

DSCA 00-01
Inclusion of Offset Costs in Letters of Offer and Acceptance (LOAs)
19 January 2000

In reply refer to:
I-012655/99

Memorandum For: Deputy Under Secretary of the Army (International Affairs)
Attn: SAUS-IA-DSZ Department of the Army
Director, Navy International Programs Office
Department of the Navy
Deputy Under Secretary of the Air Force (International Affairs)
Department of the Air Force
Director, Defense Logistics Agency
Director, National Imagery And Mapping Agency
Director, Defense Threat Reduction Agency
Director, Defense Reutilization and Marketing Service
Director, Defense Information Systems Agency
Director, Defense Logistics Information Service
Deputy Director For Security Assistance,
Defense Finance and Accounting Service -- Denver Center

Subject: Inclusion of Offset Costs in Letters of Offer and Acceptance (LOAs)
(DSCA 00-01)

Reference: OUSD (A&T) Memorandum, "*Pricing Issues in Foreign Military Sales Contracts*," July 13, 1999

The referenced memorandum (attached) provided clarification of the requirements for including offset costs in pricing of Foreign Military Sales (FMS) contracts financed wholly with customer cash or repayable Foreign Military Financing (FMF) credits. Per this memorandum, contracting officers were advised to treat all offset costs as allowable FMS contract costs. Effective 14 Sep 99, the Defense Federal Acquisition Regulation Supplement (DFARS) was changed to reflect this policy. The DFARS, section 225.7303-2(a)(3) now states that "A U.S. defense contractor may recover all costs incurred for offset agreements with a foreign government or international organization if the LOA is financed wholly with customer cash or repayable foreign military finance credits." Nonrepayable FMF funds may not be used to pay offsets. The Omnibus Appropriation Act (P.L.106-113) which incorporated H.R.3427, signed 29 Nov 99, also made some changes to offset policy. The new law requires that 36(b)(1) notifications include a "description of any offset agreement with respect to such sale" and establishes a review commission to study the use of offsets in international defense trade.

In order to ensure our guidance is consistent with the DFARS and new legal requirements, the Security Assistance Management Manual (SAMM) must be revised. The following changes are effective immediately:

a. Paragraph 80106 is deleted in its entirety and is replaced as follows:

“**80106 Offset Costs** DFARS 225.7303-2(a)(3) allows US contractors to recover, under FMS contracts based on LOAs financed wholly by Purchaser cash or repayable FMF credits, costs of any offsets which are associated with those contracts. USG agencies may not enter into or commit US firms to any offset agreement. Any Purchaser requesting offset arrangements in conjunction with FMS should be informed that the responsibility for negotiating offset arrangements and satisfying all related commitments resides with the US firm involved. It is the responsibility of the implementing agency to specify to DSCA, in the transmittal of any Congressional Notification, LOA and any subsequent LOA modification or amendment, that offset costs have been included, if known. Information regarding offset costs and their recoupment through FMS follows:

A. Offset costs should be included as part of the line item(s) unit cost in P&A data and in estimated prices quoted in the LOAs.

B. For procurements where adequate price competition exists or it is anticipated, whether conducted by the Purchaser or by the USG, the USG will normally not have visibility as to whether offset costs are included in the price or the amount of such costs.

C. When the USG anticipates a noncompetitive procurement, it is the contractor’s responsibility to inform the implementing agency when estimated offset costs have been included in the FMS pricing information provided. The costs should be included as early as possible but before submittal of the LOA. Requests to include these costs after LOA acceptance will require an LOA modification or amendment.

D. It is inappropriate for USG personnel to discuss with the Purchaser the nature or details of an offset arrangement. However, if known, the fact that offset costs have been included in the P&A or LOA price estimate will be confirmed should the Purchaser inquire. The Purchaser should be directed to the US contractor for answers to all questions regarding its offset arrangement, including questions dealing with cost. Implementing agency involvement in any discussion of offset costs (beyond confirmation of the inclusion of these costs in price estimates) with the Purchaser requires case-by-case review and approval by DSCA.

E. All LOAs will include the offset note provided in paragraph 70105.L.4.”

b. Paragraph 70105.L.4. requires the inclusion of an offset note on all LOAs. To ensure the customer is aware that offset costs may be included in the FMS case, this paragraph/note is revised to read as follows:

“4. **Offset Costs**. (See paragraph 80106) All LOAs will contain the following note:

Offset costs may be included in this LOA if it is financed wholly by Purchaser cash or repayable credit. The DoD is not a party to any offset agreements/arrangements which may be required by the Purchaser in relation to the sales made in this LOA and assumes no obligation to administer or satisfy any offset requirements or bear any of the associated costs.”

This note must be included on any new LOAs written after the date of this memorandum. There is no requirement to add this revised note retroactively to any existing cases.

- c. Paragraph 70302 is updated to eliminate the phrase “(if known on the date of certification submittal)” from line 26. This change makes the paragraph consistent with the changes in P.L.106-113.
- d. Paragraph 70302.A.3.c. is updated to eliminate the phrase “(if known on the date of transmittal of such statement)” from line 4. Again, this makes the paragraph consistent with new legal requirements.
- e. Table 703-3, “Advance Notification Data” must be updated to reflect the requirement to include offset information as part of the advance notification. Paragraph p. is relabeled “q.” and a new p. is included as follows: “p. A description of any offset agreement with respect to this sale is included in the enclosed confidential attachment (if applicable). [*Note:* See Table 703-3B for the proper format.]”
- f. Table 703-3B is added as shown in attachment 2 of this memorandum.
- g. Table 703-5, “Statutory Notification Data,” must be updated to reflect the requirement to include offset information as part of the statutory notification. Paragraph o. is relabeled “p.” and a new o. is included as follows: “o. A description of any offset agreement with respect to this sale is included in the enclosed confidential attachment (if applicable). [*Note:* See Table 703-5B for the proper format.]”
- h. Table 703-5B is added as shown in attachment 3 of this memorandum.

