94-F-1260

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01 AUG 1994

Ref: 94-F-1260

Mr. Dominic M. Nguyen
Sidley & Austin
1722 Eye Street, NW
Washington, DC 20006

Dear Mr. Nguyen:

This responds to your June 2, 1994, Freedom of Information Act (FOIA) request pertaining to records concerning Department of Defense Directive 2140.2, dated August 5, 1985. Our June 14 interim response refers.

The Office of the Department of Defense Comptroller has provided the enclosed records as responsive to your request.

The administrative cost of processing this request was $89.65, of which $71.40 is chargeable. The chargeable cost consists of two hours search at the professional level rate of $25.00 per hour ($50.00); 140 pages of office copy reproduction at $0.15 per page ($21.00); and, 20 pages of printed publications at $0.02 per page ($0.40). Please indicate our reference number, **94-F-1260**, on a check or money order payable to the U.S. Treasurer in the amount of **$71.40**. To avoid interest charges, payment must be received in this Directorate within 30 calendar days of this letter's date. Our address is:

Office of the Assistant to the Secretary of Defense
(Public Affairs)
Directorate for Freedom of Information and
Security Review, Room 2C757
1400 Defense Pentagon,
Washington, DC 20301-1400

Sincerely,

SIGNED

C. Y. Talbott
Chief, FOI Division
Directorate for Freedom of
Information and Security Review

Enclosure
Prepared by Kahn:4F1260L1:7/30/94:DFOI:X71160:gr✓pk__yl__wh__

#631

Comments on DoD Directive 2140.2

ef. E

Need to Reissue with DAR and FAR supplement

1. Page 1, reference (e): delete "DAR", change to read: Department of Defense Federal Acquisition Regulation (FAR) Supplement

Reason: To correct reference. DSAA

1. Page 1, Reference e. Revise to read:

"Defense Acquisition Regulation (DAR) Contracts initiated prior to 1 Apr 84. Federal Acquisition Regulation (FAR) contracts initiated 1 Apr 84 and subsequent date."

Reason: FAR pertains to contracts initiated 1 Apr 84 and subsequent and provides general guidance for USG Acquisitions.

Navy

adopted

Ref. E

1. Page 1, reference (a): delete "DAR", change to read: Department of Defense Federal Acquisition Regulation (FAR) Supplement

Reason: To correct reference. DSAA

1. Page 1, Reference e. Revise to read:

"Defense Acquisition Regulation (DAR) Contracts initiated prior to 1 Apr 84. Federal Acquisition Regulation (FAR) contracts initiated 1 Apr 84 and subsequent date."

Reason: FAR pertains to contracts initiated 1 Apr 84 and subsequent and provides general guidance for USG Acquisitions. Navy

Reference, (Page 1)	Change reference e to: "Department of Defense Federal Acquisition Regulation Supplement (DOD FAR Supplement)"	AF

Ref F

2. Page 1, add reference (f) DOD 5105.38-M Security Assistance Management Manual (SAMM) DSAA

Reason: To cross reference to SAMM for Security Assistance Management identification of Major Defense Equipment (MDE) items.

2. Page 1, Reference f. Add reference f:

"DOD 5105.38-M, Chapter 7, Security Assistance Management Manual"

Reason: The above reference also relates to nonrecurring recoupment policy. Navy

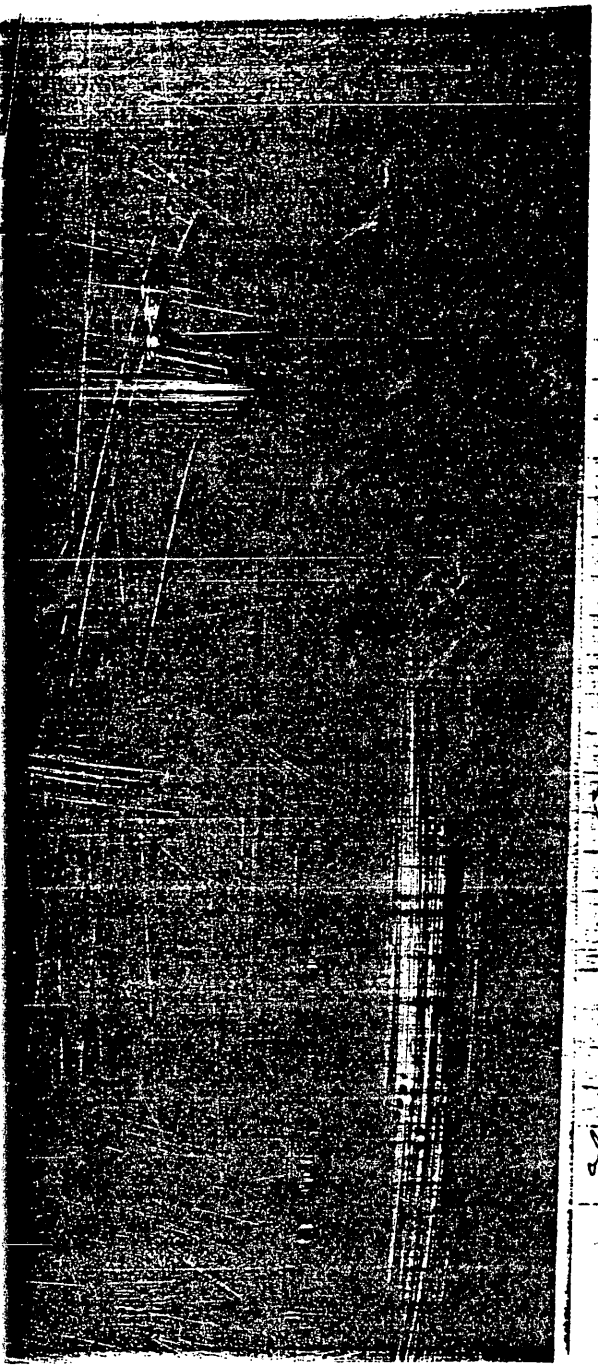
Par. B.2

Par. B.2, Application and Scope (Page 1)

The defined term (encl 1) "Domestic Organizations" should probably be inserted in line 1 since the Directive takes the trouble to define this term and it is more comprehensive than "corporations." AF

2. It is suggested that the last line of Paragraph B2 of the Directive be changed to read: international organization, foreign commercial firm, domestic organization, or private party.

DDR/E



Par. D

Par. D. Policy

In last sentence, add: "...except when an estimated recoupment charge was used when the agreement was entered into." The reason for this change is the draft as written only refers to revised NC recoupments and not to cases involving the sale of an item prior to the NC recoupment charge being established. The point made by adding these words is that NC recoupment charge should be retroactively applied when the NC recoupment was not approved prior to the sale or contract. This change will resolve a longstanding problem regarding retroactive collection. AF

3. Page 2, para. D, line 5: After approved add "or"; line 8: After approval add "or revision of the" and delete "of the revised."

Reason: No NC charges, original or revised, should be applied on a retroactive basis.

DSAA

4. Page 2, para D: add a last sentence - "When Defense items are sold at a reduced price due to age, condition or supply status (excess), the NC recoupment charge will be reduced by the same percentage reduction."

Reason: To assure that policy is in conformance with provisions of DOD 7290.3-M regarding reduction of NC charge when the item unit price is reduced. DSAA

Par. E.1

adopted

Par. E.1, Responsibilities (Page 2) — Delete Defense Acquisiton Regulation (DAR) and insert "DOD FAR Supplement". AF

3. Page 2, Paragraph E.1. Add a clause to the DAR and FAR: That final payments on DOD contracts will not be made until there has been a final determination that contractor has paid applicable nonrecurring costs on direct commercial sales.

Reason: To ensure that contractors reimburse DOD nonrecurring costs relating to direct commercial sales. Navy

Don't understand policy

[illegible] para. [illegible], lines [illegible]: After "Commercial [illegible] [illegible] shall be provided to the Deputy Assi[illegible] [illegible] Systems [illegible]

[illegible] with approved [illegible] [illegible] Security Assi[illegible] [illegible] (SAMS). The [illegible] list is requ[illegible] [illegible] recent [illegible] requirements.

5. Page 2, para E.1., line 4: delete "Defense Acquisition Regulation (DAR)" and replace with "DOD FAR Supplement"....

Reason: To update to the FAR Supplement. DSAA

added to both DAR and FAR

Par. E.3

6. Page 2, para E.3, line 2: Delete "items or" and revise to "categories of"

Reason: To establish requirement to identify categories of technology to which charges will be applied.

DSAA

Par. E.4

7. Page 2, para. E.4, lines 5-7: after "Commercial Sales." Change to read - notification of approved NC recoupment charges for MDE items shall be provided to the Deputy Assistant Secretary of Defense (Management Systems)(DASD(MS).

Reason: The MDE list, with approved NC Recoupment charges, is published in the DOD 5105.38-M, DOD Security Assistance Management Manual (SAMM). The MDE list is required in the SAMM to identify Congressional reporting requirements. To duplicate publication of the MDE list in another manual will result in considerable confusion since the two manuals could not be maintained with a concurrent publication schedule. Therefore, it is recommended that DOD 5105.38-M also publish the non-MDE listing to avoid duplication and proliferation of different data in the two manuals.

DSAA

Par. E.5

4. Page 2, Paragraph E.5. Revise to read, line 6 after "for publication":

Navy

";insert prescribed DAR clauses in contracts stating contractor responsibility to pay the U.S Government prescribed amounts for nonrecurring costs on direct commercial sales, and appropriately enforce the application of the aforementioned clauses during contract execution; collect and deposit to Miscellaneous Receipts of the Treasury nonrecurring cost recoveries on direct commercial sales."

Reason: To clearly delineate the Military Departments' responsibilities relating to nonrecurring cost charge application.

8. Page 2, para E.5, line 6: delete "the DASD(MS)" and replace with "the DSAA".

Reason: See reason 7 above.

DSAA

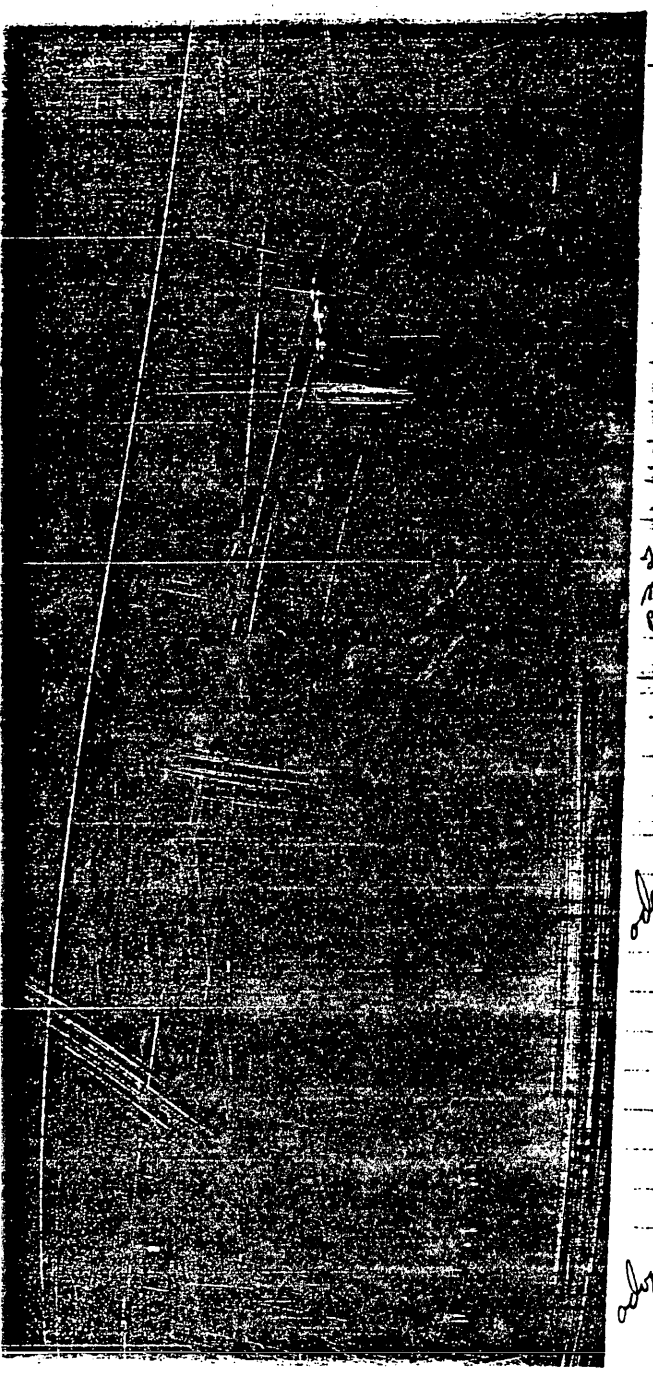
Par E.6

5. Page 2, Paragraph E.6. Add subparagraph E.6:

"The Defense Contract Audit Agency (DCAA) shall audit compliance by contractors to pay the Department of Defense nonrecurring cost unit recoveries on direct commercial sales."

Reason: To control and monitor contractor payment of nonrecurring cost to U.S. Government relating to direct commercial sales.

Navy



Par. G.1

Par. G.1, Waivers

Revise first sentence at top of page three to conform with the AECA, Section 21(e)(2). Revise second sentence to clarify that the same considerations apply to waivers in all commercial sales cases--not merely those which are "non-MDE." The existing ambiguity could be eliminated by moving the mention of commercial sales to precede mention of non-MDE.

adopted

AF

[redacted]

G.1

- Continue the existing policy of accepting waiver requests from anyone: DoD components, defense contractors, or foreign governments. The revision could make it unnecessarily difficult for the Secretary of Defense to initiate a waiver.

Dir. PA/E

adopted

6. Page 2, Paragraph G.1. Revise to read:

Line 1, after "recoupment of" add "a proportionate amount of"

Line 3, add "reductions or" preceding "waivers"

Reason: To reflect provisions of the Arms Export Control Act.

Navy

adopted

9. Page 3, para G.1 lines 1 and 2: change to read - Government (USG) interests in the North Atlantic Treaty Organization standardization and standardization with the Armed Forces of Japan, Australia or New Zealand. Waiver .....

7. Page 3, Paragraph G.1. Revise to read:

Line 1, after "Organization", add "standardization with Armed Forces of"

Line 1, after "Japan" add "New Zealand"

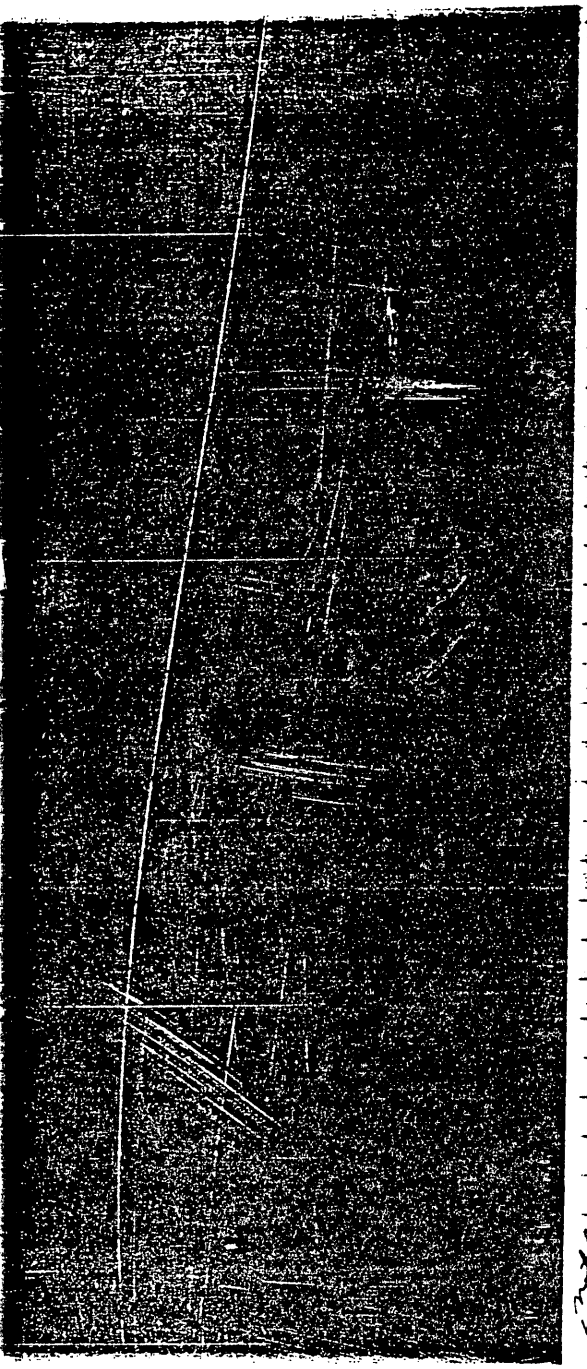
Line 2, after "Waiver", add "or reduction"

Reason: To reflect provisions of the Arms Export Control Act.

It is also recommended that economic considerations be included in the waiver of nonrecurring costs for non-major defense equipment (MDE) items.

Reason: Economic considerations should be considered for waiver of nonrecurring costs for non-major defense items.

Navy



Par G.2

Par. G.2, Waivers
(Page 3)

adopted

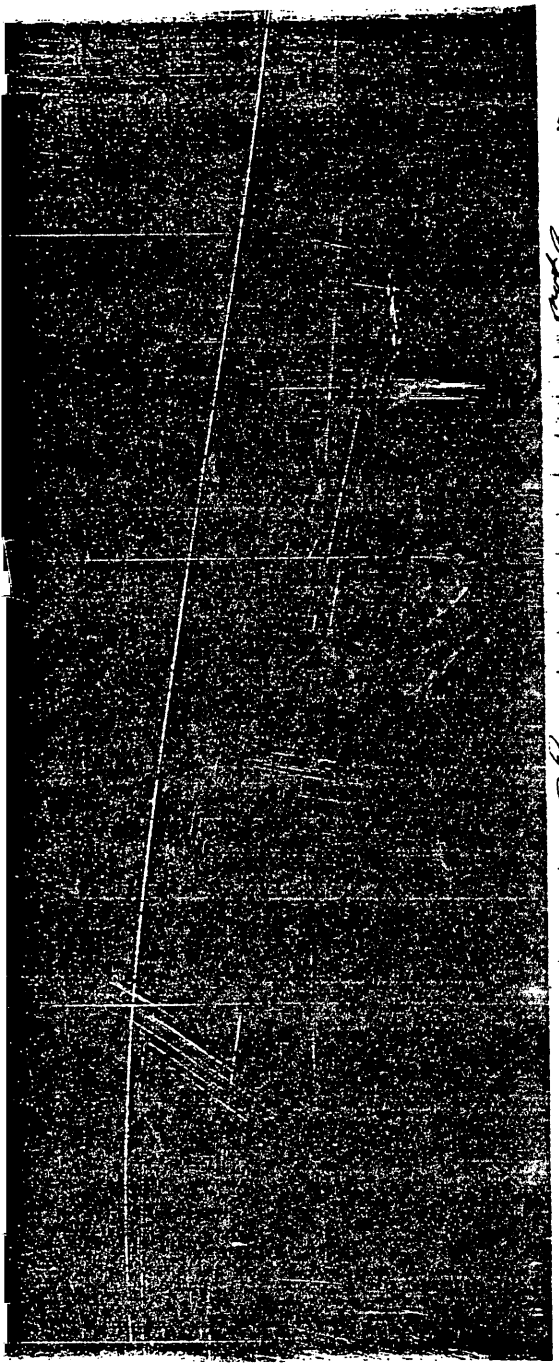
Insert the following phrase at the end of the penultimate sentence: ", and the acceptance was conditioned upon approval of the waiver request." Alternatively, delete the phrase "unless the waiver was pending at the time of acceptance" which concludes such sentence. SAF/GC and OSD/GC have opined that waivers under the Arms Export Control Act may not be granted retroactively. Only waivers which "would if made" advance standardization may be approved, and standardization is normally advanced by virtue of the sale occurring. Hence, if the sale is made without the waiver (e.g., if the FMS customer accepts the LOA irrespective of whether its pending waiver request may be rejected), then the statutorily required enhancement of standardization is already secured and the standardization justification for the waiver appears to evaporate. The concluding phrase of the penultimate sentence is also inconsistent with the last sentence of paragraph G.4, which requires the waiver determination to be completed prior to LOA signature.

Language modified

b. The definition of "blanket waiver" appears unintentionally permissive. Presumably mass or multiple waivers should still be prohibited "blanket waivers" even if they apply to less than "all" sales (e.g., request to waive NC for every sale to a particular country over the next 10 or 20 years, but not forever and therefore not for "all" sales). This definition should be revised accordingly.

AF

G.2 o Relax the revision's absolute ban on blanket waivers. In a few cases, such as the waivers that Secretary Weinberger recently granted for the commercialization of expendable launch vehicles, it may make sense to waive full recovery of sunk R&D costs for all sales of a given defense good.



Par. G.2.

8. Page 3, Paragraph G.2.

The sentence which provides that "blanket waiver requests shall not be submitted nor considered" is needlessly inflexible.

Reason: It is conceivable that blanket waivers could be justified.

Navy

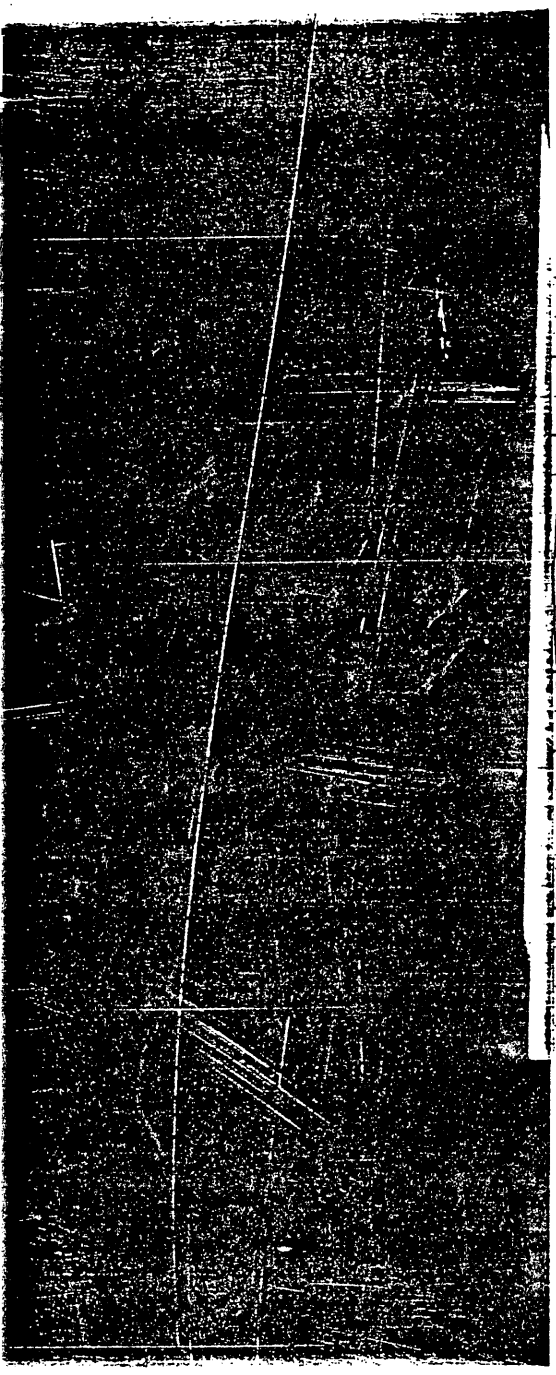
11. Page 3, para G.2., add another sentence: "Any waiver approved for a direct commercial sale requires a certification by the contractor that reductions have been passed on to the customer."

Reason: To assure that any direct sale waiver is passed on to the customer and to enable negotiation of contractor reductions corresponding to NC charge reductions.

DSAA

10. Page 3, para G.2., line 1: after charges add" "for eligible countries"; lines 9 and 10: change "determine that the waiver has resulted in a reduction of contract price." to - "quantify the waiver and the benefits to the USG."

Reason: Waivers are not authorized for all countries, only those eligible under the AECA. The waiver request should be from the foreign government. The foreign government must articulate whatever compensation it is prepared to provide to the USG in exchange for the NC recoupment waiver.



Par. G.3

Par. G.3, Waivers (Page 3)	Revise the first sentence to read: "... by the contractor through the military department's contracting representative to the Under..."	AF

2. Add the following between the words "contractor" and "to" in the first sentence of Paragraph G.3:

"through the appropriate contracting officer" DDR&E

9. Page 3, Paragraph G.3. Revise to read:

On Line 1, after "domestic sales" add: "and sales to foreign domestic purchasers."

Reason: It is considered that all waivers on sales to purchasers after other than foreign governments should be considered by Under Secretary of Defense for Research and Engineering (USDR&E).

On Line 3, after "Research and Engineering." add "via the contracting officer or the contracting activity who developed the item."

Reason: The processing of such a waiver is part of the business strategy for many defense programs and should be the responsibility of the contracting officer.

Navy

12. Page 3, para G.3., line 2: after "contractor", add "through the administrative contracting officer (ACO)" to the....

Reason: This directive establishes the ACO as the government interface with contractors for providing charges and for collection. The contractor waiver requests should therefore flow through the ACO for consistency. DSAA

through the appropriate contracting officer

DDR&E

9. Page 3, Paragraph G.3. Revise to read:

On Line 1, after "domestic sales" add: "and sales to foreign domestic purchasers."

NO

adopted

Reason: It is considered that all waivers on sales to purchasers after other than foreign governments should be considered by Under Secretary of Defense for Research and Engineering (USDR&E).

On Line 3, after "Research and Engineering." add "via the contracting officer or the contracting activity who developed the item."

adopted

Reason: The processing of such a waiver is part of the business strategy for many defense programs and should be the responsibility of the contracting officer.

Navy

[illegible] the 60 day response [illegible] considerable [illegible]

12. Page 3, para G.3., line 2: after "contractor", add "through the administrative contracting officer (ACO)" to the....

adopted DDR&E

Reason: This directive establishes the ACO as the government interface with contractors for providing charges and for collection. The contractor waiver requests should therefore flow through the ACO for consistency.

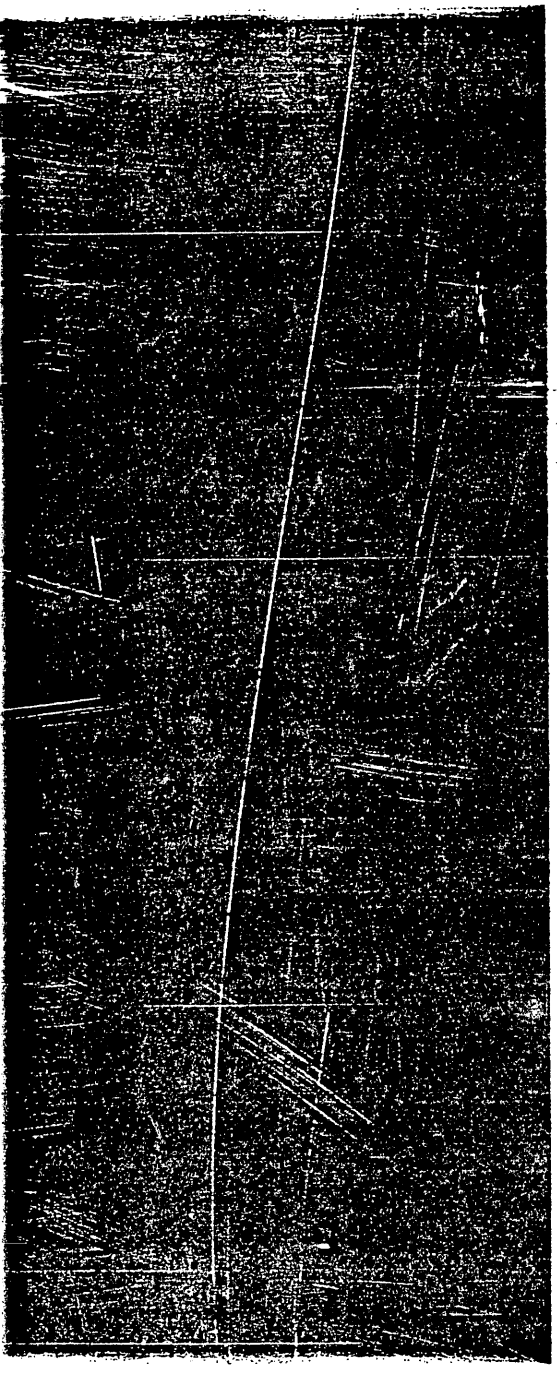
DSAA

13. Page 3, para g.3., line 3: after "Engineering". start the next sentence with, "To the extent possible, the request shall...".

adopted

Reason: The contractor may not be aware in every case, of the value of the NC recoupment charge or waiver value.

DSAA



Par. G.4

Par. G.4, Waivers (Page 4)

adopted

Insert the phrase ", or a denial of the request," immediately after "charge" in line 4 since not all requests will be approved " in whole or in part."

not necessary - OSD General Counsel knows if waiver is legal.

Previous drafts of this reissuance stated (in paragraph G.1) that requests for waivers must be accompanied by a certification by the DOD Component's legal counsel that the proposed waiver is permitted under applicable law. This protective provision should be restored, perhaps in paragraph G.4.

adopted

Revise the last sentence by deleting the words "direct sale" near the end of the sentence. Deleting these words eliminates the possible confusion between a domestic and an international or foreign sale. The term "direct sale" is commonly interpreted to mean a sale between a U.S. firm and a foreign purchaser. With this change, the paragraph will apply to both domestic and foreign contracts.

AF

alternative language

14. Page 3, para G.4, lines 3 through 6: Change to read - "disapprove the request. A waiver request shall be provided in writing to the appropriate approving authority prior to issuance of a FMS agreement (Letter of Offer and Acceptance - LOA) or signing of a direct sale contract (either domestic or foreign) for the waiver to be considered."

Reason: Clarification and to remove the 60 day response requirement. Based on policy that compensation is required from the foreign government, waivers involve considerable negotiation and the 60 day timeframe would be detrimental to U.S. interests. For major system sales involving foreign competition, the negotiations may take months and the appropriate timing of the waiver is dependent upon individual negotiations.

DSAA

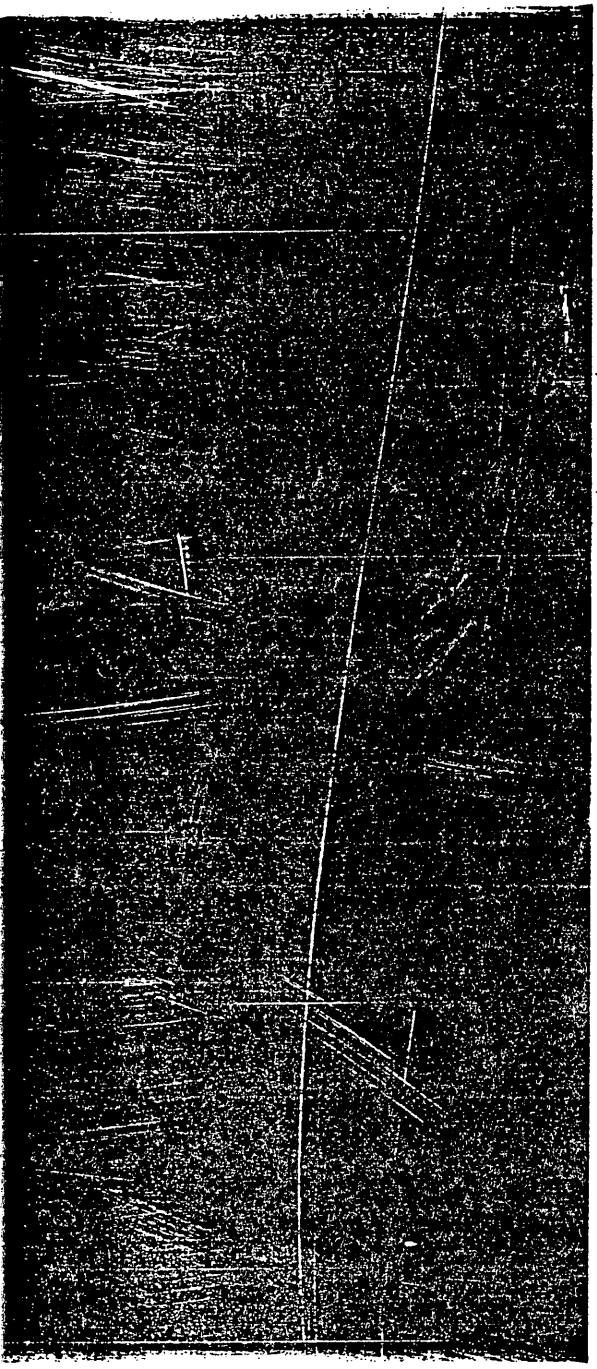
Par. G.5

15. Page 3, para G.5, lines 1 and 2: Change to read - "The decision on any waiver requires the concurrence of the Director, DSAA, ASD(C), and OUSDR&E."

