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Over the years, criticism has been directed at the United States for its restrictive Government purchasing policies. It is inaccurate to conclude, however, that the United States is more restrictive than Great Britain, France, Germany, and Japan because of present buy-national legislation. These governments and nationalized industries also exclude most foreign competition when similar items are available domestically. The Buy American Act requires Federal agencies to procure domestic materials and products. Two conditions must be present for the Buy American Act to apply: (1) the procurement must be intended for public use within the United States; and (2) the items to be procured or the materials from which they are manufactured must be present in the United States in sufficient and reasonably available commercial quantities of a satisfactory quality. The provisions of the act may be waived if the head of the procuring agency determines the act to be inconsistent with the public interest or the cost of acquiring the domestic product is unreasonable. Contracts awarded by State and local authorities under Federal grant programs are not covered by the act unless authorizing statutes explicitly provide for application of the act. Problems in administering the act involve definitions of "substantially all" of the components and definitions of "manufactured in the United States." (RRS)

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STATEMENT OF

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DIRECTOR, INTERNATIONAL DIVISION

BEFORE THE

HOUSE SUBCOMMITTEE ON LEGISLATION AND NATIONAL SECURITY

ON

THE BUY AMERICAN ACT

Mr. Chairman and Members of the Subcommittee:

We are pleased to have you consider the findings in our report "Governmental Buy-National Practices of the United States and Other Countries--An Assessment" which was issued to the Congress on September 30, 1976. While this report was issued in 1976, we are not aware of any developments that change our views as to the conclusions we made or invalidate any of the data we reported on at that time.

We are currently initiating an assignment for the House Congressional Steel Caucus that will provide us an opportunity to review Department of Defense procurement, particularly as it relates to steel and specialty steel products. Our 1976 report dealt solely with procurement at the Federal level. We will attempt, in response to the request of the House Congressional Steel Caucus, to

obtain information as to contract awards by States or their political subdivisions to foreign firms for steel products financed largely from Federal funds. We believe the information we will develop will help the Congress in its deliberations concerning the desirability or consequences of including these transactions under the aegis of the current Act.

Regarding other concerns surrounding the present Act, we have recently provided this Committee with comments on three bills and two proposed House resolutions. We are currently commenting on three other bills with similar provisions. The bills generally propose changes in (1) the basis for determining whether a product is domestic or foreign, and (2) the percent used to adjust foreign bids in the evaluation process.

Buy-National Practices of Other Countries

Over the years, criticism has been directed at the United States for its restrictive Government purchasing policies--the Buy American Act and other buy-national legislation. It is inaccurate to conclude, however, that the United States is more restrictive than Great Britain, France, Germany, and Japan because of present buy-national legislation.

We found that these governments and nationalized industries also exclude most foreign competition when similar

items are available domestically. Rather than visible laws and regulations, however, these countries often rely on subtle administrative guidance and practices which effectively preclude most foreign competition.

The governments of Great Britain, France, Germany, and Japan generally maintain closed bidding systems and their procurement practices show a pervasive bias against foreign sources. None of the foreign government officials or U.S. businessmen we interviewed could identify any major imports by these countries of materials available from domestic sources.

Some reasons cited by their governmental officials for limiting procurement to domestic sources include (1) a traditional tendency to favor domestic sources due to familiarity and ease of dealing with local suppliers and the ready availability of service, maintenance, and repair parts; (2) a desire to protect domestic companies and jobs; and (3) the national aspirations among the European countries and Japan tending to encourage high-technology industries that are competitive with American technology.

U.S. Buy-National Policies

United States policies generally limit defense procurement to U.S. sources because of national security considerations; appropriation act limitations on textiles, subsistence items, specialty metals, and shipbuilding; and

a 50-percent price differential favoring U.S. suppliers. Foreign companies have opportunities to underbid U.S. firms for nondefense procurement if they overcome the 6- or 12-percent price differentials that favor U.S. suppliers.

Much government procurement is not subject to foreign competition, not because of the buy-national practices, but because domestic suppliers have tremendous inherent practical advantages--language, proximity, and familiarity. Existing superior U.S. technology in weapon systems is also an important factor in limiting competition.

