with the GAO recommendations. I am pleased to state we have already begun implementing some of the recommendations.

After a thorough analysis, we concur with your recommendation to return the funds redistributed to the FMS Transportation Surcharge Account back to the FMS Administrative Surcharge Account. The initial redistribution allowed DSCA to fund the required FMS transportation services which supports the security cooperation community. Now that the FMS Transportation Surcharge Account is at a healthy level, we have initiated the process to return \$130 million back to the FMS Administrative Surcharge Account.

To address the recommendations pertaining to the review of our transportation rate review process, we have proactively established a FMS Transportation Working Group with the Military Departments. The Working Group will review and analyze our rates and pricing policies and will provide the necessary data required for in-depth rate reviews. The Working Group has already implemented a milSuite Working Group website for integrating Implementing Agency personnel in the development and review of FMS Transportation guidance.


I concur with your recommendation on setting an upper and lower bound levels for the FMS Transportation Surcharge Account. As we successfully implemented one of your previous recommendations by establishing an upper bound limit for both the FMS Administrative Surcharge Account and Contract Administrative Surcharge Account, we will follow the same rigor in developing one for Transportation. We are currently testing newly developed daily and annual review processes to use in establishing the upper and lower bound limits for this account.

**Appendix II: Comments from the Department
of Defense**

Thank you again for the report. The provided recommendations validates our efforts in the refinement of our processes to drive better management and compliance of FMS Transportation Surcharge Account.

Please direct any questions or comments regarding this response to my primary action officer for this matter, Ms. Jeneen Caldwell, jeneen.k.caldwell.civ@mail.mil, (703) 697-8923, or the DSCA audit liaison officer, Mr. Eric Ferguson, dsca.audit@mail.mil, (703) 697-9261.

Sincerely,


Charles W. Hooper
Lieutenant General, USA
Director

Enclosure:
As stated

GAO DRAFT REPORT DATED AUGUST 13, 2019
GAO-19-678 (GAO CODE 102811)

**“FOREIGN MILITARY SALES: DOD SHOULD STRENGTHEN OVERSIGHT OF ITS
GROWING TRANSPORTATION ACCOUNT BALANCES”**

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

RECOMMENDATION 1: The GAO recommends that the Secretary of Defense should ensure that the Director of DSCA clarify internal guidance for daily account reviews by specifying criteria for the level (such as percentage or dollar amount) of change in transportation account balances that would require DSCA to contact DFAS for further examination.

DoD RESPONSE: Concur. DSCA continues to review the daily FMS Transportation Surcharge Account balances on a daily basis. As a part of internal control processes, DSCA will establish a percentage threshold to monitor the level of change in the transportation accounts and request DFAS and MILDEPS to clarify the abnormality.

RECOMMENDATION 2: The GAO recommends that the Secretary of Defense should ensure that the Director of DSCA establish a methodology to calculate a target range, with desired upper and lower bounds, for FMS transportation account balances that could be used to better inform DSCA's account reviews.

DoD RESPONSE: Concur. DSCA is updating its internal guidance and MICP for reviews to establish specific criteria for measuring, identifying and reporting the health of DSCA transportation accounts using appropriate upper and lower bound limits.

RECOMMENDATION 3: The GAO recommends that the Secretary of Defense should ensure that the Director of DSCA modify the internal guidance for the annual review process to include the specific steps DSCA officials should take in preparing the annual report, including ensuring that they incorporate rigorous analysis into the annual reports.

DoD RESPONSE: Concur. DSCA is updating its internal guidance and MICP for annual reviews to establish specific criteria for measuring, identifying and reporting the health of DSCA transportation accounts. Additional rigorous analysis will include detailed historical information on each account.

RECOMMENDATION 4: The GAO recommends that the Secretary of Defense should ensure that the Director of DSCA develop internal guidance related to the redistribution of funds between the FMS trust fund fee accounts. Such internal guidance could include criteria for when to consider redistributing funds between accounts and for when to return those funds, how to

analyze the amount of any redistributions needed, and how to clearly report any redistributions to DSCA management.

DoD RESPONSE: Concur. DSCA is updating its annual review internal guidance, based on specific criteria, on when it is appropriate to redistribute funds between the surcharge accounts and the required analysis to make that determination. This in-depth analysis will help DSCA's ability to make informed decisions in overseeing the FMS fees.

RECOMMENDATION 5: The GAO recommends that the Secretary of Defense should ensure that the Director of DSCA assess whether funds redistributed from the administrative account to the transportation account should be moved back to the FMS administrative account and document this decision. If the Director of DSCA determines that the funds should be moved back to the FMS administrative account, the Director should ensure the movement of funds in accordance with this decision.

