



National Association of Aircraft & Communication Suppliers, Inc.

THE NAACS POSITION PAPER ON DoD'S PROPOSED TERMINATION OF ITS SURPLUS SALES PROGRAM

Introduction

Over the past several years, in the wake of the inauguration of the post-9/11 "War on Terror," there have been a number of media reports, based in most instances on anecdotal evidence, alleging illegal arms and/or technology exports to embargoed nations. Media reports have also alleged that by way of exports, both legal and illegal, and by way of inadequately monitored public sales, critical military equipment and technology have found their way into terrorists' hands. The Department of Defense ("DoD") has been the target of much of this media attention because it sells its military surplus in the public marketplace, notwithstanding that its buyers are subjected to pre-sale scrutiny. After several years, during which DoD, in response, has imposed ever-more stringent guidelines governing military surplus sales, it now contemplates terminating the surplus sales program altogether.

We are submitting this position paper not simply to present our side of the story, but in order to set the record straight. DoD has routinely sold military surplus to U.S. businesses for more than sixty (60) years. Over the same period of time these U.S. businesses have served as a vital resource for the Department of Defense – for whom they warehouse an accessible inventory of surplus parts – and the active U.S. military – to whom they supply surplus parts, frequently on an emergency-delivery basis. Much of what you have heard from or read in the media is grossly distorted. The truth of the matter is that the surplus sales program is vital to the defense of this country.

The Authors

This Paper is submitted by the National Association of Aircraft & Communication Suppliers ("NAACS"). The NAACS is an organization of approximately 120 small businesses representing a broad spectrum of the aviation community. NAACS Members include: (a) spare parts distributors who supply aircraft and electronics parts to the U.S. and friendly foreign military services; (b) operators who use military aircraft in industrial and commercial lifting operations and logging; (c) aviation repair stations and facilities who install military surplus parts; and (d) companies approved by the Department of Defense ("DoD") and Federal Aviation Administration ("FAA") to manufacture parts for installation in military and commercial aircraft. Many of the military items used by NAACS Members in their respective business activities are initially obtained through the DoD surplus disposal program.

Executive Summary

- Over the past five years, DoD's Defense Reutilization and Marking Service ("DRMS"), through its contractual partner Government Liquidation, LLC ("GL"), has made sales of surplus aircraft parts to the public, including sales to NAACS Members. These surplus aircraft parts are critical for the maintenance of aircraft heavily relied upon by the U.S. military in foreign combat.

- In response to allegations of vulnerabilities in the surplus disposal program, DRMS commissioned a study of its surplus sales program; this study was conducted by IBM Company (“IBM”) and final recommendations and conclusions are not yet available.
- Nonetheless DRMS has failed to act upon a proposal from the NAACS that the government adopt a more stringent policy to pre-qualify its buyers by having them register (as the State Department does), so as to alleviate Trade Securities concerns. Instead, rather than review and revise its surplus sales policies to address any National Security concerns, in total disregard for the critical need for readily-available surplus military aircraft parts, DRMS has elected to destroy this property and in this way moot any and all National Security issues.
- Even before commissioning the IBM study, DRMS embarked upon a program of downgrading to scrap and destroying vital military surplus parts. Based on information available to it, the NAACS estimates that **over the past year, DRMS has opted to downgrade to scrap and destroy at least \$1.5 Billion worth of such vital military surplus parts**, even though many of these parts are properly categorizable as suitable for sale for commercial use.
- Thus, on a day-to-day basis, DRMS blatantly ignores the fact that as a fundamental legal principle, the destruction of federal property without justification is in violation of federal law.

NAACS And The DoD Surplus Disposal Program

DRMS, the disposal arm of the Defense Logistics Agency (“DLA”), disposes of excess property received from the military service branches and manages the overall DoD surplus property sales program. This is done through a commercial venture partnership with GL, pursuant to which GL purchases and then re-sells to the public in the United States, Guam, Hawaii, and Puerto Rico military surplus property that has not been marked for demilitarization. Currently, and historically, under DLA regulation, Demilitarization Code B and Demilitarization Code Q (“DEMIL B” and “DEMIL Q”) surplus items may be publicly sold by GL. Items designated as DEMIL B are Non-Significant Military Equipment (Non-SME) for which demilitarization is not required. Items designated as DEMIL Q are dual-use items (items used both for military and commercial purposes), for which demilitarization is not required. DEMIL Q items are generally available in the commercial marketplace, and exports of DEMIL Q items come under the jurisdiction of the Bureau of Export Administration, U.S. Department of Commerce, through the Export Administration Regulations.

Commercial businesses, including those of the NAACS Members, regularly buy military aircraft surplus parts from GL and then hold them “in stock” in hopes of selling these surplus items back to the Government at a later time. It is undeniable, and has been repeatedly recognized by the Government, that NAACS Members act as a cost-effective alternative warehouse for DoD which does not have the capability to store, maintain and inventory all of these parts itself. DoD’s only alternative to buying from warehoused stock would be to go back to the OEMs and request new production of old parts at tremendous cost to the taxpayer. Reproduction costs are so high because some military equipment currently in use may have initially been commissioned from 5 to as much as 30 to 40 years ago, or more. The OEMs for this reason cannot meet the short delivery schedules needed to support emergency military needs, whereas NAACS Members can sometimes provide overnight delivery.

