

REPORT ON THE
RENEGOTIATION ACT OF 1951

PREPARED FOR THE USE OF THE
COMMITTEE ON WAYS AND MEANS
U.S. HOUSE OF REPRESENTATIVES

BY THE STAFF OF
THE JOINT COMMITTEE ON INTERNAL
REVENUE TAXATION



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(II)

LETTER OF TRANSMITTAL

CONGRESS OF THE UNITED STATES,
JOINT COMMITTEE ON INTERNAL REVENUE TAXATION,
Washington, D.C., April 2, 1968.

HON. WILBUR D. MILLS,
Chairman, Committee on Ways and Means, U.S. House of Representatives, Washington, D.C.

DEAR CHAIRMAN MILLS: During the debate on the Renegotiation Act the last time it was extended in 1966 you requested the staff of the joint committee to make an examination of the Renegotiation Act to help the committee in evaluating this act when its extension was next under consideration.

This report is in response to your request. The first part presents introductory material and a summary of recommendations. The report itself is divided into seven sections. The first outlines the renegotiation process, and the second the views of the administration with respect to renegotiation. The relationship of renegotiation to procurement trends, methods, and policies is dealt with in section 3. The considerations as to whether the Renegotiation Act should be extended are set forth in section 4 and the coverage of the act including considerations of the "floor" are discussed in section 5. Section 6 discusses briefly the manner of determining excessive profits and the report concludes with staff recommendations.

The Messrs. Dennis P. Bedell, Leon W. Klud, and Joseph P. Spellman of the staff of the joint committee have done the bulk of the work in preparing this report. As indicated in the introduction, they have drawn heavily on other reports made by congressional committees and subcommittees as well as other sources of information. Chairman Hartwig of the Renegotiation Board and his staff have cooperated with the staff in supplying information for this report.

Respectfully submitted.

LAURENCE N. WOODWORTH,
Chief of Staff.

CONTENTS

	Page
Introduction and summary of recommendations.....	1
Section 1. The renegotiation process.....	3
A. Outline of the renegotiation process.....	3
B. Brief history of renegotiation.....	4
C. Data on renegotiation, 1961 through 1967.....	6
1. Filings with the Renegotiation Board.....	6
2. Board's estimated workload, 1968 and 1969.....	8
3. Excessive profit determinations and voluntary refunds.....	9
4. Appeals to the Tax Court.....	9
5. Expenses and personnel.....	10
Section 2. Administration views.....	11
1. Renegotiation Board.....	11
2. Department of Defense.....	12
3. National Aeronautics and Space Administration.....	13
4. Atomic Energy Commission.....	14
5. Maritime Administration.....	15
6. General Services Administration.....	16
7. Federal Aviation Administration.....	16
Section 3. Procurement trends, methods, and policies.....	19
A. Recent trends in defense and space-related procurement.....	19
1. Trends in total defense-related procurement.....	19
2. Methods of procurement placement.....	20
3. Types of contract pricing provisions.....	20
4. Truth in Negotiations Act.....	20
5. Summary of Defense Department cost reduction program.....	23
B. Renegotiation and procurement.....	24
1. Renegotiable sales and profits—by type of contract pricing.....	24
2. Renegotiable sales and profits, and excessive profits determinations.....	24
3. DOD profit policy concepts.....	25
4. Studies of defense industry profitability.....	28
Section 4. Considerations in extending the Renegotiation Act.....	33
A. Should renegotiation be continued?.....	33
1. The policy of renegotiation.....	33
2. The results of renegotiation.....	33
3. Renegotiation and procurement.....	35
4. The recent procurement buildup.....	36
B. Should renegotiation be made permanent?.....	37
1. Administration's request for indefinite extension.....	37
2. Considerations for a limited extension.....	37
Section 5. Coverage of the act.....	39
A. Receipts and accruals and covered departments.....	39
B. Exemptions.....	40
1. Mandatory exemptions.....	40
2. Exemption for standard commercial articles and services.....	40
3. Permissive exemptions.....	48
C. The statutory minimum or "floor".....	48
1. Present law.....	48
2. Suggested changes in the "floor".....	49
3. Discussion.....	49
Section 6. Determining excessive profits.....	53
A. Determination of contractor or subcontractor.....	53
B. Determination of the contractor's fiscal year and accounting method.....	53
C. Determination of renegotiable sales, costs, and profits.....	54
D. The statutory factors.....	55

	Page
Section 7. Staff recommendations.....	59
A. Extension of the Renegotiation Act.....	59
B. Exemption for standard commercial articles.....	60
C. Additional data required for evaluation of renegotiation.....	60
D. Treatment of incentive contracts.....	61

APPENDICES

Appendix A. Suggested changes in the Renegotiation Act.....	63
A. Departments covered by the act.....	63
B. Exemptions.....	63
C. Fiscal year basis of renegotiation.....	64
D. Other.....	64
Appendix B. Procurement trends, methods, and policies.....	67
A. Recent trends in defense and space-related procurement.....	67
B. Renegotiation and procurement.....	101
Appendix C. Additional information on Department of Defense procurement.....	111
A. Formal advertisement versus negotiation in DOD contract policy.....	111
B. Negotiated authority—DOD military contracts.....	112
Appendix D. Secretary Nitze's memo of September 29, 1967, and views thereon by the Comptroller General, regarding postaward audits.....	115
Appendix E. Renegotiable profits and losses.....	119
Appendix F. Information relating to National Aeronautics and Space Administration contracts.....	121
Appendix G. Information relating to Atomic Energy Commission contracts.....	125
Appendix H. Information relating to Maritime Administration and Maritime Subsidy Board (successor to Federal Maritime Board) contracts.....	131
Appendix I. Information relating to General Services Administration contracts.....	135
Appendix J. Information relating to Federal Aviation Administration contracts.....	145
Appendix K. Renegotiation Act of 1951 as amended to date.....	147

INTRODUCTION AND SUMMARY OF RECOMMENDATIONS

Pursuant to the request of Mr. Wilbur D. Mills, chairman of the House Committee on Ways and Means, the staff of the Joint Committee on Internal Revenue Taxation prepared this report on the Renegotiation Act of 1951 to assist the Committee on Ways and Means in evaluating the act.

In preparing this report, the staff collected information and materials from a number of sources. Information was obtained regarding the procurement activities in recent years from the Government departments and agencies named in the act. With regard to procurement practices and policies, the staff was assisted by the studies which have been made by the Special Investigations Subcommittee of the House Armed Services Committee, by the Subcommittee on Federal Procurement and Regulation of the Joint Economic Committee, and by the Subcommittee on Economy in Government of the Joint Economic Committee. In August 1967, the Special Investigations Subcommittee began an overall review of military procurement policies, procedures, and practices. To date the subcommittee has held two sets of hearings and has issued two interim reports: "Part I—Truth in Negotiations," and "Part II—Small Purchases." The Subcommittee on Federal Procurement and Regulation held hearings on Government procurement, and issued two reports on the subject in 1966: "Background Material on Economic Impact of Federal Procurement" (March 1966), and "Economic Impact of Federal Procurement—1966" (May 1966). The Subcommittee on Economy in Government held hearings during 1967 on Government procurement and issued three reports recently: "Background Material on Economy in Government—1967" (April 1967), "Economy in Government" (July 1967), and "Economy in Government—1967: Updated Background Material" (November 1967).

The Renegotiation Board furnished the staff with data and materials relating to its operations and activities and to the application of the act.

The departments and agencies named in the act also furnished the staff with their views on the Renegotiation Act and its applicability to contracts awarded by them.

In addition, Representative Gonzalez furnished the staff with the materials he assembled on the Renegotiation Act and the activities of the Renegotiation Board.

In response to a request for comments contained in a press release issued by Chairman Mills, a number of interested individuals and organizations submitted their comments and views on the Renegotiation Act and the various pending bills to extend and/or modify the act.

The staff's report is intended as a discussion of the more important aspects of renegotiation and of the framework within which it functions, rather than as a discussion in detail of the renegotiation process.

As a result of its study, the staff makes the following recommendations:

(1) The Renegotiation Act should be extended for at least 2 years. In addition, the committee may wish to give consideration to extending the act for a 4-year period in view of a number of factors: the continuing procurement buildup associated with the Vietnam conflict; the timelag between procurement and renegotiation with respect to a contract; and the time required in order to meaningfully evaluate the effectiveness of new procurement methods and practices in preventing excessive profits.

(2) The committee may also wish to give consideration to revising the exemption for standard commercial articles and services in order to insure that goods and services qualifying for the exemption are, in fact, commercial items.

If the committee desires to take action in this area, the staff recommends three modifications in the exemption. First, the percentage of the sales of an article or service (or class of articles) which must be nonrenegotiable for the exemption to apply could be raised from 35 to 50 percent. Second, contractors who "self-apply" the exemption for a standard commercial article could be required to report the application, and its basis, to the Board. Third, it could be provided that for the exemption to apply, a standard commercial article (or service) must be sold to the Government at a price which is reasonably comparable to the price charged a commercial purchaser for an order of similar quantity.

(3) The Renegotiation Board should develop and maintain various additional types of information which are needed for an adequate analysis of some of the more fundamental aspects of renegotiation.

(4) The Renegotiation Board should reevaluate its position regarding the treatment in renegotiation of amounts received under incentive-type contracts and report the results of this reevaluation to the committee. This report might place particular emphasis on the manner in which amounts received under incentive contracts awarded by the National Aeronautics and Space Administration are treated.