Analysis of fiscal year 1974 procurement data from six U.S. Government agencies showed that, because of national security, specific legislation, and practical constraints, only 3 percent ($1.3 billion) of the $44.6 billion of procurement GAO reviewed was open to competition from both domestic and foreign sources. For the other 97 percent of the procurement, the sources of competition were either exclusively domestic or foreign.

It is not possible to accurately estimate the additional cost to the Government resulting from the Buy American Act and other buy-national barriers because of such unknown factors as what contractors would bid and what prices would be offered.

Also, product modifications, price fluctuations, scarcity periods, changing international economic and monetary

conditions, and other variables which are difficult to predict and evaluate make estimating the budgetary impact speculative.

Although the United States should work toward freer trade, GAO believes it is not desirable to make major concessions unilaterally to eliminate U.S. buy-national practices. Arrangements with U.S. trading partners to work toward freer trade, with due regard for national interests and safety, should:

--Be contingent on reciprocal actions by U.S. trading partners that will clearly result in opportunities for U.S. industry and labor to benefit from increased exports.

--Encourage a competitive domestic base by increasing competition from foreign sources on a price and quality basis.

--Provide for high visibility of procurement practices and surveillance and settlement mechanisms for implementing agreements.

The Buy American Act

The Buy American Act (41 U.S.C. 10a-10d) requires Federal agencies to procure domestic materials and products. There are, however, two conditions which must be present before the Buy American Act will apply.

First, the procurement must be intended for public use within the United States. Thus, for example, contracts to be performed at the U.S. base in Okinawa are not subject to the Buy American Act. Second, the items to be procured or

the materials from which they are manufactured must be present in the United States "in sufficient and reasonably available commercial quantities and of a satsifactory quality."

In addition, the provisions of the Buy American Act may be waived if the head of the procuring agency determines (1) the Act to be inconsistent with the public interest, or (2) if the cost of acquiring the domestic product is unreasonable. By Executive Order, if the price of a domestic product is more than 6 percent (or in some cases, 12 percent) than the foreign product, the cost of acquiring the domestic product is presumed to be unreasonable. The Department of Defense applies a 50 percent price differential. The price differentials are to be implemented only when there is effective price competition for a contract from both domestic and foreign suppliers.

It should be noted that contracts awarded by State and local authorities under Federal grant programs are not covered by the Buy American Act, unless the statute authorizing the Federal assistance to State and local authorities explicitly provides for application of the Buy American Act. We have identified only the Rural Electrification Act, as amended (7 U.S.C. 906a), the Public Works Employment Act of 1977 (Public Law 95-28, 91 Stat. 116), and the Clean Water Act of 1977 (Public Law 95-217, §39, December 27, 1977)

as currently imposing Federal Buy American-type requirements on procurements by State and local authorities.

Problems with Administering the Buy American Act

The Buy American Act requires the U.S. Government to procure only those manufactured goods which (1) are "substantially all" from materials produced in the United States, and (2) are "manufactured" in the United States. The Act, however, fails to define these key terms.

"Substantially all" has been interpreted to mean that the cost of domestic components exceeds 50 percent of the cost of all components. Thus, if a federal agency is procuring microscopes, more than 50 percent of the cost of the components incorporated in the manufacture of that microscope must be domestic for it to be considered a U.S.-end product. If all the components were from the United States except the lens, but the lens comprised 51 percent of the microscope's cost, the microscope would be considered a foreign-end product.

The meaning of "manufactured in the United States" has not been resolved. Many factors appear to have been considered by contracting agencies and the Comptroller General in deciding whether an item is of U.S. manufacture. These include whether the process in question involves items which are to be directly incorporated into the end

product and whether substantial changes in the physical character of those items occur. When part of the manufacturing process occurs in the United States and part abroad, it is not settled (1) if where the later or last stages of manufacturing occur should control in determining whether the item is of U.S. or foreign manufacture, or (2) if the percentage of U.S. and foreign manufacture should be taken into consideration.

Let me give you an example of this dilemma--Softballs made entirely from materials produced in the United States but assembled in Haiti, where Haitians sewed U.S.-produced softball covers to U.S.-produced core materials using U.S.-produced needles and thread, were considered foreign-end products since the softballs were not manufactured in the United States. In that case, the services performed in Haiti constituted less than 3 percent of the product's cost.