Page 3, para G.5 line 6: change to read:...."originated by the activity with approval authority and coordinated with the Director, DSAA, ASD(C), and OUSDR&E."

Reason: Clarity and consistency.

DSAA



Par. G.6

10. Page 3, Paragraph G.6. Revise to read:

On Line 5, between "domestic" and "organizations", add:

"or foreign nongovernmental"

Reason: Same reason as G.3 above

adopted

NO

It is recommended that approval for waivers granted by the Director, Defense Security Assistance Agency (DSAA) or USDR&E include rationale for such approval.

Reason: This would be consistent with recommendation IID of the report of the International Coproduction/ Industrial Participation Agreements Task Force.

Navy

[illegible]

16. Page 3, para G.6 line 1: after "DSAA", change to read - "is the waiver approval authority"....

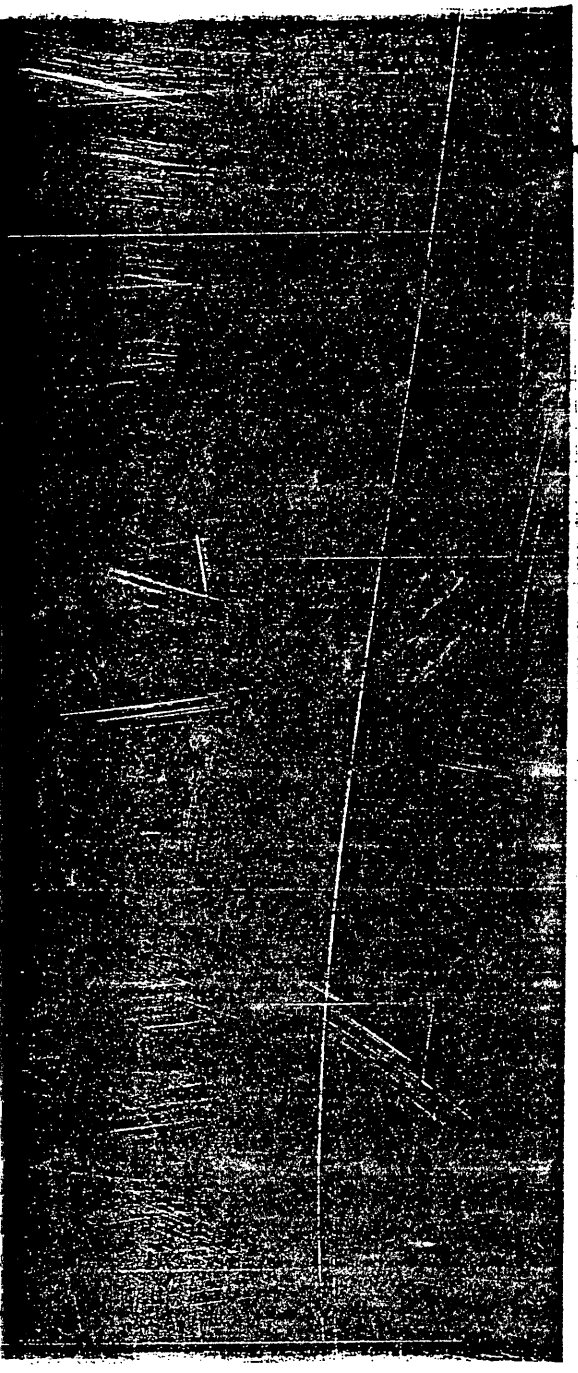
adopted

Page 3, para G.6, lines 3 and 4: change to read "Research and Engineering is the waiver approval authority".....

Page 3, para G.6, line 6: delete "copy" and revise to "notification"....

Reason: Clarity and consistency. Because the waiver is processed with a legal determination and finding, it is more appropriate to provide notifications to ASD(C) and the DOD components by memorandum rather by forwarding copies of determinations.

DSAA



Par. G.7

Par. G.7., Waivers (Page 4)

This paragraph does not belong under the "waiver" section of the Directive. AF

17. Page 4, para G.7., lines 2 and 3: end sentence with "activities."

Reason: NC charges have not been assessed for defense items after release of items to property disposal activities, whether sold on a competitive or negotiated basis. DSAA

Encl 1 Par A

10. Definitions, Enclosure 1. Suggest that the definitions be restructured in alphabetical order.

Army

11. Enclosure 1, Page 1-1, Paragraph A. Add to definition:

"significant combat equipment"

Reason: Major defense equipment definition includes significant combat equipment.

Navy

1. The subject directive defines Major Defense Equipment as items having an RDT&E cost of more than $50M or a production cost of more than $200M. This threshold was once used in DoDD 5000.1. However, it was raised and the current threshold is $200M RDT&E and $1B in production. Further, 10 U.S.C. 139a. uses the same threshold for SARs as well as other reporting requirements such as those at 10 U.S.C. 136a.(a)(2)B for the new director of Operational Test and Evaluation. You may wish to consider changing the definition in enclosure (1) to DoDD 2140.2.

DDRE

Enclosure 1 Par. A, Definitions (Page 1-1)	Revise sentence to read: "... any item of significant combat equipment on the ..." This change will put the words in line with requirements of the AECA.
Par. 1, Definitions (Page 1-1)	A clarification such as insertion of the word "equal" before "distribution" should be made to forestall misinterpretations that skewed or weighted distributions (allocating more costs to some units than others) are possible if considered "fair."
Enclosure 1, Definitions (Page 1-1)	Recommend adding a definition of Non Major Defense Equipment, such as: "Any item or technology with $2 Million or more invested as prescribed in the Implementing Procedures of this directive."

AF

Reason: Major defense equipment definition includes significant combat equipment.

Navy

1. The subject directive defines Major Defense Equipment as items having an RDT&E cost of more than $50M or a production cost of more than $200M. This threshold was once used in DoDD 5000.1. However, it was raised and the current threshold is $200M RDT&E and $1B in production. Further, 10 U.S.C. 139a. uses the same threshold for SARs as well as other reporting requirements such as those at 10 U.S.C. 136a.(a)(2)B for the new director of Operational Test and Evaluation. You may wish to consider changing the definition in enclosure (1) to DoDD 2140.2.

DDR&E

adopted	Enclosure 1 Par. A, Definitions (Page 1-1)	Revise sentence to read: "... any item of significant combat equipment on the ..." This change will put the words in line with requirements of the AECA.
adopted	Par. 1, Definitions (Page 1-1)	A clarification such as insertion of the word "equal" before "distribution" should be made to forestall misinterpretations that skewed or weighted distributions (allocating more costs to some units than others) are possible if considered "fair."
adopted	Enclosure 1, Definitions (Page 1-1)	Recommend adding a definition of Non Major Defense Equipment, such as: "Any item or technology with $2 Million or more invested as prescribed in the Implementing Procedures of this directive."

AF

[redacted]

adopted

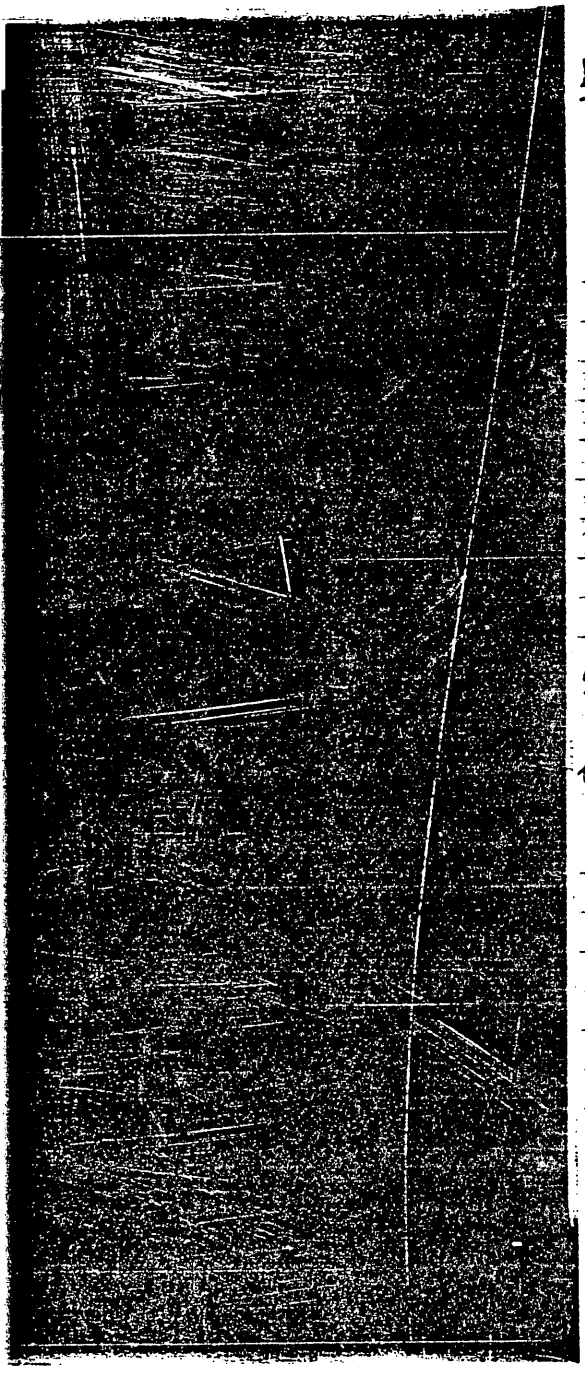
Enclosure 1

18. Page 1-1, para A: change to read - "means any item of significant combat equipment (SCE) on the United States....

Reason: To correct the definition in accordance with the definition provided in section 47(6) of the Arms Export Control Act.

DSAA

[redacted]



Encl 1 Par B

adopted

12. Enclosure 1, Page 1-1, Paragraph B. Replace "legislative acts" with: "statutes"

Reason: Common term should be used.

Navy

Encl 1 Par F

adopted

19. Page 1-1, para F; line 5: change to read - "of calculation of the NC recoupment charges, as well as projections of such costs, to the".....

Reason: The determination of costs is used to calculate the NC recoupment charge. These costs should be assembled and projected when the charge is calculated, not when a contract is made. The charges should be calculated when the stated thresholds are met, not when individual sales are made.

DSAA

Encl 1 Par G

adopted

20. Page 1-1, para G, line 6: after "evaluation." Add "This includes costs of any engineering change proposal initiated prior to date of calculation of the NC recoupment charge.

Reason: To clarify that customers should reimburse the USG for costs incurred prior to their entering the weapon system program and that ongoing direct production costs for ECP's are a direct cost to the purchaser.

Encl. 1 Par. H

13. Enclosure 1, Page 1-1, Paragraph H. On Line 1, replace "those" with: "costs"

Reason: Clarity.

Navy

Encl 1 Par. I

14. Enclosure 1, Page 1-1, Paragraph I. On Line 2, after "number of units", add:

"Sold to DOD, other U.S. Government (USG), Foreign Military Sales (FMS), Military Assistance Program (MAP) and direct commercial sales to U.S. and foreign purchasers"

Reason: Clarity.

Navy

Encl. 1 Par. J

15. Enclosure 1, Page 1-1, Paragraph J. On Line 2, after "number of units", add:

"

Encl. 1 Par. I

14. Enclosure 1, Page 1-1, Paragraph I. On Line 2, after "number of units", add:

"Sold to DOD, other U.S. Government (USG), Foreign Military Sales (FMS), Military Assistance Program (MAP) and direct commercial sales to U.S. and foreign purchasers"

Reason: Clarity.

Navy

Encl. 1 Par. J

15. Enclosure 1, Page 1-1, Paragraph J. On Line 2, after "number of units", add:

"sold to DOD, other USG, FMS, MAP and direct commercial sales to U.S. and foreign purchasers"

Reason: Clarity.

Navy

Encl. 1 Par. M

3. In Paragraph M of enclosure 1 to the Directive, Definitions, a Non-US Contractor is defined as an organization which is not incorporated in the US. This would make all single proprietorship or partnership type US organization, Non-US. This definition needs clarification.

DDR&E

Encl. 2 Par. A1

Enclosure 2, Implementing Procedures, Par. A.1. (Page 2-1)

The defined term "Domestic Organization" should be substituted for or added to the term "defense contractor" in line 1. This same refinement should be considered for all other provisions which use the undefined and potentially restrictive terms "defense contractor" or "contractor" (e.g., paragraph A.5).

Add: "The DOD Components will establish a system to identify items that require a NC recoupment charge as prescribed in DOD 7290.3-M." There is no current procedure for capturing costs to identify an eligible item for the NC recoupment charge. The DOD 7290.3-M should spell out a specific methodology for capturing costs from cost accounting records in each of the Services so as to flag an item that approaches the $2 million or $50 million threshold specified in this directive.

AF

Enclosure 2

21. Page 2-1, para A.1: add the following sentence - "The DOD components will establish a system to identify items that require a NC recoupment charge, as prescribed in DOD 7290.3-M."

Reason: The military departments need to establish a system to recognize when an item crosses the recoupment thresholds of $2M in RDT&E or $200M in production.

DSAA

Encl. 2 Par. A

adopted

Encl. 2 Par. A3

adopted

23. Page 2-1, para A.3: Lines 1 and 2 - change to read: The NC recoupment charge computation (total nonrecurring RDT&E and nonrecurring production cost divided by total production) for the sale....

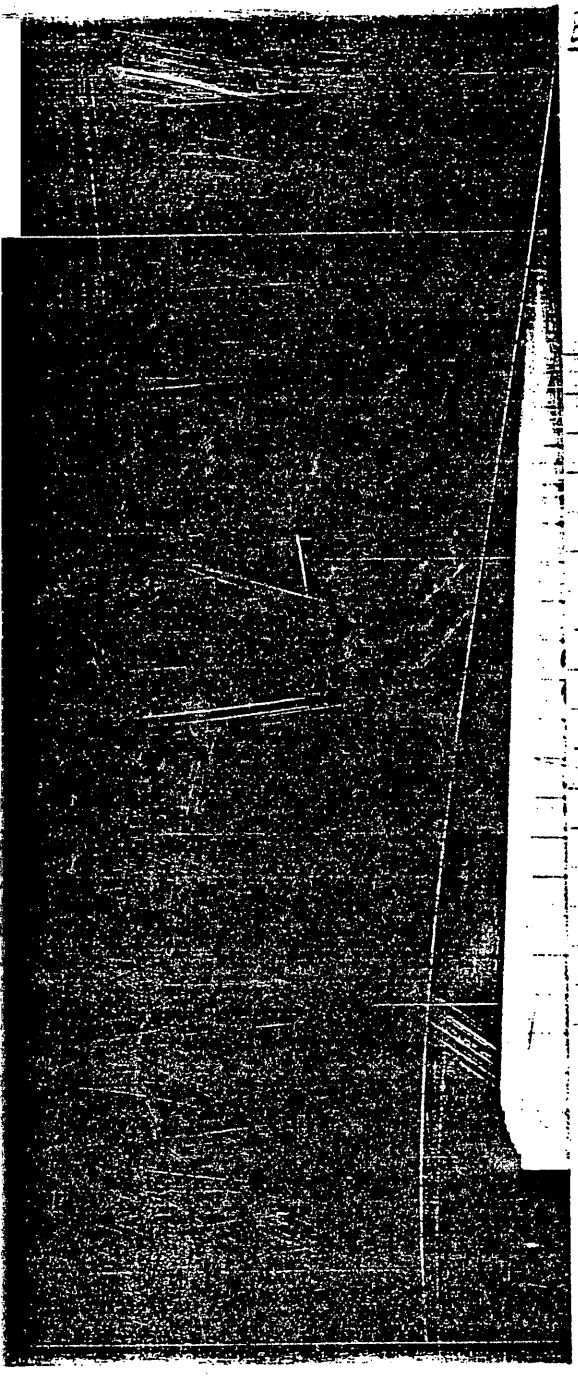
Reason: To clarify the parenthetical explanation of computation.

Same as

24. Page 2-1, para A.3: Delete last sentence.

Reason: See reason 7 above.

DSAA



Encl. 2 Par. A4

Enclosure 2, Implementing Procedures, Par. A.4. (Page 2-1)

adopted

Revise the 2nd line to read: "... a model change occurs or a major new development program occurs that changes the operational capability of the end item." These words will clarify the USAF F-15 MSIP program where no MDS change will occur, but a revision to the NC recoupment charge may be appropriate. Sentence 1 also implies that NC recoupment charges will be recomputed at the time of model change, but the penultimate sentence provides for recomputation requests only when "significant changes" occur. If, as implied by sentence 1, the event of model change is to be a milestone at which NC recoupment charges will be updated (even if the change in NC recoupment would be only 29% for example instead of 30%) then the phrase ", and when a model change occurs," should be inserted after "MDE" in line 10.

AF

adopted

Also, revise the 9th line to read: "... a NC recoupment charge collection of over $100,000 per case value exists." This change is needed to show that a significant change can be an increase or a decrease, and that the $100,000 conforms to DSAA Memo, 20 May 1981. In addition, this sentence should be revised to clarify whether the $100,000 test for "significant changes" applies to an individual recoupment or to the aggregate of all recoupments for anticipated future sales.

adopted

16. Enclosure 2, Page 2-1, Paragraph A4. Revise to read:

Lines 2 and 3, revise "have been significant changes" to "has been significant change"

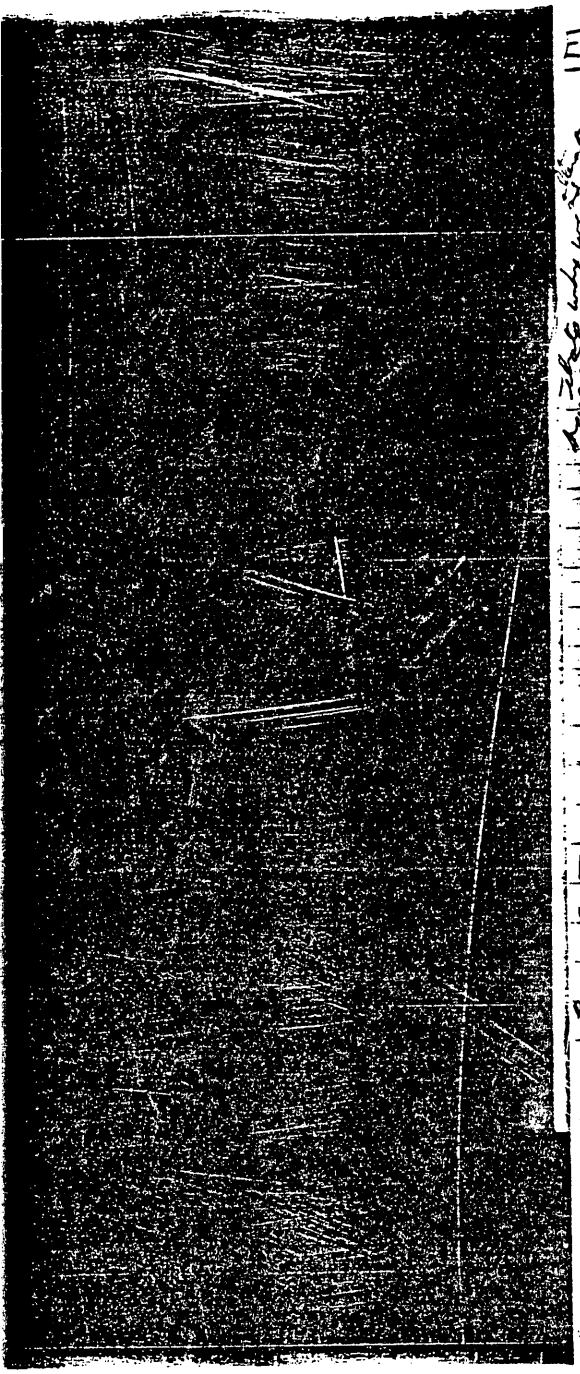
Line 10, revise "significant changes are" to "significant change is"

Line 11, after "in", add "future"

adopted

Reason: Clarity and uniformity.

Navy



Encl. 2 Par. A4

1. Enclosure 2, Paragraph A.4. Suggest a consideration of a sliding scale in lieu of a flat 30% change or an additional nonrecurring cost (NC) recoupment potential of $100K exists. It would appear that the higher dollar value of NC, a lower percentage charge should be considered.

COMMENT: The proposed significant change criteria of "30% or the potential for an additional NC recoupment charge collection of over $100,000" will require upward annual revision of MDE NC surcharges which may seem insignificant when looked at as a percentage of the current unit surcharge. For example, the M1E1 Tank has a proposed unit NC surcharge of $237,048. An increase of $270K in the M1E1 cost pools without change in the quantity pool will generate a $45/unit increase in the NC surcharge for the M1E1 Tank. Since the FMS MAP/Direct Sales quantity projection of 2231 will not begin until at least the FY 87/88 time frame, all 2231 vehicles should be considered in determining whether a potential for an additional NRC recoupment charge collection of over $100,000 exists. 2231 X $45 (increase in NC surcharge) = $100,395 in potential additional revenue. Therefore, a $45 increase in the NR surcharge for the M1E1 Tank (45/237,048 = 0.19%) would appear significant.

Army

25. Page 2-1, para A.4: lines 8 and 9 - end sentence after "recoupment charge." and delete "for an MDE item or the potential for an additional NC recoupment charge collection of over $100,000 exists."

Reason: The $100,000 potential additional charge would require excessive resources to monitor and could be easily reached for a number of MDE items. This would result in changes to charges beyond an acceptable limit. Further, it would only be applicable to increases and not to corresponding decreases. The 30% factor is much more acceptable for management purposes and fulfills the existing policy to maintain charges, once established.

DSAA

2. Enclosure 2, Paragraph A.4. Recommend the last sentence be changed to read as follows:

"The Director, DSAA, will approve MDE significant changes IAW the above stated criteria, in writing, within 60 days after receipt of the request."

Encl 2 Par. A5

Enclosure 2, Implementing Procedures, Par. A.5. (Page 2-1)

For clarity, the phrase "from the Administrative Contracting Officer (ACO)" should be merged with the phrase "from the DOD Component" in sentence 1 so that both types of charges are requested "from the Administrative Contracting Officer (ACO) of the DOD Component responsible..."

AF

17. Enclosure 2, Page 2-1, Paragraph A5.

On Line 2, expand definition of USG developed item to include items developed under commercial contract.

Reason: The phrase USG developed is too narrow. The non-recurring production cost may be enough to boost an item into a covered category. Also, USG developed can be read to be limited to items developed by USG only.

Navy

3. Enclosure 2, Paragraph A.5.

COMMENT: The Army has previously recommended to DSAA to have the Defense Acquisition Regulation (DAR) be changed to require contractors to periodically report NC collections, positively or negatively, on foreign commercial sales of military materiel. This periodic report, when implemented, will provide a means to obtain appropriate reimbursement for NC charges.

Army

17. Enclosure 2, Page 2-1, Paragraph A5.

On Line 2, expand definition of USG developed item to include items developed under commercial contract.

Reason: The phrase USG developed is too narrow. The non-recurring production cost may be enough to boost an item into a covered category. Also, USG developed can be read to be limited to items developed by USG only.

Navy

3. Enclosure 2, Paragraph A.5.

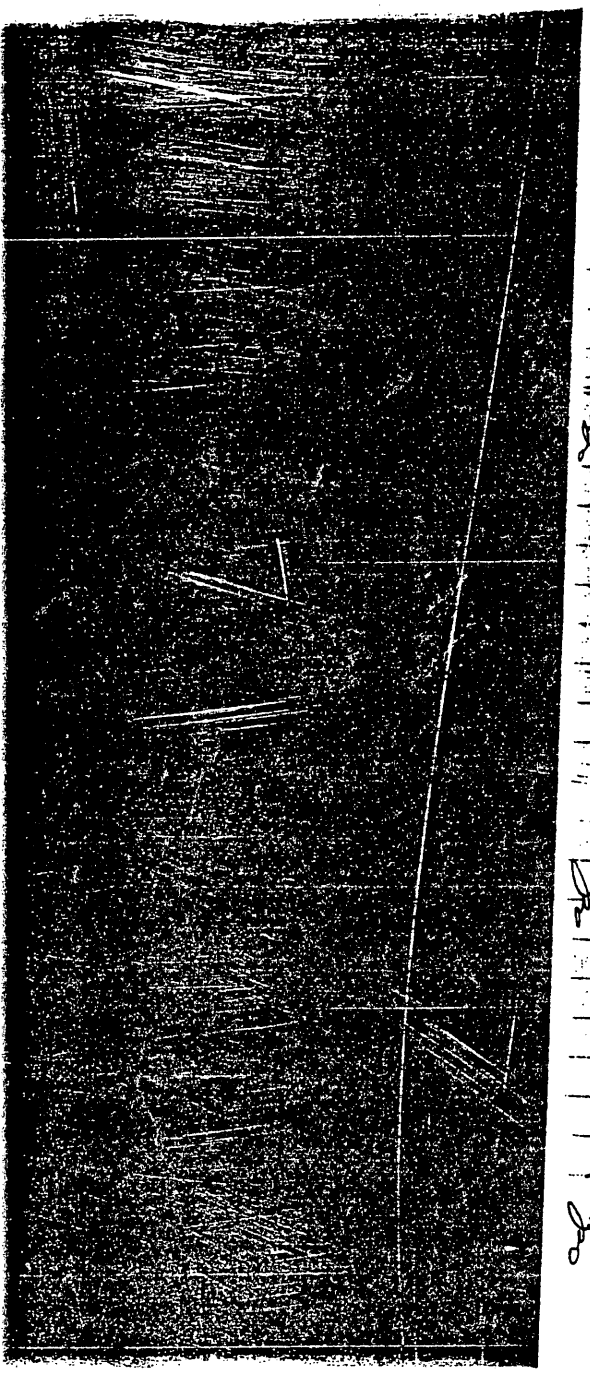
COMMENT: The Army has previously recommended to DSAA to have the Defense Acquisition Regulation (DAR) be changed to require contractors to periodically report NC collections, positively or negatively, on foreign commercial sales of military materiel. This periodic report, when implemented, will provide a means to obtain appropriate reimbursement for NC charges.

Army

1. Add the following sentence to Paragraph A.5 of the Implementing Procedures.

"Despite the absence of an established charge, the contract shall provide for full recovery of such charge in the amount which is subsequently established. The recovery will be for the total items sold and not merely applied on a prospective basis from the date the charge is established."

ODR&E



Encl.2 Par. A6

Enclosure 2, Implementing Procedures, Par. A.6. (Page 2-2)

Change "...DAR 7-104.64,..." to: "DOD FAR Supplement 52.235-7002..." Revise line 3 to read "... the contractor's facility or purchaser's acceptance, (whichever comes first) ....". Some items, after delivery, are retained at contractor's facility to train purchaser's personnel.

AF

4. Enclosure 2, Paragraph A.6, Line 3. Suggest the following change.

"__, the DOD Component (Commander of the Inventory Control Point) shall certify __."

COMMENT: It is not considered appropriate to have a Secretary of the Army or the Assistant Secretary of the Army to certify that records pertaining to NC costs have been lost or destroyed.

Army

26. Page 2-2, para A-6: line 3 - after "facility" add "or acceptance by the purchaser,"

Reason: To provide for collection from a contractor when the item is accepted by the purchaser but is not moved from the contractors facility, such as training equipment.

DSAA

27. Page 2-2, para A-6: lines 5 and 6 - after "DAR 7-104.64" add "and DOD FAR Supplement 25.7306, 35.71 and 52.235 - 7002"....

Reason: To identify the new DOD Federal Acquisition Regulation supplement which replaced the DAR.

Encl. 2 Par B.1

18. Enclosure 2, Page 2-2, Paragraph B.1. Revise to read:

"1. Nonrecurring cost (NC) recoupment charges shall be assessed on a pro rata basis. Normally charges will be established by dividing the total of NC investment (nonrecurring Research, Development, Test and Evaluation (RDT&E) + nonrecurring production) incurred to date, plus projections of future costs to be incurred, by the total estimated number of units projected to be produced over the life of the system (including DOD requirements, Military Assistance Program (MAP) requirements, FMS requirements and direct commercial sales requirements). However, there are circumstances where the projected NC investment to be incurred in developing and producing the FMS sale items is only a fraction of the total projected NC investment. In these instances, the NC pro rata charge calculation is a two step process. First, figure the sunk NC pool and divide it by the total projected number of production units. Then add to this figure a second calculation which represents that portion of the future NC pool which will be attributable to the FMS sale items. A formula representing this calculation is set forth below:

$$\text{PRO RATA CHARGE} = \frac{SI}{TOT} + \frac{PI}{FU\ TOT}$$ WHERE:

SI = Sunk NC Investment

TOT = Estimated Total Production Units

PI = Predicted NC Investment during the period starting with the time of calculation of SI + TOT above, and ending with the time of production of the last unit involved in the FMS sale.

FU TOT = Estimated production for the

of units projected to be produced over the life of the system including DOD requirements, Military Assistance Program (MAP) requirements, FMS requirements and direct commercial sales requirements). However, there are circumstances where the projected NC investment to be incurred in developing and producing the FMS sale items is only a fraction of the total projected NC investment. In these instances, the NC pro rata charge calculation is a two step process. First, figure the sunk NC pool and divide it by the total projected number of production units. Then add to this figure a second calculation which represents that portion of the future NC pool which will be attributable to the FMS sale items. A formula representing this calculation is set forth below:

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TOT = Estimated Total Production Units

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FU TOT = Estimated production for the period starting with the time of calculation of SI and TOT above, and ending with the delivery of the last unit produced."

Reason: The draft directive is not clear on the method of calculating the pro rata NC charge for MDE items and components, where there are predicted NC investments for the future, but only a portion of these are applicable to that part of the production which is involved in the FMS sale.

Navy

Encl 2 Par B.3

Enclosure 2, Implementing Procedures, Par. B.3. (Page 2-2)	Revise first line to read: "... more than one component to be sold..." The words "to be sold" must be included to structure the NC recoupment charges in line with how the system components are sold, and to preclude the need to establish NC recoupment charges on components that are never sold separately. The last part of sentence 2 (after "and") may be redundant with sentence 1 since this phrase is included in the definition of major component in sentence 1. If this phrase in sentence 2 is not deleted, the sentence should be revised to clarify whether data must be accumulated when either criterion is met (i.e., either NC is identified in records/documents or the component has multiple applications or potential) or only for components which meet both criteria. AF

19. Enclosure 2, Page 2-2, Paragraph B.3.

It is recommended that accounting guidance be provided so that the current accounting system can be modified to support recoupment calculations. For example, the system should be required to flag RDT&E amounts when it reaches a certain threshold.

Reason: The building block approach suggested in this paragraph and the example at enclosure (3) are, in general, not compatible with existing accounting systems.