SECTION 1. THE RENEGOTIATION PROCESS

A. OUTLINE OF THE RENEGOTIATION PROCESS

Renegotiation is a process whereby the Government, acting through an independent establishment in the executive branch known as the Renegotiation Board, may require a contractor to refund that portion of profits on Government contracts or related subcontracts which are determined to be "excessive." In making this determination, consideration is given to amounts received or accrued by a contractor during his fiscal year (or such other period as may be fixed by mutual agreement) on contracts or on related subcontracts with Government departments named in the act. Amounts received under such renegotiable contracts and subcontracts are sometimes referred to as "renegotiable sales," "renegotiable business," and "renegotiable receipts or accruals." The departments named in the act are the Department of Defense, the Departments of the Army, Navy, and Air Force, the Maritime Administration, the Federal Maritime Board, the General Services Administration, the National Aeronautics and Space Administration, the Federal Aviation Agency, and the Atomic Energy Commission.

A determination of "excessive profits" by the Renegotiation Board is subject to redetermination by the Tax Court of the United States, and the decision of the court is subject to review by the U.S. courts of appeals on material questions of law.

Under the Renegotiation Act of 1951 as amended to date, the Renegotiation Board is composed of five members appointed by the President, by and with the advice and consent of the Senate. The Secretaries of the Army, the Navy, and the Air Force, respectively, subject to the approval of the Secretary of Defense, and the Administrator of General Services, each recommend to the President, for his consideration, one person from civilian life to serve as a member of the Board. The President, at the time of appointment, designates one member to serve as Chairman. No member is permitted to actively engage in any business, vocation, or employment other than as a member of the Board. The principle office of the Board (frequently referred to as the headquarters office) is in Washington, D.C. Under authority granted to it by the act, the Board has established two regional boards located in Washington, D.C., and Los Angeles, California.

The act does not apply to amounts attributable to contracts exempt from its provisions under section 106 (providing for "mandatory" and "permissive" exemptions), or to those amounts which are below the minimum amount subject to renegotiation specified in section 105(f). This minimum amount presently is \$1 million, and it is commonly referred to as the "floor." Under the act, renegotiation may not be conducted with respect to individual contracts, but must be conducted with respect to all amounts received or accrued by a contractor during his fiscal year (or such other period as may have

been agreed upon) under contracts or related subcontracts with all Government departments specified in the act. Under this procedure, it is said that renegotiation determinations are made on an "aggregate" or "fiscal-year" basis, rather than on a contract-by-contract basis.

In order for the Renegotiation Board to determine "excessive profits," it is first necessary that the contractor or group of contractors to be renegotiated be determined, that the accounting period and method of accounting to be used for renegotiation be fixed, that sales, costs, and profits be determined and segregated as between renegotiable and nonrenegotiable business. Then, a determination may be made of the amount, if any, of renegotiable profits which constitute excessive profits, and this requires the application of the so-called statutory factors which are set forth in section 103(e) of the act.

The renegotiation procedures provided for by the act require that there be an administrative proceeding before the Board in which a determination of excessive profits is made either by agreement between the contractor and the Board, or by the unilateral order of the Board. Section 111 of the act excludes the functions of the Board from the operation of the Administrative Procedure Act except as to the requirement of section 3 thereof, dealing with the publication of rules, orders, and so forth. The Administrative Procedure Act was amended by Public Law 90-23, and the Board has revised its regulations (part 1480) to conform with that amendment.

After the Board has entered an order determining excessive profits with respect to any contractor or subcontractor he may, within 90 days from the date of mailing of the notice of the order of the Board, file a petition with the Tax Court of the United States for a redetermination of the amount of such excessive profits. When a petition is so filed, the Tax Court is authorized to determine that the amount of excessive profits is an amount less than, equal to, or greater than that determined by the Board.

The act requires that the proceeding before the Tax Court is not to be treated as a review of the determination of the Board, but that it shall be treated as a proceeding *de novo*. Proceedings under the Renegotiation Act are subject to the same rules of procedure applicable to other cases before the Tax Court and, therefore, the burden is upon the contractor to prove that the Board's determination is erroneous.

As a result of a July 1962 amendment (Public Law 87-520), renegotiation cases filed with the Tax Court after July 3, 1962, are subject to review by the U.S. courts of appeals in a manner, and to the same extent, generally, as decisions of Federal district courts in a civil action tried without a jury. However, the determination of the existence and the extent of excessive profits by the Tax Court is conclusive unless such findings are arbitrary or capricious. Upon reviewing a decision of the Tax Court, a circuit court may either affirm the decision of the Tax Court, or may reverse it on material questions of law and remand the case to the Tax Court for such further action as is necessary.

B. BRIEF HISTORY OF RENEGOTIATION

Renegotiation procedures under the Renegotiation Act of 1951, are similar to those which prevailed (after amendment) under an earlier statute generally known as the Renegotiation Act of 1942.

Although a few earlier attempts had been made to limit contractors' profits on contracts with the Government,¹ the 1942 act was the first renegotiation statute. As originally enacted, it provided for renegotiation on a contract-by-contract basis by the procurement officials of the departments involved. However, 6 months after enactment it was amended to place renegotiation on what is now known as a fiscal-year basis. Subsequent amendments extended it to the end of 1945, prescribed certain factors which were to be taken into consideration in determining excessive profits, and also provided for de novo redetermination proceedings before the Tax Court.

In 1948, a new Renegotiation Act was passed; it was applicable principally to certain Air Force contracts for aircraft procurement. Later in the same year, however, it was amended to authorize the Secretary of Defense to extend it to other contracts, and subsequent amendments made it applicable to all negotiated Department of Defense contracts entered into during the Government's fiscal years of 1950 and 1951. The administration of this act was placed under the Secretary of Defense who established departmental renegotiation boards which were subject to review by the Military Renegotiation and Review Board.

The Renegotiation Act of 1951 granted renegotiation authority effective with respect to amounts received or accrued on or after January 1, 1951. This act expired on December 31, 1953, but 8 months thereafter it was amended and extended for 1 year until December 31, 1954. At this time, the minimum amount renegotiable under the act, the "floor," was raised from \$250,000 to \$500,000. In addition, the amendments enlarged the exemption for contracts not connected with the national defense, modified the partial exemption for sales of durable productive equipment, provided an exemption for standard commercial articles, and modified the exemption for contracts with common carriers for transportation.

In August of 1955, 7 months after the act had expired, it was amended and extended for a period of 2 years from its expiration date, or until December 31, 1956. These amendments broadened the provisions suspending the profit limitations of the Vinson-Trammell and Merchant Marine Acts (footnote 1, *supra*) to suspend those limitations where the sales were exempt under the standard commercial articles exemption, broadened the standard commercial articles exemption to include standard commercial services, added an exemption for certain construction contracts let by competitive bidding, and further modified the exemption for sales of durable productive equipment.

In 1956, the 1951 act was extensively amended and further extended for a period of 2 years, to December 31, 1958. These amendments reduced the number of departments whose contracts were subject to the act, provided for a 2-year carryforward of losses on renegotiable business, raised the "floor" from \$500,000 to \$1 million, and modified the provisions relating to the computation of the aggregate amounts received from persons under common control for purposes of applying the "floor." The 1956 amendments also made technical amendments to the mandatory exemption for certain subcontracts related to contracts exempt from the act, substantially modified the exemption

¹ For example, the Vinson-Trammell Act of 1934 and the Merchant Marine Act of 1936, and subsequent modifications of those acts. These acts limited profits on contracts in excess of \$10,000 for the construction of vessels and aircraft, with contractors agreeing to refund to the Treasury all profits in excess of 10 percent of the total contract price with respect to the major contracts, and 12 percent of such total on aircraft contracts.

for standard commercial articles and services, and instituted a requirement that the Board file annual reports of its activities with Congress.

In September of 1958, the act was amended to bring the National Aeronautics and Space Administration under its coverage, and it was extended for a period of 6 months, or until June 30, 1959. Amendments made in July of 1959 extended the act for 3 years, or until June 30, 1962, and extended the period for carryforward of losses from 2 to 5 years.

Amendments enacted in 1962, 1964, and 1966, each extended the act for 2-year periods; the present extension expires on June 30, 1968. The 1962 amendment also provided for review by the U.S. courts of appeals, with respect to material questions of law, of re-determinations of excessive profits by the U.S. Tax Court. The 1964 amendment also provided that contracts and subcontracts of the Federal Aviation Agency would be included in the act's coverage with respect to amounts received or accrued after June 30, 1964.

C. DATA ON RENEGOTIATION, 1961 THROUGH 1967

1. Filings with the Renegotiation Board

All contractors having renegotiable business in excess of the statutory minimum (the "floor") must file a report with the headquarters office of the Renegotiation Board. Contractors whose renegotiable sales are below that minimum amount are not required to file reports with the Board, but they may do so if they desire and a number of contractors in this category do elect to file a report. For fiscal years 1961 through 1967, the number of reports filed with the Board are as follows:

REPORTS FILED

Fiscal year	Total	Above the floor	Below the floor
1961.....	13,061	3,717	9,344
1962.....	11,962	3,862	8,106
1963.....	10,375	3,913	6,462
1964.....	9,772	4,007	5,765
1965.....	7,151	3,673	3,478
1966.....	5,997	3,387	2,610
1967.....	6,065	3,737	2,328

The contractors' reports are screened at headquarters, and each filing showing renegotiable business above the statutory minimum is reviewed to determine the acceptability of the segregation which the contractor has made of sales and his allocation of costs. This information is then evaluated to determine whether the filing should be assigned to a regional board for renegotiation, or whether it may be cleared at headquarters without assignment. If the latter determination is made (for example, because a report shows a loss or obviously nonexcessive profit), then headquarters will complete action on the filing by issuing to the contractor a notice of clearance without assignment. The following tabulation, for the Board's 1961 through 1967 fiscal years, shows the number of above-the-floor filings made by contractors (and by brokers and manufacturers' agents) for those years which were screened at headquarters, the number which were cleared without assignment and the number assigned to a regional board for

renegotiation, and the average time required for the screening of a filing:

ABOVE-THE-FLOOR FILINGS

Fiscal year	Total screened at headquarters	Cleared without assignment	Assigned to a regional board	Average number of days required for screening
1961.....	3,712	2,786	926	(1)
1962.....	3,618	3,228	390	(1)
1963.....	4,068	3,517	551	66
1964.....	4,383	3,881	502	59
1965.....	3,691	3,336	355	36
1966.....	3,372	2,928	444	38
1967.....	3,782	3,147	635	48

¹ Not available.

