

A collage of three images: soldiers in camouflage gear, a group of naval officers in blue uniforms, and two pilots in flight suits shaking hands. The background is a textured blue.

Restructure of FMS Surcharges

Frequently Asked Questions

Department of Defense

Defense Security Cooperation Agency



Restructure of FMS Surcharges FAQs

1-What is the Administrative Surcharge?

The Arms Export Control Act (AECA) requires the U.S. Government to recover the full estimated cost of administration of Foreign Military Sales (FMS). The AECA mandates collection of a percentage-based Administrative Surcharge on FMS cases to recover all applicable U.S. costs to execute, manage, and oversee the FMS program. This surcharge is assessed against the value of the FMS case for defense articles and services on FMS or FMS-like cases and collected from payments made by the purchasing country or international organization.

2-What will the new Administrative Surcharge rate be?

The new rate will be 3.8 percent effective Aug. 1, 2006. This new rate will apply to any new cases “accepted” on or after that date. Any cases accepted prior to Aug. 1, 2006 will continue to be assessed the rate that was in effect at the time they were implemented— with the exception that any new lines added to these cases via amendments “accepted” on or after Aug. 1, 2006 will be charged the new rate.

3- Why a rate change now?

At the current Administrative Surcharge rate of 2.5 percent, FMS administrative costs exceed revenues. We have been reducing expenses and must now increase income to recover our costs to ensure the continued solvency of the FMS Trust Fund Administrative Account. Without this rate increase, we project the FMS Trust Fund Administrative Account would effectively become insolvent sometime in FY09.

4-When was the last Administrative Surcharge change?

The last FMS Administrative Surcharge change was in 1999 when the rate was lowered from 3.0 percent to 2.5 percent. Prior to that change, the

rate had been 3.0 percent since 1977.

5-Why did DSCA lower the Administrative Surcharge rate in 1999?

When the rate was lowered from 3 percent to 2.5 percent in 1999, we carried what some viewed as an excessive balance (also known as the “reserve”) in the FMS Trust Fund Administrative Account. The balance/“reserve” at that time was in excess of \$500M resulting from a period in the late 1980s to mid 1990s when FMS sales generated revenues faster than we incurred expenses to manage the program.

6-What do you mean by balance/“reserve” and why is it necessary?

Some “reserve” in the FMS Trust Fund Administrative Account is necessary to ensure that the balance never reaches \$0. We’ve determined that the FMS Trust Fund Administrative Account should not fall below \$250 million – we refer to this as a “Healthy Balance.” Part of this “reserve” in the balance is to:

- A. Allow for fluctuations in revenues and costs caused by low annual sales, capital investments (such as Information Technology), etc.
- B. Allow for payment of costs that are “due” at the beginning of the fiscal year including salaries and payments due on FY contracts that support the execution of our programs.
- C. Provide a sufficient buffer against bankrupting the program.

7-Are you making other changes to the FMS charge structure?

Yes, also effective Aug. 1, 2006 we will:

Update guidance to clarify FMS case related activities covered by the Administrative Surcharge and to ensure the consistent application of those activities.

Add a new “Small Case” Management Line policy to ensure that all cases collect a minimum of \$15,000 to cover administrative costs. This is necessary to ensure we recover costs necessary to write and implement smaller cases.

Eliminate the 5-percent surcharge for provision of non-standard support. Any lines for non-standard defense articles or services included on cases accepted on or after Aug. 1, 2006 will only be charged the standard 3.8 percent rate. Any lines that exist prior to of Aug. 1, 2006 with the 5-percent charge will continue to be assessed this non-standard support rate.

No later than October 2007, we will eliminate the Logistics Support Charge (LSC). This charge, assessed against specific logistics-related defense articles and services, is 3.1 percent.

8-What activities are covered by the Administrative Surcharge?

The work covered by the Administrative Surcharge includes case writing, case management/execution (cost, schedule, performance), case closure, periodic case review, etc. For a detailed list on what case-related activities are covered by the Administrative Surcharge please see the Security Assistance Management Manual (SAMM), Chapter 5, Table C5.T6 on our website (link <http://www.dsca.mil/samm/>). We will update this table as necessary to clarify FMS case related activities covered by the Administrative Surcharge.

9-What activities are not covered by the Administrative Surcharge?

SAMM Table C5.T6 includes information on specific services that may be purchased on FMS cases but would require case-funding in addition to the surcharge. For example: Meetings and reports in excess of U.S. Government-determined case management requirements; multiple iterations of Letters of Offer and Acceptance (LOAs), services provided as a membership in a US Government-sponsored group such as a Technical Coordination Group (TCG), etc.

10- How can purchasers obtain services not covered by the Administrative Surcharge?

Any service not covered by the Administrative Surcharge may be considered for case-funding – either because the FMS purchaser desires the additional support or because the U.S. Government determines that this additional support is necessary for successful delivery of the defense articles and services. A separate line (or lines) can be included on the FMS case to cover the cost of these activities.

11-What is the new “Small Case” Management Line requirement and what impact will it have on FMS cases?

We estimate that it costs a minimum of \$15,000 to prepare and process an FMS case. Because we must recover our costs, as of Aug. 1, 2006, any case that would not collect at least \$15,000 in Administrative Surcharges using the 3.8 percent calculated against the FMS case value, will include a “Small Case” Management Line to charge the difference in value between the Administrative Surcharge amount and \$15,000.

This new charge will ensure that sufficient funds are collected on all FMS cases to cover the standard service required to write and implement the case.

12-Can a small case customer minimize administrative charges?

Yes, there are two ways that a small case customer can reduce administrative charges. The first is to consolidate more purchases in fewer cases. Since this minimum charge applies to each individual case, purchasers may appropriately consolidate requirements into a single, larger FMS case that exceeds the case value to which the \$15,000 small case charge will be applied. The second is to consolidate new requirements and put them on appropriate existing cases that already exceed the maximum small case value.

13-What has DSCA done to reduce costs?

In an effort to reduce community-wide costs, we have capped FY06 spending at FY05's level and, in June 2005, we announced that operating budgets of security cooperation activities would be reduced by \$18.7M through FY09.

Further, the Director DSCA, Lt. Gen. Jeffrey B. Kohler, and his U.S. military department counterparts, established a group tasked to identify at least \$36M in projected savings through FY09. This Business Efficiencies and Action Team (BEAT) chaired by DSCA's Principal Director, Business Operations, Mr. Keith Webster, will consider process reengineering measures, identification and elimination of inefficiencies, and consolidation of functions.

14-Will the new Administrative Surcharge structure tend to drive customers away from FMS?

There are many reasons why our partners choose FMS. While cost is obviously always a consideration in a procurement strategy, we believe that it is not the only factor. Customers choose FMS to allow the U.S. Government to bring the full weight of the DoD community and its leadership into the execution and performance of the sale. Others desire to further their military-to-military relationship with the U.S. Government through FMS. In some instances, U.S. industry may prefer FMS and seek an FMS sale. These reasons remain constant regardless of surcharge changes.

We are announcing these surcharge changes now in order to allow our customers to adjust their procurement strategies to accommodate the new rates and structure.



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