Navy

redundant with sentence 1 since this phrase is included in the definition of major component in sentence 1. If this phrase in sentence 2 is not deleted, the sentence should be revised to clarify whether data must be accumulated when either criterion is met (i.e., either NC is identified in records/documents or the component has multiple applications or potential) or only for components which meet both criteria.

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19. Enclosure 2, Page 2-2, Paragraph B.3.

It is recommended that accounting guidance be provided so that the current accounting system can be modified to support recoupment calculations. For example, the system should be required to flag RDT&E amounts when it reaches a certain threshold.

Reason: The building block approach suggested in this paragraph and the example at enclosure (3) are, in general, not compatible with existing accounting systems.

Navy

28. Page 2-2, para B.3: line 6 - after "system" add: "for those systems where a NC recoupment charge has not yet been approved."

Reason: To recognize those weapons systems for which a charge was approved and which did not use the "building block" approach, such as the F-15 and F-16 aircraft.

DSAA

Encl. 2 Par. B5

Enclosure 2, Implementing Procedures, Par. B.5. (Pages 2-3)

This paragraph should be revised or supplemented to permit reduced charges based on noncommonality with particular DOD items only if the noncommon portion (75% in the example) of the item is also not common with other USG items and was not developed with USG appropriations or funds directly or indirectly (e.g., with USG Independent Research and Development (IR&D) funds). Otherwise, this paragraph will contain a serious loophole undermining the fundamental philosophy of the Directive as stated in such paragraphs as B.2, D and Encl. 2, A.1.

AF

5. Enclosure 2, Paragraph B.5, Line 2.

COMMENT: The previous version of Draft DODD 2140.2 stated "(Less than 70% common)" vs. the present version "(Less than 90% common)". Is "90%" correct or just a typing error? Based on the approach shown, we assume the USG item's NC surcharge should not be changed by factoring in a pro rata portion of the number of commercial items to the USG item's quantity pool.

Army

6. Enclosure 2, Paragraph B.5, Line 8. Suggest the following change:

"The contractor shall be advised by the Administrative Contracting Officer (ACO) in writing. . . . . ."

COMMENT:

(a) The adding of the "ACO" above makes him responsible for notifying contractors of the NC charge.

(b) For domestic sales, the contractor should request the proper NC charge from the ACO. The ACO will notify the requestor of the proper NC charge.

Army

29. Page 2-3, para B.5; line 9 - after "commonality" add

5. Enclosure 2, Paragraph B.5, Line 2.

COMMENT: The previous version of Draft DODD 2140.2 stated "(Less than 70% common)" vs. the present version "(Less than 90% common)". Is "90%" correct or just a typing error? Based on the approach shown, we assume the USG item's NC surcharge should not be changed by factoring in a pro rata portion of the number of commercial items to the USG item's quantity pool.

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6. Enclosure 2, Paragraph B.5, Line 8. Suggest the following change:

"The contractor shall be advised by the Administrative Contracting officer (ACO) in writing. . . . . ."

COMMENT:

(a) The adding of the "ACO" above makes him responsible for notifying contractors of the NC charge.

(b) For domestic sales, the contractor should request the proper NC charge from the ACO. The ACO will notify the requestor of the proper NC charge.

Army

29. Page 2-3, para B.5: line 8 - after "commonality" add "MILDEPTS will provide rationale for derivative charges to DSAA for approval of the computation methodology and the derivative NC recoupment charge." Delete last sentence.

Reason: DSAA has already been reviewing and approving these derivative charges based on GAO report recommendations. This is consistent with procedures already in effect and provides for oversight of MILDEPT computations.

DSAA

Encl. 2 Par. C1

Enclosure 2, Implementing Procedures, Par. C.1. (Page 2-3)

After last sentence, add: "Once established, the NC recoupment charge will normally not be revised unless the item subsequently qualifies as an MDE item. When a non-MDE item becomes an MDE item, a new NC recoupment charge will be established using MDE procedures." These sentences are essential to clarify the policy and action required when an item changes from non-MDE to MDE.

adopted 8% charge for non U.S. contractors

We regret that the 8% charge stipulated in previous drafts for sales by non-US contractors has been deleted, since differential charges could aid US industry and enhance the US defense industrial base, balance of payments, employment, etc. Hopefully, this text will be restored. If not, at least substitute the phrase "US or non-US contractors" for "US contractors" to avoid discriminating against US industry by making the charge applicable only to them and not to their foreign competition. Paragraphs C.2.a, C.3 and D.1.b suffer this same deficiency.

We are also concerned that this paragraph (last sentence) fixes NC recoupment charges for all future sales no matter how obsolete the charges may later become due to inflation and other factors. (The updating provisions of paragraph A.4 apply only to MDE). This is also inconsistent with paragraph C.3 and D.1.b which do not "lock in" any historic selling price.

Also, we fail to understand why the expenditure threshold here (and in paragraph C.3) is limited to RDT&E funds which is contrary to other provisions which include different types of funds (e.g., paragraph C.2.a, D.2 and all the provisions pertaining to MDE)?

AF

Encl. 2 C.1.

- Retain the existing threshold of $5M in sunk RDT&E costs. Since that figure is in current dollars, it still represents a 40 percent lowering of the threshold since the current version of the directive was signed.

Dir. PA&E

20. Enclosure 2, Page 2-3, Paragraph C.1.

Threshold of $2 million relates only to RDT&E costs and does not include nonrecurring production cost. Is nonrecurring production cost being omitted intentionally? Also, this paragraph provides that after application of a percentage surcharge on non-MDE items, a unit charge, expressed in dollars, will be established. It would appear that continued application of the percentage surcharge would be easier and as equitable as charging a fixed amount for subsequent sales.

Reason: Clarification.

Navy

7. Enclosure 2, Paragraph C.1.

COMMENT: Since no significant change criteria is stated for Non-MDE, we assume the intent is to establish a fixed NC surcharge which would never change. This policy could fail to recoup significant dollar amounts unless a significant change criteria is established.

RECOMMENDATIONS:

(1) Non-MDE items should be reviewed annually as currently required.

(2) A significant change criteria should be established for Non-MDE items. 30% of the approved Non-MDE surcharge is suggested since this percentage has been proposed for MDE items.

(3) Clarify whether previously approved Non-MDE surcharges should be revised based on 5% of the FMS price (less NC surcharges) or "grandfathered" at the current approved rate.

(4) For Non-MDE items with approved NC surcharges based on nonrecurring (NR) production only, do we now eliminate the NC surcharge, suggest the surcharge be grandfathered.

(5) Establish a NR production threshold of $2M, or allow the responsible DOD component to establish a Non-MDE NR surcharge on an exception basis if RDTE is less than $2M and NR production cost pools are significant.

(6) Clarify how the NC surcharge for Non-MDE is to be split between RDTE and NR production.

Encl. 2 Par. C1

30. Page 2-3, para C1: Delete last sentence.

Reason: See reason 7 above.

OSAA

Encl. 2 Par. C2

Enclosure 2, Implementing Procedures, Par. C.2 (Pages 2-3, 2-4)

will publicate in 7290.3-M as ASD(C) amplification

not responsible response

After the above revisions, revise line 8 to read: "... by a DOD Component. Specific procedures for calculating the appropriate CIP reduction for a country that participated in the NC pool are published in DOD 7290.3-M." Because CIP investments may be spread over many years between many countries, specific guidance in DOD 7290.3-M on how to calculate potential reduction of NC recoupments for CIP investments is essential.

Add a new subparagraph c as follows:
"c. The provisions of paragraphs a & b above do not alter the requirement that modifications (such as ECPs) will be cost shared on a pro rata basis among all known users of the modification at the time the NCs are incurred, and that these charges are not waivable." This revision is required to comply with the AECA and international agreements (e.g., F-16 MOU signed by SECDEF with four European Governments) which require DOD to cost share modifications such as Engineering Change Proposals (ECPs) with all foreign governments receiving the modifications at the time. Neither the Arms Export Control Act nor such international agreements authorize substitution of an arbitrary 5% surcharge (or perhaps no charge at all under paragraph 2.b) in lieu of proper pro rata sharing of actual costs which may be more or less than 5%. The problem is exacerbated by the fact that the Directive would permit these costs to be waived (Section G) despite the fact that they may constitute current and future (as opposed to "sunk") cost for which no waiver is legally possible. AF

Encl. 2 Par. C3

adopted

21. Enclosure 2, Page 2-4, Paragraph C.3.

Substitute "component" for "parts"

Reason: This paragraph deals with components; parts are at a lower level than components.

Navy

charges, (e.g., copying, preparation and handling and shipping) are required by law and this fact should receive at least some mention in paragraph D. AF

22. Enclosure 2, Page 2-4, Paragraph D.1.A.

It is suggested that the means by which the nonrecurring recoupment will be collected be specified, so that implementing clauses will be on a common ground.

Reason: The paragraph provides that recoupment charges are to be made for MDE item data packages in lieu of a royalty fee. Although licenses authorizing the export of hardware may provide for the U.S. to recover sunk cost by charging royalty fees or recoupment charge, how a firm will collect royalty fees or nonrecurring charges is not clear. Navy

8. Enclosure 2, Paragraph D.1.a.

COMMENT: Paragraph 71502 of DODD 7290.3-M states: "A royalty fee represents payment for the right to use a U.S. Government TDP to manufacture Defense Articles outside the United States. The royalty fee is a technology charge and should not be confused with R&D recoupment." There may be conditions where both may apply, e.g., the Republic of Korea Indigenous Tank (ROKIT) will be manufactured in Korea using a TDP, but with the USG supplying the 60% commonality of parts. Since royalty charges are waived thru 1988, it would appear that the NC for the 60% commonality would be applicable.

9. Enclosure 2, Paragraph D.1.b.

COMMENT: As is Paragraph D.1.a, both royalty and NC surcharges appear to apply to Non-MDE manufactured or produced for Non-USG use through the transfer and use of a USG TDP. For items with non NC surcharges, royalty charges only apply based on percentages shown in Paragraph D.1.b(1)(2) applies to the USG standard price. Army

available in the Military Department inventory, the royalty fee for "in-country" consumption or the royalty fee for production for a third party may be reduced. The royalty fee may be reduced if the production is authorized for a country which is a current recipient of Military Assistance Program (MAP) funds. Reduction of royalty fees is required to be approved in writing by the Director, DSAA, in coordination with the OASD (Comptroller).

Reason: To provide for royalty fee waivers IAW DOD 7290.3-M. DSAA

Encl. 2 Pg. D2

adopted

In D.2, delete the words "USG developed" in line one since, as stated later in this sentence, the key is not who developed the software (e.g., USG or US contractors) but whether DOD has invested $2 million or more in that development. See for example, Paragraphs B.2 and D of the Directive proper. AF

adopted

23. Enclosure 2, Page 2-5, Paragraph D.2.

Expand on definition of USG developed; i.e., USG developed items include those items developed under contract. Also, what standard is to be chosen if both the number of weapons system and number of software packages are used?

Reason: Clarification.

Navy

24. Enclosure 2, Page 2-5, Paragraph D.3.

It is recommended that procedures be provided in calculating the fair market value of other technology transfers.

Reason: It is not clear whether calculation of fair market value addressed in paragraph D.1b pertains.

Navy

Encl 2 Par F1

25. Enclosure 2, Page 2-5, Paragraph F.1.

The statement "a pro rata share may be paid by the subsequent purchaser" is interpreted to mean that it is not mandatory to pay pro rata share in all instances. What or when will these instances occur? Also, the eight year period from acceptance of the Letter of Offer and Acceptance for the special costs may prove quite short if the feature involved takes some time to develop after the DD 1513 is signed.

Reason: Clarification.

Navy

32. Page 2-5, Para F: line 7 - after "$5 million." Add "The pro rata share shall be a unit charge determined by the DOD component as the result of distribution of the total costs divided by the total production."

Reason: To prescribe the calculation of pro rata share.

DSAA

Enclosure 2, Implementing Procedures, Par. F.1. (Page 2-5)	Revise line 9 to read: "... by the original customer unless otherwise authorized by DSAA." These words are required to let the reader know that an exception to the eight year period may be authorized when the DD Form 1513 was accepted in 1976, but actual investment for special RDT&E did not occur until 1984. AF

number current par. 3 to 3.f.

"G. Munitions Export License Application Reviews. Military Departments shall routinely comment on nonrecurring cost recoupment candidacy as a part of their review of Munitions Export License Applications. Sales which are obviously recoupment candidates shall be flagged with a recommendation for "Conditional Approval" to DSAA along with the recommendation that the exporting contractor be informed of the requirement for recoupment and that for specifics, the Military Department contracting office be contacted for recoupment charges, etc."

Reason: Notification of a recoupable foreign commercial direct sale of Munitions List items currently comes to the Military Department only through review of records of proposed sales, i.e., Munitions Export License applications. Military Departments are currently commenting on nonrecurring cost recoupment as a normal part of the review of Munitions Export License applications. However, the new Directive does not mention this vital link to, and dependency on, the Munitions Export License review process.

Navy

Encl. 2 Par. H

27. Enclosure 2, Paragraph H. Add new paragraph H:

"H. Review of Munitions Export License "Greens." DSAA will acquire from State Department, copies ("Greens") of all completed Munitions Export License applications and will distribute these to the appropriate Military Department(s) for review of nonrecurring cost candidacy. Military Departments shall establish a reliable process for recouping nonrecurring costs from those contractors whose export sales of Munitions List items are suitable candidates for recoupment."

Reason: The draft Directive makes no provision for notifying Military Departments of the approximately 85% of Munitions List item sales which are not offered to them for review and comment. Those sales are therefore unknown to the Military Departments and cannot be the subject of a recoupment effort. This problem can be remedied by acquiring copies ("Greens") of all completed Munitions Export License Applications from the State Department and distributing them to the Military Departments for review of nonrecurring cost recoupment candidacy.

Navy

Encl. 2 Par. I

28. Enclosure 2, Paragraph I. Add new paragraph I:

"I. Contractor Interrogatories. Military Departments shall make annual written interrogatories of appropriate Defense contractors whose products might be subject to nonrecurring cost recoupment of direct sales to foreign or domestic sources, and which sales would not require State Department Munitions Licenses. The Departments shall establish reliable procedures to accomplish nonrecurring cost recoupment on sales discovered as a result of these interrogatories."

Reason: The draft Directive makes no mention of any notification process to the Military Departments for direct foreign sales of non-Munitions List items (with dual defense/civilian application), nor of direct sales to domestic customers of these items, or of Munitions List items. Such notification is a necessary prerequisite for recoupment. The best option for accomplishing such notification appears to be in annual interrogatory of appropriate Defense contractors by the Military Departments through their contract administration officers.

Navy

Encl 2 Par. J

29. Enclosure 2, Paragraph J. Add new paragraph J:

"J. Parallel Development Contracts. Where competitive multiple Research and Development (R&D) or development contracts were let, the full cost of all such contracts shall be included in the NC investment pool for figuring the pro rata charge."

Reason: The draft Directive does not make it clear that the

sales discovered as a result of these interrogatories."

Reason: The draft Directive makes no mention of any notification process to the Military Departments for direct foreign sales of non-Munitions List items (with dual defense/civilian application), nor of direct sales to domestic customers of these items, or of Munitions List items. Such notification is a necessary prerequisite for recoupment. The best option for accomplishing such notification appears to be in annual interrogatory of appropriate Defense contractors by the Military Departments through their contract administration officers. Navy

Encl 2 Par J

29. Enclosure 2, Paragraph J. Add new paragraph J:

"J. Parallel Development Contracts. Where competitive multiple Research and Development (R&D) or development contracts were let, the full cost of all such contracts shall be included in the NC investment pool for figuring the pro rata charge."

Reason: The draft Directive does not make it clear that the full cost of all parallel development R&D contracts must be included in the NC pool when figuring the NC pro rata charge.

Navy

"K. Calculation of Subsystem Cost for Master Contracts. When an FMS sale involves an item developed by a subcontractor at his expense (not under Government contract) for a master weapon system contract, and when such an item has not previously been sold to the Government, the military department's NC investment for Test and Evaluation of that item as a part of the weapon system may be calculated in the following fashion:

a. First, calculate the percentage of the Master Weapon System Contract which represents the DOD's Test and Evaluation (T&E) of the overall weapon system (including the subsystem of interest for FMS sale).

b. Next, multiply that percentage times the FMS sale cost per item, to arrive at the DOD Test and Evaluation NC pro rata investment."

Reason: Many weapon system procurements are made as one master contract with the prime contractor supplying most of the subsystems and their components. Sometimes a subsystem of such a weapon system is developed and purchased for the master weapon system with no investment of government funds except for test and evaluation of the master system itself. In such cases, provision should be made for the military department to "back into" calculation of the NC investment pool for subsystem by finding what percentage of the master contract was for T&E, and applying that percentage to the cost of the subsystem to determine the subsystem's NC investment pool. Navy

31. Enclosure 2, Paragraph L. Add new paragraph L:

Move current paragraph G to L.

Reason: Rearrange according to subject sequence.

Navy

32. Enclosure 2, Paragraph L.1. Following "reference (d)", add:

"Section 104"

Reason: Clarity.

Navy

33. Enclosure 3, Page 3-1. Revise Part A, B, and C to read:

"Part A - Nonrecurring R&D Investment (Numerator)

Part B - Nonrecurring Production Investment (Numerator)

Part C - Projected Units (Denominator)"

Reason: Clarity and consistency.

Navy

Page 5-1

33. Page 5-1: Revise the DSAA Comptroller report to include quantity being sold and year of the sale as a fiscal year - after column 3 (Item) add a column entitled "Quantity"; in column 4 add "Fiscal" in year of sale and amount. Delete requirement for "Part 1", and all of Part 2.

Reason: A two-part report is not required. With the addition of a quantity column and reporting of all open cases, the report will provide sufficient management information.

DSAA

Comments on the proposed revision to DoD Directive 2140.2 from various industries.

adopted - can give waiver if only competition is foreign. Gives flexibility in DoDD

General:

General Comment

As currently drafted, the Directive would apply not only to current government contractors who also make sales abroad, but to small businesses which may assemble modification kits and have no contractual relationship with the government. The lowering of the threshold for Nonrecurring Cost (NC) recoupment from $5 million to $2 million indicates that many small businesses will be adversely affected by the regulation, unless it is modified.

FMS

General Comments

Reject - GAO believes it is appropriate for contractors to pay pro rata share of US Govt RDT&E + prod mix costs -

Finally, AEA believes that DoD's recoupment policy, both existing and proposed, falls outside the scope of the Arms Export Control Act and contradicts both the letter and intent of the Act.

AEA

General Comments:

It is the consensus of our members that this proposed Directive revision is overreaching in its purpose and scope and is unduly complicated.

It would appear that the thrust of the directive could be accommodated by recoupment on the major equipment or systems sales without application to components, modification kits, technical data packages, etc. Implementation of the requirements set forth in the directive will significantly slow down the proposal cycle and increase administrative time and effort on the part of both government and contractors. It will also tend to create ill will in dealings with foreign government representatives due to inordinate delays which can be occasioned by the increased requirements, and therefore adversely further affect the balance of trade. Moreover, it will make U.S. industry less competitive with those companies which are owned or directly subsidized by foreign governments.

The impact will be principally in increased costs through additional costs passed on directly and indirectly (because of added administrative effort). This result is obvious and reflected in the DoD Directive. The impact at the functional level is unknown, but expected to be small.

The entire picture is unclear as to how one can adequately judge the amount of future FMS or commercial sales of a product at the first sale to a non-USG customer. If the estimate is low, over recovery is possible (at a higher inequitable cost share to non-DoD customers). Conversely, if the estimate is high (resulting in lower recovery) does the U.S. Government accept this and absorb the difference or will non-USG customers be subsequently assessed?

Another scenerio might be that a product is modified or improved at the expense of a particular non-USG customer. If this improvement is subsequently procured in a product sold to the USG, it would seem logical for the USG to pay the non-USG customer a "royalty" for the USG's share of avoided non-recurring costs.

Finally, if the logic of the control and bookkeeping problems as well as reduced competitive position do not prevail, and it is deemed necessary by the DoD to impose this surtax on foreign customers, it would seem appropriate that since the government must evaluate data supplied by contractors and determine the amount to be assessed and added to the contractor's price, it would be far more efficient, and less burdensome to the contractors if - on FMS cases - the DoD just add these costs to their FMS administrative burden and collect it off the top as they are paid by the FMS customer, rather than have the contractor add it to their price and pay it back to the government. In this way they cut out the middleman and that associated bookkeeping work for the contractor.

Reject arguments, time + against reimbursement -

The DoD Directive will cut costs and administrative burden if each Military Department of Defense Agency involved will provide timely and efficient implementation of subject Directive with standard procedures. If the systems and procedures for implementation vary among the various agencies, administration of the industry portion will be more costly and time consuming.

AIA

Par. D

Section 221.4. Policy.

Par. D Revise last sentence to read as follows:

Approved revised NC recoupment charges may not be applied retroactively where (1) a Letter of Offer and Acceptance (LOA) has been signed by a U.S. official and released to the FMS Customer, or (2) where a formal written offer has been signed by the contractor and released to the direct sales customer.

accepted - answers para in DoDD gives sufficient flexibility -

Rationale. The last sentence of this Section provided a modest "grandfathering" clause to protect FMS and direct sales from applicability of the new standards where the sale is based on the assumption that no NC recoupment is required. The sentence should be revised to expand the grandfather clause to include those situations where firm bids have already been submitted to the customer. Both the military departments and commercial contractors currently have negotiations in progress that have reached the formal offer stage. Although there may be no signed contract, these offers are intended to bind both the government and the private contractor to a certain price. Such a grandfathering provision seems not only appropriate, but equitable.

FMS

Par. G.1

adopted in para G.3.

- 221.7 Waivers (Including Reductions) section should be changed by including an additional paragraph which recognizes the existence of foreign producers competitive with American producers and that recoupment charges can and do, sometimes, disadvantage unfairly American producers in competition with those foreign producers.

VARO

Par. G.4

rejected DoD needs at least 60 days.

2. Waivers - Para. G. 4 provides that decisions will be reached on waivers within "60 days after receipt of the request." In cases where other nations request waiver of non-recurring cost charges for articles or services included in a direct Commercial sale, U.S. contractors are often under severe time constraints to submit Proposals in time to meet international competition. A processing time of no more than 30 to 45 days would be most helpful.

AIA

Encl. 1 Par. F & G

adopted Para C.2.b. Encl clarifies this -

1. Encl. 1 Definitions
   Para. F. Non-recurring Research, Development, Test and Evaluation (RDT&E)
   Para. G. Non-recurring Production Costs
   Encl. 2 Implementing Procedures
   Para. B-1 Calculation of Charges on MDE and Components

The non-recurring development and production cost of ECP's which are authorized after contract award is shared by USAF and all FMS countries on a per aircraft basis. The projected total cost defined in F. and G. could be interpreted to include these costs which would amount to double bidding on ECP's. However, review of Implementing Procedures Paragraph C.2.b. indicates this is not the intent. Some clarification of definitions F. and G. as related to FMS sharing of ECP development costs after contract award is desirable.

AIA

Encl 2-Par A2

221.6 Procedures section should be changed in a way which sets a maximum recoupment charge at 5 percent of the current selling price; and the

VARO

Repeal - law requires a pro rata share of recoupment on MDE-

Encl. 2 Par. A5

221.6. Procedures. Encl. 2 Para. A5

(5) Change, "When a defense contractor negotiates the direct sale of a defense article or technology," as follows:

When a defense contractor negotiates the direct sale of MDE articles or technology,

accepted - AP will publish a list of approved charges

And, add at the end of the paragraph the following:

For non-MDE items the contractor shall review DOD Dir. 7290.3M to determine the applicable NC charge, or if an NC charge applies.

accepted see AP C. Encl 2

As currently written, prior to submitting a bid or negotiating a direct sale of any item of defense equipment, a defense contractor will have to check with the ACO for the item to verify the applicability of a NC. Such a procedure seems cumbersome and unnecessary, since DOD Dir. 7290.3M now includes a list which provides applicability and identification of approved NC recoupment charges. For small business which does not have an ACO, the checking process would be, at best, time-consuming and difficult. There appears to be no reason why DOD Dir. 7290.3M is not a better way to verify the NC applicability for non-MDE items and components of MDE that meet the requisite thresholds.

Without this recommended change, the ACOs and military departments will be required to perform new and administratively burdensome tasks where a better mechanism--DOD Dir. 7290.3M--already exists.

Our recommended change will simplify the process of determining if NC recoupment applies to certain modification kits supplied by small business. In this area of sales, the customer usually provides a detailed parts list of the items

For non-MDE items the contractor shall review DOD Dir. 7290.3M to determine the applicable NC charge, or if an NC charge applies.

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Without this recommended change, the ACOs and military departments will be required to perform new and administratively burdensome tasks where a better mechanism--DOD Dir. 7290.3M--already exists.

Our recommended change will simplify the process of determining if NC recoupment applies to certain modification kits supplied by small business. In this area of sales, the customer usually provides a detailed parts list of the items which are to be quoted. Together, the components comprise a kit, which the government usually buys as a kit from the prime system contractor. Thus, the small business kit supplier is placed at a competitive disadvantage unless he can readily check DOD Dir. 7290.3M and determine applicable charges immediately. If he must check with an ACO each time, he will not be able to meet thirty- or sixty-day response times on invitations for bid.

FMS

Encl. 2 Par. A6

Reject 30 days is reasonable

3. Encl. 2 Implementing Procedures
Para. A.6. General

Contractor Payments of Nonrecurring Cost Charges - Para. A. 6 of Encl. 2 "Implementing Procedures" provides that U.S. contractors will be required to pay the U.S. GOVT. (USG) within 30 days following "the delivery of each item from the contractors facility." Thirty (30) days after the delivery of each item is not considered sufficient time in the light of international billing and payment procedures. A more appropriate payment period would be 30-45 days after the U.S. contractor receives payment from the customer for articles or services delivered.

In addition, referring payment within thirty (30) days of an affected item is not feasible since in the current multinational market contractors do not receive payment in some cases for years.

AIA

Encl. 2 Par. B1 See comments to Encl. 1 Par. F & G

Encl. 2 Par. B2

5. Consultation with Defense Contractors in Determining Direct Commercial Sales Quantities - In Para. B.2 of Encl. 2 it indicates that "Defense Contractors should be contacted if necessary in determining direct sales quantities." Suggest elimination of the words "if necessary." Contractors should be asked for any inputs they may have in all cases involving direct commercial sales.

AIA

Reject would result in redundant requirement for information -

Encl. 2 Par. B4

4. Encl. 2 A.6 General
B.4 Calculation of Charges on MDE and Components

The contractor does not pay recoupments on FMS programs. Recoupments are handled outside the hardware contracts. Direct sale contracts may also require payment of recoupment charges outside the contract if FMS credits are used. Payments would be through a USG/FMS customer LOA for services and recoupments. If recoupment charges are included in a direct sale contract, payment to the USG should be upon or after payment by the direct sale customer to contractor

Reject - see reason

Encl. 2 Par. C1

Encl. 2 Par. C.1 As indicated in our comments, our primary concern as a small business is the change in the non-recurring cost threshold from $5 million to $2 million and the unknown, but possibly great, impact this will have on non-MDE items to be subject to this charge. FMS

adopted new para C.4. was written - Enough flexibility in the DoDD (manner) -

Encl. 2 Par. C2

6. Encl. 2 Para. C 2b, sentences 1 and 2

"Developed to improve the safety, reliability, and maintainability. The cost of programs designed to improve the safety, reliability, availability and maintainability for the projected life of the equipment shall be included in the end item/major component NC pools. In the event an FMS customer funds part of the development cost through a Component Improvement Program (CIP) or comparable program, then a pricing exception for an appropriate adjustment of the established NC recoupment charge may be requested by a DoD Component."

AIA

COMMENT: It will be a common occurrence for purchasers to qualify for an NC adjustment because of their CIP participation. Will DSAA be asked to adjust the NC on an individual country/case basis? It would be more efficient for the DoD components to adjust the NC based on a DSAA approved formula. Will the same rule apply to ICP's members? If a country discontinued CIP participation would the NC for the end item have to be adjusted?

adopted new paragraph developed jointly by the Office of General Counsel, DSAA + acctg Policy -

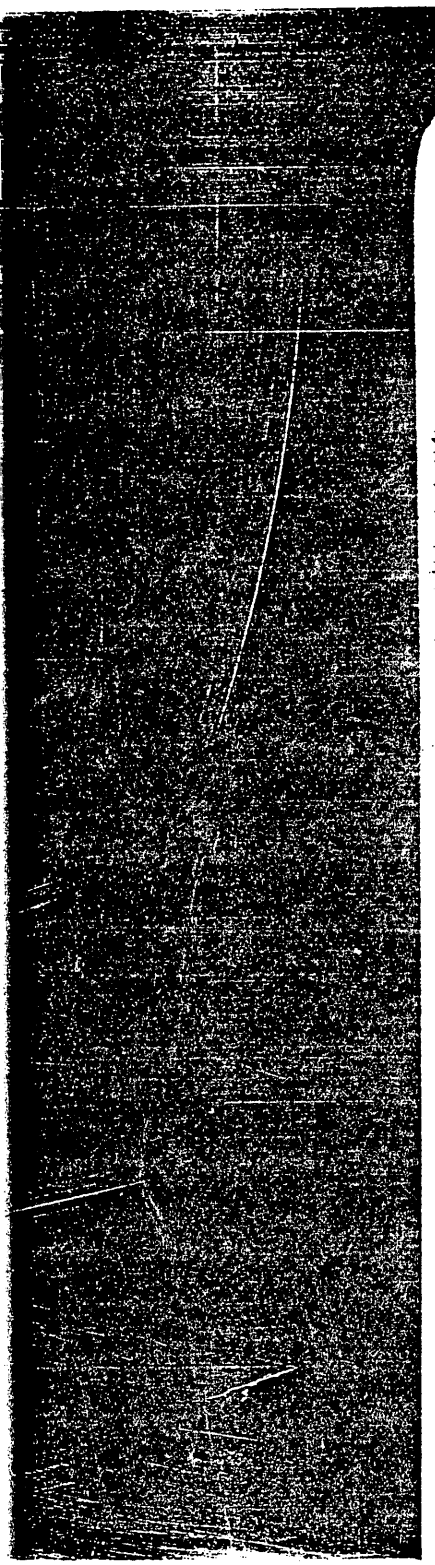
Encl. 2 Par. D1

7. Encl. 2 Para. D. 1a, Technical Data Packages

COMMENT: Establishing unit prices for commercial sales would be very difficult, since no existing mechanisms are in effect at this time. The entire proposal method of collecting dollars on technical publications in place of royalty fees would be hard to accept by either the multinational customers or the manufacturers required to implement such a procedure. In fact, this method would not be acceptable.

AIA

adopted added additional clarification



FMS	[illegible]	[illegible]	AEA
A General	Gen.		General
F Par. D			
		Par. G.1	
	Par. G.4		
	Encl. 1 Par. F		
	Encl. 1 Par. G		
		Encl 2 Par. A2	
Encl 2 Par. A5			
	Encl 2 Par. A6		
	Encl 2 Par. B2		
	Encl 2 Par. B4		
Encl 2 Par. C1			
	Encl 2 Par. C2		
	Encl. 2 Par. D1		

OFFICE OF THE ASSISTANT SECRETARY OF DEFENSE

WASHINGTON D.C. 20301

COMPTROLLER
(Management Systems)

5 APR 1984

MEMORANDUM FOR MR. PURITANO

SUBJECT: Reissuance of DoDD 2140.2, "Recoupment of Nonrecurring Costs on Sales of USG Products and Technology"

The attached SD Form 106 requests coordination on a proposed reissuance of DoD Directive 2140.2.