The amount of renegotiable sales, in total and by contract type, reviewed by the Board for the fiscal years 1963 through 1967 are as follows:

RENEGOTIABLE SALES REVIEWED, BY CONTRACT TYPES
(In millions of dollars)

Fiscal year	Total sales	Types of contracts		
		Cost plus fixed fee	Fixed price	Other ¹
1963.....	\$31,227	\$11,052	\$14,389	\$5,786
1964.....	39,283	14,135	16,109	9,038
1965.....	34,758	10,130	14,893	9,774
1966.....	31,841	7,820	14,436	9,585
1967.....	33,124	6,020	17,288	9,816

¹ "Other" contracts include incentive, price redetermination, and time and material contracts.

The amount of renegotiable sales, profits, and losses, on contracts involved in the above the floor filings (other than filings by brokers or manufacturers' agents) screened for the fiscal years 1963 through 1967 are as follows:

RENEGOTIABLE SALES, PROFITS, AND LOSSES IN ABOVE THE FLOOR FILINGS SCREENED
(Dollar amounts in millions)

Fiscal year	Number of filings screened	Renegotiable sales and profits			
		Net profit reports		Net loss reports	
		Sales	Profits	Sales	Losses
1963.....	3,487	\$26,208	\$1,250	\$5,020	\$333
1964.....	3,990	34,073	1,492	5,210	359
1965.....	3,315	29,953	1,333	4,845	291
1966.....	3,072	26,915	1,245	4,926	283
1967.....	3,447	28,914	1,443	4,210	272

The profit and loss figures in the preceding table are net figures, reflecting the fact that both profitable and loss contracts may be involved in individual cases. Also, the figures are based on cost allowances required for renegotiation purposes, which differ in significant respects from costs allowable for procurement purposes.

The amounts of renegotiable sales, profits, and losses reported in filings which the Board receives in a given fiscal year generally relate to contractors' receipts or accruals during the preceding 2 calendar years. Thus, filings during fiscal 1968 would relate to receipts and accruals during the calendar years 1966 and 1967. This timelag occurs

because contractors are not required to file a report with the Board until 4 months after their business year ends, and also because many of them request and are granted extensions of time (usually for 90 days) for filing their reports.

The Board has reported that most of the substantial increase in cases assigned to the regional boards in fiscal 1967 occurred in the last quarter of that year when the first filings reflecting the increase of Vietnam procurement were processed, and that it indicated the beginning of an upward trend in the Board's workload.

Cases assigned to the regional boards generally involve substantial questions, and require more extensive examination and analysis than those which are screened at the headquarters office. (The average time for processing such cases from filing to determination is 15 months, although the time required for a given case might vary considerably from that average.) The regional board formally commences renegotiation in each case it is assigned, it obtains such additional information as it may need, and it then determines the amount of the contractor's excessive profits, if any.

The regional boards have been delegated final authority to issue clearances or make refund agreement in cases involving aggregate renegotiable profits of \$800,000 or less. If a determination of excessive profits is made and the contractor will not enter into an agreement to refund such profits, the regional board issues an order directing a payment of the refund. The contractor may appeal such an order to the Board. The regional boards do not have final authority in cases involving more than \$800,000 renegotiable profits, and their recommendations must be approved by the Board before refund agreements may be executed or clearances issued. If a recommendation of the regional board is not acceptable either to the Board or to the contractor, the case is reassigned from the regional board to the Board for further processing and completion.

For fiscal years 1963 through 1967, the following tabulation shows the number of cases worked on by the regional boards, their disposition of those cases, and the number of cases completed at headquarters after reassignment to it:

FILINGS CONSIDERED BY THE REGIONAL BOARDS

Fiscal year	Assignment	Completed	Pending	Disposition of completed cases		Cases completed at headquarters after further processing
				Refund agreement, clearance, or decision not to proceed	Transferred to headquarters for further processing	
1963.....	551	464	543	265	199	212
1964.....	502	521	524	294	227	234
1965.....	355	457	422	222	235	259
1966.....	444	402	464	193	209	184
1967.....	635	421	678	213	208	201

2. Board's estimated workload, 1968 and 1969

The Renegotiation Board estimates that in the fiscal years 1968 and 1969 it will receive a significantly increased number of filings reflecting substantially greater renegotiable sales. In addition, the Board estimates that the number of cases assigned to the regional boards for renegotiation also will increase significantly in these years. The

Board's estimates for fiscal years 1968 and 1969, and the actual amounts in fiscal years 1966 and 1967, of the number of the above the floor filings received, the amount of renegotiable sales reported in those filings, and the number of cases assigned to regional boards are as follows:

BOARD'S WORKLOAD
[Dollar amounts in millions]

Fiscal year	Filings received	Renegotiable sales	Cases assigned to a regional board
1966.....	3,387	\$31,841	444
1967.....	3,737	33,124	635
1968 (est.).....	4,400	40,300	725
1969 (est.).....	4,800	44,600	800

3. Excessive profit determinations and voluntary refunds

The following table shows the number and amount (before adjustment for Federal income and excess profits tax credits) of excessive profit determinations made by the Board for fiscal years 1961 through 1967, the amounts determined by agreement and by order, and the amount of voluntary refunds and price reductions made by contractors for those years:

DETERMINATIONS OF EXCESSIVE PROFITS AND VOLUNTARY REFUNDS AND PRICE REDUCTIONS
[Dollar amounts in thousands]

Fiscal year	Total number of determinations	Amount determined by agreement	Amount determined by unilateral order	Total excessive profits	Amount of voluntary refunds and price reductions
1961.....	68	\$7,738	\$9,462	\$17,200	\$31,490
1962.....	41	6,573	1,271	7,844	17,842
1963.....	48	4,350	5,720	10,070	28,047
1964.....	56	6,861	17,299	24,160	41,097
1965.....	52	10,689	5,458	16,147	16,403
1966.....	21	2,598	21,916	24,514	23,249
1967.....	18	5,753	10,227	15,980	30,319

It should be noted that the excessive profits determinations in a given fiscal year generally relate to amounts received by contractors during the second and third preceding calendar years. In other words, excessive profit determinations in fiscal 1967 generally relate to amounts received by contractors during the calendar years 1965 and 1964 under contracts awarded in those or prior years. This substantial time lag between the awarding of a contract and an excessive profits determination with respect to amounts received under the contract is a result of the combined effect of the time lag between the receipt of amounts under contracts subject to renegotiation and the reporting of those amounts by contractors to the Renegotiation Board, and also the time required to process a case from filing to determination.

4. Appeals to the Tax Court

In those cases where a contractor does not agree with the Board's determination of excessive profits (that is, where the Board has issued a unilateral order directing the contractor to refund such amounts to the Government), he may appeal to the Tax Court of the United States for a redetermination. In such a proceeding, the Tax Court may determine an amount of excessive profits which is less

than, equal to, or greater than that determined by the Board. The following tabulation, for fiscal years 1961 through 1967, shows the number and amount of the Board's determinations appealed to the Tax Court, and the number and amount involved in cases pending before the court at fiscal yearend:

APPEALS FROM UNILATERAL ORDERS

Fiscal year	Unilateral orders appealed to Tax Court		Cases pending in Tax Court at fiscal year end	
	Number	Amounts involved (thousands)	Number	Amount of determinations (thousands)
1961.....	10	\$8,497	66	\$120,619
1962.....	3	344	61	113,159
1963.....	8	5,372	60	95,689
1964.....	5	8,979	61	98,144
1965.....	3	1,946	45	40,891
1966.....	4	4,326	39	41,091
1967.....	2	8,644	31	26,331

5. Expenses and personnel

The number of personnel employed by the Board at its headquarters office and at its regional boards on June 30 of each of the years 1961-67, and the Board's expenses for those fiscal years, are as follows:

Fiscal year	PERSONNEL			EXPENSES (Thousands of dollars)		
	Total	Head-quarters	Regional boards	Total	Salaries	Other
1961.....	271	123	148	\$2,912	\$2,601	\$311
1962.....	193	114	79	2,580	2,247	333
1963.....	223	131	92	2,325	2,025	300
1964.....	206	121	85	2,507	2,230	277
1965.....	184	108	76	2,577	2,286	291
1966.....	179	101	78	2,469	2,180	289
1967.....	178	102	76	2,536	2,239	297

SECTION 2. ADMINISTRATION VIEWS

1. *Renegotiation Board.*—Under present law, the Renegotiation Act expires on June 30, 1968. In identical letters dated February 23, 1968, to the President of the Senate and to the Speaker of the House, the Renegotiation Board recommended that the Renegotiation Act be extended indefinitely. The Renegotiation Board made the following statement on this matter:

Forwarded herewith and recommended for enactment is a draft of legislation "To extend the Renegotiation Act of 1951, and for other purposes."

The Bureau of the Budget has advised that enactment of this legislation is in accord with the program of the President.