DoD RESPONSE: Concur. The FMS Transportation Surcharge Account has returned to healthy levels over the past 5 years. Therefore, DSCA has initiated the process to return \$130 million from the FMS Transportation Surcharge Account back to the FMS Administrative Surcharge Account from which the funds originated.

RECOMMENDATION 6: The GAO recommends that the Secretary of Defense should ensure that the Director of DSCA develop internal guidance for the steps that DSCA, in combination with DFAS, should undertake when a BPC-specific transportation account closes to help ensure that any remaining unused funds are transferred to the miscellaneous receipts of the U.S. Treasury in accordance with DOD officials' stated intention to do so.

DoD RESPONSE: Concur. DSCA is developing guidance, instructing DFAS to close specific BPC transportation accounts after all appropriations within the account have cancelled and transfer the unused funds to the miscellaneous receipts of the U.S. Treasury.

RECOMMENDATION 7: The GAO recommends that the Secretary of Defense should ensure that the Director of DSCA create specific internal guidance for how and from where data should be obtained to be used for its transportation fee rate reviews and the timeframes the data should cover to ensure DSCA has a systematic sample upon which to base its rate setting decisions. This updated internal guidance should be based on consultations with the military departments, DFAS, and TRANSCOM on which sources of transportation cost and fee data are the most reliable and comparable for use in its FMS transportation fee rate reviews.

DoD RESPONSE: Concur. DSCA proactively established a Transportation Working Group with the relevant DoD Agencies to address the proper data sources for rate reviews. Based on our review of previously provided data and in-depth discussions with the Working Group, the decision was made that all data for the rate reviews will come from common data systems and will be submitted in a uniform manner, to ensure commonality and comparability throughout.

Upon finalization of data selection and review process, this will be documented via internal guidance and MICP update.

RECOMMENDATION 8: The GAO recommends that the Secretary of Defense should ensure that the Director of DSCA develop specific internal guidance to follow when performing transportation fee rate reviews. Such internal guidance could specify when these reviews should occur, a process to obtain management commitment to complete a review before DSCA requests that the military departments compile data for it, and a process for performing the reviews that includes developing clear, documented goals and an appropriate level of analysis to best ensure that DSCA's analysis meets those goals.

DoD RESPONSE: Concur. DSCA is developing clear internal guidance to ensure that comprehensive reviews of the transportation fee rate are to be completed every 5 years. As the most recent review was completed in 2018. The next transportation fee rate review is scheduled to be conducted in fiscal year 2023.

RECOMMENDATION 9: The GAO recommends that the Secretary of Defense should ensure that the Director of DSCA conduct a review of the current structure of the FMS transportation fee rate, in consultation with other relevant DOD agencies, to determine if other rate structures could better balance considerations related to administrative burden, equity, efficiency, and revenue adequacy.

DoD RESPONSE: Concur. DSCA proactively established a Transportation Working Group, with relevant DoD Agencies, to review the current rates and cost structure used for calculating costs that go into the FMS Transportation Account. The pricing methodology will go through a rigorous review and analysis, to determine if it still valid or if another methodology should be used. Upon completion, the process will be documented via internal guidance and MICP update.

RECOMMENDATION 10: The GAO recommends that the Secretary of Defense should ensure that the Director of DSCA clarify internal guidance for the military departments on how to calculate the estimated actual transportation prices to charge FMS purchasers for certain items, such as by specifying a calculation methodology. This updated internal guidance should be based on consultations with the military departments, TRANSCOM, and any other relevant DOD components on which sources of data and which calculation methodologies would be most accurate.

DoD RESPONSE: Concur. DSCA proactively established a Transportation Working Group, with relevant DoD Agencies, to review the transportation fee structure and the variances in pricing calculation methodologies used for costing the transportation of sensitive and hazardous end items. The review is to have the revised calculation method better align with TRANSCOM's transportation routes and contracting costs. Upon completion, the revised process and pricing calculation methodology will be documented via internal guidance and MICP update.

Appendix III: GAO Contact and Staff Acknowledgments

GAO Contact

Jason Bair, (202) 512-6881 or BairJ@gao.gov

Staff Acknowledgments

In addition to the contact named above, Cheryl Goodman (Assistant Director), Heather Latta (analyst in charge), Adam Peterson, Benjamin L. Sponholtz, John (Ryan) Bolt, Ming Chen, John Hussey, and Brandon Voss made key contributions to this report. Martin de Alteriis, Christopher Keblitis, Grace Lui, Susan E. Murphy, Laurel Plume, Heather Rasmussen, and Chanetta Reed also contributed to this report.

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