The Department of Defense Office of the Inspector General (“DoD IG”) concluded in an August 9, 2000 report that surplus dealers speculating in surplus material provide a *legitimate, cost-effective, and expeditious avenue* for DoD customers, through DLA, to satisfy demands for surplus material. See DoD Office of the Inspector General Report No. D-2000-171, entitled, “*Reacquisition of Surplus Material by the Defense Logistics Agency*,” dated Aug. 9, 2000, at page 6 (emphasis added). The OIG Report concluded that if a DoD customer needed an item that was out of production, reacquiring surplus materiel from surplus dealers may cost less than if the out-of-inventory, out-of-production item were purchased from the original equipment manufacturers. *Id.* The Report also concluded that surplus can be a readily available alternative for urgent DoD requirements. *Id.*

Urgent Contracts

Further evidence of the essential role that surplus aircraft dealers have played in supporting U.S. Troop military activities is shown by the sheer volume of urgent wartime contracts that NAACS Members have performed in very recent years. Indeed, NAACS Members have received commendations from the U.S. military for their parts supply involvement in the Desert Storm and Desert Shield conflicts and continue their efforts today in the ongoing Iraqi and Afghanistan campaigns. Moreover, during just the seven (7)-month period between November 2003 and May 2004, DLA awarded nearly 400 “urgent” contracts to NAACS Members to provide critically needed replacement parts for our troops in Iraq and Afghanistan, including parts for the H-46 Sea Knight, the CH-47 Chinook, the CH-53, the OH-58, the SH-60 Seahawk, the UH-60 Blackhawk, the AH-64 Apache, and the AH series Cobra helicopters and the Hawkeye E-2C, the Orion P-3, the C-5 Galaxy, the Viking S-3B, the EA-6B Prowler, the A-10 Thunderbolt, the F-15, the F-18 Hornet, the B-52 Stratofortress, the C-130 Hercules, the KC-135 Stratolifter, and the C-141 Starlifter fixed wing aircraft. Unlike large prime manufacturers that take up to a year to fill such orders, NAACS Members supplied these needed parts, on average, in 28 days.

Therefore, it is without question that military aircraft surplus, in particular, is essential to support U.S. military operations.

National Security Concerns: Surplus Dealers versus the OEMs

DoD has increasingly expressed concerns about the security of its surplus sales program however and, in particular, about the feasibility of DoD’s continued sale of certain surplus parts to commercial contractors. These parts include parts categorized as DEMIL B and DEMIL Q military parts, F-14 parts, and possibly other Munitions List Items and Commerce Department Control List items. These security concerns purportedly led DRMS to enter into a contract with IBM under which IBM was required to perform an impact analysis of future public sales of specific Trade Security Control Items through the DoD Surplus Disposal Program (the “IBM Study”). The IBM Study was also allegedly precipitated by a June 2006 Government Accountability Office (GAO) report which alleged various vulnerabilities in the DoD surplus disposal program that might constitute National Security risks. DRMS has not shown equivalent concern about the activities of the OEMs however, even though it is the OEMs that have repeatedly violated provisions of the Arms Control Export Act through illegal export transactions.

Despite the fact that there have never been wide-spread charged violations in the surplus suppliers industry or headlines-worthy civil or criminal prosecutions of individual companies, the surplus sales program has been disproportionately subject to Government scrutiny as perpetuating National Security problems when this is obviously not the case. In contrast, a number of OEMs have been charged with such violations and have been assessed multimillion-dollar fines and penalties as a result. Several examples of recent OEM export violations are as follows:

- In January of 2002, Space Systems/Loral Inc., was assessed a fine in the amount of **\$14 million** for violating the express terms and conditions of the Department of State's munitions licenses and exporting defense services without a munitions license or other authorization to China.
- In March of 2003, Hughes Electronics Corp., and Boeing Satellite Systems were assessed fines in the amount of **\$12 million** for violating the terms and conditions of the Department of State's munitions licenses and exporting defense services without munitions licenses or other authorizations (and conduct relating to two failed launches of rockets carrying spacecraft) to China.
- In November of 2004, General Motors Corporation was assessed a fine in the amount of **\$8 million** for exporting defense articles and services (to foreign person employees of proscribed countries) in violation of the terms or conditions or other approvals that were provided by the Department of State.
- Boeing Company and Hughes Electronics Corp. were both charged with **123 violations** of the Arms Export Control Act and the ITAR for illegally transferring space-related technology including technical assistance to China, which China could use to enhance its military capability. The companies were jointly assessed **\$32 million** in fines.
- In March of 2006, Boeing was again assessed a fine for exporting unauthorized defense articles and services (to foreign person employees of proscribed countries) in violation of the terms and conditions of the International Traffic in Arms Regulations, this time in the total amount of **\$15 million**.

There is simply no legal basis for the destruction of military surplus parts that are critical to the nation's military preparedness, and so certainly there is no justification for effectively closing down the businesses that keep these parts in accessible inventories. Moreover, although there have been a small number of small-business violators of export laws and regulations, given the outstanding record established by the surplus suppliers industry overall, there is no basis for singling out that industry as a National Security risk – especially given the less-than exemplary, **unexamined** record established by the OEMs, the only alternative suppliers should the surplus sales program come to an end.

We therefore ask that you please contact DoD's Defense Logistics Agency in our behalf to urge them to continue the surplus sales program. Sales to U.S. businesses should not be interrupted.