The Directive establishes the DoD policies for recoupment of nonrecurring RDT&E and procurement costs. Policies reflected in the Directive are a combination of legal requirements and administrative decisions. The policy on recovering a pro rata share of nonrecurring cost on Major Defense Items sold to FMS customers is required by law. The policy of recovering nonrecurring cost on commercial sales to foreign countries, international organizations and the public was established in 1977 by the President.

The reissuance implements recommendations made by a Subcommittee of the Committee on Government Operations, House of Representatives and improvements recommended by a special study group chaired by Mike Melburn, Accounting Policy Staff. The study group report was issued in November 1983. Major changes are to:

- Lower the RDT&E investment threshold for recouping nonrecurring costs on non-major items from $5 million to $2 million.
- Eliminate the requirement to accumulate the nonrecurring production cost on non-Major Defense Items.
- Establish a percentage method for recouping nonrecurring costs for non-Major Defense Items in which over $2 million of RDT&E funds have been expended.
- Correct deficiencies in current procedural statements that hamper the collection of nonrecurring costs.

The changes in investment thresholds for non-Major Defense Items are required because our special study disclosed that accounting systems cannot readily identify nonrecurring costs funded by the procurement appropriations. The RDT&E investment is identifiable at very low dollar thresholds; e.g., $10,000 on an RDT&E task to develop fireproof gloves. The $2 million RDT&E

threshold is a general concensus of DoD action officers of a reasonable threshold amount at which to initiate recoupment action.

Policies in the Directive have an impact on the public. Therefore, the proposed reissuance will be published in the Federal Register to provide for public comment on the policies.

Recommend signature on the SD Form 106. P/B and OAGC(FM) concur.

E. Rosen

Enclosure

DoD DIRECTIVES SYSTEM COORDINATION AND CONTROL RECORD

1. TYPE OF ISSUANCE	2. SUBJECT NUMBER	3. SUBJECT CAPTION
DoDD	2140.2	Recoupment of Nonrecurring Costs on Sales of USG Products and Technology

4a. SIGNATURE OF OSD PRINCIPAL STAFF ASSISTANT OR PRINCIPAL DEPUTY	5a. SIGNATURE OF CONTACT OFFICER
[signature]	[signature]
b. TYPED NAME (Last, First, M.I.) Puritano. Vincent	b. TYPED NAME (Last, First, M.I.) Melburn, Michael J.
c. TITLE Asst. Secretary of Defense (C)	c. OFFICE SYMBOL DASD(MS)/AP
	d. EXTENSION 75135
	e. ROOM NUMBER 3A882

6. REMARKS The proposed reissuance of DoDD 2140.2 incorporates recommendations made by a subcommittee of the Committee on Government Operations, House of Representatives. The Directive establishes DoD policies on the recoupment of nonrecurring costs from foreign countries, international organizations and the public when they purchase items developed by DoD or use technology developed by DoD to manufacture items. The major policy changes are that a recoupment charge will be made whenever DoD has invested $2 million of Research, Development, Test and Evaluation Funds and that a percentage surcharge will be used for most non-Major Defense items in lieu of a pro rata calculation.

7. DATE FORWARDED (YYMMDD)	8. RETURN DATE (YYMMDD)
4-9-84	5-9-84

FOR USE OF ORIGINATING OFFICE ONLY (Check appropriate box(es) below)

THE CLASSIFICATION IS: (See DoD Regulation 5200.1-R)

- ☐ TOP SECRET
- ☐ SECRET
- ☐ CONFIDENTIAL
- ☒ UNCLASSIFIED
- ☐ OTHER (Specify)

THE DOCUMENT WILL BE PUBLISHED AS A RULEMAKING DOCUMENT IN THE F[illegible] (See DoD Directive 5410.9)

☒ YES ☐ NO

9. TO ADDRESSEES LISTED BELOW: The attached draft is forwarded for review and comment.

a. If the draft as written is approved, please indicate concurrence by signing and dating the appropriate space below. (Signature level must comply with paragraphs D.2.b. through D.2.d., Chapter 2, DoD 5025.1-M.)

b. If changes are recommended please attach a separate memorandum covering the recommendations and so indicate in the appropriate space below.

X	UNDER SEC DEF FOR POLICY	X	SECY OF THE ARMY
X	UNDER SEC DEF FOR RESEARCH AND ENGINEERING	X	SECY OF THE NAVY
X	ASST. SEC DEF (Comptroller)	X	SECY OF THE AIR FORCE
	ASST. SEC DEF (Health Affairs)	X	CHAIRMAN, JOINT CHIEFS OF STAFF
X	ASST. SEC DEF (International Security Affairs)	X	DIR, DEFENSE ADVANCED RESEARCH PROJECTS AGENCY
X	ASST. SEC DEF (International Security Policy)	X	DIR, DEFENSE AUDIOVISUAL AGENCY
X	ASST. SEC DEF (Legislative Affairs)	X	DIR, DEFENSE COMMUNICATIONS AGENCY
X	ASST. SEC DEF (Manpower, Reserve Affairs, and Logistics)	X	DIR, DEFENSE CONTRACT AUDIT AGENCY
X	ASST. SEC DEF (Public Affairs)	X	DIR, DEFENSE INTELLIGENCE AGENCY
X	GENERAL COUNSEL, DoD	X	DIR, DEFENSE INVESTIGATIVE SERVICE
X	INSPECTOR GENERAL, DoD	X	DIR, DEFENSE LOGISTICS AGENCY
	ASST. TO THE SEC DEF (Atomic Energy)	X	DIR, DEFENSE MAPPING AGENCY
	ASST. TO THE SEC DEF (Intelligence Oversight)	X	DIR, DEFENSE NUCLEAR AGENCY
X	DIRECTOR, PROGRAM ANALYSIS & EVALUATION	X	DIR, DEFENSE SECURITY ASSISTANCE AGENCY
		X	DIR, NATIONAL SECURITY AGENCY/CHIEF, CENTRAL SECURITY SERVICE

SD FORM 83 MAR 106

PREVIOUS EDITIONS ARE OBSOLETE.

Department of Defense

DIRECTIVE

NUMBER

SUBJECT: Recoupment of Nonrecurring Costs on Sales of U.S. Products and Technology

References:
(a) DoD Directive 2140.2, "Recoupment of Nonrecurring Costs on Sales of USG Products and Technology," January 5, 1977 (hereby canceled)
(b) Arms Export Control Act (P.L. 90-629), as amended
(c) Council on International Economic Policy Decision Memorandum No. 23, "R&D Recoupment," August 2, 1974
(d) DoD 7290.3-M, "Foreign Military Sales Financial Management Manual," June 1981
(e) Defense Acquisition Regulation (DAR)

A. REISSUANCE AND PURPOSE

This Directive reissues reference (a); establishes policy to conform with references (b) and (c) for calculating and assessing nonrecurring cost (NC) recoupment charges on sales of defense articles or technology to non-U.S. government customers; and assigns responsibilities, and prescribes procedures to implement established policies.

B. APPLICABILITY AND SCOPE

1. The provisions of this Directive apply to the Office of the Secretary of Defense, the Military Departments, the Organization of the Joint Chiefs of Staff, the Unified and Specified Commands, and the Defense Agencies (hereafter referred to as "DoD Components").

2. Its provisions shall be applied contractually to corporations and private parties who sell defense articles or technology developed with DoD appropriations or funds (and in special cases, customer funds) or use such technology to manufacture items sold commercially to a foreign government, international organization, foreign commercial firm, or domestic organization.

C. DEFINITIONS

The terms used in this Directive are defined in enclosure 1.

D. POLICY

Non-U.S. Government purchasers shall pay a fair price, determined in accordance with this Directive, for the values of the DoD nonrecurring investment in the development and production of defense articles and development of technology unless an NC recoupment charge waiver has been approved by the DoD official designated in section G of this Directive. Approved revised NC recoupment charges shall not be retroactively applied to accepted FMS agreements or to direct sales which were entered into prior to the date of approval of the revised NC recoupment charge.

E. RESPONSIBILITIES

1. The Under Secretary of Defense for Research & Engineering shall monitor and exercise control over nonrecurring cost recoupment aspects of domestic commercial sales of defense articles and technology and shall take appropriate action to revise the Defense Acquisition Regulation (DAR) to agree with this Directive.

2. The Under Secretary of Defense (Policy) shall monitor the application of this Directive and exercise control over foreign sales of DoD-developed articles and technology.

3. The Assistant Secretary of Defense (Comptroller) shall provide necessary cost accounting guidance and publish a listing of the items or technology to which NC recoupment charges are applicable.

4. The Director, Defense Security Assistance Agency (DSAA), shall serve as the DoD focal point for review and approval of NC recoupment charges for Major Defense Equipment (MDE) items and for processing NC recoupment charge waiver requests received from foreign countries and international organizations for Foreign Military Sales (FMS) or direct commercial sales. Approved NC recoupment charges for MDE items shall be provided to the Deputy Assistant Secretary of Defense (Management Systems) (DASD(MS)) for publication.

5. Heads of Military Departments and Defense Agencies shall determine the DoD nonrecurring investment in defense articles or technology and perform required pro rata calculations in accordance with cost accounting guidance from the ASD(C); provide recommended charges for MDE items to DSAA; determine the appropriate charges for non-MDE articles and technology; provide the approved non-MDE item and technology charges to the DASD(MS) for publication and submit quarterly reports of anticipated and actual NC recoupment charge collections to DSAA.

F. PROCEDURES

All DoD Components shall follow the implementing procedures contained in Enclosure 2.

G. WAIVERS (INCLUDING REDUCTIONS)

1. The Arms Export Control Act (reference (b)) requires the recoupment of nonrecurring costs of MDE from FMS customers but authorizes consideration of waivers for particular sales which, if made, significantly advance United States

Government (USG) interests in the North Atlantic Treaty Organization, Japan, or Australia. Waiver for non-MDE items under FMS and for direct commercial sales shall be based upon the same considerations.

2. Requests for waivers of NC recoupment charges for sales of defense articles under the FMS program or on direct commercial sales to foreign governments and international organizations shall be submitted to the Director, DSAA. Requests should originate with the foreign government and shall provide information regarding the extent of standardization to be derived as a result of the waiver and other benefits which would accrue to the USG as a result of the sale. The request shall contain a summary statement of the facts regarding the program, benefits expected and justification therefor, and any calculations necessary to determine that the waiver has resulted in a reduction of contract price. Blanket waiver requests shall not be submitted nor considered. The term "blanket waiver" refers to a NC recoupment charge waiver for all sales to a particular country or all sales of a weapon system. A waiver request shall not be approved for a sale which was accepted without a NC recoupment charge waiver, unless the waiver was pending at the time of acceptance. A waiver shall not be granted in connection with a direct commercial sale if such a waiver could not have been legally granted in connection with a sale made under the FMS program.

3. Requests for waivers of NC recoupment charges for domestic sales of defense articles shall be submitted by the contractor to the Under Secretary of Defense for Research and Engineering. The request shall provide information regarding the dollar value of the waiver, benefit to be derived by the DoD, the names of foreign and domestic competitors, impact on the USG balance of payments, demonstrable rights of the manufacturer or purchaser, and any other justification for the waiver.

4. Requests for waivers shall be processed expeditiously, and a decision made by the approving authority (see paragraph G.6) to either approve or disapprove the request within 60 days after receipt. A waiver in whole or in part of the recoupment charge shall be provided in writing to the appropriate DoD Component prior to issuance of the FMS agreement or signing of the direct sale commercial contract.

5. The approving authority shall request the concurrence of the Director, DSAA; ASD(C); and OUSDR&E, as appropriate in his decision. If an issue concerning the waiver request cannot be resolved, the approving authority shall refer the waiver request to the Deputy Secretary of Defense for final determination. The action memorandum to the Deputy Secretary of Defense shall be coordinated with the Director, DSAA, ASD(C) and USDR&E, as appropriate.

6. The Director, DSAA, is the approving authority and will state in writing any approvals granted for waivers associated with FMS and direct foreign sales. The Under Secretary of Defense for Research and Engineering is the approving authority and will state in writing any approvals granted for waivers involving sales of defense articles or technology to domestic organizations. This authority shall not be redelegated. A copy of each approved waiver will be forwarded to the Assistant Secretary of Defense (Comptroller) and to the concerned DoD Component(s) by the approving authority.

7. This Directive does not apply to sales of excess property when accountability has been transferred to property disposal activities and the property is sold in open competition to the highest bidder.

H. INFORMATION REQUIREMENTS

The recordkeeping and reporting requirements prescribed in paragraph G.2 of enclosure 2 are assigned Report Control Symbol DSAA(Q)1112.

I. EFFECTIVE DATE AND IMPLEMENTATION

This Directive is effective immediately. Forward two copies of implementing documents to the Assistant Secretary of Defense (Comptroller) within 120 days.

Enclosures - 5
1. Definitions
2. Procedures
3. Format for MDE Calculation
4. Format, Recoupment of Nonrecurring Costs on MDE items.
5. Quarterly report format on status of
   NC recoupment charge collections

DEFINITIONS

A. Major Defense Equipment means any item of equipment on the United States Munitions List having a nonrecurring RDT&E cost of more than $50 million or a total production cost of more than $200 million.

B. Government Sale means a sale of articles and/or services to customers by any DoD Component under authority of appropriate legislative acts.

C. Direct Sale means a commercial sale to a customer by a defense contractor of products, technology, materiel, services, and/or development or production techniques which were originally developed, improved or produced using DoD appropriations or funds.

D. Domestic Organization means any U.S. nongovernmental organization or private commercial firm.

E. Technology means information of any kind that can be used or adapted for use in the design, production, manufacture, utilization or reconstruction of articles or materiel. The data may take a tangible form, such as a scale model, prototype, blueprint or an operating manual, or may take an intangible form, such as technical advice.

F. Nonrecurring Research, Development, Test and Evaluation (RDT&E) costs are those costs funded by an RDT&E appropriation to develop or improve the product or technology under consideration either through contract or in-house effort. This includes costs of any engineering change proposal initiated prior to date of the contract with the customer, as well as projections of such costs, to the extent additional effort applicable to the sale model or technology is necessary or planned. It does not include costs funded by either Procurement or Operations and Maintenance appropriations.

G. Nonrecurring Production Costs are those one-time costs incurred in support of previous production of the model specified and those costs specifically incurred in support of the total projected production run. These nonrecurring costs include DoD expenditures for preproduction engineering, rate and special tooling, special test equipment, production engineering, product improvement, destructive testing, and pilot model production, testing and evaluation. Nonrecurring production costs do not include DoD expenditures for machine tools, capital equipment or facilities for which contractor rental payments are made in accordance with the DAR (reference (e)) or asset use charges assessed in accordance with DoD 7290.3-M (reference (d)).

H. "Special" RDT&E and Nonrecurring Production Costs are those incurred at the request of, or for the benefit of, the customer in developing a special feature or unique requirement. These costs must be paid by the customer as they are incurred.

I. Pro Rata Recovery of Nonrecurring Costs means distribution (proration) of a pool to a specific number of units which benefit from the investment so that a DoD Component will collect from a customer a fair (prorata) share of the investment in the product being sold.

J. A Cost Pool represents the total cost to be distributed across the specific number of units. The nonrecurring RDT&E cost pool comprises the costs described in Definition F. The nonrecurring production cost pool comprises costs described in Definition G.

K. Foreign Military Sale (FMS) means a sale of defense articles or defense services to a foreign government or international organization under authority of the Arms Export Control Act (reference (b)).

L. Model is a basic alpha-numeric designation within a weapon system series, such as a ship hull series, an equipment or system series, an airframe series, or a vehicle series. For example, the F5A and the F5F are different models within the same F-5 system series.

M. Non-U.S. Contractor. A non-U.S. citizen, or an organization which is not incorporated in the U.S.

IMPLEMENTING PROCEDURES

A. General.

1. Each DoD Component and defense contractor negotiating the sale of products and/or technology developed with DoD appropriations or funds shall ensure the assessment of the charges as set forth in this Enclosure.

2. Each DoD Component shall calculate a NC recoupment charge for items or technology releasable to foreign countries and international organizations when FMS or direct commercial sales are anticipated. The NC recoupment charge shall be based upon information recorded in DoD accounting records or DoD budget justification documents. Engineering cost estimates may be used to determine NC expected to be incurred in periods not covered by budget justification documents.

3. The NC recoupment charge computation (nonrecurring RDT&E and production) for the sale of MDE items shall be submitted to the Director, DSAA, for approval of the amount to be applied to pending FMS or direct sales. The NC recoupment computation shall be supported with the MDE calculation worksheet illustrated at Enclosure 3. A summary report on each MDE item shall be provided to DSAA following the format illustrated at enclosure 4. The Director, DSAA, will review each DoD Component's calculations and provide approved NC recoupment charges for MDE items to the DoD Component. A copy of all approvals shall be provided to the DASD(MS) for publishing in DoD 7290.3-M (reference (d)).

4. Once the approved charge has been used in an authorized sale, the charge will normally not be revised until a model change occurs. However, each DoD Component shall annually review approved MDE charges to determine if there have been significant changes in factors or assumptions used to compute the original NC recoupment charge established for a model (for example, significant changes in identifiable RDT&E costs or the anticipated production run). A significant change occurs when a new calculation shows a change of more than 30 percent of the current system NC recoupment charge for an MDE item or the potential for an additional NC recoupment charge collection of over $100,000 exists. When significant changes are identified for MDE, the DoD Component shall submit a request to the Director, DSAA, for authority to make appropriate changes in NC recoupment charges. The Director, DSAA, shall respond to the request in writing within 60 days after receipt of the request.

5. When a defense contractor negotiates the direct sale of a defense article or technology, or a derivative of a USG developed item, he shall request the amount of the NC recoupment charge from the Administrative Contracting Officer (ACO) or (for technology sales) the technology charge from the DoD Component responsible for DoD acquisition of the article. When making this request, the contractor will submit such information as may be necessary to comply with this Directive. If the NC recoupment charge has not already been established, as provided for under this Directive, the ACO shall contact the DoD Component activity responsible for establishment of the charge and advise the contractor of the estimated date the amount of the charge will be made available.

6. All DoD contracts for RDT&E or acquisition shall include a mandatory clause which requires the contractor to pay the USG, within 30 days following delivery of each item from the contractor's facility, the established NC recoupment charge for any domestic or international direct sale, coproduction, or licensed production of defense articles or technology (see DAR 7-104.64, reference (e)).

7. The cognizant DoD Component shall deposit collections in payment of an NC recoupment charge without delay in the nearest Federal Reserve Bank to accounts prescribed in DoD 7290.3-M, reference (d). Notification of the deposit shall be provided to the DoD Component activity responsible for submission of reports required in paragraph G.2. of this enclosure.

B. Calulation of Charges on MDE and Components. MDE items are defined in Enclosure 1. The determination of whether an item meets the MDE dollar threshold shall be based on obligations recorded to the date the equipment is offered for sale. Production costs shall include cost incurred for DoD, FMS and known direct sales production. For the FMS program, the sales offer date shall be the date a Letter of Offer and Acceptance (LOA) is signed by a U.S. official and released to the FMS customer; for commercial sales, the sales offer date shall be the date of contract signature.

1. NC recoupment charges shall be assessed on a pro rata basis. The charges shall be established by dividing the total of NC investment (nonrecurring RDT&E + nonrecurring production) incurred to date plus projections of future costs to be incurred, by the total estimated number of units projected to be produced over the life of the system (including DoD requirements, Military Assistance Program (MAP) requirements, FMS requirements and direct commercial sales requirements). The computation of the cost pool shall exclude costs for those items which are restricted to U.S. Government use only (for example, U.S.-unique nuclear devices, countermeasures, security devices and aircraft carrier-unique adaptations).

2. The number of units to be produced for DoD shall be obtained from budget backup data. FMS quantity projections and direct commercial sales quantity projections shall be jointly derived as best estimates by the Military Department and DSAA. Defense contractors should be consulted in determining direct commercial sales quantities, if necessary. In the case of disagreement on estimated FMS and direct commercial quantities and sales projections, the Director, DSAA, will make the final determination in coordination with the ASD (Comptroller) and USDR&E.

3. For a weapon system which includes more than one component which meets the MDE threshold or contains a component which has application to several weapons systems or a commercial sale potential, hereinafter referred to as a major individual component, a "building block" approach (i.e., the sum of NC recoupment charges for individual components) shall be used to determine the NC recoupment charge for the sale of the entire system. Data must be accumulated for each major component when NC is identified in accounting records or budget documents and when the component has application to more than one

weapon system or a potential for individual FMS or direct commercial sales. The sum of the various component NC recoupment charges and any remaining NC for the weapon system will be applied to the sale of a complete system. Individual NC recoupment charges shall be applied to sales of individual components. The format for performing the required calculation is at Enclosure 3. DoD Components involved with a sale shall assure that components are not purchased separately for ultimate assembly as an end item in an attempt to circumvent this Directive.

4. The established NC recoupment charge shall be included in the FMS unit price or, for commercial sales, provided to the seller, and paid by the seller to the USG.

5. In the event a commercial item being sold is substantially different (less than 90 percent common) from the USG item for which the NC recoupment charge was developed, the charge shall be assessed based on the extent of commonality with the USG item. For example, if the commercial item is 25 percent common with the DoD item, then only 25 percent of the established NC recoupment charge for the DoD item shall be assessed. The DoD Component office with system engineering responsibility for the item will be responsible for determining the degree of such commonality. The contractors shall be advised in writing of the NC recoupment charge for derived items. A copy of the notification shall be provided to the Director, DSAA.

6. If records necessary to enable a pro rata NC calculation have been lost or destroyed for particular MDE items in which the USG has an NC investment, the DoD Component (Assistant Secretary or higher) shall certify that the records have been lost or destroyed and shall determine a unit NC recoupment charge equal to 4 percent of the most recent USG contract price. The certification of lost or destroyed documents and recommended fixed charge per unit shall be forwarded to the Director, DSAA, for approval. The Director, DSAA shall then establish a fixed unit NC recoupment charge for all subsequent sales.

C. Calculation of Charges on Non-Major Defense Equipment

1. End Items. A percentage NC recoupment charge shall be assessed on non-MDE end items whenever $2 million of RDT&E funded cost has been or is expected to be incurred on the item. The applicable surcharge shall be 5 percent of the item's current FMS selling price exclusive of NC recoupment charges, for items sold under the FMS program or sold commercially by U.S. contractors. The DoD Component shall establish a unit NC recoupment charge for all subsequent sales and the unit charge shall be published in DoD 7290.3-M (reference (d)).

2. Modification Kits.

a. Developed to provide an end item with new or improved capability. An NC percentage charge shall be made whenever $2 million of RDT&E, procurement or operation and maintance funds have been expended on engineering, development, or testing of the kit. The applicable surcharge shall be 5 percent of the modification kit's selling price for kits transferred under the FMS program or sold commercially by U.S. contractors.

b. Developed to improve the safety, reliability, availability, and maintainability. The cost of programs designed to improve the safety, reliability, availability and maintainability for the projected life of the equipment shall be included in the end item/major component NC pools. In the event an FMS customer funds part of the development cost through a Component Improvement Program (CIP) or comparable program, then a pricing exception for an appropriate adjustment of the established NC recoupment charge may be requested by a DoD Component. Modification kits developed to improve safety, reliability, availability and maintainability are issued to FMS customers or incorporated into end items/major components without an additional NC recoupment charge because the applicable development cost is either included in the end item/major component NC recoupment charge or recouped as CIP or comparable program charges on the end item or major component.

3. Components of non-MDE items. A percentage NC recoupment charge shall be made on any non-MDE item component whenever $2 million of RDT&E appropriations has been or is expected to be expended on the component. The applicable charge shall be 5 percent of the component's current FMS selling price for parts transferred under the FMS program or sold commercially by a U.S. contractor.

D. Calculation of Charges for Technology Sales This paragraph establishes procedures for calculation of charges after receipt of authorization to release technology.

1. Technical data packages

a. An NC recoupment charge shall be assessed for the transfer and use of Technical Data Packages (TDPs) to be used to manufacture or produce items for non-U.S. Government use. Charges for the use of TDPs are normally referred to as royalty fees. However, for MDE items, the approved MDE NC recoupment charge shall be assessed for each item manufactured or coproduced in lieu of a royalty fee.

b. For a non-MDE item an NC percentage surcharge shall be applied as the royalty fee on the basis of the item's current FMS selling price. Prescribed charges for non-MDE items are as follows:

(1) Foreign Governments - 5% on items manufactured for in-country use and 8% on items manufactured for third party use by or on behalf of foreign governments or international organizations.

(2) U.S. Contractors - 3% on items manufactured for consumption in the U.S. and 5% on items manufactured for export.

c. The above charges will be deemed to constitute the "fair market price" for U.S. technology.

d. A TDP developed with USG funds shall not be released to any non-USG parties, including contractors, unless the recipient has agreed in writing to pay the applicable charges prescribed by this Directive.

2. Software. A charge shall be made for sales of USG developed software whenever $2 million or more has been, or is expected to be, expended by the DoD Component to develop the software regardless of appropriation account. The charge shall be a pro rata charge. The numerator shall be the cost incurred by the DoD Component. The denominator shall be either the number of weapons systems to be supported by the software package or the number of software packages to be duplicated, as applicable.

3. Other Technology Transfers. For all other technology transfers, including transfers of TDPs for purposes other than manufacturing and all transfers of industrial or manufacturing processes, the amount of the charge will equal the fair market value of the technology involved. For transfers to any U.S. domestic organization this charge will be the lower of either: (1) a proportionate share of the DoD investment cost identified to the development of the technical data/technology involved; or (2) a fair market price for the technology/technical data involved based on demand or the potential monetary return on investment. For transfers to any non-U.S. contractor or other foreign customer, this charge will be the greater of the foregoing two alternatives. Accordingly, the lower domestic price will be applied only if the prospective domestic purchaser signs a written commitment to DoD that the technology/ technical data will not be transferred to any other party.

E. Joint DoD Component Development Effort. DSAA shall designate a lead DoD Component to perform a consolidated calculation when appropriations of more than one DoD Component are involved in the NC investment in an MDE item.

F. "Special" RDT&E and Nonrecurring Production Costs

1. The full amount of "Special" RDT&E and nonrecurring production costs incurred for the benefit of a particular customer(s) shall be paid by that customer(s). However, when a subsequent purchaser requests the same specialized features which resulted from the added special RDT&E and nonrecurring production costs, a pro rata share of these costs may be paid by the subsequent purchaser and transferred to the original customer provided those special nonrecurring costs exceed $5 million. Such reimbursements shall not be transferred to the original customer if eight years have elapsed since acceptance of DD Form 1513 by the original customer. The USG shall not be charged any NC recoupment charge if it adopts the features for its own use or provides equipment containing such features under a U.S. Grant Aid or similar program.

2. For coproduction or codevelopment/cooperative development or cooperative production agreements, the policy set forth in this Directive shall generally determine the allocation basis for recouping from the third party purchasers the investment costs of the participants. Such agreements shall provide for the application of the policies in this Directive to sales to third parties by any of the parties to the agreement and for the distribution of recoupments and technology charges among the parties to the agreement.

G. Reporting NC Recoupment Collections

1. Funds collected for NC recoupment charges shall be disposed of in accordance with DoD 7290.3-M (reference (d)).

2. Components shall maintain records of anticipated and actual NC recoupment charge collections for each FMS case and commercial contract. Commercial contracts may be consolidated and reported under a control number if such a grouping is considered cost effective. A quarterly report on the status of NC collections shall be forwarded to the DSAA Comptroller with a copy to the Director for Accounting Policy, Office of the Deputy Assistant Secretary of Defense (Management Systems), 45 days following the close of each quarter. The report format is at Enclosure 5.

FORMAT FOR MDE CALCULATION
(With Illustrative Entries

Date Prepared

DoD Component

Preparer's Name,
Job Series and Grade

ITEM DESCRIPTION:

Identification No.:

PART A - NONRECURRING R&D INVESTMENT

	R&D Projects			
	X	Y	Z	Total
Major Components				
Air Frame	80,000,000			$80,000,000
Engine (JXX)		58,000,000		58,000,000
Radar			5,000,000	5,000,000
Avionics	1,000,000			1,000,000
Undistributed to Component	20,000,000			20,000,000
Air Vehicle				$164,000,000

PART B - NONRECURRING PRODUCTION INVESTMENT

	AF 1537 Sep 1, 1981	Contract XX	Contract ZZ	Total
Major Components				
Air Frame	5,000,000			$ 5,000,000
Engine (JXX)	7,000,000			7,000,000
Radar	3,000,000			3,000,000
Avionics	5,000,000			5,000,000
Undistributed to Component	10,000,000			10,000,000
Air Vehicle				$30,000,000

PART C - DENOMINATOR

	Source Documents					
	DoD Quantities		MAP/FMS		Commercial Est. by Contracting Officer	Totals
	FYDP Proc. Annex	ADP Project 311	Five Year Security Assistance Plans	ADP Project 311		
Air Frame		1,500		850		2,350
Engine (JXX)		3,050		2,500	2,000	7,550
Radar		2,700		950	100	3,750
Avionics		1,500		850		2,350
Air Vehicle	1,500		750			2,250

PART D - COMPONENT NC

	R&D	Production	Total	Projected Units	Unit NC Recoupment Charge
Major Components					
Air Frame	$80,000,000	$ 5,000,000	$85,000,000	2,350	$36,170 (1)
Engine (JXX)	58,000,000	7,000,000	65,000,000	7,550	8,609 (1)
Radar	5,000,000	3,000,000	8,000,000	3,750	2,133 (2)
Avionics	1,000,000	5,000,000	6,000,000	2,350	2,553 (2)
Undistributed	20,000,000	10,000,000	30,000,000	2,250	13,334 (3)

PART E - SYSTEM NC CHARGE

1. Current Development Costs:

Air Frame (1 each system)	$36,170
Engines (2 each system)	17,218
Radar (1 each system)	2,133
Avionics (1 each system)	2,553
Undistributed (Allocated to end items)	13,334

2. GFM Development Costs:

ISS Cannon (2 each system)	500
HR X Radio (1 each system)	250
XM Bomb Sight (1 each system)	300
Access II Scat (1 each system)	700
TOTAL SYSTEM CHARGE	$73,158 (1)

Notes

(1) Unit NC recoupment charge calculation for MDE item must be submitted to DSAA for review and approval.
(2) Unit NC recoupment charge for non MDE item is added to DoD Component schedule of non-MDE charges and reported to the DASD(MS) for publication in DoD 7290.3-M.
(3) Undistributed systems' NC is recouped on end items.

RECOUPMENT OF NONRECURRING COSTS ON SALES OF MDE ITEMS

DATE PREPARED	DOD COMPONENT
AS OF DATE	NAME AND TELEPHONE NUMBER OF CONTRACT POINT

SECTION A

(a)	(b)			(c)						(d)			(e)
WEAPON SYSTEM OR COMPONENT	NONRECURRING COSTS (IN THOUSANDS)			PRODUCTION QUANTITY						RECOMMENDED PPO RATA UNIT CHARGE			PREVIOUS UNIT CHARGE
	RDT&E	PRODUCTION	TOTAL	ARMY	MARINE/NAVY	AIR FORCE	MAP/FMS/DIRECT SALE		TOTAL	RDT&E/PRODUCTION		TOTAL	

SECTION B

PRODUCTION QUANTITIES

	ACTUAL		PROJECTION		TOTAL
MAP					
DIRECT SALE					
FMS					
TOTALS					

Completion of Section C on Reverse is Required

RECOUPMENT OF NONRECURRING COSTS ON SALES OF USG PRODUCTS AND TECHNOLOGY

Department of the _____ .
($ Thousands)

Report Control Symbol: DSAA(Q)1112
Report Preparation Date _____
Report Cut-Off Date _____

Case Designator (1)	Purchaser	Item	Year of Sale and Amount	Total Anticipated NC Charge (2)(3)	Actual Collections: Amount Collected This Quarter	Actual Collections: Amount Collected This Fiscal Year to Date	Actual Collections: Cumulati Collectio

Part 1 - Cases open at the start of the fiscal year

A. Recoveries on U.S. Government sales to foreign governments and international organizations.
B. Recoveries on direct sales to foreign governments, international organizations and foreign commercial firms.
C. Recoveries on sales to domestic commercial firms.

