

Statement of Kenneth I. Juster
Under Secretary for Export Administration
Department of Commerce
before the
Subcommittee on Domestic Monetary Policy,
Technology, and Economic Growth
of the
Committee on Financial Services
U.S. House of Representatives

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Mr. Chairman, Congresswoman Maloney, and Members of the Subcommittee:

I appreciate the opportunity to testify on the reauthorization of the Defense Production Act, which expires on September 30 of this year.

For more than fifty years, the Defense Production Act (DPA) of 1950, as amended (50 U.S.C. App. 2061, et seq.), has enabled the President to ensure our nation's defense, civil emergency preparedness, and military readiness. The DPA provides the statutory framework that will enable the Administration to meet future threats to our national security in light of a streamlined armed forces, a consolidated defense industrial base, and a globalized economy.

I will focus my comments on the DPA authorities that are relevant to the Department of Commerce. The Department of Commerce plays several roles in implementing those DPA authorities that relate to the defense industrial base. First, under Title I of the DPA, the Department administers the Defense Priorities and Allocations System. Second, under Title III, the Department reports on defense trade offsets. Third, under Title VII, the Department analyzes the health of U.S. defense industrial base sectors. And fourth, also under Title VII, the Department plays a significant role in analyzing the impact of foreign investments on the national security of the United States. I will briefly discuss each of these roles.

I. Defense Priorities and Allocations System

The Defense Priorities and Allocation System (known as "DPAS") has two purposes. First, it ensures the timely availability of products, materials, and services that are needed to meet current national defense and emergency preparedness requirements with minimal interference to the conduct of normal business activity. Second, it provides an operating structure to support a timely and comprehensive response by U.S. industry in the event of a national security emergency.

Under Executive Order 12919, the Department of Commerce administers this system in accordance with the priorities and allocations provisions of the DPA. Those provisions provide authority for requiring U.S. companies to accept and perform contracts or orders necessary to

meet national defense and civil emergency needs. They also provide authority for managing the distribution of scarce and critical materials in an emergency.

The DPAS is not used solely for defense items and military crises. It also may be implemented to meet urgent requirements for energy and law enforcement programs. Under the DPAS, the Department of Commerce delegates the authority to use the system to obtain critical products, materials, and services as quickly as needed by several federal agencies, including the Departments of Defense and Energy. To implement this authority, the Department of Defense and the other agencies -- called Delegate Agencies -- place what are known as "rated orders" on essentially all procurement contracts with industry. The prime contractors, in turn, place "rated orders" with their subcontractors for parts and components down through the vendor base. The "rated orders" notify the contractors that they are accepting contracts with the U.S. government that must be given priority over unrated orders to meet the delivery dates of the rated orders.

In the vast majority of these cases, the procuring federal agency and the contractor quickly come to mutually acceptable terms for priority production and delivery. If the company and the delegated federal agency cannot reach such agreement, the Department of Commerce, as the primary liaison with U.S. industry, plays a crucial role in resolving the issue. The Department provides "Special Priorities Assistance" to resolve critical production bottlenecks for many military and national emergency requirements.

I would like to share some examples of the Department's work in this important area.

A. Operation Desert Shield and Desert Storm

One of the best examples of the Commerce Department's work was its support of U.S. and allied requirements for Operation Desert Shield and Desert Storm in 1990-1991. The Commerce Department worked closely with U.S. industry and the Department of Defense on 135 Special Priorities Assistance cases to assure timely delivery of critical items, such as avionics components for aircraft, precision guided munitions, communications equipment, and protective gear for chemical weapons. Due to the Commerce Department's involvement, in the majority of cases delivery schedules were reduced from months to weeks or from weeks to days.

B. Coalition Action in the Balkans

The North Atlantic Treaty Organization (NATO) coalition action in the Balkans resulted in a number of instances of industrial bottlenecks for critical equipment. Starting in 1993 and continuing through 2000, the Department of Commerce worked 73 Special Priorities Assistance cases in support of U.S. forces, allied forces, and NATO command and control requirements. Although most of these cases pertained to NATO acquisition in the United States of communication and computer equipment, Special Priorities Assistance under DPAS also was used to expedite the production and delivery of such military items as antennas, positional beacons, and precision guided munitions for both U.S. and allied forces.

C. Federal Bureau of Investigation

In 1995, the Federal Bureau of Investigation (FBI) urgently required delivery of special communications equipment to meet the needs of a critical and classified national defense related anti-terrorist law enforcement program. Accordingly, Commerce staff worked with four contractors and their lower tier vendors to achieve timely delivery of parts and components to meet the FBI deployment requirement in the face of conflicting customer demands.