The proposed legislation would amend section 102(c) of the Renegotiation Act of 1951, as amended (50 U.S.C. app., sec. 1212(c)) by striking out the renegotiation termination date; would repeal the exemption of standard commercial articles and services provided in section 106(e) in its entirety; and would modify the profit limitation suspension section 102(e) by eliminating the reference to section 106(e).

1. *Elimination of termination date.*—The continuation of statutory renegotiation for an indefinite period is considered essential in the national interest. Renegotiation has been the subject of temporary legislation for almost 25 years. The present act has been extended 8 times since 1951. It is now recommended that the act be continued indefinitely because there is no foreseeable end to the conditions which make it necessary.

Even if the Vietnam conflict were to end in the near future, the end of international tensions is not in sight. Hence, there will be a continuing demand for new and increasingly complex aircraft, missiles, space vehicles and other specialized items; and huge purchases will continue to be made under conditions similar to those now prevailing. Market-tested prices do not and cannot exist for costly, novel and complex military and space products. For this reason, prices must be negotiated, often with sole source contractors. Such negotiated prices are necessarily based upon uncertain cost estimates because reliable cost experience is not available. Improved purchasing techniques cannot alter these basic characteristics of military and space procurement in a period of advancing technology.

Furthermore, although awards will continue to be made on a contract-by-contract basis, the profitability of the contracts cannot be known until the profits resulting from the contractor's performance of all his contracts are recorded for his fiscal year. Renegotiation provides an after-the-fact review of such profits. Thus it affords the only means for

assuring that the profit outcome of procurement is reasonable.

An indefinite extension would greatly assist the Board's effort to recruit skilled personnel and would otherwise improve the administration of the act.

The present proposal is not new. In 1960, a special subcommittee of the House Committee on Armed Services recommended among other things, that the Renegotiation Act of 1951, as amended, "be made permanent law" (H. Rep. No. 1959, 86th Cong., 2d sess. 38 (1960)).

* * * * *

Sincerely yours,

(Signed)

Lawrence E. Hartwig
LAWRENCE E. HARTWIG,
Chairman.

A BILL To amend the Renegotiation Act of 1951, and for other purposes

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled, That this Act may be cited as the "Renegotiation Amendments Act of 1968".

ELIMINATION OF TERMINATION DATE

SEC. 2. Section 102(c) of the Renegotiation Act of 1951, as amended (50 U.S.C. App., 1212(c)), is amended by striking out the heading thereof and paragraph (1) in its entirety; by redesignating paragraph 2 as subsection (c); and by striking out "paragraph" in the last sentence and inserting in lieu thereof "subsection".

* * * * *

2. *Department of Defense.*—In a letter dated March 7, 1968, the Deputy Assistant Secretary of Defense (Procurement), made the following comments on behalf of the Departments of Defense, the Army, the Navy, and the Air Force as to the applicability of the Renegotiation Act to contracts placed by those departments:

Reference is made to your letter, dated February 23, 1968, to the General Counsel of the Department of Defense and the General Counsels of the Military Departments requesting their views with respect to the effect of changes in procurement policies on the need for renegotiation. Your letters have been referred to this office for reply.

In recent years we have made substantial progress in improving our procurement practices and we have gradually shifted from cost-plus-fixed-fee contracts to fixed-price contract types which we consider more desirable. In this process, we have managed to shift considerably more risk to our major contractors.

Notwithstanding the improvements that have been made, the Department of Defense feels that the Renegotiation Act should be continued at this time. We have experienced a large increase in procurement volume in recent years,

from \$28 billion in fiscal year 1965 to \$44.6 billion in fiscal year 1967. This increase in volume is due to the impact of our SEA activities and we feel that, under these circumstances, there is a need for continuation of the renegotiation process.

3. *National Aeronautics and Space Administration.*—The National Aeronautics and Space Administration in a letter dated March 13, 1968, made the following comments regarding contracts placed by it and the applicability of the Renegotiation Act to those contracts:

As I understand it, the determination of excessive profits must, in each instance, reflect the judgment of the Board on the application of each of the statutory factors enumerated in Section 103 of the Renegotiation Act. Among these factors is subparagraph (6) which reads in part: "Such other factors the consideration of which the public interest and fair and equitable dealing may require * * *."

We believe that the Renegotiation Board might well give added weight to special factors involved in performing work under NASA contracts. We believe that it should be recognized that NASA's work involves complex, long leadtime, advanced research and development in which progress, development plans, and costs cannot always be laid out with assurance of meeting every goal established. Every effort is made to plan the work in such a way that potential problems are anticipated and so that guidance is given to contractors by the Government to assure that the work proceeds as satisfactorily as possible. These circumstances require close monitoring of contractor activities by NASA laboratories having a strong technical interface with the contractor. Through our laboratory competence we must provide constructive criticism all through the program, rather than waiting for demonstration of successful achievement of program goals only when the end product is delivered and flown. Nevertheless, the final test of the success of the development program and of the work aimed at solving and reducing the number of problems encountered through the course of the development program is in the final flight operations of the aeronautical or space system involved.

While we are aware that the Board under its regulation and policy pronouncements recognizes the objectives of incentive contracts, we believe the Board has not given full recognition to the difficult performance requirements of our major research and development programs. NASA has relied on extensive management and technical program reviews, as well as innovative contractual arrangements, to assure that the Government receives the result it is seeking through the expenditures of Government funds. These reviews, and the incentive contract arrangements wherein the contractor's profit is based on evaluation of the quality of his work and his ability to achieve specified program requirements, provide for a thoughtful control of the profit paid to the contractor. This control considers the difficulty of the job, the risk of the contractor's reputation and financial status, the investment made by the contractor in undertaking the

work, including his financial and management commitment to the job, and the overall management responsibility that he assumes for the work that he directly performs or that his subcontractors perform. In our effort to get the best possible performance and in recognition of these various factors, our incentive fee contract arrangements are so established that added profit goes with high performance by the contractor.

In summary, then, we believe that the complexity of our work, its public visibility and the long time required for completion of any individual part of it argue for some special consideration when the reasonableness of the fees we have paid are rejudged. We do believe, however, that the Renegotiation Act of 1951 should have continuing effect. We support legislation removing the provision of that act which limits to June 30, 1968, the contracts subject to renegotiation under that act.

Because of the urgency of your committee's most recent request, this report has not been submitted to the Bureau of the Budget for advice as to its relationship to the program of the President.

4. *Atomic Energy Commission.*—In a letter dated February 26, 1968, the Atomic Energy Commission made the following comments regarding contracts placed by it and the applicability of the Renegotiation Act to those contracts:

You will note that there was a substantial decline in the percentage of dollars awarded under fixed-price contracts after fiscal year 1962. This was due to a significant reduction in the program for the purchase of uranium ore.

Our cost contracts are basically all either cost plus a fixed fee or, in the case of educational institutions and nonprofit organizations, straight cost contracts. In the case of our cost-plus-a-fixed-fee contracts, we have adopted declining fee curves which are based upon the scope, character, and estimated cost of the work to be performed by the contractor and which provides for fees which we feel are fair and reasonable.

Expenditures under our cost contracts are closely controlled by established cost principles, periodic audits, establishment of approved procurement and contracting procedures for subcontracting and purchasing, and specific approval of subcontracts over a specified dollar amount. We do not have readily available information as to overruns and underruns of estimated cost. In the case of cost-plus-a-fixed fee contracts, the fee, which includes the contractor's profit, of course would not change because of overruns or underruns of estimated cost.

While our contracts cover the entire range from off-the-shelf items to first-of-a-kind production items to basic research, the major part of our prime contracting is carried on under cost or cost-plus-a-fixed-fee operating contracts, which provide little, if any, opportunity for excessive profits, therefore, the Renegotiation Act has a limited impact on our programs. However, in view of the possibility that there may

be some direct fixed-price procurements for which there is relatively little cost and production experience available and, for fixed-price procurements by our cost-type contractors, we believe the Renegotiation Act may be a deterrent to excessive pricing and provides a measure of insurance against excessive profits. We do not have any specific suggestions for improvement in the act.

5. *Maritime Administration.*—The Maritime Administration in a letter dated March 1, 1968, made the following comments regarding contracts placed by it and by the Maritime Subsidy Board:

You have asked about the extent of overrun or underrun of estimated costs employed in initial pricing. Overruns or underruns arise primarily in connection with the administration's research and development cost reimbursable contracts. An analysis of the research and development contracts completed during fiscal years 1961 through 1967, indicates that overruns and underruns have not been in excessive amounts. As the attached tabulation shows [see appendix H], however, in fiscal year 1967, there was a 20-percent overrun in a ship construction contract.

The procurements of the Maritime Administration (Maritime Subsidy Board) are of ships employed in the foreign commerce of the United States, under the Merchant Marine Act of 1936, as amended. Under these three-party contracts the owner, the ship operator, pays to the contractor a sum equal to the Maritime Subsidy Board's estimate of the cost of building the vessel of the owner to similar plans and specifications in a foreign shipyard. The Board pays the difference between the estimated foreign cost and the domestic price. The Maritime Administration also enters into ship construction contracts with shipbuilders on the basis of orders placed by other Federal agencies under the Economy Act of 1932, as amended.

The dollar values shown for new ship construction and ship conversion do not represent, in the entirety, Government expenditures in the indicated amounts. With respect to procurements under the Merchant Marine Act of 1936, as amended, Government expenditures amounted to approximately 51 percent of the total contract expenditures. The balance is paid by the owner. Of course, under the Economy Act contracts, the Government is responsible for the total price.

