



AF Life Cycle Management Center



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FMS Offsets June 2015

**David Reagan
AFLCMC/WFG
DSN: 656-2684**



Agenda



- **Definition**
- **USG Offset Policy**
- **Offset Allowability**
- **Offset Types**
- **Offset Costs**
- **Issues**
- **Breaking News**
- **Disclosure of Offset Information**



Offset Definition



- **An offset is a package of additional benefits that the seller agrees to provide or perform in addition to delivering the primary product or service**
- **Offsets generally apply only to acquisitions of major systems**
- **Offsets are recognized as a legitimate, legal business arrangement found in international acquisitions**



USG Offset Policy



- The Presidential Policy on offsets in military exports was announced by President George H.W. Bush on 16 April 1990 and was subsequently codified into law by the Defense Production Act Amendments of 1992. The key provisions of the policy on offsets are:
 - No USG agency shall encourage, enter directly into, or commit US firms to any offset arrangement related to the sale of US defense articles or services
 - USG funds shall not be used to finance offsets
 - Negotiations or decisions regarding offset commitments reside with the companies involved
 - Exceptions require Presidential approval through the National Security Council (NSC)

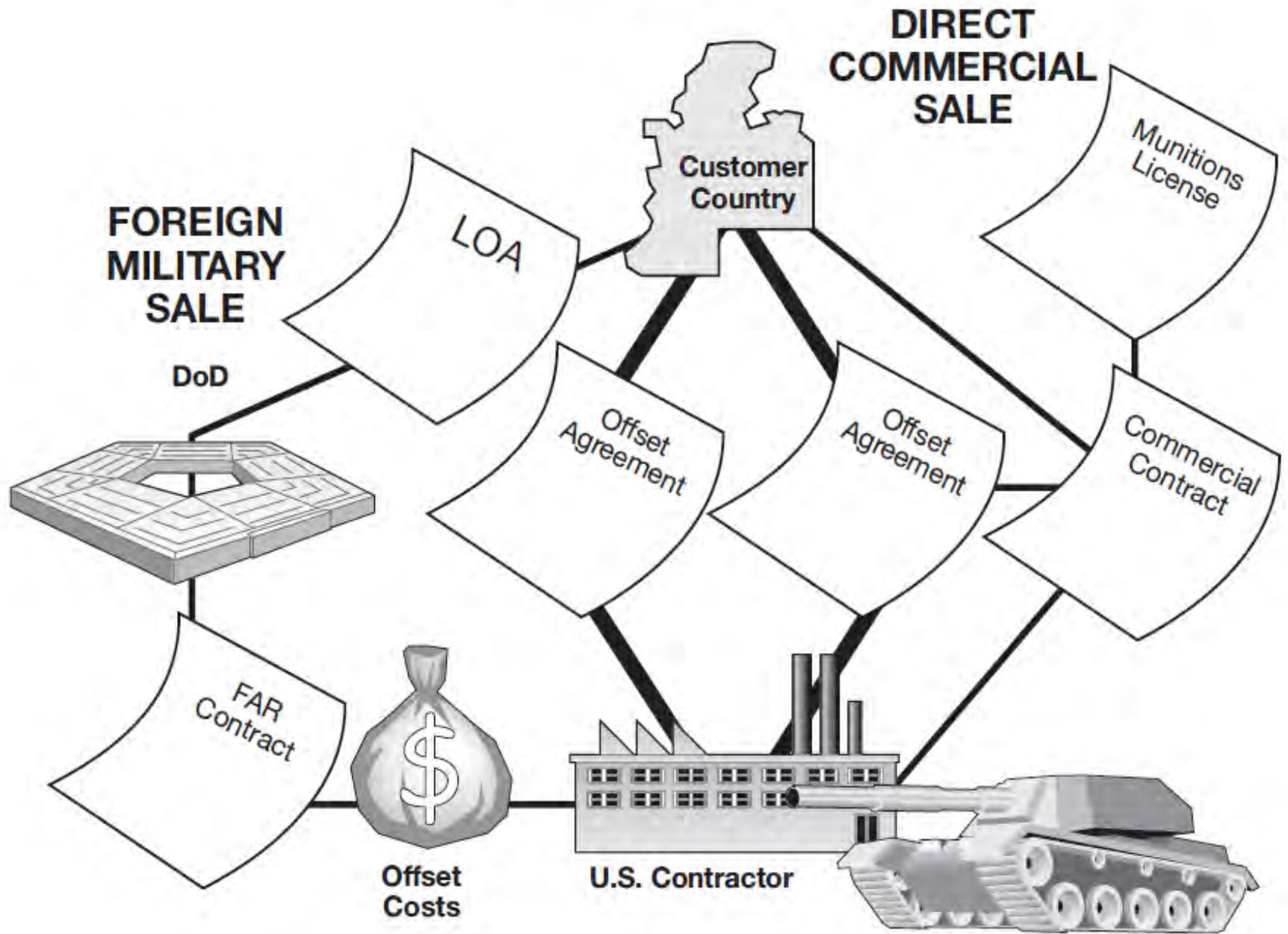


USG Offset Policy



- **Offsets are permissible under Foreign Military Sales (FMS)**
- **The offset agreement is between the purchasing country and the US contractor**
- **The USG is not a party to the agreement and does not retain any obligation to enforce the contractor's performance of the agreement**
- **The USG would prefer that offset agreements did not exist**
- **If the USG would prohibit offsets from being offered under FMS, the US firms would be at a huge disadvantage in competing internationally**