D. United Kingdom's Royal Air Force (RAF) Apache Longbow Helicopters

The Commerce Department's involvement in the DPAS supports not only the requirements of U.S. armed forces, but also the requirements of our allies. The Department is currently working with U.S. industry, the Department of Defense, and the United Kingdom's Ministry of Defence to meet a Royal Air Force requirement for Apache Longbow helicopters. Without the DPAS, U.S. firms supplying transponders and Hellfire missile launchers would not be able to meet RAF requirements while also meeting urgent U.S. Army requirements. It is important to note that the Department of Commerce will not take action on behalf of an allied government unless the Department of Defense determines it is in the U.S. national interest to do so.

As demonstrated by these examples, the DPAS provides the means for clearing any commercial bottlenecks that might otherwise interfere with meeting the critical production and service requirements of the U.S. armed forces, other Federal agencies, NATO, and our close allies.

II. Defense Trade Offsets

Pursuant to Section 309 of the DPA, the Department of Commerce provides Congress with an annual report on the impact of offsets in defense trade. Defense trade offsets are industrial compensation practices required as a condition of purchase in either government-to-government or commercial sales of defense articles and/or services, as defined by the International Traffic in Arms Regulations. For example, a foreign government may agree to purchase fighters from an American company but could insist that the engines for the jets be produced in the foreign country using local suppliers. We believe that offsets are economically inefficient when the foreign customer is basing the purchase decision on something other than the quality of the product or service being provided. Furthermore, offsets do a disservice to the defense supplier base in the United States by transferring work and technology overseas.

The Department of Commerce's annual report on defense trade offsets has become an integral part of the U.S. government's effort to monitor this critical issue for the U.S. defense industry. On the basis of the trends that we have identified through these reports, a Presidential Commission has been established to investigate more formally the economic and competitiveness effects of offsets on U.S. prime contractors and their suppliers.

III. Defense Industrial Base Studies

Under Section 705 of the DPA and Executive Order 12656, the Department of Commerce conducts analyses and prepares reports on individual sectors of the defense industry. These studies are either self-initiated or requested by the Armed Services, Congress, or industry. Using these industrial base studies, the Departments of Commerce and Defense can, for example, measure industry capabilities in an area such as shipbuilding or measure industry dependence on foreign components in U.S. weapons systems. The studies provide a comprehensive view of specific sectors within the U.S. defense industrial base, and they gauge the current capabilities of these sectors to provide defense items to the U.S. military services. The studies provide detailed data that are unavailable from other sources.

To give you a recent example of one of these studies, the Department of Commerce is about to release a detailed assessment of the shipbuilding and repair industry in the United States. This is one in a series of analyses related to the maritime industry that were requested by the U.S. Navy. We understand that the Navy is very pleased with the quality and thoroughness of the report and looks forward to future cooperative efforts. In another instance, the U.S. Air Force requested the Commerce Department to conduct an assessment of the ejection seat sector in the United States. Several of the recommendations in that report have been implemented by the Air Force and industry.

IV. Committee on Foreign Investment in the United States (CFIUS)

The Committee on Foreign Investment in the United States (known as “CFIUS”) was originally established by Executive Order 11858 in 1975. The Department of Commerce is an integral member of CFIUS. In 1988, the President, pursuant to Executive Order 12661, delegated to CFIUS certain of his responsibilities under Section 721 of the DPA (known as the “Exon-Florio” provision). Exon-Florio provides for a national security review of foreign mergers and acquisitions of U.S. companies. The Committee, which is chaired by the Department of the Treasury, implements Exon-Florio in the context of an open investment policy. The intent of Exon-Florio is to provide a mechanism to review and, if the President finds necessary, to suspend or prohibit a foreign direct investment that threatens the national security, but not to discourage foreign direct investment generally. The Department of Commerce’s contribution to the CFIUS process includes providing a defense industrial base and export control perspective to the CFIUS reviews. In the last year, there have been several contentious CFIUS cases. Although I cannot discuss the details of these cases because of the confidentiality extended to CFIUS reviews by Exon-Florio, the Department of Commerce was actively involved in each of the reviews, focusing particular attention on the national security impact of the acquisition. In this period of rapid globalization, continuation of this interagency review process is vital.

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In sum, the DPA provides authority for a variety of programs at the Department of Commerce. My remarks illustrate the importance of the DPAS not only to our military services, but also to NATO and our close allies that operate our weapons systems. The Department of Commerce, in its role of primary liaison to U.S. industry, has been able, through DPAS, to ensure timely delivery of products and services essential to U.S. and allied forces.

The DPA also affords the Department of Commerce the opportunity to assess fully the economic efficiency of defense trade offsets and the national security implications of international consolidation of the defense trade industry. In addition, the DPA enables the U.S. government to monitor the U.S. defense industrial base in this era of globalized markets, coalition military campaigns, and electronic battlefields.

For all these reasons, the Department of Commerce fully supports extending the Defense Production Act for at least a three-year period.

Thank you.