The maintenance and repair contracts noted in the attached tabulation, represent specific job orders awarded on the basis of competitive bid or negotiation, and are referable to master lump sum repair contracts entered into by the Maritime Administration with shipyards in the several coastal regions. A ship, undergoing maintenance and repair after each voyage, will have a considerable number of job orders to be performed. Because of the magnitude of the number of maintenance and repair job orders brought about by the increased activity due to the Southeast Asian conflict, currently involving approximately 650 voyages each year, estimates of the total number of contracts, and the total

dollars connected therewith, are based upon sampling of ships and voyages as they relate to geographic and traffic factors. The sampling is necessary only for fiscal years 1966 and 1967. In the earlier fiscal years, the number of contracts and dollar amounts shown were based upon actual data.

6. *General Services Administration.*—In a letter dated March 1, 1968, the General Services Administration made the following comments regarding contracts placed by it and the applicability of the Renegotiation Act to those contracts:

The vast majority of the Federal Supply Service contracts are on a fixed price basis and do not involve the problem of initial pricing and subsequent price redeterminations as in the case in cost-type contracts. We do encounter cases where there is little cost and production experience available for new items being introduced into the supply system; however, in most cases it is possible to extrapolate pricing data available with respect to similar supply items involving closely related types of cost and production. Variances in the products and services procured from year to year are experienced but the differences normally do not relate to commodity or service areas in which we have not had some prior experience. The footnotes shown on schedule II [see appendix I] are self-explanatory regarding PMDS contracts.

Due to the nature of our programs and operations, the Renegotiation Act has limited application to contracts placed by this agency. The basic statutory exemptions in the act, particularly the one covering standard commercial articles and standard commercial services, are applicable to a wide range of our procurement activities. In addition, the Renegotiation Board has determined that major areas of GSA contracting do not have a direct and immediate connection with the national defense and, therefore, are exempt from renegotiation (see paragraph 5-53.804.1 of the attached copy of General Services Administration procurement regulations, subpart 5-53.8).

With respect to the proposed amendments to the Renegotiation Act of 1951, GSA has no objection to the enactment of the Board's draft bill which was submitted to the Speaker of the House by letter dated February 23, 1968 from Mr. Lawrence E. Hartwig, Chairman of the Renegotiation Board.

7. *Federal Aviation Administration.*—The Federal Aviation Administration in a letter dated March 1, 1968, made the following comments regarding contracts placed by it and the applicability of the Renegotiation Act to those contracts:

The materials/services procured by this agency cover a wide range of cost type study, design, or design and initial production of hardware. The fixed price type contracts cover production or performance type specifications, follow on supply type of procurement, and the bulk of our construction contracting. To illustrate this point, our current active contracts list contains 479 contracts that are not completed for a variety of reasons. A breakdown of the 479 contracts

is as follows: Fixed price—256 (53 percent); cost type—147 (30 percent); issued to other Government agencies—48 (10 percent); labor hour and time and materiel—28 (7 percent). Many of our contracts are entered into for which there is no previous cost or production experience. We find that there is little change in the variety of supplies and services that are procured from year to year.

At this time the FAA has no particular comment to make as to the merits of any proposed extension of the Renegotiation Act. It is expected that the Office of the Secretary will in the future be making one comment on the effects of such legislation on all elements of the Department of Transportation.

SECTION 3. PROCUREMENT TRENDS, METHODS, AND POLICIES

A. RECENT TRENDS IN DEFENSE- AND SPACE-RELATED PROCUREMENT

The need for renegotiation generally is predicated on various aspects of military and space procurement: the lack of competition, the extensive use of negotiated contracts, and the inability of procurement methods to insure against excessive profits. The amount and the nature of the procurement buildup associated with Vietnam is also relevant since the buildup is another reason advanced for continuing renegotiation. In this part of the report, various aspects of the procurement framework within which renegotiation functions are considered: trends in procurement; the use of advertisement and negotiation in awarding contracts; the types of contract pricing used; the Truth in Negotiations Act; and the Defense Department cost reduction program. In addition, various aspects of renegotiation and the relationship between procurement and renegotiation are discussed. The major emphasis with regard to procurement is focused, of course, upon the Department of Defense in view of the relative magnitude of its procurement activities within the overall framework of defense- and space-related procurement. A more detailed analysis of this topic is presented in appendix B.

1. Trends in total defense-related procurement

In 1967, total Defense Department military procurement rose to \$44.6 billion, surpassing the previous peak of \$43.6 billion which occurred in the Korean conflict year of 1952. Although the 1967 military procurement surpassed the previous peak level, it was the result of a much slower buildup than occurred during the Korean conflict. Military contract awards to business firms for work in the United States increased from \$5.4 billion in 1950 to \$30.8 billion in 1951, or 476 percent. From 1950 to 1952, the increase was from \$5.4 billion to \$41.5 billion, or 675 percent. The Vietnam buildup, on the other hand, was more gradual. Military procurement increased \$8.7 billion from 1965 to 1966, or 35 percent. The 2-year buildup (1965-67) was \$14.5 billion, or 57 percent. In addition, only 39 percent of the Vietnam procurement buildup was accounted for by "costly, novel, and complex" items such as aircraft, missile and space systems, ships, and electronics and communications equipment.

Small business firms have been participating in military contract awards to an increasing extent. In the last 7 years, small businesses' share of military prime contract awards increased from 16 percent of total awards to over 20 percent. The amount of military subcontracts awarded to small business also increased during this period from 37 percent of total subcontracting to over 43 percent. Thus, the total share (prime contracts and subcontracts) of small business in military procurement has increased from 31 percent in 1961 to 37 percent in 1967.

2. *Methods of procurement placement*

There are two basic methods by which the Defense Department awards military contracts: through formal advertisement and through negotiation. From 1961 to 1965, the percentage of contracts awarded through formal advertisement increased, reaching 18 percent of military procurement in 1965. This was followed by a decline to 13 percent in 1967. The percentage of military contracts awarded to small business firms through formal advertisement has remained relatively stable at about 20 percent during the last 5 years. The percentage of contracts awarded to large business firms by formal advertisement has also remained relatively stable at about 13 percent, except for 1965 when it rose to 18 percent.

The bulk of procurement (about 95 percent) in recent years of NASA and AEC, which account for most of the procurement of the nondefense agencies covered by renegotiation, has been obtained through negotiation rather than formal advertisement.

In determining the degree of price competition which exists in its procurement, the Defense Department considers price competition to be present when a contract is awarded by formal advertisement and also in certain situations when a contract is awarded by negotiation. From 1960 to 1967, the degree of price competition in Department of Defense military procurement rose from 30 to 43 percent. Negotiated price competition, the largest component within the price competition category, accounted for almost one-half of price competition in 1966 and 1967.

3. *Types of contract pricing provisions*

The basic principle behind Defense Department procurement actions is that the business profit motive should be utilized effectively in order to achieve economical contract performance. To make effective use of the profit motive in private business, the Defense Department believes the contractor should be given cost responsibility as soon as possible and to the maximum extent possible. For this reason some variation of the fixed-price contract is preferred by the Department.

Prior to 1960, the use of fixed-price contracts was declining. This trend was reversed, however, from 1960 to 1967, during which the use of fixed-price contracts rose from 57 percent of military procurement to 79 percent.

From 1960 to 1967, the use of cost-plus-fixed-fee contracts declined from 37 percent of procurement to 10 percent, and the use of fixed-price (other than incentive) contracts rose from 44 percent of procurement to 61 percent.

The use of incentive-type contracts (fixed-price and cost) was declining prior to 1961; however, from 1961 to 1964 the use of incentive contracts increased from 14 percent of procurement to 33 percent. This was followed by a decline to 26 percent in 1967.

4. *Truth in Negotiations Act*

(a) *In general*

The Truth in Negotiations Act (Public Law 87-653) was enacted September 10, 1962, to strengthen the ability of procurement officials in the military departments and the National Aeronautics and Space Administration to ascertain and obtain "accurate, complete, and current cost or pricing data" upon which to establish fair and reasonable

prices. This was largely due to a number of reports by the General Accounting Office (GAO) during 1957-62 on instances of increased costs to the Government due to the lack of "accurate, complete, and current cost or pricing data" in negotiating contracts. Selected audits during this period indicated that the failure to obtain appropriate cost data resulted in higher prices to the Government of at least \$61 million.¹

The Truth in Negotiations Act stated and reconfirmed a general congressional policy to (1) maximize the use of formal advertising where feasible and practicable, and (2) solicit as many proposals, in all negotiated procurements over \$2,500, from a maximum number of qualified sources ("where rates or prices are not fixed by law or regulation and in which time of delivery will permit") to obtain "competitive" prices (considering other factors consistent with the requirements of the goods or services needed).

Furthermore, the act specified that a prime contractor or any subcontractor shall be required to submit and certify that cost or pricing data are "accurate, complete, and current" if the negotiated contract award exceeds \$100,000 (for prime contracts, modifications or changes in contracts and subcontracts).

Where this certificate is required, the contract must also contain a provision to insure against "defective pricing (or cost)." A price adjustment would be required if the cost or pricing data were "inaccurate, incomplete, or noncurrent."

The Truth in Negotiations Act, however, does not apply to contracts or subcontracts where the price is negotiated on "adequate price competition, established catalog or market prices of commercial items sold in substantial quantities to the general public, prices set by law or regulation," or in exceptional cases where the head of the agency states in writing his reasons for waiver of application.

In addition, the Act provided that decisions to award a contract under certain of the statutory provisions (10 U.S.C. 2304(a)) allowing contracts to be negotiated rather than advertised formally, and choices of the type of contract to be used, were to be substantiated by written reasons as to why the contract qualified for negotiation (including the reasons why formal advertising was not feasible and practicable) and why the type of contract selected was likely to be less costly than another type.