Offset Relationships





Offset Allowability



- **Offsets are permitted in association with FMS when the Letter of Offer and Acceptance (LOA) funding the procurement contract is financed by customer cash or repayable credit.**
- **If the LOA is funded by USG provided grant funds, offset costs claimed by the contractor will be considered unallowable.**



Offset Types



- **Direct Offsets:** a form of compensation provided to a purchaser that involves goods directly **related** to the item being purchased
- **Indirect Offsets:** a form of compensation provided to a purchaser that involves goods which are **unrelated** to the item being purchased



Offset Costs



- **Under FMS, the offset cost recovery process is awkward**
 - Under FMS, the contractor is actually working directly for the DOD, but the USG permits this same contractor to concurrently enter an offset agreement directly with the FMS purchaser
 - Although not a party to the offset agreement, the USG serves as the banker for the offset
 - **USG prices FMS contracts using the same principles used in pricing other defense contracts**
 - **Some exceptions (e.g. indirect offsets)**
 - **On an FMS contract, the pricing principles in FAR Parts 15 and 31 may result in prices that differ from other defense contract prices for the same item due to the exceptions**



Offset Issues



- **CO determination that offset costs are both allocable and reasonable**
 - **USG is not privy to the Offset Agreement**
 - **Where adequate price competition exists, whether conducted by the Purchaser or by the USG, the USG will not have visibility as to whether offset costs are included in the price or the amount of such costs**
 - **In noncompetitive procurements, it is the contractor's responsibility to inform the implementing agency when estimated offset costs have been included in the FMS pricing information provided.**
 - **The costs should be included in the FMS pricing information as early as possible but before submittal of the LOA.**
 - **Requests to include these costs after LOA acceptance will require an LOA modification or amendment.**



Offset Issues



- **Difficult to estimate costs because offset plans are usually not required by procuring government (FMS customer) before contract award**
- **Even when provided, offset requirements are often incompletely defined**
- **Indirect offsets are often outside the contractor's business sector, no historic experience to develop a basis of estimate**
- **Offset requirements may change and evolve over time at the customer's discretion**



Breaking News



- **DFARS Case 2015–D028 Offset Costs**

- **Issued and effective 2 June 2015**

- **DFARS 225.7303–2(a)(3)(iii)**

All offset costs that involve benefits provided by the U.S. defense contractor to the FMS customer that are unrelated to the item being purchased under the LOA (indirect offset costs) are deemed reasonable for purposes of FAR part 31 with no further analysis necessary on the part of the contracting officer, provided that the U.S. defense contractor submits to the contracting officer a signed offset agreement or other documentation showing that the FMS customer has made the provision of an indirect offset of a certain dollar value a condition of the FMS acquisition. FMS customers are placed on notice through the LOA that indirect offset costs are deemed reasonable without any further analysis by the contracting officer.



NEW Offset LOA Language



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- **LOA standard term and condition 2.8 addresses offsets. This condition summarizes the USG policy regarding offsets in association with FMS.**
 - **The USG is not a party to any offset agreements/ arrangements that may be required by the Purchaser in relation to the sales made in this LOA. The USG assumes no obligation to administer or satisfy any offset requirements or bear any of the associated costs. To the extent that the Purchaser requires offsets in conjunction with this sale, offset costs may be included in the price of contracts negotiated under this LOA. **Such costs shall be determined or deemed to be reasonable in accordance with SUBPART 225.73 of the Defense Federal Acquisition Regulation Supplement (DFARS).** If the Purchaser desires visibility into these costs, the Purchaser should raise this with the contractor during negotiation of offset arrangements."**



Disclosure of Offset Information



- **It is inappropriate for USG personnel to discuss with the foreign government the nature or details of an offset arrangement with a US contractor**
 - **However, the fact offset costs have been included in the Price and Availability Data or LOA price estimates will be confirmed, should the customer inquire**
 - **The customer should be directed to the US contractor for answers to all questions regarding its offset arrangement, including the offset costs**



Summary



- **Offsets are an international market reality**
- **The USG is not a party in the Offset Agreement but serves as the banker for the offset**
- **The offset cost recovery process is awkward and time consuming**
- **Partial relief has recently been provided in DFARS for indirect offset reasonableness determinations**
- **No changes in guidance for direct offsets**



References



- **The Management of Security Cooperation (Green Book), [Chapter 9](#)**
- **DFARS subparts 225.7303-2 and 225.7306**
- **DFARS PGI 225.7303–2(a)(3))**



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OLD Offset LOA Language



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