Part 2 - New cases accepted during the fiscal year.

A. Recoveries on U.S. Government sales to foreign governments and international organizations.
B. Recoveries on direct sales to foreign governments, international organizations and foreign commercial firms.
C. Recoveries on sales to domestic commercial firms.

Notes:

(1) Applicable to U.S. Government sales to foreign governments and international organizations. For direct sales, it will be necessary to establish a "dummy" case number for control purpose.
(2) When collection results from the sales of technology, rather than product, place a (T) after the anticipated charge.
(3) Place an asterisk after charge when collection is completed.

OFFICE OF THE ASSISTANT SECRETARY OF DEFENSE

WASHINGTON, D.C. 20301

COMPTROLLER
(Management Systems)

25 APR 1983

Ms. Judith D. Hendrickson
Deputy Associate Administrator
for Policy Development
Office of Federal Procurement Policy
Office of Management & Budget
Washington, D.C. 20503

Dear Judith,

Your April 18, 1983, letter requested my comments on correspondence you received from VARO concerning DoD policies on the recoupment of nonrecurring R&D costs on commercial sales. The VARO correspondence stated that DoD had promulgated a recoupment policy that:

- is inconsistent with the intent of the Congress of the United States;
- results in a net drain to the U.S. Treasury;
- is adversely affecting the U.S. Balance of Payments;
- is grossly unfair to U.S. contractors who must compete with foreign subsidized contractors;
- cannot be enforced in a cost-effective way;
- is not based on statutory authority.

I do not agree with any of the VARO statements.

Our current recoupment policies are based upon Council On International Economic Policy (CIEP) Decision Memorandum 23, August 2, 1974. The CIEP recommended that recoupment be sought on government-owned and financed technologies and products when they are proposed for sale to non-U.S. Government buyers. This recommendation was approved by the President and, of course, implemented by DoD.

We have testified on this recoupment policy before a Subcommittee of the Committee on Government Operations, House of Representatives, and that Committee recommended (H.R. 97-214) that DoD increase its efforts in the area of recoupment of R&D on commercial sales. Thus, we have direction from both the

President and the Congress to recoup nonrecurring R&D costs on commercial sales.

The legal basis for collection of these costs from contractors is signature of contract containing DAR clause 7-104.64. If a contractor refuses to accept this DAR clause, the issue is raised to top DoD management levels and use of the clause may be waived.

Obviously, if we have competing contractors, and one declines to accept the clause, award is made to a contractor willing to accept the clause. It should be noted that there is provision for a contractor to request waiver of the R&D recoupment charge. Such waivers have been granted when required by a U.S. contractor to compete with a foreign contractor for foreign non-government sales. However, requests for waiver have been denied when the competitor was a U.S. contractor who developed the competing piece of equipment with private monies. We believe this waiver authority adequately assures that U.S. contractors can compete with foreign contractors.

The additional cost to DoD for collection of R&D recoupment charges on commercial sales is minimal. The major cost to DoD results from calculation of the amount due on various items of equipment, and we accomplish this calculation to meet the requirements of the Arms Export Control Act.

In summary, I believe the current R&D recoupment policies are reasonable and in the best interest of the U.S. taxpayer. I appreciate this opportunity to comment on the correspondence you received from VARO.

Sincerely,

Michael J. Melburn

Aerospace Industries Association of America, Inc.

June 1, 1984

OASD (Comptroller)
ATTN: Mr. Michael J. Melburn
Director, Policy Promulgation
Room 3A882, The Pentagon
Department of Defense
Washington, D.C. 20301

SUBJECT: AIA Comments on Proposed Revision to DoD Directive 2140.2 "Recoupment of Non-recurring Costs on Sales of U.S. Products and Technology"

Dear Mr. Melburn:

In furtherance of the industry interest on recoupment shown during our DoD meeting of June 23, 1983 and the subsequent follow-on actions culminating in the opportunity provided during April 1984 to review and provide comments on the proposed DoD Directive 2140.2, our members have completed these review efforts. Their consolidated views divided into "General" and "Specific" sections are provided for your consideration.

General Comments:

It is the consensus of our members that this proposed Directive revision is overreaching in its purpose and scope and is unduly complicated.

It would appear that the thrust of the directive could be accommodated by recoupment on the major equipment or systems sales without application to components, modification kits, technical data packages, etc. Implementation of the requirements set forth in the directive will significantly slow down the proposal cycle and increase administrative time and effort on the part of both government and contractors. It will also tend to create ill will in dealings with foreign government representatives due to inordinate delays which can be occasioned by the increased requirements, and therefore adversely further affect the balance of trade. Moreover, it will make U.S. industry less competitive with those companies which are owned or directly subsidized by foreign governments.

The impact will be principally in increased costs through additional costs passed on directly and indirectly (because of added administrative effort). This result is obvious and reflected in the DoD Directive. The impact at the functional level is unknown, but expected to be small.

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The entire picture is unclear as to how one can adequately judge the amount of future FMS or commercial sales of a product at the first sale to a non-USG customer. If the estimate is low, over recovery is possible (at a higher inequitable cost share to non-DoD customers). Conversely, if the estimate is high (resulting in lower recovery) does the U.S. Government accept this and absorb the difference or will non-USG customers be subsequently assessed?

Another scenerio might be that a product is modified or improved at the expense of a particular non-USG customer. If this improvement is subsequently procured in a product sold to the USG, it would seem logical for the USG to pay the non-USG customer a "royalty" for the USG's share of avoided non-recurring costs.

Finally, if the logic of the control and bookkeeping problems as well as reduced competitive position do not prevail, and it is deemed necessary by the DoD to impose this surtax on foreign customers, it would seem appropriate that since the government must evaluate data supplied by contractors and determine the amount to be assessed and added to the contractor's price, it would be far more efficient, and less burdensome to the contractors if - on FMS cases - the DoD just add these costs to their FMS administrative burden and collect it off the top as they are paid by the FMS customer, rather than have the contractor add it to their price and pay it back to the government. In this way they cut out the middleman and that associated bookkeeping work for the contractor.

The DoD Directive will cut costs and administrative burden if each Military Department of Defense Agency involved will provide timely and efficient implementation of subject Directive with standard procedures. If the systems and procedures for implementation vary among the various agencies, administration of the industry portion will be more costly and time consuming.

Specific Comments

1. Encl. 1 Definitions
   Para. F. Non-recurring Research, Development, Test and Evaluation (RDT&E)
   Para. G. Non-recurring Production Costs
   Encl. 2 Implementing Procedures
   Para. B-1 Calculation of Charges on MDE and Components

   The non-recurring development and production cost of ECP's which are authorized after contract award is shared by USAF and all FMS countries on a per aircraft basis. The projected total cost defined in F. and G. could be interpreted to include these costs which would amount to double bidding on ECP's. However, review of Implementing Procedures Paragraph C.2.b. indicates this is not the intent. Some clarification of definitions F. and G. as related to FMS sharing of ECP development costs after contract award is desirable.

2. Waivers - Para. G. 4 provides that decisions will be reached on waivers within "60 days after receipt of the request." In cases where other nations request waiver of non-recurring cost charges for articles or services included in a direct Commercial sale, U.S. contractors are often under severe time constraints to submit Proposals in time to meet international competition. A processing time of no more than 30 to 45 days would be most helpful.

3. Encl. 2 Implementing Procedures
Para. A.6. General

Contractor Payments of Nonrecurring Cost Charges - Para. A. 6 of Encl. 2 "Implementing Procedures" provides that U.S. contractors will be required to pay the U.S. GOVT. (USG) within 30 days following "the delivery of each item from the contractors facility." Thirty (30) days after the delivery of each item is not considered sufficient time in the light of international billing and payment procedures. A more appropriate payment period would be 30-45 days after the U.S. contractor receives payment from the customer for articles or services delivered.

In addition, referring payment within thirty (30) days of an affected item is not feasible since in the current multinational market contractors do not receive payment in some cases for years.

4. Encl. 2 A.6 General
B.4 Calculation of Charges on MDE and Components

The contractor does not pay recoupments on FMS programs. Recoupments are handled outside the hardware contracts. Direct sale contracts may also require payment of recoupment charges outside the contract if FMS credits are used. Payments would be through a USG/FMS customer LOA for services and recoupments. If recoupment charges are included in a direct sale contract, payment to the USG should be upon or after payment by the direct sale customer to contractor.

5. Consultation with Defense Contractors in Determining Direct Commercial Sales Quantities - In Para. B.2 of Encl. 2 it indicates that "Defense Contractors should be contacted if necessary in determining direct sales quantities." Suggest elimination of the words "if necessary." Contractors should be asked for any inputs they may have in all cases involving direct commercial sales.

6. Encl. 2 Para. C 2b, sentences 1 and 2

"Developed to improve the safety, reliability, and maintainability. The cost of programs designed to improve the safety, reliability, availability and maintainability for the projected life of the equipment shall be included in the end item/major component NC pools. In the event an FMS customer funds part of the development cost through a Component Improvement Program (CIP) or comparable program, then a pricing exception for an appropriate adjustment of the established NC recoupment charge may be requested by a DoD Component."

COMMENT: It will be a common occurrence for purchasers to qualify for an NC adjustment because of their CIP participation. Will DSAA be asked to adjust the NC on an individual country/case basis? It would be more efficient for the DoD components to adjust the NC based on a DSAA approved formula. Will the same rule apply to TCP members? If a country discontinued CIP participation would the NC for the end item have to be adjusted?

7. Encl. 2 Para. D. 1a, Technical Data Packages

COMMENT: Establishing unit prices for commercial sales would be very difficult, since no existing mechanisms are in effect at this time. The entire proposal method of collecting dollars on technical publications in place of royalty fees would be hard to accept by either the multinational customers or the manufacturers required to implement such a procedure. In fact, this method would not be acceptable.

Our aerospace industry recognizes the legal requirement to recover all Government costs associated with Research, Development, Test and Engineering, and the production of defense articles and services that are sold to other customers. We believe that favorable consideration of these industry views and recommended changes to the proposed Directive revison will facilitate its implementation more effectively. Thank you for providing this opportunity. Should there be a need for any clarification, our members will be happy to comply.

Very truly yours,

John W. Stahl Jr.

John W. Stahl, Jr.
Director, Product Support
AEROSPACE OPERATIONS SERVICE

an extension of the comment period would be provided.

In response to the proposal, Beecham Laboratories requested that an informal conference be held on the proposal. In the Federal Register of March 6, 1984 (49 FR 8260), FDA issued a notice of informal conference and extension of comment period. The notice announced that an informal conference would be held on April 2, 1984, and extended the period for submission of written comments to May 2, 1984.

On April 17, 1984, FDA received from Beecham Laboratories a request for a 30-day extension of the comment period. Beecham states that it is now compiling the data and information requested by the agency at the informal conference but will be unable to complete a comprehensive and detailed response in the comment period specified in the notice.

Beecham also stated that the delay in the availability of the written transcript of the informal conference has decreased the time for a sufficient review of information presented at the informal conference and to prepare and submit written comments.

FDA has carefully considered the request. The agency has determined that additional time for the preparation and submission of meaningful information and data is in the public interest. Accordingly, the comment period for submissions by any interested person is extended to June 1, 1984.

Interested persons may, on or before June 1, 1984, submit to the Dockets Management Branch (address above) written comments regarding this proposal. Two copies of any comments are to be submitted, except that individuals may submit one copy. Comments are to be identified with the docket number found in brackets in the heading of this document. Received comments may be seen in the office above between 9 a.m. and 4 p.m., Monday through Friday.

Dated: April 25, 1984.

Sammie R. Young,

Deputy Director, Office of Compliance.

[FR Doc. 84-11631 Filed 4-26-84; 10:46 am]

BILLING CODE 4160-01-M

DEPARTMENT OF DEFENSE

Office of the Secretary

32 CFR Part 221

[DoD Directive 2140.2]

Recoupment of Nonrecurring Costs on Sales of U.S. Products and Technology

AGENCY: Office of the Secretary, DoD.

ACTION: Proposed rule.

SUMMARY: This proposed rule will incorporate recommendations made in a Committee on Government Operations Report, H.R. No. 97-241. This proposed rule provides specific guidance to all Heads of DoD Components on the recoupment of nonrecurring costs when products or technology developed with appropriated funds are sold commercially or through the Foreign Military Sales program. Recoupment charges will be made whenever the Department of Defense has incurred $2 million or more of nonrecurring costs in developing an item or technology, unless a written waiver has been obtained from appropriate DoD officials. The rule contains necessary instructions for preparation and submission of waiver requests.

DATE: Written comments must be received by May 9, 1984.

ADDRESS: Office of the Assistant Secretary of Defense, (Comptroller), ATTN: Director for Policy Promulgation, The Pentagon, Room 3A882, Washington, DC 20301.

FOR FURTHER INFORMATION CONTACT: Mr. Michael Melburn, 202-697-3135.

SUPPLEMENTARY INFORMATION: DoD procurement activities develop contractual language to implement the nonrecurring cost recoupment policies that are incorporated into acquisition regulations, which are also published in the Federal Register for public comment. The term, "acquisition regulation," refers to the Defense Acquisition Regulation, the Federal Acquisition Regulation (FAR), and the DoD FAR Supplement.

Executive Order 12291

The Department of Defense has determined that this proposed rule is not a major rule, because it is not likely to result in an annual effect on the economy of $100 million or more.

Paperwork Reduction Act

This rule imposes no obligatory information requirements beyond internal DoD use.

Regulatory Flexibility Act of 1980

The Assistant Secretary of Defense (Comptroller) certifies that this rule, if promulgated, shall be exempt from the requirements under 5 U.S.C. 601-612. In addition, this rule does not have a significant economic impact on small entities as defined in the Act.

List of Subjects in 32 CFR Part 221

Foreign military sales, Foreign trade, Armed forces.

Accordingly, it is proposed that 32 CFR be amended by adding a new Part 221, reading as follows:

PART 221—RECOUPMENT OF NONRECURRING COSTS ON SALES OF U.S. PRODUCTS AND TECHNOLOGY

Sec.

221.1 Purpose.
221.2 Applicability and Scope.
221.3 Definitions.
221.4 Policy.
221.5 Responsibilities.
221.6 Procedures.
221.7 Waivers (Including Reductions).
221.8 Information Requirements.

Authority: Title 10, United States Code.

§ 221.1 Purpose.

This proposed rule establishes policy to conform with the Arms Export Control Act as amended, and the Council on Interntional Economic Policy Decision Memorandum No. 23 for calculating and assessing nonrecurring cost (NC) recoupment charges on sales of defense articles or technology to non-U.S. government customers; and assigns responsibilities, and prescribes procedures.

§ 221.2 Applicability and scope.

(a) This rule applies to the Office of the Securetary of Defense, the Military Departments, the Organization of the Joint Chiefs of Staff, the Unified and Specified Commands, and the Defense Agencies (hereafter referred to collectively as "DoD Components").

(b) Its provisions shall be applied contractually to corporations and private parties who sell defense articles or technology developed with DoD appropriations or funds (and in special cases, customer funds) or use such technology to manufacture items sold commercially to a foreign government, international organization, foreign commercial firm, or domestic organization.

§ 221.3 Definitions.

(a) *Major Defense Equipment.* Any item of equipment on the United States Munitions List having a nonrecurring RDT&E cost of more than $50 million or a total production cost of more than $200 million.

(b) *Government Sale.* A sale of articles or services, or both, to customers by and DoD Component under authority of appropriate legislative acts.

(c) *Direct Sale.* A commercial sale to a customer by a defense contractor of products, technology, material, services, or development or production techniques that were originally

developed, improved, or produced using DoD appropriations or funds.

(d) *Domestic Organization.* Any U.S. nongovernmental organization or private commercial firm.

(e) *Technology.* Information of any kind that can be used or adapted for use in the design, production, manufacture, utilization or reconstruction of articles or materiel. The data may take a tangible form, such as a scale model, prototype, blueprint or an operating manual, or may take an intangible form, such as technical advice.

(f) *Nonrecurring Research, Development, Test and Evaluation (RDT&E) costs.* Those costs funded by an RDT&E appropriation to develop or improve the product or technology under consideration either through contract or in-house effort. This includes costs of any engineering change proposal initiated before the date of the contract with the customer as well as projections of such costs to the extent additional effort applicable to the sale model or technology is necessary or planned. It *does not* include costs funded by either procurement or operations and maintenance appropriations.

(g) *Nonrecurring Production Costs.* Those one-time costs incurred in support or previous production of the model specified and those costs specifically incurred in support of the total projected production run. These nonrecurring costs include DoD expenditures for preproduction engineering, rate and special tooling, special test equipment, production engineering, product improvement, destructive testing, and pilot model production, testing and evaluation. Non-recurring production costs do not include DoD expenditures for machine tools, capital equipment or facilities for which contractor rental payments are made in accordance with the DAR or asset use charges assessed in accordance with DoD 7290.3–M.

(h) *"Special" RDT&E and Nonrecurring Production Costs.* Those costs incurred at the request of, or for the benefit of, the customer in developing a special feature or unique requirement. These costs must be paid by the customer as they are incurred.

(i) *Pro Rata Recovery of Nonrecurring Costs.* Distribution (proration) of a pool to a specific number of units that benefit from the investment so that a DoD Component will collect from a customer a fair (prorata) share of the investment in the product being sold.

(j) *A Cost Pool.* Represents the total cost to be distributed across the specific number of units. The nonrecurring RDT&E cost pool comprises the costs described in § 221.3(f). The nonrecurring production cost pool comprises costs described in § 221.3(g).

(k) *Foreign Military Sale (FMS).* A sale of defense articles or defense services to a foreign government or international organization under authority of the Arms Export Control Act.

(l) *Model.* A basic alpha-numeric designation within a weapon system series, such as a ship hull series, an equipment or system series, an airframe series, or a vehicle series. For example, the F5A and the F5F are different models within the same F–5 system series.

(m) *Non-U.S. Contractor.* A non-U.S. citizen or an organization which is not incorporated in the U.S.

§ 221.4 Policy.

Non-U.S. Government purchasers shall pay a fair price, determined in accordance with this rule, for the values of the DoD nonrecurring investment in the development and production of defense articles and development of technology unless an NC recoupment charge waiver has been approved by the DoD official designated in § 221.7. Approved revised NC recoupment charges may not be applied retroactively to accepted FMS agreements or to direct sales that were entered into before the date of approval of the revised NC recoupment charge.

§ 221.5 Responsibilities.

(a) The *Under Secretary of Defense for Research and Engineering* (USDR&E) shall monitor and exercise control over NC recoupment aspect of domestic commercial sales of defense articles and technology and shall take appropriate action to revise the Defense Acquisition Regulation (DAR) to agree with this Rule.

(b) The *Under Secretary of Defense for Policy* shall monitor the application of this Directive and exercise control over foreign sales of DoD-developed articles and technology.

(c) The *Assistant Secretary of Defense (Comptroller)* shall provide necessary cost accounting guidance and publish a listing of the items or technology to which NC recoupment charges are applicable.

(d) The *Director, Defense Security Assistance Agency (DSAA),* shall serve as the DoD focal point for review and approval of NC recoupment charges for major defense equipment (MDE) items and for processing NC recoupment charge waiver requests received from foreign countries and international organizations for foreign military sales (FMS) or direct commercial sales. Approved NC recoupment charges for MDE items shall be provided to the Deputy Assistant Secretary of Defense (Management Systems) (DASD(MS)) for publication.

(e) Heads of *Military Departments and Defense Agencies* shall determine the DoD nonrecurring investment in defense articles or technology and perform required pro rata calculations in accordance with cost accounting guidance from the ASD(C); provide recommended charges for MDE items to DSAA; determine the appropriate charges for non-MDE articles and technology; provide the approved non-MDE item and technology charges to the DASD(MS) for publication and submit quarterly reports of anticipated and actual NC recoupment charge collections to DSAA.

§ 221.6 Procedures.

(a) *General.* (1) Each DoD Component and defense contractor negotiating the sale of products or technology developed with DoD appropriations or funds shall ensure the assessment of the charges as set forth in this paragraph.

(2) Each DoD Component shall calculate a NC recoupment charge for items or technology releasable to foreign countries and international organizations when FMS or direct commercial sales are anticipated. The NC recoupment charge shall be based upon information recorded in DoD accounting records or DoD budget justification documents. Engineering cost estimates may be used to determine NC expected to be incurred in periods not covered by budget justification documents.

(3) The NC recoupment charge computation (nonrecurring RDT&E and production) for the sale of MDE items shall be submitted to the Director, DSAA, for approval of the amount to be applied to pending FMS or direct sales. A summary report on each MDE item shall be provided to DSAA. The Director, DSAA, shall review each DoD Component's calculations and provide approved NC recoupment charges for MDE items to the DoD Component. A copy of all approvals shall be provided to the DASD(MS) for publishing in DoD 7290.3–M.

(4) Once the approved charge has been used in an authorized sale, the charge normally will not be revised until a model change occurs. However, each DoD Component annually shall review approved MDE charges to determine if there have been significant changes in factors or assumptions used to compute the original NC recoupment charge established for a model (for example, significant changes in identifiable

RDT&E costs or the anticipated production run). A significant change occurs when a new calculation shows a change of more than 30 percent of the current system NC recoupment charge for an MDE item or the potential for an additional NC recoupment charge collection of over $100,000 exists. When significant changes are identified for MDE, the DoD Component shall submit a request to the Director, DSAA, for authority to make appropriate changes in NC recoupment charges. The Director, DSAA, shall respond to the request in writing within 60 days after receipt of the request.

(5) When a defense contractor negotiates the direct sale of a defense article or technology, or a derivative of a USG developed item, he shall request the amount of the NC recoupment charge from the administrative contracting officer (ACO) or (for technology sales) the technology charge from the DoD Component responsible for DoD acquisition of the article. When making this request, the contractor shall submit such information as may be necessary to comply with this rule. If the NC recoupment charge has not already been established as provided for under this rule, the ACO shall contact the DoD Component activity responsible for establishment of the charge and advise the contractor of the estimated date the amount of the charge will be made available.

(6) All DoD contracts for RDT&E or acquisitions shall include a mandatory clause that requires the contractor to pay the USG, within 30 days following delivery of each item from the contractor's facility, the established NC recoupment charge for any domestic or international direct sale, corporation, or licensed production of defense articles or technology (see DAR 7-104.64).

(7) The cognizant DoD Component shall deposit collections in payment of an NC recoupment charge without delay in the nearest federal reserve bank to accounts prescribed in DoD 7290.3-M. Notification of the deposit shall be provided to the DoD Component activity responsbile for submission of reports required in § 221.6(g)(2).

(b) *Calculation of Charges on MDE and Components.*—MDE items are defined in § 221.3(a). The determination of whether an item meets the MDE dollar threshold shall be based on obligations recorded to the date the equipment is offered for sale. Production costs shall include cost incurred for DoD, FMS, and known direct sales production. For the FMS program, the sales offer date shall be the date a Letter of Offer and Acceptance (LOA) is signed by a U.S. official and released to the FMS customer; for commercial sales, the sales offer date shall be the date of contract signature.

(1) NC recoupment charges shall be assessed on a pro rata basis. The charges shall be established by dividing the total of NC investment (nonrecurring RDT&E + nonrecurring production) incurred to date plus projections of future costs to be incurrred, by the total estimated number of units projected to be produced over the life of the system (including DoD requirements, Military Assistance Program (MAP) requirements, FMS requirements, and direct commercial sales requirements). The computation of the cost pool shall exclude costs for those items which are restricted to U.S. Government use only (for example, U.S.-unique nuclear devices, countermeasures, security devices and aircraft carrier-unique adaptations).

(2) The number of units to be produced for the Department of Defense shall be obtained from budget backup data. FMS quantity projections and direct commercial sales quantity projections shall be derived jointly as best estimates by the Military Department and DSAA. Defense contractors shall be consulted in determining direct commercial sales quantities, if necessary. In the case of disagreement on estimated FMS and direct commercial quantities and sales projections, the Director, DSAA, will make the final determination in coordination with the ASD(C) and the USDR&E.

(3) For a weapon system that includes more than one component which meets the MDE threshold or contains a component that has application to several weapons systems or a commercial sale potential (hereafter referred to as a major individual component), a "building block" approach (that is, the sum of NC recoupment charges for individual components) shall be used to determine the NC recoupment charge for the sale of the entire system. Data must be accumulated for each major component when NC is identified in accounting records or budget documents *and* when the component has application to more than one weapon system or a potential for individual FMS or direct commercial sales. The sum of the various component NC recoupment charges and any remaining NC for the weapon system shall be applied to the sale of a complete system. Individual NC recoupment charges shall be applied to sales of individual components. DoD Components involved with a sale shall ensure that components are not purchased separately for ultimate assembly as an end item in an attempt to circumvent this rule.

(4) The established NC recoupment charge shall be included in the FMS unit price or, for commercial sales, provided to the seller, and paid by the seller to the USG.

(5) If a commercial item being sold is substantially different (less than 90 percent common) from the USG item for which the NC recoupment charge was developed, the charge shall be assessed based on the extent of commonality with the USG item. For example, if the commercial item is 25 percent common with the DoD item, only 25 percent of the established NC recoupment charge for the DoD item shall be assessed. The DoD Component office with system engineering responsibility for the item shall be responsible for determining the degree of such commonality. The contractors shall be advised in writing of the NC recoupment charge for derived items. A copy of the notification shall be provided to the Director, DSAA.

(6) If records necessary to enable a pro rata NC calculation have been lost or destroyed for particular MDE items in which the USG has an NC investment, the head of the DoD Component concerned, or designee at the level of Assistant Secretary or higher, shall certify that the records have been lost or destroyed and shall determine a unit NC recoupment charge equal to 4 percent of the most recent USG contract price. The certification of lost or destroyed documents and recommend fixed charge per unit shall be forwarded to the Director, DSAA, for approval. The Director, DSAA, then shall establish a fixed unit NC recoupement charge for all subsequent sales.

(c) *Calculation of Charges on Nonmajor Defense Equipment*—(1) *End Items.* A percentage NC recoupment charge shall be assessed on non-MDE end items whenever $2 million of RDT&E funded cost has been or is expected to be incurred on the item. The applicable surcharge shall be 5 percent of the item's current FMS selling price exclusive of NC recoupment charges for items sold under the FMS program or sold commercially by U.S. contractors. The DoD Components shall establish a unit NC recoupment charge for all subsequent sales and the unit charge shall be published in DoD 7290.3-M.

(2) *Modification Kits*—(i) *Developed to provide an end item with new or improved capability.* An NC percentage charge shall be made whenever $2 million of RDT&E, procurement or operation and maintenance funds have been expended on engineering, development, or testing of the kit. The

applicable surcharge shall be 5 percent of the modification kit's selling price for kits transferred under the FMS program or sold commercially by U.S. contractors.

(ii) *Developed to improve the safety, reliability, availability, and maintainability.* The cost of programs designed to improve the safety, reliability, availability and maintainability for the projected life of the equipment shall be included in the end item/major component NC pools. If an FMS customer funds part of the development cost through a Component Improvement Program (CIP) or comparable program, a pricing exception for an appropriate adjustment of the established NC recoupment charge may be requested by a DoD Component. Modification kits developed to improve safety, reliability, availability, and maintainability are issued to FMS customers or incorporated into end items/major components without an additional NC recoupment charge because the applicable development cost is either included in the end item/major component NC recoupment charge or recouped as CIP or comparable program charges in the end item or major component.

(3) *Components of non-MDE items.* A percentage NC recoupment charge shall be made on any non-MDE item component whenever $2 million of RDT&E appropriations has been or is expected to be expended on the component. The applicable charge shall be 5 percent of the component's current FMS selling price for parts transferred under the FMS program or sold commercially by a U.S. contractor.

(d) *Calculation of Charges for Technology Sales.* This paragraph establishes procedures for calculation of charges after receipt of authorization to release technology.

(1) *Technical data packages.* (i) An NC recoupment charge shall be assessed for the transfer and use of Technical Data Packages (TDPs) to be used to manufacture or produce items for non-U.S. Government use. Charges for the use of TDPs normally are referred to as royalty fees. However, for MDE items, the approved MDE NC recoupment charge shall be assessed for each item manufactured or coproduced instead of a royalty fee.

(ii) For a non-MDE item an NC percentage surcharge shall be applied as the royalty fee on the basis of the item's current FMS selling price. Prescribed charges for non-MDE items are as follows:

(A) Foreign Governments. Five percent on items manufactured for in-country use and eight percent on items manufactured for third party use by or on behalf of foreign governments or international organizations.

(B) U.S. Contractors. Three percent on items manufactured for consumption in the U.S. and five percent on items manufactured for export.

(iii) The above charges will be considered to constitute the "fair market price" for U.S. technology.

(iv) A TDP developed with USG funds may not be released to any non-USG parties, including contractors, unless the recipient has agreed in writing to pay the applicable charges prescribed by this rule.

(2) *Software.* A charge shall be made for sales of USG-developed software whenever $2 million or more has been, or is expected to be, expended by the DoD Component to develop the software, regardless of appropriation account. The charge shall be a pro rata charge. The numerator shall be the cost incurred by the DoD Component. The denominator shall be either the number of weapons systems to be supported by the software package or the number of software packages to be duplicated, as applicable.

(3) *Other Technology Transfers.* For all other technology transfers, including transfers of TDPs for purposes other than manufacturing and all transfers of industrial or manufacturing processes, the amount of the charge shall equal the fair market value of the technology involved. For transfers to any U.S. domestic organization this charge shall be the lower of either: (i) a proportionate share of the DoD investment cost identified to the development of the technical data or technology involved; or (ii) a fair market price for the technology or technical data involved based on demand or the potential monetary return on investment. For transfers to any non-U.S. contractor or other foreign customer, this charge will be the greater of the foregoing two alternatives. Accordingly, the lower domestic price shall be applied only if the prospective domestic purchaser signs a written commitment to the Department of Defense that the technology or technical data will not be transferred to any other party.

(e) *Joint DoD Component Development Effort.* DSAA shall designate a lead DoD Component to perform a consolidated calculation when appropriations of more than one DoD Component are involved in the NC investment in an MDE item.

(f) *"Special" RDT&E and Nonrecurring Production Costs.* (1) The full amount of "special" RDT&E and nonrecurring production costs incurred for the benefit of a particular customer or customers shall be paid by that customer or customers. However, when a later purchaser requests the same specialized features which resulted from the added special RDT&E and nonrecurring production costs, a pro rata share of these costs may be paid by the later purchaser and transferred to the original customer, provided those special nonrecurring costs exceed $5 million. Such reimbursements shall not be transferred to the original customer if 8 years have elapsed since acceptance of DD Form 1513 by the original customer. The USG shall not be charged any NC recoupment charge if it adopts the features for its own use or provides equipment containing such features under a U.S. Grant Aid or similar program.

(2) For coproduction or codevelopment/cooperative development or cooperative production agreements, the policy set forth in this rule generally shall determine the allocation basis for recouping from the third party purchasers the investment costs of the participants. Such agreements shall provide for the application of the policies in this rule to sales to third parties by any of the parties to the agreement and for the distribution of recoupments and technology charges among the parties to the agreement.

(g) *Reporting NC Recoupment Collections.* (1) Funds collected for NC recoupment charges shall be disposed of in accordance with DoD 7290.3–M.