(b) GAO findings and recommendations

Continuing its program of selected postaward audits of Government contracts, the GAO issued Report B-158193, February 23, 1966, recommending: (1) that the DOD's Defense Contract Audit Agency (DCAA) establish an organized and regular postaward review of "noncompetitive" negotiated contracts, and (2) a revision of the armed services procurement regulation (ASPR) to provide a clause to give DCAA auditors access to the books of contractors affected under Public Law 87-653.

GAO Report B-39995 January 16, 1967, testimony at the May 1967 hearings by the Joint Economic Committee's Subcommittee on Economy in Government, and testimony at hearings by the House Armed Services' Subcommittee for Special Investigations (August 3 and September 25, 1967) indicated a lack of complete compliance by the

¹ House Armed Services Committee, Subcommittee on Special Investigations, "Review of Defense Procurement Policies, Procedures, and Practices: Part I—Truth in Negotiations," (Feb. 29, 1968), p. 3.

DOD with Public Law 87-653. Report B-39995 revealed that from a sample of 242 negotiated prime contracts and subcontracts (awarded after October 1964), 185, or 76.4 percent, complied with the general requirements of submission and certification of cost or pricing data under Public Law 87-653. The remaining 57 of the 242 awards did not submit the certificates because they were apparently legally exempted. However, the records of these 52 exempted awards did not contain a written explanation of why they were classified as being "competitive," etc., and thus exempted. Also, of the 185 that did comply, 165, or 89.2 percent, did not provide written records identifying the cost or pricing data submitted and certified.

Furthermore, the GAO found that prime contractors "had no record identifying the cost or pricing data submitted by subcontractors in support of significant cost estimates even though agency contracting officials were required, under negotiated prime contracts other than firm-fixed-price type, to ascertain that such data were being obtained."

Also, the DOD contracting officials were not requiring prime contractors to use the new contract pricing proposal form (DD Form 633, December 1, 1964).

Therefore, in addition to its February 1966 report recommending a postaward audit system and obtaining the right of access to performance cost information on noncompetitive firm fixed-price contracts, the GAO recommended in its January 1967 report, and in the May 1967 Joint Economic Committee hearings, that the DOD—

- (1) obtain written identification of data submitted by the contractor;
- (2) revise the ASPR to make it clear that making data available to the auditors without identification in writing does not constitute data "submitted," in terms of the law;
- (3) document procurement files where cost or pricing data were not requested to indicate the basis of decision to waive the requirements; and that
- (4) DOD utilize the DD Form 633.

The report of the House Armed Services Subcommittee for Special Investigations, "Review of Defense Procurement Policies, Procedures, and Practices: Part I—Truth in Negotiations" (February 29, 1968), contained very similar findings and recommendations (pp. 3-4) as did the July 1967 report of the Joint Economic Committee's May 1967 hearings.

(c) DOD response to GAO recommendations

Following the February 1966 GAO report, the DOD's Defense Contract Audit Agency (DCAA) took steps to implement a regularly scheduled postaward audit system. The DCAA had been established in 1965, but only provided for general audit surveillance.

The second GAO recommendation of February 1966, regarding obtaining the right of access to performance cost information on noncompetitive firm fixed-price contracts, was not implemented until a September 29, 1967, memorandum was issued by the Deputy Secretary of Defense (see appendix D for text of memorandum and views thereon by the Comptroller General).

The Defense Department in DOD Circular 57 (November 30, 1967) issued an order for implementation of the requirements regarding access to a contractor's performance records for negotiated noncompeti-

tive firm fixed-price contracts and fixed-price with escalation contracts. This order applied to contracts over \$100,000 for which a cost certificate had been obtained, including subcontracts subject to Public Law 87-653. Access to a contractor's performance records was already available in the case of cost-reimbursement contracts. Circular 57 also included provisions regarding compliance with Public Law 87-653's cost documentation requirements (including certificates of cost documentation). In addition, a revised defective cost or pricing clause was prescribed (i.e., a clause requiring price readjustment in the case of "inaccurate, incomplete, or noncurrent cost or pricing data"). This order was to be effective upon receipt.²

Further testimony by the DOD in the Joint Economic Committee's November 1967 hearings indicated increased efforts were being made to improve training for procurement officials and personnel, including seminars on implementation of Public Law 87-653 and explanation of the new DOD regulations.³ The GAO indicated at the November 1967 hearings that, in general, the DOD Circular 57 did include all of their recommended changes.⁴

In its testimony at the November 1967 Joint Economic Committee hearings, the Bureau of the Budget stated that "Our investigation and our discussions with officials of GAO and the Department of Defense since the May 1967 hearings [JEC] indicate that substantial progress has been made. A period of operational testing will be necessary to assure that desired results are being achieved."⁵

The GAO testified, however, that it would be at least 6 months, or a year, before they could adequately evaluate the effectiveness of the new DOD regulations in terms of compliance with the Truth in Negotiations Act.⁶

According to a recent speech before the Electronics Industries Association Spring Conference, "Symposium on Economics for the Defense Industry" (March 5, 1968, Washington, D.C.), Comptroller General Elmer B. Staats stated that the GAO has begun a broad survey of contract administration by the Defense Contract Administration Services and by the military departments.

This survey will cover the trend toward shifting cost responsibility to the contractor, including special emphasis on the effects of incentive type contracts. In addition, the GAO will examine such newer management contracting concepts as "multiyear procurement," "total package" contracts, and "life cycle costing." Hence, there appears to be more research to be done to ascertain the effectiveness of these newer procurement policies and techniques.

5. Summary of Defense Department cost reduction program

In fiscal year 1962, the Department of Defense instituted a cost reduction program. One of the more important aspects of this program was shifting from noncompetitive procurement to price competitive procurement. The Department estimates that the savings from shifting to price competitive procurement averages about 25 percent. Another aspect of the cost reduction program was reducing the use of cost-plus-fixed-fee contracts and increasing the use of fixed and

² Joint Economic Committee, Hearings, "Economy in Government Procurement and Property Management," (Nov. 27-30 and Dec. 8, 1967), pp. 162-177.

³ *Ibid.*, pp. 80-135; e.g., DOD Training Seminar on "Certified Cost or Pricing Data and Public Law 87-653," (September 1967).

⁴ *Ibid.*, p. 376.

⁵ *Ibid.*, p. 305.

⁶ *Ibid.*, p. 379.

incentive price contracts. Savings are estimated at 10 percent per dollar converted from cost-plus-fixed-fee contract pricing to fixed or incentive type contract pricing. Other aspects of the cost reduction program included purchasing items directly from the manufacturer rather than through a prime contractor, and the multiyear procurement procedure which is used in lieu of awarding a separate contract each year.

B. RENEGOTIATION AND PROCUREMENT

In analyzing the relationship between renegotiation and procurement policies and methods, it is useful to consider the types of contracts represented in renegotiable sales and their relative profitability. It also would be helpful in attempting to determine the types of procurement which result in "excessive profits" to examine the types of contracts, and their profitability, represented in the sales of contractors with respect to which excessive profits determinations were made. This latter information was not provided to the staff. The available data, however, do afford some indication of the relative magnitude of excessive profits within the overall framework of renegotiation. In addition, some indications are provided of the relative profitability of those contractors with respect to which excessive profits determinations were made.

The objective of renegotiation is to limit "excessive profits." In this connection, it is worthwhile to consider the profit policy of the Defense Department and recent studies of defense industry profitability.

1. *Renegotiable sales and profits—By type of contract pricing*

The changes in the procurement patterns of the Department of Defense in recent years are reflected in the types of renegotiable sales reported to the Renegotiation Board. An increasing percentage of renegotiable sales is attributable to fixed-price type and incentive type contracts. On the other hand, the percentage of renegotiable sales attributable to cost-plus-fixed-fee contracts has declined.

An analysis of the ratio of renegotiable profits to total renegotiable sales for various types of contracts in recent years indicates that incentive type contracts (both fixed-price and cost-reimbursement) have a profit/sales ratio about twice that of nonincentive type contracts. On the other hand, if only profitable renegotiable sales are considered, firm fixed-price contracts generally show the highest profit/sales ratios. Firm fixed-price contracts also show the highest rate of losses when only loss renegotiable sales are considered.

2. *Renegotiable sales and profits, and excessive profits determinations*

The magnitude of excessive profits within the overall context of renegotiation is relatively small. In recent years, excessive profits have averaged less than one-tenth of 1 percent of renegotiable sales and about 1.3 percent of renegotiable profits. When the amount of excessive profits actually returned to the Government (i.e., after reduction for the Federal income tax credit) is considered, these percentages are approximately halved.

Those contractors with respect to which excessive profits determinations were made had profit/sales ratios on their renegotiable business which were substantially higher than the profit/sales ratios for all contractors reporting to the Renegotiation Board. On the other hand, the profit/sales ratios on the nonrenegotiable business (all other

sales of the contractor—commercial and nonrenegotiable Government) of those contractors with respect to which excessive profits determinations were made were significantly higher than the profit/sales ratios on the renegotiable business of these firms.

3. DOD profit policy concepts

(a) DOD profit policy

Basically, it is the policy of the DOD to utilize the business profit motive to encourage competent and resourceful private industry to compete for the sales the DOD generates.⁷ In order to facilitate the achievement of this goal, adequate targeted profits must be available in the negotiation of defense contracts. The DOD promulgated a new profit policy on August 15, 1963 (ASPR, sec. 3-808), for all contracts negotiated after January 1, 1964. This policy included the following statement:⁸

* * * Effective national defense in a free enterprise economy requires that the best industrial capabilities be attracted to defense contracts. These capabilities will be driven away from the defense market if defense contracts are characterized by low profit opportunities. Consequently, negotiations aimed merely at reducing profits, with no realization of the function of profit cannot be condoned * * * .