The revised paragraphs and tables are effective immediately and will be included in the automated version of the SAMM found in the Defense Acquisition Deskbook. If you have any questions concerning this change, please contact Beth Baker, DSCA/PSD-PMD, (703) 604-6612, DSN 664-6612 or e-mail: beth.baker@osd.pentagon.mil.

Attachments:

1. OUSD(A&T) Memorandum, 13 Jul 99
 2. New SAMM Table 703-3B
 3. New SAMM Table 703-5B
- cc: AMSAC-OL-MP

Attachment 1.
OUSD(A&T) Memorandum, Pricing Issues in Foreign Military Sales Contracts 13 Jul 99

**Pricing Issues in Foreign Military Sales
Contracts
13 July 1999**

**Office of the Under Secretary of Defense
3000 Defense Pentagon
Washington DC 20301-3000**

Acquisition and Technology
DP/CPF

July 13, 1999

Memorandum For: Directors of Defense Agencies
Deputy for Acquisition and Business Management,
ASN(RD&A)/ABM
Deputy Assistant Secretary of Air Force (Contracting)
Deputy Assistant Secretary of the Army (Procurement)
Executive Director for Procurement Management (DLSC/DLA)

Subject: Pricing Issues in Foreign Military Sales Contracts

I want to clarify the requirements for pricing Foreign Military Sales (FMS) contracts, including the treatment of offset 'costs.

In today's global marketplace, there is significant competition for sales of military equipment, with U.S. systems competing against foreign systems and other U.S. systems (for example, F-15 vs. F-16) to meet foreign governments' requirements. In these situations, competitions run by foreign governments should determine the price to be paid. This is true even if the sale to the foreign government is then processed as a foreign military sale and even if DoD is buying the same item sole source. The contracting officer should consult with the foreign government through security assistance personnel to determine whether adequate price competition occurred. If so, this meets the requirement of FAR 15.403-1(b)(1), which states that the submission of certified cost or pricing data shall not be required when the contract price is based on adequate price competition. No further data to support the price should be requested.

In pricing noncompetitive FMS contracts where cost or pricing data is obtained, DFARS 225.7303-2(a) instructs contracting officers to recognize the reasonable and allocable costs of doing business with a foreign government, including offset implementation costs, except when the purchase is financed with funds made available on a nonrepayable basis. In 1995, the language at DFARS 225.7303-2 (a) (3) was changed to allow all costs of implementing an offset agreement. There appear to be differences in how this language is being interpreted and

implemented. Contracting officers should treat all offset costs as allowable FMS contract costs. To disallow such costs means that U.S. companies must absorb offset costs that are required by the foreign government as a condition of making the sale. It is only reasonable that foreign governments that require offsets should bear the costs of those offsets.

/Signed/
Eleanor R. Spector
Director, Defense Procurement

Attachment 2.
Offset Information -- Advance Notification

Table 703-3B -- Offset Information -- Advance Notification

(Classification)

Reporting of offset agreements in accordance with Section 36(b)(1) of the Arms Export Control Act (AECA), as amended by Section 1245 of H.R.3427 enacted by P.L.106-113 dated November 29, 1999, requires a description of any offset agreement with respect to this proposed sale. Section 36(b)(1)(g) of the AECA (as amended) provides that reported information related to offset agreements be treated as confidential information in accordance with section 12(c) of the Export Administration Act of 1979 (50 U.S.C. App. 2411(c)). Information about offsets for this proposed sale are described below:

-- general description of the performance required for the offset agreement.

Section 36(b)(1)(g) of the Arms Export Control Act (22 U.S.C. 2776) requires this information to be treated as “**Confidential Information**” in accordance with section 12(c) of the Export Administration Act of 1979 (50 U.S.C. App. 2411(c)). This information is exempt from disclosure under section 552 of title 5, United States Code, and shall not be published or disclosed without a determination that withholding is contrary to the national interest.

Derived From: SEC 12(C) of the EAA of 1979 (50 U.S.C. APP.2411(C))

Declassify On: OADR

(Classification)

Attachment 3.
Offset Information -- Statutory Notification

Table 703-5B -- Offset Information – Statutory Notification

(Classification)

Reporting of offset agreements in accordance with Section 36(b)(1) of the Arms Export Control Act (AECA), as amended by Section 1245 of H.R.3427 enacted by P.L.106-113 dated November 29, 1999, requires a description of any offset agreement with respect to this proposed sale. Section 36(b)(1)(g) of the AECA (as amended) provides that reported information related to offset agreements be treated as confidential information in accordance with section 12(c) of the Export Administration Act of 1979 (50 U.S.C. App. 2411(c)). Information about offsets for this proposed sale are described below:

-- general description of the performance required for the offset agreement.

Section 36(b)(1)(g) of the Arms Export Control Act (22 U.S.C. 2776) requires this information to be treated as “**Confidential Information**” in accordance with section 12(c) of the Export Administration Act of 1979 (50 U.S.C. App. 2411(c)). This information is exempt from disclosure under section 552 of title 5, United States Code, and shall not be published or disclosed without a determination that withholding is contrary to the national interest.

Derived From: SEC 12(C) of the EAA of 1979 (50 U.S.C. APP. 2411(C))

Declassify On: OADR

(Classification)