When passed in 1933, in the wake of the depression, the Buy American Act was intended to help stimulate the U.S. economy and encourage U.S. employment. Under a system which permits 49 percent of the cost of the components of any end product to be foreign made and where U.S. manufacture may represent only a tiny fraction of the item's overall cost, it is at least questionable to what degree the domestic labor market and the economy are being aided by the Buy American program.

GAO's Recommendations

GAO made several recommendations to the Director, Office of Management and Budget, and the Administrator, Office of Federal Procurement Policy for mitigating some of the outstanding problems in administering the Buy American Act. In a letter to your committee dated December 7, 1976, the Administrator, Office of Federal Procurement Policy agreed with our recommendations and described their intended actions, none of which have been completed.

One recommendation called for amendment of the Executive Order implementing the Buy American Act to define "manufactured in the United States." The Administrator, Office of Federal Procurement Policy agreed to issue a clarification through implementing regulations to define the term "manufacture."

Another recommendation to the Administrator, Office of Federal Procurement Policy, in coordination with concerned agencies, would:

--Require, on a sampling basis, that Federal agencies request bidders in high-value procurements to disclose in their bids the percentage, the dollar value, and the nature of components of foreign origin delivered to the point of assembly of the finished products. It should be clearly stated that disclosure is sought for information purposes and, barring foreign componency costs in excess of 50 percent of all components, will not be a factor in contract evaluation. The information will be useful both to the concerned agencies and to the Congress in evaluating the extent the price differentials should apply to foreign components in domestic procurements.

We believe a valid congressional concern exists as to what the facts are.

The Administrator, Office of Federal Procurement Policy reported to you on December 7, 1976, that his office would develop a reliable sampling procedure with several of the major procurement agencies to obtain the information. The Agency did not favor acquisition of this information in bids for the reason that reliable data on the origin of components or parts frequently is not available prior to contract award and because it violates the Agency's objective to simplify contractor bids and proposals. The Administrator noted that this information can be obtained on a one-time basis by contract administration activities located at contractor facilities. We believe that this effort should be made.

A recommendation that may be more difficult to resolve was to:

--Establish the same price differentials under the Buy American Act for both civilian and military agencies. Such price differentials should be periodically reviewed to both recognize a preference for U.S. sources and, contingent on reciprocal actions by our trading partners, to encourage domestic competition.

The Administrator, Office of Federal Procurement Policy reported to this committee that examination of the "price differental" area was undertaken by his office early in 1976,

and that comments were received from Government agencies, business firms, and industry associations which disclosed a wide divergence in views on this matter. He commented that his office would attempt to arrive at a common rule for all agencies to follow.

The Administrator agreed with our final recommendation to consider for inclusion in legislative proposals to the Congress raising to $10,000 the minimum for procurement transactions that would be subject to requirements under the Buy American Act.

An agency official subsequently told us that actions on our recommendations are being held up because of trade negotiations that relate to these matters. We believe that work on these recommendations should proceed since they do not involve any unilateral concessions to our trading partners, but rather should mitigate some of the outstanding problems in administering the Buy American Act.

Recommendations to the Congress

In our 1976 report, we also recommended that congressional committess should review with the Department of Defense (1) whether the specialty metals provision in the Defense Appropriation Act has had any significant impact in increasing Government procurement of domestic specialty metals and (2) the consequence of this provision on efforts to arrange NATO standardization agreements, particularly

as it affects sales of U.S.-designed military weapons systems.

Public Law 95-111, enacted September 21, 1977, added a waiver provision that permits the Department of Defense, under certain conditions, to procure specialty metals produced outside the United States or its possessions when such procurement is necessary to comply with agreements with foreign governments requiring the United States to purchase supplies from foreign sources for the purposes of offsetting sales made by the United States Government or United States firms or where such procurement is necessary in furtherance of the standardization and interoperability of equipment requirements within NATO. The recent request from the House Congressional Steel Caucus asks, in part, that we provide them with information as to the use of the waiver under this new legislative provision.

Mr. Chairman, this concludes my prepared statement. We will be pleased to respond to any questions you may have.