Furthermore, any particular average percentage of profits earned is not to be used to set a limit on a given contract, as "negotiation of very low profits, the use of historical averages, or the automatic application of a predetermined percentage to the total estimated cost of a product, does not provide the motivation to accomplish such performance";⁹ i.e., more effective and economical contract performance.

To provide this motivation, "the profit objective must be fitted to the circumstances of the particular procurement, giving due weight to each of the performance, risk, and other factors * * * . This will result in a wider range of profits, which, in many cases, will be significantly higher than previous norms * * * , [since] low average profit rates on defense contracts overall are detrimental to the public interest."¹⁰

The overall objective of the new DOD profit policy on negotiated contracts (which, in 1967, accounted for 86 percent of the dollar amount of military procurement with business firms in the United States) is to set up adequate inducement for a "broad reduction in defense costs"; and, at the same time, to shift as much cost responsibility as possible to the contractors. Thus, as indicated above, higher rewards (i.e., profits) will go to contractors who: undertake more difficult assignments requiring high technical skills; assume greater cost risk; show excellent past performance records; and undertake the responsibility to provide their own facilities and financing.¹¹

The DOD profit policy operates in conjunction with the change in contract pricing policies discussed previously. Changes in DOD procurement policies during the 1960's have tended to increase the contractor's risk by increasing his cost responsibility: the use of

⁷ Armed Services Procurement Regulation (ASPR), secs. 3-402(a)(1) and 3-808.1(a).

⁸ ASPR, sec. 3-808.1(a).

⁹ Ibid.

¹⁰ Ibid.

¹¹ Ibid.

cost-plus-fixed-fee contracts has declined rapidly; conversely, increased use has been made of firm fixed-price and incentive contracts; in addition, price competitive procurement has been rising steadily.

This shift from cost-type contracts to fixed-price type contracts has also increased the contractor's working capital requirements because progress payments by the DOD have been at a lower rate of costs incurred for fixed-price contracts than for cost contracts (70 percent vs. 100 percent for cost).¹²

The recent trend toward higher risk contracts (firm fixed-price) includes a potential for greater contractor profit (if performance exceeds expectations) or lower profits (or losses, if costs are not managed efficiently).

As indicated previously, overall profit/sales ratios for firm fixed-price contracts of renegotiable sales were much lower than for incentive type contracts. This was due to the high rate of losses reported on firm fixed-price contracts. Considering only reported profitable renegotiable sales, however, firm fixed-price contracts revealed the highest profit/sales ratio of the three major categories of contracts reported by the Renegotiation Board.

(b) DOD profit review system

The DOD established a profit review system to implement the new profit policy stated in ASPR, sec. 3-808. This set up "Weighted Guidelines" for negotiating target profits, based upon weighted percentages for certain inputs and costs.¹³

The factors to be considered included the following: past contract performance (e.g., management quality, cost efficiency, cost reduction program, value engineering, quality of product, delivery efficiency, inventive contribution, and small business and labor surplus area participation); contractor risk (e.g., type of contract pricing, difficulty of contract task); high technical skill requirements (and other material and engineering inputs); and contractor investment (i.e., whether government supplied).¹⁴ Weighted Guidelines are to be used in all contracts where cost analysis is performed, except certain service and construction contracts.

The DOD also developed a contractor performance evaluation system to allow analysis of the efficiency of defense contractors and properly reward them by establishing targeted profits befitting past performance and contractor risk.¹⁵ In all negotiated contracts over \$200,000, the contracting officer must complete a report of the individual contract profit plan, reflecting the cost weighting that resulted in the negotiated target profit.¹⁶ Following completion of such a negotiated contract, a report must be made to provide a comparison of the effectiveness of the targeted ("going in") profit and the cost performance, which is reflected in the final earned ("coming out") profit.¹⁷

¹² DOD reported that progress payments would be 80 percent for fixed-price contracts as of Mar. 1, 1968. Small business was increased from 75 percent to 85 percent. These recommendations were made during hearings by the Subcommittee on Government Procurement, Senate Select Committee on Small Business, Feb. 6, 7, 1968.

¹³ ASPR, sec. 4-808.2.

¹⁴ ASPR, sec. 3-808.4.

¹⁵ DOD Directive 5126.38, Dec. 3, 1965.

¹⁶ DD form 1499, Aug. 1, 1966, ASPR, sec. 21-300.

¹⁷ Prior to the Weighted Guideline period (1958-63), reports were only required on all contracts over \$1,000,000. From 1964 to July 1, 1966, all contracts over \$500,000 were reported; since July 1, 1966, the figure has been lowered to the present \$200,000. "Smaller contract negotiations were covered by limited sampling." Logistics Management Institute, Defense Profit Review (November 1967), vol. I, p. 33.

¹⁸ DD form 1500, ASPR, sec. 21-400.

To compare the negotiated "going in" profit rates (before taxes) during the Weighted Guideline period (1964-67) with previous "going in" profit rates, the DOD developed comparative data on "going in" target profit rates for 3,615 contracts negotiated during 1959-63 and 6,440 contracts negotiated during 1964-67 (see table 1).

TABLE 1.—DOD PROFIT REVIEW: NEGOTIATED "GOING IN" PROFIT RATES (BEFORE TAXES), FISCAL YEARS 1959-63 AND 1964-67

Type of contract	(Dollar amounts in millions)							
	Base period, Fiscal Years 1959-63				WGL period, Fiscal Years 1964-67			
	Number	Dollar Cost	Profit rate on—		Number	Dollar Cost	Profit rate on—	
			Cost	Sales			Cost	Sales
		Percent	Percent			Percent	Percent	
Firm fixed-price.....	1,582	\$6,565	9.0	8.3	3,064	\$9,490	11.0	9.9
Fixed-price-incentive-fee.....	396	10,749	8.9	8.2	915	9,116	9.4	8.6
Cost-plus-incentive-fee.....	136	3,948	6.0	5.7	971	4,605	7.4	6.9
Cost-plus-fixed-fee.....	1,501	10,059	6.2	5.8	1,490	2,601	6.9	6.4
Total.....	3,615	31,321	7.7	7.1	6,440	25,812	9.4	8.6

Source: Cited in Logistics Management Institute, Defense Profit Review (November 1967), vol. I, p. 36.

In the case of each type of contract pricing in table 1, negotiated "going in" profits were higher (as a percentage of both cost and sales) during the recent Weighted Guideline period, 1964-67, than during the prior 5-year period.

(c) *DOD profit policy and the renegotiation process*

The renegotiation process does not focus directly on the problem of unreasonable prices to the Government (or "excessive" profits) on any single contract award. A firm's renegotiable business is aggregated (profits and loss contracts) for each fiscal year. Therefore, the Government may have paid an excessive price on part of a contractor's sales, but this may have been partially offset by other factors; namely, low or average profits on other contracts; losses on current work (due to underbidding or lack of effective cost control); or loss carryforwards from prior years. In other words, the renegotiation process emphasizes the elimination of "excessive profits" on a firm's aggregate renegotiable business during the fiscal year, and the Defense Department procurement process emphasizes the attainment of "reasonable prices" by the Government on its procurements.

The profit policy of the Department of Defense states the relationship between costs, prices, and profits for procurement purposes as follows:¹⁸

* * * while the public interest requires that excessive profits be avoided, the contracting officer should not become so preoccupied with particular elements of a contractor's estimate of cost and profit that the most important consideration, the total price itself, is distorted or diminished in its significance. Government procurement is concerned primarily with the reasonableness of the price which the Government ultimately pays, and only secondarily with the eventual cost and profit to the contractor.

¹⁸ ASPR, sec. 3-806(b).

In cases where adequate price competition exists (formally advertised contracts and certain negotiated contracts), the cost-price-profit policy of the Defense Department is stated more specifically as follows:¹⁹

* * * fixed-price type contracts will be awarded to the lowest responsible offerors without regard to the amount of their profits. Under these circumstances, the profit which is anticipated, or in fact earned, should not be of concern to the Government. In such cases, if a low offeror earns a large profit, it should be considered the normal reward of efficiency in a competitive system and efforts should not be made to reduce such profits.

According to the Department of Defense, "adequate price competition" existed in over 40 percent of the dollar amount of procurement in 1967. In addition, slightly more than 90 percent of 11.7 million procurement actions in 1967 (excluding intragovernmental) were classified as "price competitive."²⁰ Thus, less than 10 percent of procurement actions in 1967 accounted for almost 60 percent of the dollar amount.

It is possible, therefore, that these relatively few noncompetitive negotiated contract actions will become more effectively "policeable" in light of various factors such as the following: the recent tightening of the implementation of the Truth in Negotiations Act; preaudit and postaward audits by the Defense Contract Audit Agency; postaudits by the General Accounting Office on the reasonableness of contract costs and effectiveness of contract management by the DOD; and improved accuracy by the DOD in applying the Weighted Guidelines in negotiating target costs and profits.

4. *Studies of defense industry profitability*

A recent study by the Logistics Management Institute (LMI), Defense Industry Profit Review (November 1967), indicated that average profits on defense business were declining relative to average profits on commercial business, 1958-66 (i.e., for the firms in the sample, defense profit ratios were declining, while commercial profit ratios were increasing). The sample of firms doing defense business included: (a) 23 firms defined as high volume (\$200 million or more defense sales); (b) 17 medium volume firms (\$25 million to \$200 million defense sales); and (c) 25 low volume firms (\$1 million to \$25 million defense sales).²¹ Defense sales to these firms were estimated as representing the following percentages of the total defense sales to all firms within each category: (a) high volume—92 percent; (b) medium volume—50 percent; and (c) low volume—3 percent.²²

Inasmuch as the low volume companies in the sample only accounted for a small percentage of defense sales to all low volume companies, conclusions were drawn only with respect to the 40 high and medium volume firms. For purposes of making profitability comparisons, profit/sales ratios (before tax) were derived for the commercial sales of the firms, as well as for the sales of a sample of 3,500 industrial firms chosen from Federal Trade Commission (FTC) and

¹⁹ ASPR, sec. 3-808.1(c).