(2) Components shall maintain records of anticipated and actual NC recoupment charge collections for each FMS case and commercial contract. Commercial contracts may be consolidated and reported under a control number if such a grouping is considered cost effective. A quarterly report on the status of NC collections shall be forwarded to the DSAA Comptroller with a copy to the Director for Accounting Policy, Office of the Deputy Assistant Secretary of Defense (Management Systems) Office of the ASD(C), 45 days following the close of each quarter.

§ 221.7 Waivers (Including Reductions).

(a) The Arms Export Control Act requires the recoupment of NCs of MDE from FMS customers but authorizes consideration of waivers for particular sales that, if made, significantly advance U.S. Government (USG) interests in the North Atlantic Treaty Organization, Japan, or Australia. Waiver for non-MDE items under FMS and for direct

commercial sales shall be based upon the same considerations.

(b) Requests for waivers of NC recoupment charges for sales of defense articles under the FMS program or on direct commercial sales to foreign governments and international organizations shall be submitted to the Director, DSAA. Requests shall originate with the foreign government and shall provide information regarding the extent of standardization to be derived as a result of the waiver and other benefits which would accrue to the USG as a result of the sale. The request shall contain a summary statement of the facts regarding the program, benefits expected and justification therefor, and any calculations necessary to determine that the waiver has resulted in a reduction of contract price. Blanket waiver requests may not be submitted nor considered. The term "blank waiver" refers to an NC recoupment charge waiver for all sales to a particular country or all sales of a weapon system. A waiver request may not be approved for a sale that was accepted without an NC recoupment charge waiver, unless the waiver was pending at the time of acceptance. A waiver may not be granted in connection with a direct commercial sale if such a waver could not have been legally granted in connection with a sale made under the FMS program.

(c) Requests for waivers of NC recoupment charges for domestic sales of defense articles shall be submitted by the contractor to the USDR&E. The request shall provide information regarding the dollar value of the waiver, benefit to be derived by the Department of Defense, the names of foreign and domestic competitors, impact on the USG balance of payments, demonstrable rights of the manufacturer or purchaser, and any other justification for the waiver.

(d) Requests for waivers shall be processed expeditiously, and a decision made by the approving authority (see § 221.7(f)) either to approve or disapprove the request within 60 days after receipt. A waiver in whole or in part of the recoupment charge shall be provided in writing to the DoD Component concerned before issuance of the FMS agreement or signing of the direct sale commercial contract.

(e) The approving authority shall request the concurrence of the Director, DSAA; the ASD(C); and the USDR&E, as appropriate, in his or her decision. If an issue concerning the waiver request cannot be resolved, the approving authority shall refer the waiver request to the Deputy Secretary of Defense for final determination. The action memorandum to the Deputy Secretary of Defense shall be coordinated with the Director, DSAA, the ASD(C) and the USDR&E, as appropriate.

(f) The Director, DSAA, is the approving authority and shall state in writing any approvals granted for waivers associated with FMS and direct foreign sales. The USDR&E is the approving authority and shall state in writing any approvals granted for waivers involving sales of defense articles or technology to domestic organizations. This authority shall not be redelegated. A copy of each approved waiver shall be forwarded to the ASD(C) and to the concerned DoD Components by the approving authority.

(g) This rule does not apply to sales of excess property when accountability has been transferred to property disposal activities and the property is sold in open competition to the highest bidder.

§ 221.8 Information requirements.

The recordkeeping and reporting requirements prescribed in § 221.6(g)(2) are assigned Report Control Symbol DSAA(Q)1112.

M. S. Healy,

OSD Federal Register Liaison Officer, Department of Defense.

April 26, 1984.

[FR Doc. 84-11353 Filed 4-30-84; 8:45 am]

BILLING CODE 3810-01-M

SELECTIVE SERVICE SYSTEM

32 CFR Part 1699

Enforcement of Nondiscrimination on the Basis of Handicap in Selective Service System Programs

AGENCY: Selective Service System.

ACTION: Notice of proposed rulemaking.

SUMMARY: This proposed regulation provides for the enforcement of Section 504 of the Rehabilitation Act of 1973, as amended, which prohibits discrimination on the basis of handicap, as it applies to programs or activities conducted by the Selective Service System.

DATES: To be assured of consideration, comments must be in writing and must be received on or before August 28, 1984. Comments should refer to specific sections in the regulation.

ADDRESSES: Comments should be sent to: Henry N. Williams, General Counsel, Selective Service System, Washington, D.C. 20435.

Comments received will be available for public inspection in Office of the General Counsel, Selective Service System, 1023 31st Street, NW., Washington, D.C. 20435. Copies of this notice are available on tape for those with impaired vision. They may be obtained at the above address.

FOR FURTHER INFORMATION CONTACT: Henry N. Williams, General Counsel, Selective Service System, Washington, D.C. 20435. Phone 202-724-1167. TDD Phone 202-724-0408.

SUPPLEMENTARY INFORMATION:

Background

The purpose of this proposed rule is to provide for the enforcement of section 504 of the Rehabilitation Act of 1973, as amended (29 U.S.C. 794), as it applies to programs and activities conducted by the Selective Service System. As amended by the Rehabilitation, Comprehensive Services, and Developmental Disabilities Amendments of 1978 (Sec. 119, Pub. L. 95-602, 92 Stat. 2982), section 504 of the Rehabilitation Act of 1973 states that:

> No otherwise qualified handicapped individual in the United States, . . . shall, solely by reason of his handicap, be excluded from the participation in, be denied the benefits of, or be subjected to discrimination under any program or activity receiving Federal financial assistance *or under any program or activity conducted by any Executive agency or by the United States Postal Service. The head of each such agency shall promulgate such regulations as may be necessary to carry out the amendments to this section made by the Rehabilitation, Comprehensive Services, and Developmental Disabilities Act of 1978. Copies of any proposed regulation shall be submitted to appropriate authorizing committees of the Congress, and such regulation may take effect no earlier than the thirtieth day after the date on which such regulation is so submitted to such committees.*
>
> (29 U.S.C. 794) (amendment italicized).

The substantive nondiscrimination obligations of the agency, as set forth in this proposed rule, are identical, for the most part, to those established by Federal regulations for programs or activities receiving Federal financial assistance. *See* 28 CFR Part 41 (section 504 coordination regulation for federally assisted programs). This general parallelism is in accord with the intent expressed by supporters of the 1978 amendment in floor debate, including its sponsor, Rep. James M. Jeffords, that the Federal Government should have the same section 504 obligations as recipients of Federal financial assistance. 124 Cong. Rec. 13,901 (1978) (remarks of Rep. Jeffords); 124 Cong. Rec. E2668, E2670 (daily ed. May 17, 1978) *id.*; Cong. Rec. 13,897 (remarks of Rep. Brademas); *id.* at 38,552 (remarks of Rep. Sarasin).

General Comments

AMERICAN ELECTRONIC ASSOCIATION

GOVERNMENT PROCUREMENT COMMITTEE

POSITION PAPER

ON

DEPARTMENT OF DEFENSE RECOUPMENT POLICY

DEPARTMENT OF DEFENSE RECOUPMENT POLICY

EXECUTIVE SUMMARY

The Department of Defense has promulgated a recoupment policy that

- is inconsistent with the intent of the Congress of the United States;
- results in a net drain to the U. S. Treasury;
- is adversely affecting the U. S. Balance of Payments;
- is grossly unfair to U. S. contractors who must compete with foreign subsidized contractors;
- cannot be enforced in a cost effective way; and
- is not based on statutory authority.

It is recommended that the DoD rescind its present regulations (DAR 1-2400, 4-110 and 7-104.64) and levy recoupment charges only as required by law, as specified in the Arms Export Control Act of 1976. This recoupment would apply only to "major defense equipment" on government-to-government sales.

This document includes a discussion of the present policy, legislative history, validity of the regulation, and other considerations which completely justify the recommendation that the present DoD regulation be rescinded.

RECOUPMENT

Recoupment is the recovery by the United States of certain nonrecurring costs on sales of defense equipment, components and related technology developed with federal appropriations. The objective, according to Defense Department procurement regulations (DAR 1-2400), "is to ensure that a customer pays a fair share of the nonrecurring investment cost incurred by the Department of Defense."

AUTHORIZATION

The recoupment of nonrecurring costs on certain sales of defense equipment is authorized by the Arms Export Control Act of 1976, PL 94-329. This Act established in 22 U.S.C. Section 2761(e)(1) that "letters of offer for the sale of defense articles or for the sale of defense services...shall include charges for...(C) a proportionate amount of any nonrecurring costs of research, development, and production of major defense equipment..." (emphasis added).

It is important to understand the application of recoupment by the Arms Export Control Act both from a legal and policy perspective. Legally, 22 U. S. C. Section 2761(e)(1) specifically deals with certain charges associated with "the sale of defense articles or for the sale of defense services." "Defense articles and defense services", with respect to commercial exports, are defined by the Act as items placed on the U. S. Munitions List by the President to provide "foreign policy guidance to persons of the United States involved in the export and import of such articles and services." 22 U. S. C. Section 2778(a)(1). In other words, one of the primary purposes for enactment of the Arms Export Control Act by Congress was to increase the exercise of its oversight powers with respect to the rapidly growing arms sales program. H.R. Rep. No. 1144, 94th Cong. 2 Sess. 12, Reprinted in (1976) U. S. Code & Ad. News 1378, 1388.

Section 22 U. S. C. Section 2761(e)(1)(A), (B), and (D) all specifically call for "appropriate charges" for various costs associated with "such articles and services"; "such defense articles"; and "such articles", respectively. However, the subsection dealing with recoupment specifically singles out nonrecurring costs associated with "major defense equipment."

"Major defense equipment" is defined as "any item of significant combat equipment on the United States Munitions List having a nonrecurring research and development cost of more than $50,000,000 or a total production cost of more than $200,000,000." 22 U. S. C. Section 2794(6). It is clear, therefore, that Congress intended to apply recoupment charges only to sales of major defense equipment.

The Act further restricts the sale of major defense equipment to government-to-government transactions. P. L. 94-329. Thus, the Act makes clear distinctions between "defense articles and services," sold commercially and subject to the Act's provisions, and "major defense equipment", sold only in government-to-government transactions.

DEPARTMENT OF DEFENSE IMPLEMENTATION OF RECOUPMENT

According to Defense Department procurement regulations, (DAR Section 1-2401 (a)), "it is the policy of the Department of Defense to recover a fair share of its investment in nonrecurring costs related to products...when the products are sold, and when technology relating to the manufacture of the products is sold or licensed, to a foreign government, international organization, foreign commercial firm, or domestic organization."

This policy is applied by DoD to "those products and technologies for which investment costs equal or exceed $5 million...". DAR Section 1-2402(a). All RDT&E and production contracts of $1 million or more are required to include a defense acquisition clause titled "Recovery of Nonrecurring Costs on Commercial Sales of Defense Products and Technology". (DAR 7-104.64). This clause requires that "in the event the Contractor intends to enter into domestic or foreign commercial sales for items in [the] contract, or essentially similar items...to obtain the applicable nonrecurring recoupment charge" from the contracting officer (emphasis added).

Applying its recoupment policy even further to commercial sales, the Defense Department's regulation states that "[i]n a combination FMS [foreign military sale] and commercial sale of a product, the Contractor agrees to reimburse the Government for the nonrecurring costs associated with the commercial portion of the customer's purchase". DAR 7-104.64(b)(3).

The DoD's original recoupment regulations were cited as being authorized by the Armed Services Procurement Act. 10 U. S. C. Sections 2301-2314 (1956). However, a careful review of these sections reveal that no reference is made to "recoupment" policy. Furthermore, there is nothing in the legislative history of this general procurement statute to indicate that Congress intended this authority. Additionally, whatever authority had been implied in the procurement statute may also have been restricted or limited by the specific treatment in the Arms Export Control Act.

Later, in adopting the present regulations on recoupment of nonrecurring research and development costs, DoD cited the Arms Export Control Act as authority. DoD Directive 2140.2 (January 5, 1977). Although this Act authorizes recoupment of government-to-government sales of major defense equipment, it clearly does not authorize the broader coverage of the regulations (i.e., application to direct domestic and foreign commercial sales and to sales of "non-major" defense equipment).

Thus, it is clear that the Department of Defense applies recoupment charges to situations specifically precluded in the Arms Export Control Act. While the Act limits the application of recoupment charges to the sale of "major defense equipment", which can be sold only in a government-to-government transaction, the Pentagon requires recoupment on both government-to-government and commercial contracts in which government investment equals or exceeds $5 million. Therefore, those DAR regulations that fall outside the scope of the Arms Export Control Act or contradict its letter or purpose, are invalid.

EFFECTS OF DOD'S RECOUPMENT POLICY

There are other serious policy issues related to the government recouping nonrecurring costs from the commercial sales of government contractors to foreign and domestic customers.

Government expenditures for Research and Development are in the nation's best interest and help to promote both domestic and international competition, to advance technology and to foster economic growth. The imposition of broad recoupment regulations act as a disincentive for performing organizations in undertaking Federal R&D because it reduces

the opportunity for commercial gains. Potential performers are already burdened with start-up, production and marketing costs. Additional requirements for recoupment of R&D costs would only further discourage their involvement.

Foreign concerns and governments now seek to become less dependent on the United States for commercial and military products and to also gain a significant share of the U.S. market. In some instances, they are outbidding U. S. concerns, particularly with conditions for favorable financing. As a result, the U. S. business industry faces the prospect of a significantly smaller share of the world market.

The United States can no longer be complacent about presumed technical superiority in the international competition for markets. The impact of this situation is apparent in the high technology industries in the United States, such as electronics and computers, which are faced with increased competition from foreign countries, many of which benefit from support and stimulation of their own governments.

The sale of any product or technology by our American companies helps to bring about a natural public benefit in this country. An economic benefit to the public is derived from the taxes which are attached to a sale.' Another benefit to the public is derived from the exposure to and use of advanced technology. According to proposed policy issued by the Office of Federal Procurement policy, recoupment should not be sought when to do so would result in conflict with important "public considerations..." 45 Fed. Reg. 86954 (December 31, 1980). Moreover, the Commission on Government Procurement found after careful study that the government's efforts to levy and collect nonrecurring development costs were decidedly not cost effective. 2 Report of the Commission on Government Procurement 29 (December, 1972).

The Department of Defense imposes recoupment charges on all its contractors, not just those who actually perform government R&D work. For example, following an R&D activity, DoD generally procures follow-on production activity on a competitive basis from the drawings and specifications developed in the R&D activity. These production contracts are frequently, if not generally, won by contractors who had nothing to do with the development effort or the prototype production. It cannot be said that these contractors were subsidized by the R&D expenditures because they did not participate in

them. In fact, they more than likely had to invest their own money in tooling and start-up costs for the production effort. Yet, these contractors are saddled with the burden of paying recoupment charges to the Government on their foreign and domestic sales.

This application of recoupment policy particularly discriminates against small businesses since the entry level investment in major weapons systems is sufficiently high to preclude participation by those who did not receive support from DoD at the development and prototype stages.

DoD's recoupment policy also appears to be applied only selectively by the Department. For example, the Pentagon partially waived unit recoupment charges estimated at $1.45 million per plane to promote the sale of F-18 fighters to the Canadian government.

Furthermore, when it is time to actually charge contractors for nonrecurring costs, it becomes nearly impossible to accurately determine what is to be "recouped." This is because recoupment charges must be based on a proportion of present and future sales of a product or technology. Obviously, determining future sales for purposes of computing the appropriate recoupment charge is difficult at best. Additionally, the government does not necessarily allocate its R&D expenditures on a per contract basis. Rather, R&D funds are spread over programs, making it impracticable for the government to determine what portion of program R&D funding is allocable to a specific contract.

Finally, by applying recoupment to commercial contracts, rather than to government-to-government contracts involving major defense equipment, serious Constitutional questions are raised. As a charge to be levied by the federal government on its own sales, recoupment is unquestionably within the government's power and Constitutional right. However, as a levy on U. S. citizens in the conduct of commercial business, which the recoupment charge is when implemented by DoD, recoupment threatens individual liberties guaranteed by the Constitution.

CONCLUSION

If the government can procure a defense article competitively, in all likelihood the technology is such that foreign competitors can and do produce comparable articles.

Thus, the production contractor must try to sell the article in the foreign marketplace with the burden of this recoupment charge while his foreign competitors suffer no such burden. It is hardly surprising that a customer will buy from the foreign competitor rather than pay the recoupment charge. Under these circumstances, the U. S. company must either refuse to take a government production contract, which would saddle him with this competitive disadvantage, or must simply forego the export market for that product. Neither alternative is in the government's best interest. (The Pentagon effectively recognizes this when it waives recoupment charges on many large contracts.) Either the government loses potential competitors on its acquisitions or it loses foreign sales, and the resultant tax revenues and balance of payment benefits.

In enacting the Arms Export Control Act, Congress sought to strike a balance between the interests of supplementing Department of Defense funds and of not interfering with foreign trade. Congress determined that such a balance could be sustained by applying recoupment charges only at one level. The Department of Defense has upset that balance under its present recoupment policy.

Not only is DoD's authority for these regulations highly questionable, policy reasons demand that the current recoupment policy be re-evaluated. The enforcement of the policy is not cost effective, resulting in a net drain to the treasury, and is adversely impacting the U. S. balance of payments. The adverse foreign policy effect of these regulations on our relation with our allies is immeasurable. The present policy is unrealistic in light of our diminishing competitive advantage over foreign high technology companies.

For the aforementioned reasons, DoD's present recoupment policy should be rescinded. The levy of recoupment charges should be limited to that required by law. Congress intended to apply recoupment only to the sale of major defense equipment sold in government-to-government transactions. Congress must, therefore, clarify the intent of the Arms Export Control Act to the Department of Defense.

Aerospace Industries Association of America, Inc.

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June 1, 1984

OASD (Comptroller)
ATTN: Mr. Michael J. Melburn
Director, Policy Promulgation
Room 3A882, The Pentagon
Department of Defense
Washington, D.C. 20301

SUBJECT: AIA Comments on Proposed Revision to DoD Directive 2140.2 "Recoupment of Non-recurring Costs on Sales of U.S. Products and Technology"

Dear Mr. Melburn:

In furtherance of the industry interest on recoupment shown during our DoD meeting of June 23, 1983 and the subsequent follow-on actions culminating in the opportunity provided during April 1984 to review and provide comments on the proposed DoD Directive 2140.2, our members have completed these review efforts. Their consolidated views divided into "General" and "Specific" sections are provided for your consideration.

General Comments:

It is the consensus of our members that this proposed Directive revision is overreaching in its purpose and scope and is unduly complicated.

It would appear that the thrust of the directive could be accommodated by recoupment on the major equipment or systems sales without application to components, modification kits, technical data packages, etc. Implementation of the requirements set forth in the directive will significantly slow down the proposal cycle and increase administrative time and effort on the part of both government and contractors. It will also tend to create ill will in dealings with foreign government representatives due to inordinate delays which can be occasioned by the increased requirements, and therefore adversely further affect the balance of trade. Moreover, it will make U.S. industry less competitive with those companies which are owned or directly subsidized by foreign governments.

The impact will be principally in increased costs through additional costs passed on directly and indirectly (because of added administrative effort). This result is obvious and reflected in the DoD Directive. The impact at the functional level is unknown, but expected to be small.

1725 DeSales Street, N.W. Washington, D.C. 20036 • (202)429-4600

The entire picture is unclear as to how one can adequately judge the amount of future FMS or commercial sales of a product at the first sale to a non-USG customer. If the estimate is low, over recovery is possible (at a higher inequitable cost share to non-DoD customers). Conversely, if the estimate is high (resulting in lower recovery) does the U.S. Government accept this and absorb the difference or will non-USG customers be subsequently assessed?

Another scenerio might be that a product is modified or improved at the expense of a particular non-USG customer. If this improvement is subsequently procured in a product sold to the USG, it would seem logical for the USG to pay the non-USG customer a "royalty" for the USG's share of avoided non-recurring costs.

Finally, if the logic of the control and bookkeeping problems as well as reduced competitive position do not prevail, and it is deemed necessary by the DoD to impose this surtax on foreign customers, it would seem appropriate that since the government must evaluate data supplied by contractors and determine the amount to be assessed and added to the contractor's price, it would be far more efficient, and less burdensome to the contractors if - on FMS cases - the DoD just add these costs to their FMS administrative burden and collect it off the top as they are paid by the FMS customer, rather than have the contractor add it to their price and pay it back to the government. In this way they cut out the middleman and that associated bookkeeping work for the contractor.

The DoD Directive will cut costs and administrative burden if each Military Department of Defense Agency involved will provide timely and efficient implementation of subject Directive with standard procedures. If the systems and procedures for implementation vary among the various agencies, administration of the industry portion will be more costly and time consuming.

Specific Comments

1. Encl. 1 Definitions
   Para. F. Non-recurring Research, Development, Test and Evaluation (RDT&E)
   Para. G. Non-recurring Production Costs
   Encl. 2 Implementing Procedures
   Para. B-1 Calculation of Charges on MDE and Components

   The non-recurring development and production cost of ECP's which are authorized after contract award is shared by USAF and all FMS countries on a per aircraft basis. The projected total cost defined in F. and G. could be interpreted to include these costs which would amount to double bidding on ECP's. However, review of Implementing Procedures Paragraph C.2.b. indicates this is not the intent. Some clarification of definitions F. and G. as related to FMS sharing of ECP development costs after contract award is desirable.

2. Waivers - Para. G. 4 provides that decisions will be reached on waivers within "60 days after receipt of the request." In cases where other nations request waiver of non-recurring cost charges for articles or services included in a direct Commercial sale, U.S. contractors are often under severe time constraints to submit Proposals in time to meet international competition. A processing time of no more than 30 to 45 days would be most helpful.

3. Encl. 2 Implementing Procedures
Para. A.6. General

Contractor Payments of Nonrecurring Cost Charges - Para. A. 6 of Encl. 2 "Implementing Procedures" provides that U.S. contractors will be required to pay the U.S. GOVT. (USG) within 30 days following "the delivery of each item from the contractors facility." Thirty (30) days after the delivery of each item is not considered sufficient time in the light of international billing and payment procedures. A more appropriate payment period would be 30-45 days after the U.S. contractor receives payment from the customer for articles or services delivered.

In addition, referring payment within thirty (30) days of an affected item is not feasible since in the current multinational market contractors do not receive payment in some cases for years.

4. Encl. 2 A.6 General
B.4 Calculation of Charges on MDE and Components

The contractor does not pay recoupments on FMS programs. Recoupments are handled outside the hardware contracts. Direct sale contracts may also require payment of recoupment charges outside the contract if FMS credits are used. Payments would be through a USG/FMS customer LOA for services and recoupments. If recoupment charges are included in a direct sale contract, payment to the USG should be upon or after payment by the direct sale customer to contractor.

5. Consultation with Defense Contractors in Determining Direct Commercial Sales Quantities - In Para. B.2 of Encl. 2 it indicates that "Defense Contractors should be contacted if necessary in determining direct sales quantities." Suggest elimination of the words "if necessary." Contractors should be asked for any inputs they may have in all cases involving direct commercial sales.

6. Encl. 2 Para. C 2b, sentences 1 and 2

"Developed to improve the safety, reliability, and maintainability. The cost of programs designed to improve the safety, reliability, availability and maintainability for the projected life of the equipment shall be included in the end item/major component NC pools. In the event an FMS customer funds part of the development cost through a Component Improvement Program (CIP) or comparable program, then a pricing exception for an appropriate adjustment of the established NC recoupment charge may be requested by a DoD Component."

COMMENT: It will be a common occurrence for purchasers to qualify for an NC adjustment because of their CIP participation. Will DSAA be asked to adjust the NC on an individual country/case basis? It would be more efficient for the DoD components to adjust the NC based on a DSAA approved formula. Will the same rule apply to TCP members? If a country discontinued CIP participation would the NC for the end item have to be adjusted?

7. Encl. 2 Para. D. 1a, Technical Data Packages

COMMENT: Establishing unit prices for commercial sales would be very difficult, since no existing mechanisms are in effect at this time. The entire proposal method of collecting dollars on technical publications in place of royalty fees would be hard to accept by either the multinational customers or the manufacturers required to implement such a procedure. In fact, this method would not be acceptable.

Our aerospace industry recognizes the legal requirement to recover all Government costs associated with Research, Development, Test and Engineering, and the production of defense articles and services that are sold to other customers. We believe that favorable consideration of these industry views and recommended changes to the proposed Directive revison will facilitate its implementation more effectively. Thank you for providing this opportunity. Should there be a need for any clarification, our members will be happy to comply.

Very truly yours,

John W. Stahl Jr.

John W. Stahl, Jr.
Director, Product Support
AEROSPACE OPERATIONS SERVICE

FRANK ANNUNZIO
11TH DISTRICT, ILLINOIS

COMMITTEES:
BANKING, FINANCE AND URBAN AFFAIRS
SUBCOMMITTEES:
CHAIRMAN, CONSUMER AFFAIRS AND COINAGE
FINANCIAL INSTITUTIONS SUPERVISION, REGULATION AND INSURANCE
HOUSE ADMINISTRATION
SUBCOMMITTEES:
CHAIRMAN, ACCOUNTS

Congress of the United States
House of Representatives
Washington, D.C. 20515

June 8, 1983

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WASHINGTON, D.C. 20515
(202) 25-6661

Colonel Hershell Murray
Chief
House Liaison Division
The Pentagon
Washington, D.C. 20301

Dear Colonel:

Please find enclosed a copy of a letter from Mr. C.M. Wood, President and Chief Executive Officer, NI-TEC Incorporated located in the 11th Illinois Congressional District which I am privileged to represent, along with enclosures, in which he expresses his concern about the adverse effects that the present Department of Defense regulations concerning recoupment charges have on his company, and also outlines his support for repealing these regulations "and levy recoupment charges only as required by law as specified in the Arms Export Control Act of 1976."

As you will note, Mr. Wood states that the Department's policy is inconsistent with the intent of the Congress which authorized recoupment of non-recurring costs only on major defense equipment. Mr. Wood mentions that the present policy of extending recoupment charges to "any and all products that cost $5 million to develop" is "grossly unfair to the U.S. contractors who must compete with foreign contractors and is adversely affecting their ability to export."

I would be most appreciative if you would give Mr. Wood's views your most thorough consideration, and also let me know on his behalf, why the Department of Defense has chosen to extend recoupment charges beyond the foreign military sales of major defense equipment.

Thank you for your cooperation and assistance in this matter.

Sincerely,

Frank Annunzio

FRANK ANNUNZIO
Member of Congress

FA/dah
Enclosures

NI-TEC Incorporated
5600 West Jarvis
Niles, Illinois 60648
312-647-7702. Telex 724367

C. M. Wood, President and
Chief Executive Officer

JUN 6 1983

May 31, 1983

The Honorable Frank Annunzio
U.S. House of Representatives
Rayburn Office Building, Room 2303
Washington, D.C.

Dear Sir:

Thank you very much for your time during my visit to your office on May 18. It was the first opportunity to visit since I moved to Illinois in 1981. I was very impressed with the enthusiasm that was shown to me by you and your staff. Unfortunately, the visit was prompted by a problem we are experiencing here at Ni-Tec.

As I told you, we are in the business of manufacturing night vision equipment for the military. At the present time, the procurement activity for our type of equipment is at a low level. As a result, we have had to reduce our workforce by approximately 100 people, which is 25%. We have also increased our marketing activities abroad in an attempt to keep our business at the same level. Foreign sales serves several purposes that is not only good for Ni-Tec, but also benefits the U.S. Government.

Ni-Tec is a planned producer of night vision tubes and devices under the Industrial Mobilization Program. Foreign orders helps to keep these production capabilities operating without any cost to the U.S. Government. Foreign sales also assist in reducing the balance of deficits, as all exports do.

Our problem is this:

In the Arms Export Control Act of 1976, there is a provision that requires D.O.D. to recoup the non-recurring costs that were expended on major defense equipment when sales of this equipment are made to foreign customers. The act defined major defense equipment as that which cost more than $50 million to develop and more than $200 million to produce. The act only requires the

recoupment of non-recurring on FMS sales of major defense equipment as defined above. However, the D.O.D. has interpreted that it has the authority to extend that recoupment policy to include any and all products that cost $5 million to develop. They further directed the D.O.D. procurement activities to include the recoupment of non-recurring costs in all their contracts.

This clause places the burden of collecting this recoupment fee on the contractors, such as Ni-Tec. We feel that this policy is inconsistent with the intent of the Congress when it passed the Act. It is grossly unfair to the U.S. contractors who must compete with foreign contractors and is adversely affecting their ability to export.

The method of recoupment is to bill the contractors a recoupment fee when the equipment is exported. A copy of one of these bills is attached (Attachment 1).

Since all the contracts involved were won in a very competitive situation, to pay such a fee would place us in a loss situation. There is literally no way we can pass these charges on to the foreign customers.

Further complicating the situation is the fact that in many instances our competition is the U.S. Government offering our own equipment under Foreign Military Sales (FMS) which obviously does not have the recoupment charge included.

I am enclosing a Position Paper (Attachment 2) written by Mr. J. M. Jett, which discusses the whole situation from legal and policy standpoint. Please review it carefully and you can see that the policy places the burden of recoupment on the U.S. companies and not on the foreign governments.

In summary, I re-emphasize that the recoupment policy as it is now enforced

- o is inconsistent with the intent of Congress;
- o results in a net drain to the U.S. Treasury;
- o is adversely affecting the U.S. balance of payments;
- o is grossly unfair to the U.S. contractors;
- o cannot be enforced in a cost-effective way;
- o is not based on statutory authority.

Please help us to get this albatross from around our necks so we can compete on an equal basis with foreign suppliers. The benefits gained through such exports will far outweigh whatever funds can be collected from the U.S. companies.

If you need me for further information or testimony, please call. Incidently, I not only represent Ni-Tec, Inc., but I am also presently the President of the Association of United States Night Vision Manufacturers.

Thank you for your help.

Very truly yours,

NI-TEC, INC.

C. M. Wood
President and
Chief Executive Officer

CMW/je
Attachments

January 4, 1983

DEPARTMENT OF DEFENSE RECOUPMENT POLICY
EXECUTIVE SUMMARY

The Department of Defense has promulgated a recoupment policy that

- is inconsistent with the intent of the Congress of the United States,
- results in a net drain to the U.S. Treasury,
- is adversely affecting the U.S. Balance of Payments,
- is grossly unfair to U.S. contractors who must compete with foreign subsidized contractors,
- cannot be enforced in a cost effective way,
- is not based on statutory authority.

It is recommended that DoD rescind its present regulations (DAR 1-2400, 4-110 and 7-104.64) and levy recoupment charges only as required by law as specified in the Arms Export Control Act of 1976. This recoupment would apply only to "major defense equipment not ordinarily subject to intensive foreign competition".

This document includes a complete summary of the present policy, legislative history, validity of the regulation and other considerations which completely justify the recommendation that the present DoD regulation be rescinded.

DEPARTMENT OF THE ARMY

HEADQUARTERS US ARMY COMMUNICATIONS-ELECTRONICS COMMAND
AND FORT MONMOUTH
FORT MONMOUTH, NEW JERSEY 07703

REPLY TO ATTENTION OF:

April 5, 1983

Electronic Procurement Branch

Ni-Tec International, Ltd.
5600 West Jarvis
Niles, Illinois 60648

Gentlemen:

In accordance with the policy set forth in the Department of Defense Directive 2140.2 dated 5 January 1977 and in accordance with the approval of the export licenses for the following munitions cases.

Munitions Case No.	Country	Item	Qty	Amount Due	Date App'd
175797	TW	MX-9622/UV	110	$ 9,680.00	20 Oct 1982
149675	IT	MX-9644/UV	650	57,200.00	03 Nov 1981
147934	IS	AN/PVS-4	100	65,600.00	30 Sep 1981
145905	EG	NVS-900 (MX-9644-UV)	100	8,800.00	31 Aug 1981
128166	EG	NVS-800 (AN/TVS-5)	150	13,380.00	29 Jan 1981
				$154,660.00	

? 656

Please forward your check for $154,660.00 payable to the Treasurer of the United States or your payment of these RDT&E Non/Recurring Production costs. All payments should be identified with the appropriate export license in order for us to properly close these accounts.

Sincerely,

ALICE A. ALLEN
Contracting Officer

POSITION PAPER PREPARED BY

J. M. JETT
XEROX ELECTRO-OPTICAL SYSTEMS

on

DEPARTMENT OF DEFENSE RECOUPMENT POLICY

Submitted by:

S. T. Yanagisawa
February 9, 1983

ATTACHMENT "2"

DEPARTMENT OF DEFENSE RECOUPMENT POLICY

INTRODUCTION

United States defense contractors when selling certain items that were originally developed with government appropriations/funds are mandated to include in the selling price of these items a charge to reimburse the government for a fair share of its original investment in the manufacture of the products and/or development of the related technology.(1)

RECOUPMENT POLICY

There are two types of situations in which the government seeks to recover part of its costs for research and development from commercial firms that benefit from the results of government appropriations. The first type involves cost recovery from defense contractors on their commercial sales of defense products to both domestic and foreign customers. The second type involves cost recovery on foreign military sales.(2)

The government's recoupment policy is based, first, on the theory that where a direct beneficiary of government action can be identified, that beneficiary and not the general taxpayer should pay the cost of providing the benefit conferred. Under this program, research and development costs, that are indirectly paid by the general taxpayer, are returned from the beneficiaries of R&D appropriations: the consumer and the firm making the commercial sales.

- A second and highly questionable justification for the government's program is a desire to prevent favoritism toward incumbent contractors. When a commercial product is developed with government funds, the firm that obtains the original development contract may have a distinct advantage over its competitors who develop a similar product without government support. Thus, the contractor, who is the recipient of government appropriations, may be in a better position to make a profit, to undersell his competition and even to prevent them from entering the market.

Department of Defense recoupment policy requires contractors to reimburse the government for a portion of nonrecurring costs when defense equipment is sold to foreign or domestic commercial buyers. The definition of nonrecurring costs includes "research, development, tests, evaluation, production engineering, product improvement, destructive testing, pilot model production, testing and evaluation;"(3) not only those incurred by the contractor on his government contract but by all government departments and labs involved with development.

Recoupment policy for the Department of Defense originated with a decision made by the Secretary of Defense in 1964 which determined that Foreign Military Sales (FMS) customers for defense items originally developed with government funds should pay the same cost as that paid by the government. This policy became department-wide policy in 1968 with the enactment of the Foreign Military Sales Act.(4) The Act implies that nonrecurring costs and prior development costs are a portion of the total costs of an item, and as such must be included in the FMS sales price to foreign nations.

LEGISLATIVE HISTORY

The government's attempt to recover nonrecurring costs originated with the promulgation of a new subpart "A" to the then existing Part 4 of the Defense Acquisition Regulations (formally ASPR and now hereinafter referred to as "DAR") in 1967.(5) This new provision had no specific language or discussion of "recoupment of nonrecurring costs" but instead included a section on "Cost-Sharing" which stated:

> "It is the policy of the Department of Defense to utilize cost-sharing in research or development procurements with contractors, other than educational institutions and foreign governments, only when there is a high probability that the contractor will receive substantial present or future commercial benefits . . ."(6)

The statutory provision referred to as authority for this new provision read as follows:

> "Notwithstanding any other provision of law, an officer or agency of the Department of Defense may obligate funds for procuring, producing, warehousing, or distributing supplies, or for related functions of supply management, only under regulations prescribed by the Secretary of Defense. The purpose of this section is to achieve the efficient, economical, and practical operation of an integrated supply system to meet the needs of the military departments without duplicate or overlapping operations or functions."

The regulations were cited as being authorized by the Armed Services Procurement Act.(7) However, a careful review of these sections reveal that no reference is made to either "cost-sharing" or "recoupment" policy.

In November of 1967, the Federal Register reported an additional amendment to DAR, Section 4-110 that specifically included a policy for the recoupment of nonrecurring costs on the sale of major defense equipment.

> "It is the Department of Defense policy that foreign buyers of major defense equipment shall pay a fair share of nonrecurring costs associated with the equipment..."(8)

This revised section also called for the insertion of a new compliance clause in all Department of Defense Contracts.(9) No authority was mentioned for either the promulgation of the revised regulations or the new contract provisions although a specific citation is referenced for the definition of "major defense equipment."(10)

In 1969 the regulations were revised again. The option was given the agency to include the recoupment clause in contracts for "non-major" defense equipment as long as the research and development costs of the items exceeded $10 million. DAR Section 4-110

(1970), 34 Fed. Reg. 13841 (1969). Again, no specific statutory authority was given for the revised regulation. Earlier that year, a set of new contract provisions had been issued. 34 Fed. Reg. 9267 (1969). They included a clause requiring recoupment of nonrecurring costs (DAR Section 7-104.64) to which the revised regulation referred. DoD Directive 4105.30, 24 Fed. Reg. 2260 (March 11, 1959) was cited as authority for their issuance. However, this directive merely stated that its purpose was to "continue the Armed Services Procurement Regulation as a regulation of the Department of Defense . . . under the provisions of Section 2202, Title 10, United States Code . . ."

Thus, the early regulations quickly developed specific requirements concerning recoupment of nonrecurring costs where major defense equipment or equipment having research and development costs greater than $10 million was involved. Little in the statutes cited as authority can be construed to authorize the regulations. Perhaps it could be argued that the expressed aim "to meet the needs of the military department without, duplicate or overlapping operations or functions," 10 U.S.C. Section 2202 (1976), can be construed as authorizing regulations designed to prevent buyers from avoiding their fair share of development costs. The section seems, however, to be directed at coordinating procurement among the various government departments to avoid unnecessary expense. Perhaps the regulations can be said to be interpretations of the preference for advertised procurements and awards to the bidder whose bid is the "most advantageous to the United States, price and other factors considered." 10 U.S.C. Section 2305 (c) (1976). Clearly, however, the concept of recoupment arose in the regulations of the Department of Defense and apart from specific statutory authority.

The requirement of recoupment remained essentially unchanged from 1969 through 1976, though the number of the provision requiring recoupment was changed (DAR Section 4-109 (1974), and the definition of major defense equipment was modified (see DoD Directive 5000.1). Then, in 1977, a new DoD Directive was issued, which signaled two changes in the regulations. DoD Directive 2140.2 (January 5, 1977). First, recoupment

would be required whenever nonrecurring production costs or RDT&E costs exceeded $5 million. Secondly, the insertion of the contract clause requiring recoupment of nonrecurring costs was no longer optional but mandatory when non-major defense equipment was involved. The sources cited in the directive did not include 10 U.S.C. Section 2202 but did include the Arms Export Control Act of 1976 (without citation to any specific section). Defense Procurement Circular No. 76-9 (August 30, 1977) contained a version of DAR Section 4-109 that included the $5 million threshold and required placing the clause requiring recoupment of nonrecurring costs in all contracts where the threshold was met.

Finally, new regulations were promulgated to replace former ASPR Section 4-109. DAR Sections 1-2400 to -2404 (1981), Defense Acquisition Circular No. 76-20, (VI) (September 17, 1979). The new regulations require the nonrecurring costs clause to be placed in all "RDT&E and production contracts and subcontracts of $1 million or more." DAR, Section 102403 (a) (1981).

Arms Export Control Act

The Arms Export Control Act was enacted in 1976. 22 U.S.C.A. Sections 2751-2794 (West 1979). The legislative history of the bill reveals it to be "a historic initiative by Congress to phase out grant military assistance and to increase the exercise of its oversight powers with respect to the rapidly growing arms sales program." H.R. Rep. No. 1144, 94th Cong. 2d Sess. 12, reprinted in (1976) U.S. Code Cong. & Ad. News 1378, 1388.

The policies of the Act include the supervision of export of arms by commercial firms and limitation of the total amount of military exports. 22 U.S.C.A. Section 2751 (West 1979).

The Act also specifically provides for recoupment of "a proportionate amount of any nonrecurring costs of research, development, and production of major defense equipment" on sales by the United States Government (i.e. FMS sales). 22 U.S.C.A. Section 2761 (e) (1) (c) (West 1979).

Major defense equipment is defined as:

> "Any item of significant combat equipment on the United States Munitions List having a nonrecurring research and development cost of more than $50,000,000 or a total production cost of more than $200,000,000 . . ."(11)

Overall, the Arms Export Control Act provides a detailed scheme for control of both governmental and commercial sales of both major defense equipment and defense articles and services. However, the Act provides for the recoupment of nonrecurring costs only on FMS sales of major defense equipment. For eight years prior to the passage of the Act, however, the DAR had provided for recoupment of nonrecurring costs in government-to-government sales of major defense equipment:

> "It is the Department of Defense policy that foreign buyers of major defense equipment shall pay a fair share of nonrecurring costs associated with the equipment."(12)

The regulations included the method of calculating the charge for nonrecurring costs in each foreign sale or license agreement (DAR Section 4-110 (d) (3) (1969)), and the phrase "foreign sale or license agreement" includes all sales to or license agreements with foreign buyers, including foreign governments and international organizations, whether made through the U.S. government or directly by U.S. domestic firms. DAR Section 4-110 (d) (c) (ii) (1969).

The long-standing DAR regulations also, however, required recoupment on foreign sales of major defense equipment by commercial sellers (DAR Section 4-110 (d) (1) (1969)) and allowed clauses requiring recoupment to be inserted in contracts for foreign sales of "non-major" defense equipment where research and development costs were greater than $10 million and for domestic commercial sales (DAR Section 4-110 (d) (1) (1969)). The Arms Export Control Act makes no provision for any of these last three situations, even

though it regulates, in detail, foreign sales by commercial contractors (whereas the Act under the authority of which the regulations were issued has nothing approximating such specific provisions). 10 U.S.C. Sections 2202, 2301-2314 (1959).

VALIDITY OF REGULATIONS

There are several arguments against the validity of the current regulations. First, the Arms Export Control Act, by virtue of its specific coverage of the issue of nonrecurring costs can be seen as preempting the subject, so that any regulations concerning nonrecurring costs must be judged by the Act's terms rather than by those of 10 U.S.C. Sections 2202, 2301-2314 (1956). Thus, the fact that regulations covering nonrecurring costs have been in existence for over ten years may not be entitled to much weight.

Second, because the Arms Exports Control Act includes a provision which requires recoupment in a situation where recoupment had long been required by the regulations, but does not require recoupment in any other situation where it had been required by the regulations, the Act may be seen as validating the prior regulations only in the area it addresses. The Act makes clear the intention of Congress to oversee more closely the export of arms, and it does contain specific provisions in many areas. The Act specifically addresses commercial export on non-major defense equipment and does not provide for recoupment of nonrecurring costs in that situation. It can be argued that Congress intended to leave unregulated those areas it did not choose to regulate in the exercise of its oversight powers. Congress, struck a delicate balance between the objectives to avoid proliferation of military goods and the contravening policy of encouraging export sales (improving the balance of payments) and lending military support to our allies. The decision to levy nonrecurring charges only on government-to-government sales, and then only when the sales involve major defense equipment, optimized this balance. If so, DoD should not be authorized to disrupt this balance by extending the application of the recoupment concept.

Third, the fact that the Arms Export Control Act calls for recoupment in only a single situation argues against the validity of subsequent regulations which expand the requirements for recoupment established in the regulations promulgated before the passage of the Act. Had the Arms Export Control Act not been enacted, one might argue that the latest regulations were a permissible modification of the prior regulations (in lowering the threshold dollar amount to $5 million and in requiring the insertion of the contract clause providing for recoupment in all research and development and production contracts of greater than $1 million). The new Act, however, may actually signal a restriction on the allowable regulations; it is certainly not authority for expanding them. Thus, the new regulations would seem to be invalid and even the old regulations allowing recoupment to be required on commercial sales of equipment whose research and development costs exceed $10 million might have been (had they not been changed) open to question after the passage of the Act.

The DoD Directive announcing the new regulations cited the Arms Export Control Act as authority. DoD Directive 2140.2 (January 5, 1977). The Defense Procurement Circular that contained the new version of DAR Section 4-109 cited as authority 10 U.S.C. Section 2202 and did not refer to the Arms Export Control Act. Defense Procurement Circular No. 76-9 (August 30, 1977). It can be argued that the new regulations are merely a modification of the old rather than being issued under the Arms Export Control Act. The fact that the Act addresses the area specifically, however, is an effective rebuttal to this argument.

While the Arms Export Control Act specifically addresses the issue of recoupment of nonrecurring costs on government sales of major defense equipment, it leaves ample discretion to the President in the area of commercial export of defense articles and services to justify the present regulations. See 22 U.S.C.A. Section 2778(a)(1)(West 1979). One answer to this argument is that such an interpretation might mean that no recoupment would be required on government sales of non-major defense equipment,

because that area is specifically covered in the statute without a provision for recoupment, while such sales of commercial equipment could require recoupment. The Act contemplates recoupment only on sales of major defense equipment. Another answer is that Section 2270 concerns the President's discretion to establish the contents of the United States Munitions List and rules limiting or qualifying the export of such items and is not intended to authorize regulations concerning recoupment of nonrecurring costs.

POLICY CONSIDERATIONS

There are other serious policy issues related to the government recouping nonrecurring costs from the commercial sales of government contractors to foreign and domestic customers.

Government expenditures for Research and Development are in the nation's best interest and help to promote both domestic and international competition, to advance technology and to foster economic growth. The imposition of broad recoupment regulations act as a disincentive for performing organizations in undertaking Federal R&D because it reduces the opportunity for commercial gains. Potential performers are already burdened with start-up, production and marketing costs. Additional requirements for recoupment of R&D costs would only further discourage their involvement.

Foreign concerns and governments now seek to become less dependent on the United States for commercial and military products and to also gain a significant share of the U.S. market. In some instances, they are outbidding U.S. concerns, particularly with conditions for favorable financing. As a result, the U.S. business industry faces the prospect of a significantly smaller share of the world market.

The United States can no longer be complacent about presumed technical superiority in the international competition for markets. The impact of this situation is apparent in the high technology industries in the United States, such as electronics and computers, which

are faced with increased competition from foreign countries, many of which benefit from support and stimulation of their own governments.

The sale of any product or technology by our American companies helps to bring about a natural public benefit in this country. An economic benefit to the public is derived from the taxes which are attached to a sale. Another benefit to the public is derived from the exposure to and use of advanced technology. According to proposed policy issued by the Office of Federal Procurement policy, recoupment should not be sought when to do so would result in conflict with important "public considerations..." 45 Fed. Reg. 86954 (December 31, 1980). Moreover, the Commission on Government Procurement found after careful study that the government's efforts to levy and collect nonrecurring development costs were decidedly not cost effective.(13)

There is a need for a determined, cooperative effort involving government and industry in the United States to maximize the competitive position of U.S. suppliers and, more importantly, to remove impediments to the early application of R&D results for commercial purposes.

In enacting the Arms Export Act, Congress sought to strike a balance between the interests of supplementing Department of Defense funds and of not interfering with foreign trade. Once Congress determined that such a balance could be sustained at one level, it was inappropriate for the Department of Defense to upset that balance by readjusting and lowering the recoupment threshold.

CONCLUSION

In adopting the present regulations on recoupment of nonrecurring research and development costs, DoD cited the Arms Export Control Act as authority. While that act authorizes recoupment of FMS sales of major defense equipment, it clearly does not authorize the broader coverage of the regulations (i.e., application to direct domestic and foreign commercial sales and to sales of "non-major" defense equipment).

Whether DoD's original regulations were authorized under the Armed Services Procurement Act is highly questionable. DoD's interpretation depends on an implied grant of authority for these specific regulations from a general procurement statute. There is nothing in the legislative history of this general procurement statute to indicate Congress intended this authority. Whatever authority has been implied in the procurement statute may also have been restricted or limited by the specific treatment in the Arms Export Control Act.

Not only is DoD's authority for these regulations highly questionable, policy reasons demand that the current recoupment policy be reevaluated. The enforcement of the policy is not cost effective, resulting in a net drain to the treasury, and is adversely impacting the U.S. balance of payments. The adverse foreign policy effect of these regulations on our relation with our allies is immeasurable. The present policy is unrealistic in light of our diminishing competitive advantage over foreign high technology companies.

For these reasons, DoD's present recoupment policy should be rescinded. The levy of recoupment charges should be limited to that required by law--only on FMS sales of major defense equipment.

Bibliography

(1) Defense Acquisition Regulations, Section 1-2401 (a).

(2) 2 Report of the Commission on Government Procurement 28-31 (December, 1972).

(3) DAR Sections 4-110 and 7-104.64 (August, 1969).

(4) U.S. Congress, House, An Act to Consolidate and Revise Foreign Legislation Relating to Reimbursable Military Exports, Public Law 90-629, 90th Cong. 2 sess., H.R. 15681, (October, 1968).

(5) 32 Federal Register 10161 (1967).

(6) DAR Section 4-110 (a) 32, Fed. Reg. 10164 (1967).

(7) 10 U.S.C. Sections 2301-2314 (1956).

(8) DAR Section 4-110 (d), 32 Fed. Reg. 16403 (1967).

(9) Id.

(10) DAR Section 4-110 (d) (1), 32 Fed. Reg. 16403 (1967).

(11) 22 U.S.C.A. Section 2761 (6) (West 1979).

(12) 22 U.S.C.A. Section 2794 (6) (West 1979).

(13) 2 Report of the Commission on Government Procurement 29 (December 1972).

OFFICE OF THE ASSISTANT SECRETARY OF DEFENSE

WASHINGTON, D.C. 20301

COMPTROLLER

(Management Systems)

24 JUN 1985

MEMORANDUM FOR MR. KRAFT

SUBJECT: Proposed DoD Directive 2140.2, "Recoupment of Nonrecurring Costs on Sales of U.S. Products and Technology"

Enclosed is a proposed ACTION MEMORANDUM for the Deputy Secretary of Defense that recommends his signature on the subject Directive. Enclosures to the memorandum summarize major changes to the Directive and pertinent background information.

Also enclosed are a memo to Mr. Helm; reports from the House Subcommittee, the Tri-Service Study conducted by my office, and the General Accounting Office; a list of coordinating officials; and the coordinating papers. The proposed ACTION MEMORANDUM and Enclosures 1 and 2 discuss the relevancy of the three reports.

Recommend your signature on the memo to Mr. Helm.

Michael J. Melburn

Enclosures

ASSISTANT SECRETARY OF DEFENSE

WASHINGTON, D.C. 20301

COMPTROLLER

DRB

85 JUL 1 P 3:3 9 JUL 1985

DIRECTIVES DIVISION

MEMORANDUM FOR DEPUTY SECRETARY OF DEFENSE

SUBJECT: Proposed DoD Directive 2140.2, "Recoupment of Nonrecurring Costs on Sales of U.S. Products and Technology" - ACTION MEMORANDUM

Attached for your approval is a proposed reissuance of the subject Directive (TAB A).

The reissuance of this Directive implements the recommendations of the Subcommittee of the Committee on Government Operations, House of Representatives (TAB B), and includes improvements recommended by a Tri-Service Study Group (TAB C)-chaired by my office. Enclosure 1 summarizes the major changes to this Directive, and Enclosure 2 summarizes pertinent background information.

Policies in this Directive have an impact on the public sector. Therefore, we published the proposed reissuance in the Federal Register to provide for public comment on the policies. Only four comments were received (TAB D).

This limited response indicates that the recoupment policies have widespread acceptance and recognition by DoD contractors. Two of the responses were from associations which questioned the legality of collections on commercial sales. The General Accounting Office has recently audited this issue (TAB E) and concluded that it was appropriate for contractors to pay the U.S. Government a pro rata share of its Research, Development, Test, and Evaluation (RDT&E) and production investment costs when commercial sales are made. The other comments were from two individual companies and offered suggestions which we accommodated to the extent authorized by law.

We also accommodated the comments and recommendations of the coordinating DoD Components where feasible. A list of coordinating DoD officials and coordinating documents are attached at TAB F.

Recommend you sign the proposed Directive.

Robert W. Helm

Enclosures

AUG 5 1985

DEP SEC HAS SEEN

ISWHT, IV

Robert W. Helm
Assistant Secretary of Defense
(Comptroller)

8/26

OFFICE OF THE ASSISTANT SECRETARY OF DEFENSE

WASHINGTON, D.C. 20301

19 JUL 1985

COMPTROLLER
(Management Systems)

MEMORANDUM FOR MR. HELM

SUBJECT: Proposed DoD Directive 2140.2 "Recoupment of Nonrecurring Costs on Sales of U.S. Products and Technology"

Attached for your signature is a proposed ACTION MEMORANDUM for the Deputy Secretary of Defense that recommends his signature on a revised DoD Directive 2140.2.

Enclosure 1 to the proposed memorandum for Mr. Taft summarizes the major changes made to the Directive. Backup material includes the House Subcommittee Report, the Tri-Service Study Report, and the GAO Report. The proposed memorandum discusses the relevancy of the backup material.

Recommend your signature.

H. H. Kraft, Jr.

Enclosures

Bob: Because this has been around for some time, I provided Chase (A), Phillips (N), and Boddie (AF) a copy informally last week for a final check. They agree it's OK.

Hub.

Signed

Enclosure 1

Major Changes - DoD Directive 2140.2, "Recoupment of Nonrecurring Costs on Sales of U.S. Products and Technology"

- Lowers the RDT&E investment threshold for recouping nonrecurring costs on non-major Defense items from $5 million to $2 million. (See comments below.)
- Eliminates the requirement to accumulate nonrecurring production cost data on non-major Defense items.
- Establishes a percentage method for recouping nonrecurring costs for non-major Defense items when over $2 million of RDT&E funds have been expended.
- Expands and clarifies procedural requirements for the collection of nonrecurring costs.
- Assigns responsibility to the Defense Contract Audit Agency to verify that DoD contractors have paid appropriate charges on commercial sales, as required by the provisions of the DoD Supplement to the Federal Acquisition Regulation.
- Requires that recipients of DoD technical data packages agree to pay applicable nonrecurring cost recoupment charges if they use the package to manufacture DoD-developed items.
- Provides guidance for the Component Improvement Program which was jointly worked out by the Office of General Counsel, DSAA, and my office. This guidance will resolve the problems identified in recent DoD Inspector General audit reports.

Comments on the change in the RDT&E investment threshold

The change in the investment threshold for non-major Defense equipment items is required because the House Subcommittee of the Committee on Government Operations found the existing $5 million threshold to be too high (TAB B). The Tri-Service Study (TAB C) disclosed that accounting systems cannot readily identify all nonrecurring costs funded by procurement appropriations. The $2 million RDT&E threshold is a general consensus of DoD action officers of a reasonable threshold amount at which to initiate recoupment action.

Background - DoD Directive 2140.2, "Recoupment of Nonrecurring Costs on Sales of U.S. Products and Technology"

Nonrecurring Costs

Nonrecurring costs are costs incurred by the U.S. Government to develop and/or improve a specific product or technology and to prepare for the manufacture of the product. Excluded are expenditures for capital assets and normal production costs.

The concept of recouping nonrecurring costs dates back to 1967 when significant sales of DoD-developed products began. It was felt that the customers should pay for some of the development costs as well as current production costs. Congress included this recoupment requirement in the Arms Export Control Act of 1976 for major Defense items, and the General Accounting Office recently confirmed that this requirement is applicable to commercial sales (TAB E).

Summary of General Accounting Office Conclusion on Recovering US Government Research and Development Costs from Foreign Customers (GAO/NSIAD-84-156)

"Although not legislatively mandated, we believe it is appropriate for DOD to require contractors to pay the U.S. government a pro rata share of U.S. government RDT&E and production investment costs when commercial sales are made by defense contractors. Further, unless the regulations governing recoupment of these costs are amended by proper authority or determined to be invalid by the judiciary, the regulations must be followed by defense contractors." (See page 3 of the report (TAB E) for additional information.)

ASSISTANT SECRETARY OF DEFENSE

WASHINGTON, D.C. 20301

27 MAY 1986

COMPTROLLER

MEMORANDUM FOR SECRETARIES OF THE MILITARY DEPARTMENTS
DIRECTORS OF THE DEFENSE AGENCIES

SUBJECT: DoD Directive 2140.2, "Recoupment of Nonrecurring Costs on Sales of U.S. Products and Technology," dated August 5, 1985

The Inspector General, DoD has identified the need for additional cost accounting guidance in the recoupment of nonrecurring charges when (1) a new major defense item rate is derived from an existing major defense item recoupment rate and (2) multiple source procurements are involved.

The Enclosure to this memorandum provides the necessary cost accounting guidance for the calculation of a nonrecurring charge for a new major defense item derived from an existing major defense item.

The calculation of a nonrecurring recoupment rate when multi-source procurements are involved is implicit in the current guidance. The guidance requires the identification of the total nonrecurring cost investment and the total quantities to be produced and then to divide the total cost pool by the total quantity. Sources of supply (contractors) are not relevant to the calculations.

Any questions on the implementation of this guidance may be referred to Mr. Michael Melburn, Director for Accounting Policy, Room 3A882 of the Pentagon. His telephone number is 697-7296.

for Robert W. Helm
Assistant Secretary of Defense
(Comptroller)

Enclosure

RECOUPMENT OF NC CHARGES FOR MAJOR DEFENSE EQUIPMENT
NEW MODELS DERIVED FROM EXISTING MODELS

FACTS:

1.

MODEL	COST POOL	QUANTITY	OLD CHARGE
A(OLD)	$500,000,000	1,000	$500,000
B(NEW)	100,000,000	1,000	
	$600,000,000		

2.

OLD MODEL	NEW MODEL
1000 Parts	1200 Parts

(Assume 900 parts are common to both models)

Step 1: Determine New Model Commonality: New model commonality is the percentage of the parts in the new model that are common to the old model.

$$\text{COMMONALITY} \quad \frac{900}{1{,}000} = 90\%$$

Step 2: Determine the amount of the old item cost pool which benefits new items.

$500,000,000	Old Item Cost Pool
90%	Commonality
$450,000,000	Common Cost Pool

Step 3: Determine NC charge for new item.

a. Common Cost Pool	divided by	Benefiting Units		
$450,000,000		2,000	=	$225,000.00
b. New Item Cost Pool	divided by	Benefiting Units		
$100,000,000		1,000	=	$100,000.00
UNIT CHARGE FOR NEW MODEL				$325,000.00

Step 4: Determine Cost Pool of Non-common Items.

a.	Old Item Cost Pool	$500,000,000
	Less:	
b.	New Common Cost Pool	450,000,000
	Remainder: Old Item Cost Pool which does not contain commonality	$ 50,000,000

Step 5: Determine if old item NC charge meets 30% threshold for submission to DSAA.

a.	Old Item Cost Pool	divided by	Benefiting Units		
	$50,000,000		1,000	=	$50,000
b.	New Common Cost Pool	divided by	Benefiting Units		
	$450,000,000		2,000	=	$225,000
	Total new charge for old item				$275,000

c. Recalculate Old Item NC charge

Recalculated Old Item Charge	divided by	Old Item Charge	
$275,000		$500,000	= 55%-Decrease

Step 6: Prepare DSAA package if the results in Step 5 exceed 30%.

Step 7: Proof: Verify that Cost Pool has been fully allocated.

Old Item	1,000 QTY X $275,000 (Old Item Charge)	= $275,000,000
New Item	1,000 QTY X $325,000 (New Item Charge)	= 325,000,000
	Total	$600,000,000

	Cost Pool
Old Item	$500,000,000
New Item	100,000,000
	600,000,000
Difference	-0-

Step 7: (Continued)

NOTE: The proof is designed only to show that costs are evenly distributed to all units, and the fact that there may have been previous charges at the old rate is to be disregarded for purposes of calculation.

RECOUPMENT OF NC CHARGES FOR MAJOR DEFENSE EQUIPMENT
NEW MODELS DERIVED FROM EXISTING MODELS

FACTS:

1.

MODEL	COST POOL	QUANTITY	OLD CHARGE
A(OLD)	$400,000,000	1,000	$400,000
B(NEW)	200,000,000	2,500	
	$600,000,000		

2.

OLD MODEL	NEW MODEL
1000 Parts	1200 Parts

(Assume 600 parts are common to both models)

Step 1: Determine new model commonality: New model commonality is the percentage of the parts in the new model that are common to the old model.

$$\text{COMMONALITY} \quad \frac{600}{1,000} = 60\%$$

Step 2: Determine the amount of the old item cost pool which benefits new items.

$400,000,000	Old Item Cost Pool
60%	Commonality
$240,000,000	Common Cost Pool

Step 3: Determine NC charge for new item.

a. Common Cost Pool		divided by	Benefiting Units	
$240,000,000			3,500	= $68,571
b. New Cost Pool		divided by	Benefiting Units	
$200,000,000			2,500	= $80,000
UNIT CHARGE FOR NEW MODEL				$148,571

Step 4: Determine Cost Pool of Non-Common Items.

a.	Old Item Cost Pool	$400,000,000
	Less:	
b.	New Common Cost Pool	$240,000,000
	Remainder: Old Item Cost Pool which does not contain commonality	$160,000,000

Step 5: Determine if old item NC charge meets 30% threshold for submission to DSAA.

a.	Old Item Cost Pool $160,000,000	divided by	Benefiting Units 1,000	=	$160,000
b.	New Common Cost Pool $240,000,000	divided by	3,500	=	$68,571
	Recalculated Old Item NC Charge				$228,571

c.	Recalculated Old Item Charge $228,571	divided by	Old Item Charge $400,000 = 57%

Step 6: Prepare DSAA package if the results in Step 5 exceed 30%.

Step 7: Proof: Verify that cost pools have been fully allocated.

Old Item 1,000 QTY X $228,571 (Old Item Charge) = $228,571,000

New Item 2,500 QTY X $148,571 (New Item Charge) = 371,430,800

$600,001,800

Rounded to: $600,000,000

	COST POOL
Total	
Old Item	$400,000,000
New Item	200,000,000
	600,000,000
Difference	-0-

Step 7: (Continued)

NOTE: The proof is designed only to show that costs are evenly distributed to all units. The fact that there may have been previouys charges at the old rate is to be disregarded for purposes of calculation.

List of Coordinating Officials

DDR&E	Robert N. Parker	Principal Deputy Director
I&L	John J. Bennett	Acting ASD(I&L)
ASD(ISA)	LTG H. M. Fish	Deputy Ass't Secy (ISA)
Gen. Counsel	Richard A. Wiley	DoD Gen. Counsel
Army	Jack E. Hobbs	Acting ASA(FM)
Navy	G. D. Penisten	ASN(FM)
Air Force	Arnold C. Bueter	Prin. Deputy ASAF(FM)
JCS	Maj. Gen. Adrian St. John	Vice Director, Joint Staff
DSAA	LTG H. M. Fish	Director

Department of Defense
DIRECTIVE

August 5, 1985
NUMBER 2140.2

ASD(C)

SUBJECT: Recoupment of Nonrecurring Costs on Sales of U.S. Products and Technology

References:
(a) DoD Directive 2140.2, "Recoupment of Nonrecurring Costs on Sales of USG Products and Technology," January 5, 1977 (hereby canceled)
(b) Public Law 90-629, "Arms Export Control Act," October 22, 1968, as amended
(c) Council on International Economic Policy Decision Memorandum No. 23, "R&D Recoupment," August 2, 1974
(d) Department of Defense Federal Acquisition Regulation (FAR) Supplement
(e) Defense Acquisition Regulation (DAR)
(f) DoD 7290.3-M, "Foreign Military Sales Financial Management Manual," June 1981

A. REISSUANCE AND PURPOSE

This Directive reissues reference (a), establishes policy to conform with references (b) and (c) for calculating and assessing nonrecurring cost (NC) recoupment charges on sales of DoD-developed items and technology to non-U.S. Government (USG) customers, assigns responsibilities, and prescribes procedures to implement established policies.

B. APPLICABILITY AND SCOPE

1. This Directive applies to the Office of the Secretary of Defense, the Military Departments, the Organization of the Joint Chiefs of Staff, the Unified and Specified Commands, and the Defense Agencies (hereafter referred to collectively as "DoD Components").

2. Its provisions shall be applied contractually to DoD contractors and recipients of DoD technical data packages (TDPs) who sell defense articles or technology developed with DoD appropriations or funds (and in special cases, customer funds) or use such technology to manufacture items sold commercially to a foreign government, international organization, foreign commercial firm, domestic organization, or private party.

3. Its provisions do not apply to sales of excess property when accountability has been transferred to property disposal activities and the property is sold in open competition to the highest bidder.

C. DEFINITIONS

The terms used in this Directive are defined in enclosure 1.

D. POLICY

Non-USG purchasers shall pay a fair price, determined in accordance with this Directive, for the values of the DoD nonrecurring investment in the development and production of defense articles and/or development of technology, unless an NC recoupment charge waiver has been approved by the DoD official designated in section G. of this Directive. Approved revised NC recoupment charges shall not be applied retroactively to accepted Foreign Military Sales (FMS) agreements or to direct sales that were entered into before the date of approval of the revised NC recoupment charge. When defense items are sold at a reduced price due to age or condition, the NC recoupment charge shall be reduced by the same percentage reduction.

E. RESPONSIBILITIES

1. The Under Secretary of Defense for Research and Engineering (USDR&E) shall monitor and exercise control over NC cost recoupment aspects of domestic commercial sales of DoD-developed items and technology and shall take appropriate action to revise the DoD FAR Supplement (reference (d)) to agree with this Directive.

2. The Under Secretary of Defense for Policy shall monitor the application of this Directive and exercise control over foreign sales of DoD-developed items and technology.

3. The Assistant Secretary of Defense (Comptroller) (ASD(C)) shall provide necessary cost accounting guidance and ensure publication of a listing of DoD-developed items or categories of technology to which NC recoupment charges are applicable.

4. The Director, Defense Security Assistance Agency (DSAA), shall serve as the DoD focal point for review and approval of NC recoupment charges for major defense equipment (MDE) items and for processing NC recoupment charge waiver requests received from foreign countries and international organizations for FMS or direct commercial sales. Notification of approved NC recoupment charges for MDE items shall be provided to the Deputy Assistant Secretary of Defense (Management Systems) (DASD(MS)).

5. The Heads of Military Departments and Defense Agencies shall:

a. Determine the DoD nonrecurring investment in DoD-developed items or technology and perform required pro rata calculations in accordance with cost accounting guidance from the ASD(C).

b. Validate and provide recommended charges for MDE items to DSAA.

c. Determine the appropriate charges for non-MDE articles and technology.

d. Provide the approved non-MDE item and technology charges to the DASD(MS).

e. Insert prescribed reference (d) clauses in contracts.

f. Enforce the application of the aforementioned clauses.

g. Deposit collections to accounts prescribed by the ASD(C).

h. Submit quarterly reports of anticipated and actual NC recoupment charge collections to the DSAA.

6. The Director, Defense Contract Audit Agency (DCAA), shall ensure that any evaluation of a contractor accounting system includes an analysis of the internal controls established to ensure compliance with the requirement to pay NC recoupment charges. If DCAA audit work on a bid proposal, claim for incurred costs, etc., discloses contractor noncompliance with the requirement to pay an NC recoupment charge, an audit report shall be issued promptly to the cognizant DoD contracting officer, with a copy of the report submitted to the DASD(MS).

F. PROCEDURES

All DoD Components shall follow the implementing procedures contained in enclosure 2.

G. WAIVERS (INCLUDING REDUCTIONS)

1. The Arms Export Control Act (reference (b)) requires the recoupment of a proportionate amount of nonrecurring costs of MDE from FMS customers but authorizes consideration of reductions or waivers for particular sales which, if made, significantly advance USG interests in North Atlantic Treaty Organization standardization or standardization with the Armed Forces of Japan, Australia, or New Zealand in furtherance of the mutual defense treaties between the United States and those countries. Waiver for direct commercial sales and for non-MDE items under FMS shall be based upon the same considerations.

2. Requests for waivers of NC recoupment charges for eligible countries for sales of DoD-developed items under the FMS program or on direct commercial sales to foreign governments and international organizations shall be submitted to the Director, DSAA.

a. Requests should originate with the foreign government and shall provide information regarding the extent of standardization to be derived as a result of the waiver and other benefits that would accrue to the USG as a result of the sale. The request shall contain a summary statement of the facts regarding the program, benefits expected and justification therefor, and any calculations necessary to quantify the waiver and the benefits to the USG.

b. Blanket waiver requests shall not be submitted nor considered. The term "blanket waiver" refers to an NC recoupment charge waiver that is not related to a particular sale; for example, waivers for all sales to a country or all sales of a weapon system.

c. A waiver request shall not be approved for a sale that was accepted without an NC recoupment charge waiver, unless the acceptance was conditional upon approval of the waiver. A waiver shall not be granted in connection with a direct commercial sale if such a waiver could not have been granted legally

in connection with a sale made under the FMS program. Any waiver approved for a direct commercial sale requires a certification by the contractor that reductions have been passed on to the customer.

3. A DoD Component or defense contractor (vice president or higher) may request waivers of NC recoupment charges for domestic sales of DoD-developed items. Contractor requests shall be submitted through the appropriate contracting officer to the USDR&E. To the extent possible, the request shall provide information regarding the dollar value of the waiver, benefit to be derived by the Department of Defense, the names of foreign and domestic competitors, impact on the USG balance of payments, demonstrable rights of the manufacturer or purchaser, and any other justification for the waiver. Blanket waiver requests for domestic sales are discouraged, but may be granted in extraordinary circumstances.

4. Requests for waivers shall be processed expeditiously, and a decision normally made by the approving authority (see subsection G.6., below) to either approve or disapprove the request within 60 days after receipt. A waiver in whole or in part of the recoupment charge or a denial of the request shall be provided in writing to the appropriate DoD Component before issuance of the FMS agreement or signing of the commercial contract.

5. The decision on any waiver requires the concurrence of the Director, DSAA; the ASD(C); and the USDR&E. If an issue concerning the waiver request cannot be resolved, the normal waiver approval authority shall prepare an action memorandum on the waiver request to the Deputy Secretary of Defense for final determination. The action memorandum to the Deputy Secretary of Defense shall be coordinated with the Director, DSAA; the ASD(C); and the USDR&E.

6. The Director, DSAA, is the waiver approval authority and will state in writing any approvals granted for waivers associated with FMS and direct foreign sales. The USDR&E is the waiver approval authority and will state in writing any approvals granted for waivers involving sales of DoD-developed items and technology to domestic organizations. This authority shall not be redelegated. A notification of each approved waiver will be forwarded to the ASD(C) and to the concerned DoD Components by the approving authority.

H. INFORMATION REQUIREMENTS

The record keeping and reporting requirements prescribed in subsection H.2. of enclosure 2 are assigned Reports Control Symbol DSAA(Q)1112.

I. EFFECTIVE DATE AND IMPLEMENTATION

This Directive is effective immediately for all NC recoupment calculations that have not been approved previously. Forward two copies of implementing documents to the Assistant Secretary of Defense (Comptroller) within 120 days.

William H. Taft, IV
Deputy Secretary of Defense

Enclosures - 5
1. Definitions
2. Implementing Procedures
3. Format for MDE Calculation
4. Recoupment of Nonrecurring Costs on Sales of MDE Items
5. Recoupment of Nonrecurring Costs on Sales of Products and Technology

DEFINITIONS

1. Cost Pool. Represents the total cost to be distributed across the specific number of units. The nonrecurring research, development, test, and evaluation (RDT&E) cost pool comprises the costs described in definition 11. The nonrecurring production cost pool comprises costs described in definition 10.

2. Direct Sale. A commercial sale to a customer by a defense contractor of products, technology, materiel, services, and development or production techniques that originally were developed, improved, or produced using DoD appropriations or funds.

3. Domestic Organization. Any U.S. non-governmental organization or private commercial firm.

4. Foreign Military Sale (FMS). A sale of defense articles or defense services to a foreign government or international organization under authority of the Arms Export Control Act (reference (b)).

5. Government Sale. A sale of articles or services, or both, to customers by any DoD Component under appropriate statutes.

6. Major Defense Equipment (MDE). Any item of significant combat equipment on the United States Munitions List having a nonrecurring RDT&E cost of more than $50 million or a total production cost of more than $200 million.

7. Model. A basic alpha-numeric designation within a weapon system series, such as a ship hull series, an equipment or system series, an airframe series, or a vehicle series. For example, the F5A and the F5F are different models within the same F-5 system series.

8. Non-Major Defense Equipment (Non-MDE). Any item of equipment or component that is not identified as major defense equipment.

9. Non-U.S. Contractor. A contractor or subcontractor organized or existing under the laws of a country other than the United States, its territories, or possessions.

10. Nonrecurring Production Costs. Those one-time costs incurred in support of previous production of the model specified and those costs specifically incurred in support of the total projected production run. These NCs include DoD expenditures for preproduction engineering; rate and special tooling; special test equipment; production engineering; product improvement; destructive testing; and pilot model production, testing, and evaluation. This includes costs of any engineering change proposals initiated before the date of calculations of the NC recoupment charge. Nonrecurring production costs do not include DoD expenditures for machine tools, capital equipment, or facilities for which contractor rental payments are made in accordance with the DAR or DoD FAR Supplement (references (e) and (d), respectively) or asset use charges assessed in accordance with DoD 7290.3-M (reference (f)).

11. Nonrecurring Research, Development, Test, and Evaluation (RDT&E) Costs. Those costs funded by an RDT&E appropriation to develop or improve the product or technology under consideration either through contract or in-house effort. This includes costs of any engineering change proposal initiated before the date of calculation of the NC recoupment charges as well as projections of such costs, to the extent additional effort applicable to the sale model or technology is necessary or planned. It does not include costs funded by either procurement or operation and maintenance (O&M) appropriations.

12. Pro Rata Recovery of Nonrecurring Costs (NC). Equal distribution (proration) of a pool to a specific number of units that benefit from the investment so that a DoD Component will collect from a customer a fair (pro rata) share of the investment in the product being sold.

13. "Special" RDT&E and Nonrecurring Production Costs. Costs incurred at the request of, or for the benefit of, the customer in developing a special feature or unique requirement. These costs must be paid by the customer as they are incurred.

14. Technology. Information of any kind that can be used or adapted for use in the design, production, manufacture, utilization, or reconstruction of articles or materiel. The data may take a tangible form, such as a scale model, prototype, blueprint, or an operating manual, or may take an intangible form, such as technical advice.

IMPLEMENTING PROCEDURES

A. GENERAL

1. Each DoD Component, defense contractor, or recipient of DoD TDP negotiating the sale of items or technology, or both, developed with DoD appropriations or funds shall ensure the assessment of the charges as set forth in this implementing procedure.

2. Each DoD Component shall establish a system to accumulate cost pools, recognize when a cost pool meets recoupment thresholds and calculate an NC recoupment charge for items or technology releasable to foreign countries and international organizations when FMS or direct commercial sales are anticipated. The NC recoupment charge shall be based upon information recorded in DoD accounting records or DoD budget justification documents. Cost estimates may be used to determine the NC expected to be incurred in periods not covered by budget justification documents.

3. The NC recoupment charge computation (nonrecurring RDT&E and nonrecurring production cost pools divided by benefitting units) for the sale of MDE items shall be submitted to the Director, DSAA, for approval. The NC recoupment computation shall be supported with the MDE calculation worksheet illustrated at enclosure 3. A summary report on each MDE item shall be provided to DSAA following the format illustrated at enclosure 4. The Director, DSAA, will review each DoD Component's calculations and provide approved NC recoupment charges for MDE items to the DoD Component and the DASD(MS).

4. Once the approved charge has been used in an authorized sale, the charge normally will not be revised until a model change occurs or a major new development program occurs that changes the operational capability of the end item.

a. Each DoD Component shall review approved MDE charges annually to determine if there has been significant change in factors or assumptions used to compute the original NC recoupment charge established for a model (for example, a significant change in identifiable RDT&E costs or the anticipated production run). A significant change occurs when a new calculation shows either a change of more than 30 percent of the current system NC recoupment charge for an MDE item or, for ammunition items, the potential for a change of over $100,000 aggregate on future sales collections exists.

b. When significant changes are identified for MDE and/or when a model change occurs, the DoD Component shall submit a request to the Director, DSAA, for consideration of appropriate changes in future NC recoupment charges. The Director, DSAA, normally shall respond to the request in writing within 60 days after receipt of the request.

5. When a defense contractor negotiates the direct sale of a DoD-developed item or technology, or a derivative of a USG-developed item, he or she shall request the amount of the NC recoupment charge from the Administrative Contracting Officer (ACO) or (for technology sales) the technology charge from the DoD Component responsible for DoD acquisition of the article.

a. When making this request, the contractor shall submit such information as may be necessary to comply with this Directive. If the NC recoupment charge has not been established already, as provided for under this Directive, the ACO shall contact the DoD Component responsible for establishment of the charge and advise the contractor of the estimated date the charge will be made available.

b. Despite the absence of an established charge, the contract shall provide for full recovery of such charge in the amount that is subsequently established. The recovery will be for the total items sold and not merely applied on a prospective basis from the date the charge is established.

6. All DoD contracts for RDT&E or acquisition shall include a mandatory clause that requires the contractor to pay the USG, within 30 days following delivery of each item from the contractor's facility or purchaser's acceptance (whichever comes first), the established NC recoupment charge for any domestic or international direct sale, coproduction, or licensed production of DoD-developed items or technology (see DoD FAR Supplement 25.7306, 35.71, and 52.235-7002, reference (d)).

7. It is mandatory that each DoD Component complete and submit to DSAA for approval, a proposed NC charge not later than 60 days after award of a DoD contract for RDT&E or acquisition whenever there is a potential for commercial sale of an item (see subsection A.5., above). The ACO is responsible for initiating this action into appropriate Military Department channels and for notifying the contractor of the appropriate charge.

8. The cognizant DoD Component shall deposit collections in payment of an NC recoupment charge without delay in the nearest Federal Reserve Bank to accounts prescribed by the ASD(C). Notification of the deposit shall be provided to the DoD Component activity responsible for submission of reports required in subsection H. of this enclosure.

B. CALCULATION OF CHARGES ON MDE AND COMPONENTS

MDE items are defined in enclosure 1. The determination of whether an item meets the MDE dollar threshold shall be based on obligations recorded to the date the equipment is offered for sale. Production costs shall include cost incurred for the Department of Defense, FMS, and known direct sales production. For the FMS program, the sales offer date shall be the date a Letter of Offer and Acceptance (LOA) is signed by a U.S. official and released to the FMS customer; for commercial sales, the sales offer date shall be the date of contract signature.

1. NC recoupment charges shall be assessed on a pro rata basis. The charges shall be established by dividing the total of NC investment (nonrecurring RDT&E + nonrecurring production) incurred to date plus projections of future costs to be incurred, by the total estimated number of units projected to be produced over the life of the system (including DoD requirements, Military Assistance Program (MAP) requirements, FMS requirements, and direct commercial sales requirements). The computation of the cost pool shall exclude costs for those items that are restricted to USG use only (for example, U.S.-unique nuclear devices, countermeasures, security devices, and aircraft carrier-unique adaptations).

2. The number of units to be produced for DoD shall be obtained from budget backup data. FMS quantity projections and direct commercial sales quantity projections shall be derived jointly as best estimates by the Military Department and DSAA. Defense contractors should be consulted in determining direct commercial sales quantities, if necessary. When disagreement on estimated FMS and direct commercial quantities and sales projections occur, the Director, DSAA, will make the final determination in coordination with the ASD(C) and the USDR&E.

3. For a weapon system that includes more than one component that meets the MDE threshold or contains a component that has application to several weapons systems or a commercial sale potential, hereinafter referred to as a major individual component, a "building block" approach (that is the sum of NC recoupment charges for individual components) shall be used to determine the NC recoupment charge for the sale of the entire system.

a. Data must be accumulated for each major component when NC is identified in accounting records or budget documents. The sum of the various component NC recoupment charges and any remaining NC for the weapon system shall be applied to the sale of a complete system. Individual NC recoupment charges shall be applied to sales of individual components. The format for performing the required calculation is at enclosure 3.

b. DoD Components involved with a sale shall ensure that components are not purchased separately for ultimate assembly as an end item in an attempt to circumvent this Directive.

4. The established NC recoupment charge shall be included in the FMS unit price or, for commercial sales, provided to the seller, and paid by the seller to the USG.

5. If a commercial item being sold is substantially different (less than 90 percent common) from the USG item for which the NC recoupment charge was developed, the charge shall be assessed based on the extent of commonality with the USG item. For example, if the commercial item is 25 percent common with the DoD item, then only 25 percent of the established NC recoupment charge for the DoD item shall be assessed. The DoD Component office with system engineering responsibility for the item shall be responsible for determining the degree of such commonality.

a. The cognizant DoD contract administrative office shall request DCAA to review contractor accounting records to ensure that the commercial item was not fully or partly funded by charges against DoD contracts.

b. The contract administration office shall provide its calculations and rationale to DSAA for review and approval. Upon receipt of the DSAA approval, the DoD Component shall notify the contractor in writing of the applicable derivative NC recoupment charge.

6. If records necessary to enable a pro rata NC calculation have been lost or destroyed for particular MDE items in which the USG has an NC investment, the DoD Component (Assistant Secretary or a designee) shall certify that the records have been lost or destroyed and shall determine a unit NC

recoupment charge equal to 4 percent of the most recent USG contract price. The certification of lost or destroyed documents and recommended fixed charge per unit shall be forwarded to the Director, DSAA, for approval. The Director, DSAA, shall then establish a fixed unit NC recoupment charge for all subsequent sales.

C. CALCULATION OF CHARGES ON NON-MAJOR DEFENSE EQUIPEMENT

NC recoupment charges on Non-MDE shall be established in accordance with procedures set forth in this subsection. Once established, the charge normally shall not be revised unless the item subsequently qualifies as an MDE item. When a non-MDE item becomes an MDE item, a new NC recoupment charge shall be established using MDE procedures. The DoD Components shall provide established charges for non-MDE to the DASD(MS) for publication in a document that is readily accessible by DoD Components, contractors, and the public.

1. Components of MDE Items. The pro rata amount, as determined through use of the building block approach, required by in subsection B.3., above, shall be assessed whenever a major component is sold. There shall be no charge on sales of other components because applicable NC recoupment charges are recovered on MDE item sales.

2. Non-MDE End Items. A percentage NC recoupment charge shall be assessed on non-MDE end items whenever $2 million of RDT&E funded cost has been or is expected to be incurred on the item. The applicable surcharge shall be 5 percent of the item's current DoD inventory price.

3. Modification Kits

a. Developed to Provide an End Item With New or Improved Capability. An NC percentage charge shall be made whenever $2 million of RDT&E, procurement, or O&M funds have been expended on engineering, development, or testing of the kit. The applicable surcharge shall be 5 percent of the selling price of modification kits transferred under the FMS program or sold commercially by U.S. contractors.

b. Developed to Improve the Safety, Reliability, Availability, and Maintainability. The costs of improvement programs that are designed to continuously improve the safety, reliability, availability, and maintainability of an end item or major component over the projected life of the item will be shared equitably by all users of the item. Normally, each user will pay a share of the total annual cost through a Component Improvement Program (CIP) or comparable program. All users are expected to participate in such programs. However, if a user does not participate in a CIP or comparable program, the user will pay an appropriate share of the development costs for any modification purchased after delivery of the system. The calculation of these charges is as follows:

(1) New items. For new items entering the system, the cost sharing calculation will be established at the time the NC cost pool is established and the NC recoupment charge is approved. First, the total life of the item will be projected, then the point in time when half of all projected deliveries to non-DoD customers will occur will be estimated. Using actual cost data and data from historical files for similar CIP or comparable programs, the

total U.S. investment costs over the life of the program will be estimated. The amount of U.S. investment projected to be incurred up to the previously determined point of half of the deliveries to non-DoD customers will be included in the weapon system NC cost pool. The annual cost of operating the CIP or comparable program will be shared in proportion to the number of items in the possession of each user. This will ensure that the remaining costs of operating the CIP or comparable program will be shared equally by all users of the item.

(2) Existing Items/Improved Items. For items already in the inventory that have established NC pro rata charges, or for improved items that meet the criteria for NC pro rata charge revision, all U.S. investment costs incurred before the date of calculation of the revised NC recoupment charge will be included in the NC cost pool. Additionally, all users shall be required to pay on an annual basis in proportion to the number of existing items for participation in the program.

(3) Modification Kits. Modification kits designed to improve safety, reliability, availability, and maintainability are issued to FMS customers and incorporated into end item/major components without the additional NC recoupment charge because the applicable development cost is either included in the end item/major component NC recoupment charge or recouped as CIP or comparable program charges on the end item or major components. In exceptional circumstances when a user does not participate in the CIP or comparable program, the user shall be assessed an NC charge for any modifications purchased after delivery of the systems. This charge shall be based on 5 percent of the acquisition cost of each modification kit.

4. Components of Non-MDE End Items. A percentage NC recoupment charge shall be made on any non-MDE item component whenever $2 million of RDT&E appropriations has been or is expected to be expended on the component. The applicable charge shall be 5 percent of the component's current FMS selling price for components transferred under the FMS program or sold commercially by a U.S. contractor.

D. CALCULATION OF CHARGES FOR TECHNOLOGY SALES

The procedures for the calculation of charges after receipt of authorization to release technology are as follows:

1. Technical Data Packages

a. An NC recoupment charge shall be assessed for the transfer and use of TDPs to be used to manufacture or produce items for non-USG use. This charge is in addition to normal costs associated with reproduction and shipping of TDPs. Charges for the use of TDPs normally are referred to as royalty fees. However, for MDE items, the approved MDE NC recoupment charge shall be assessed for each item manufactured or coproduced in place of a royalty fee.

b. For a non-MDE item, an NC percentage surcharge shall be applied as the royalty fee on the basis of the item's current DoD inventory price. Prescribed charges for non-MDE items are as follows:

(1) Foreign Governments and non-U.S. contractors - 5 percent on items manufactured for in-country use and 8 percent on items manufactured for third party use by or on behalf of foreign governments or international organizations.

(2) U.S. Contractors - 3 percent on items manufactured for consumption in the U.S. and 5 percent on items manufactured for export.

c. The above charges will be deemed necessary to constitute the "fair market price" for U.S. technology.

d. A TDP developed with USG funds shall not be released to any non-USG parties, including contractors, unless the recipient has agreed in writing to pay the applicable charges prescribed by this Directive and to pay applicable charges within 30 days after manufacture of applicable items.

2. Software. A charge shall be made for sales of software whenever $2 million or more has been, or is expected to be, expended by the DoD Component to develop the software regardless of appropriation account. The charge shall be a pro rata charge. The numerator shall be the cost incurred by the DoD Component. The denominator shall be either the number of weapons systems to be supported by the software package or the number of software packages to be duplicated, whichever is the most equitable in the opinion of the DoD Component.

3. Other Technology Transfers. For all other technology transfers, including transfers of TDPs for purposes other than manufacturing, and all transfers of industrial or manufacturing processes, the amount of the charge shall equal the fair market value of the technology involved. For transfers to any U.S. domestic organization, this charge shall be the lower of either: (a) a proportionate share of the DoD investment cost identified to the development of the technical data and technology involved; or (b) a fair market price for the technical data and technology involved based on an engineering analysis of demand or the potential monetary return on investment. For transfers to any non-U.S. contractor or other foreign customer, this charge will be the greater of the foregoing two alternatives. Accordingly, the lower domestic price shall be applied only if the prospective domestic purchaser signs a written commitment to the Department of Defense that the technical data and technology shall not be transferred to any other party.

E. JOINT DOD COMPONENT DEVELOPMENT EFFORTS

DSAA shall designate a lead DoD Component to perform a consolidated calculation when appropriations of more than one DoD Component are involved in the NC investment of an MDE item.

F. "SPECIAL" RDT&E AND NONRECURRING PRODUCTION COSTS

1. The full amount of "special" RDT&E and nonrecurring production costs incurred for the benefit of particular customers shall be paid by those customers. However, when a subsequent purchaser requests the same specialized features that resulted from the added "special" RDT&E and nonrecurring production costs, a pro rata share of these costs may be paid by the subsequent purchaser and transferred to the original customer provided those special nonrecurring costs exceed $5 million. The pro rata share may be a unit charge determined

by the DoD Component as a result of distribution of the total costs divided by the total production. Such reimbursements shall not be transferred to the original customer if 8 years have elapsed since acceptance of DD Form 1513, "U.S. DoD Offer and Acceptance," by the original customer, unless otherwise authorized by DSAA. The USG shall not be charged any NC recoupment charge if it adopts the features for its own use or provides equipment containing such features under a U.S. Grant Aid or similar program.

2. For coproduction, codevelopment and cooperative development, or cooperative production agreements, the policy set forth in this Directive generally shall determine the allocation basis for recouping from the third party purchasers the investment costs of the participants. Such agreements shall provide for the application of the policies in this Directive to sales to third parties by any of the parties to the agreement and for the distribution of recoupments and technology charges among the parties to the agreement.

G. MUNITIONS EXPORT LICENSE APPLICATION REVIEWS

Military Departments shall comment routinely on nonrecurring cost recoupment candidacy as a part of their review of Munitions Export license applications. Sales that are obviously recoupment candidates should be identified to DSAA along with the recommendation that the exporting contractor be informed of the requirement for recoupment and that for specifics, the DoD plant representative should be contacted.

H. REPORTING NC RECOUPMENT COLLECTIONS

1. Funds collected for NC recoupment charges shall be disposed of in accordance with ASD(C) instructions.

2. DoD Components shall provide a quarterly report on the status of NC collections. The Reports Control Symbol is DSAA(Q)1112 (format at enclosure 5). The report shall be forwarded to the DSAA Comptroller within 45 days following the close of each fiscal quarter, with a copy furnished to the DASD(MS). Components shall maintain records of anticipated and actual NC charge collections for the FMS case and known direct commercial sale. Data on direct commercial sales may be obtained from export licenses or from other information provided by DSAA.

FORMAT FOR MDE CALCULATION
(With Illustrative Entries)

Date Prepared

DoD Component

Preparer's Name,
Job Series, and Grade

ITEM DESCRIPTION:

Identification No.:

PART A - NONRECURRING R&D INVESTMENT (NUMERATOR)

	R&D Projects			
	X	Y	Z	Total
Major Components				
Air Frame	80,000,000			$80,000,000
Engine (JXX)		58,000,000		58,000,000
Radar			5,000,000	5,000,000
Avionics	1,000,000			1,000,000
Undistributed to Component	20,000,000			20,000,000
Air Vehicle				$164,000,000

PART B - NONRECURRING PRODUCTION INVESTMENT (NUMERATOR)

	AF 1537 Sep 1, 1981	Contract XX	Contract ZZ	Total
Major Components				
Air Frame	5,000,000			$ 5,000,000
Engine (JXX)	7,000,000			7,000,000
Radar	3,000,000			3,000,000
Avionics	5,000,000			5,000,000
Undistributed to Component	10,000,000			10,000,000
Air Vehicle				$30,000,000

PART C - PROJECTED UNITS (DENOMINATOR)

	Source Documents					
	DoD Quantities		MAP/FMS		Commercial Est. by Contracting	
	FYDP Proc. Annex	ADP Project 311	5 - Year Security Assistance Plans	ADP Project 311	Officer	Totals
Air Frame		1,500		850		$2,350
Engine (JXX)		3,050		2,500	2,000	7,550
Radar		2,700		950	100	3,750
Avionics		1,500		850		2,350
Air Vehicle	1,500		750			2,250

PART D - COMPONENT NC

	R&D	Production	Total	Projected Units	Unit NC Recoupment Charge
Major Components					
Air Frame	$80,000,000	$ 5,000,000	$85,000,000	2,350	$36,170 (1)
Engine (JXX)	58,000,000	7,000,000	65,000,000	7,550	8,609 (1)
Radar	5,000,000	3,000,000	8,000,000	3,750	2,133 (2)
Avionics	1,000,000	5,000,000	6,000,000	2,350	2,553 (2)
Undistributed	20,000,000	10,000,000	30,000,000	2,250	13,334 (3)

PART E - SYSTEM NC CHARGE

1. Current Development Costs:

Air Frame (1 each system)	$36,170
Engines (2 each system)	17,218
Radar (1 each system)	2,133
Avionics (1 each system)	2,553
Undistributed (allocated to end items)	13,334

2. GFM Development Costs:

ISS Cannon (2 each system)	500
HR X Radio (1 each system)	250
XM Bomb Sight (1 each system)	300
Access II Scat (1 each system)	700
TOTAL SYSTEM CHARGE	$73,158 (1)

Notes

(1) Unit NC recoupment charge calculation for MDE item must be submitted to DSAA for review and approval.
(2) Unit NC recoupment charge for non-MDE item is added to DoD Component schedule of non-MDE charges and reported to the DASD(MS) for publication.
(3) Undistributed systems' NC is recouped on end items.

RECOUPMENT OF NONRECURRING COSTS ON SALES OF MDE ITEMS	DATE PREPARED	DOD COMPONENT
	AS OF DATE	NAME AND TELEPHONE NUMBER OF CONTRACT POINT

SECTION A

(a)	(b)			(c)						(d)			(e)
WEAPON SYSTEM OR COMPONENT	NONRECURRING COSTS *($ THOUSANDS)*			PRODUCTION QUANTITY						RECOMMENDED PPO RATA UNIT CHARGE			PREVIOUS UNIT CHARGE
	R&D&E	PRODUCTION	TOTAL	ARMY	MARINE NAVY	AIR FORCE	MAP FMS DIRECT SALE		TOTAL	R&D&E PRODUCTION		TOTAL	

SECTION B

PRODUCTION QUANTITIES

	ACTUAL		PROJECTION		TOTAL
MAP					
DIRECT SALE					
FMS					
TOTALS					

Completion of Section C on Reverse is Required

RECOUPMENT OF NONRECURRING COSTS ON SALES OF USG ITEMS AND TECHNOLOGY

Department of the _____
($ Thousands)

Reports Control Symbol: DSAA(Q)1112
Report Preparation Date _____
Report Cutoff Date _____

Case Designator (1)	Purchaser	Item	Quantity	Fiscal Year of Sale	Delivery Date (4)	Total Anticipated NC Charge (2)(3)	Actual Collections: Amount Collected This Quarter	Actual Collections: Amount Collected This Fiscal Year to Date	Actual Collections: Cumulative Collections (5)

Part 1. Recoveries on USG sales to foreign governments and international organizations.

Part 2. Recoveries on direct sales to foreign governments, international organizations, and foreign commercial firms.

Part 3. Recoveries on sales to domestic commercial firms.

Notes:

(1) Applicable to USG sales to foreign governments and international organizations. For direct sales, use the license number. For domestic sales, establish a "dummy" case number for control purpose.
(2) When collection results from the sales of technology, rather than product, place a (T) after the anticipated charge.
(3) Place an asterisk after charge when collection is completed.
(4) For proposed or pending direct sales, place a "P" in this column.
(5) Collections that are completed during the fiscal year will be dropped on the first quarterly report of the subsequent fiscal year.