²⁰ Office of the Secretary of Defense, "Military Prime Contract Awards and Subcontract Payments or Commitments, July 1966-June 1967," p. 33.

²¹ Logistics Management Institute, Defense Industry Profit Review," (Nov. 1967), vol. II, p. 3:

²² *Ibid.*, p. 101.

Securities and Exchange Commission (SEC) quarterly financial reports. These FTC/SEC manufacturing firms were drawn from six industrial categories comparable to defense industries: transportation equipment, electrical machinery, equipment and supplies, other machinery, other fabricated metal products, instruments and related products, and miscellaneous manufacturing and ordinance.²³

Profit/sales ratios (before taxes) for the defense business of the combined 40 high and medium volume firms declined from 5.4 percent in 1958 to a low of 3.9 percent in 1963, rose to 4.8 percent in 1965, and declined slightly to 4.5 percent in 1966. Ignoring the 2 low years of 1960 and 1961, profit/sales ratios for the commercial business of these firms rose from 6.6 percent in 1958 to a high of 10.1 percent in 1965, and declined to 9.2 percent in 1966. At the same time, profit/sales ratios for the FTC/SEC sample increased from 7.1 percent in 1958 to a high of 10.4 percent in 1965, and declined slightly to 10.0 percent in 1966 (see table 2).

An additional overall profit/sales ratio included in table 2 compares net renegotiable profits (net of losses) to total renegotiable sales reviewed by the Renegotiation Board. This profit/sales ratio declined from 6.5 percent in 1956 to a low of 2.9 percent in 1963 and 1964, increased to 3.0 percent in 1965 and 1966, and increased again to 3.5 percent in 1967. It should be noted that the data from which this ratio is derived are based on cost allowances required for renegotiation purposes.

Additional Renegotiation Board data are presented in tables 25 and 26 of appendix B for firms determined to have excessive profits, 1963-67. Before renegotiation, renegotiable profit/sales ratios of these firms ranged from 8.8 percent in 1963, to 12.8 percent in 1964, and to 16.0 percent in 1967. On the other hand, the profit/sales ratios on the nonrenegotiable sales of these firms rose from 19.9 percent in 1964 to 31.4 percent in 1967; and overall profit/sales ratios increased from 17.8 percent in 1964 to 29.2 percent in 1967.

TABLE 2.—COMPARISONS OF PROFITABILITY RATIOS OF DEFENSE AND COMMERCIAL INDUSTRIES,¹
1958-66

[In percent]

Category	1958	1959	1960	1961	1962	1963	1964	1965	1966
Profits/sales (before taxes):									
Defense business.....	5.4	5.1	4.0	4.3	4.2	3.9	4.0	4.8	4.5
Commercial business.....	6.6	6.7	4.3	5.9	8.2	8.4	9.6	10.1	9.2
FTC/SEC sample firms.....	7.1	8.9	7.8	7.7	8.9	9.1	9.5	10.4	10.0
Renegotiation Board data ²	4.9	4.2	4.0	3.6	3.1	2.9	2.9	3.0	3.0
Profits/equity capital investment: ³									
Defense.....	25.0	23.7	21.1	18.5	18.3	16.1	15.6	18.2	17.4
Commercial.....	17.3	17.7	11.8	16.8	23.5	23.1	27.4	28.7	27.5
FTC/SEC.....	16.5	21.9	18.5	17.8	21.9	22.6	24.1	27.4	27.1
Profits/total capital investment: ³									
Defense.....	20.4	19.1	17.0	14.6	14.3	12.5	12.2	14.3	13.0
Commercial.....	13.4	13.8	9.2	13.2	18.1	17.2	20.6	21.4	19.7
FTC/SEC.....	14.1	18.8	15.9	15.1	18.5	19.2	20.4	23.1	22.6

¹ Logistics Management Institute sample of high- and medium-volume firms doing defense and commercial business, and sample of FTC/SEC manufacturing industry groups (averages weighted by company sales).

² Reported renegotiable profits and sales (net of reported renegotiable losses); data for 1956 and 1957 were 6.5 and 5.8 percent respectively; 1967 was 3.5 percent.

³ Does not include equity or investment furnished by the Government.

Source: LMI, Defense Industry Profit Review (November 1967), vol. 1, pp. 26-27.

²³ *Ibid.*, p. 7.

The Renegotiation Board did not furnish data on profits as a percentage of corporate net worth (or as a rate of return on capital investment) for individual cases or in total. Therefore, comparisons are not available between Renegotiation Board data and the LMI data on profit/capital investment ratios.

The LMI study also segregated defense sales and profits by type of contract, the results of which are summarized in table 3. On the average, subcontracts revealed a slightly lower profit/sales ratio than prime contracts, except in 1966 when subcontract profits averaged 6.5 percent of sales as compared to 4.9 percent for prime contracts. In recent years, fixed-price incentive contracts revealed the highest profit/sales ratios, and firm fixed-price contracts had the lowest ratios.

TABLE 3.—COMPARISONS OF DEFENSE PROFIT/SALES RATIOS, BY TYPE OF CONTRACT PRICING, 1952-66
(AVERAGES WEIGHTED BY COMPANY SALES)

Year	[In percent]					
	Prime contracts	Subcontracts	Cost plus fixed fee	Cost plus incentive fee	Firm fixed price	Fixed price incentive fee
1958-----	5.2	4.2	3.9	2.7	7.2	6.3
1959-----	4.8	5.2	3.8	4.6	7.3	5.7
1960-----	4.9	3.9	3.7	6.1	5.4	5.8
1961-----	4.8	4.8	3.6	4.4	3.8	6.8
1962-----	4.5	4.7	3.5	4.0	3.9	6.3
1963-----	4.0	4.1	3.3	4.6	2.4	5.6
1964-----	4.1	4.6	3.7	4.9	.9	6.1
1965-----	5.2	4.3	4.7	5.0	3.7	6.5
1966-----	4.9	6.5	4.6	5.3	2.9	5.9

Source: LMI, Defense Industry Profit Review (November 1967), vol. 1, p. 32.

The profit/sales ratios in table 3 for the LMI study were roughly comparable to the profit/sales ratios for total renegotiable sales and profits (net of losses) in 1965-67 (table 22 of appendix B); for example, fixed-price incentive contracts had the highest ratios in both cases, and firm fixed price contracts had the lowest.

Another recent study of comparative profitability of "defense business" and commercial business was reported by Dr. Murray L. Weidenbaum, professor of economics, in "Department of Economics Working Papers 6717," Washington University, St. Louis, Mo. His sample included six large defense firms whose defense or space sales accounted for over 75 percent of their total sales in 1965. Six commercial firms were selected on the basis of similar sales volume; these samples were compared for 1962-65 and for 1952-55.

This study differed from the LMI profit study in various respects. The LMI study selected a larger sample (40) of representative firms having both defense and commercial sales (high and medium volume defense sales—over \$25 million). In addition, the firms in the LMI study were compared with commercially oriented firms (FTC/SEC sample of 3,500 firms) in industries producing durable equipment similar to that produced by the defense sample. In other words, it appears that Professor Weidenbaum's sample of the six large defense oriented firms was less representative of firms doing defense business than the LMI study.

Professor Weidenbaum's findings revealed a higher profit/capital investment ratio (return on net worth) for the six defense firms (17.5 percent) than for the six commercial firms (10.6 percent). On the

other hand, the "profit margin on sales" was only 2.6 percent for the defense firms, while the commercial firms had a 4.5 percent margin. This was due to the higher "capital turnover" of 6.8 times yearly for the defense companies, as contrasted to 2.3 times yearly for the nondefense companies. The greater "capital turnover" rates for the six defense firms was related to the presence of Government furnished capital and equipment investment. Professor Weidenbaum has noted the limitations of the study data regarding the coverage of the sample and the fact that the capital investment ratios did not take into account Government supplied capital. This capital, if properly accounted for, would reduce the profit/capital investment ratios for certain defense oriented companies.

The LMI survey indicated significantly lower "capital turnover" rates for its larger, more representative sample of defense businesses. The commercially oriented firms had even lower turnover ratios, but they had much higher profit/sales ratios than did Professor Weidenbaum's sample of six commercial firms.

The LMI study also indicated declining profit/capital investment ratios for its defense sample; at the same time, the commercial business of these 40 firms and the FTC/SEC sample of 3,500 firms in comparable industries revealed increasing profit/capital investment ratios (see table 2).

The Logistics Management Institute is continuing its study in an attempt to further evaluate the data collected. It is also making further efforts to improve the coverage of small volume defense businesses (\$1-25 million in defense sales) so as to obtain a statistically reliable sample.

A fourth indicator of defense business profitability is the continuing analysis under the DOD profit review system. The purpose of this analysis is to calculate realized profit rates on completed contracts, by type of contract, and compare average earned profit rates to average negotiated target profit rates. Limited data are available at the present time, however, concerning earned ("coming out") profits of contractors during the period the Weighted Guidelines have been in effect. The 1,842 contracts covered in table 4, which include only \$11.2 billion in costs, were all awarded before the initiation of the Weighted Guidelines; this is due to the length of time between a contract award and the determination of profits earned on the completed contract.

The data in table 4 are also limited since no reports were tabulated for firm fixed-price contracts (which have accounted for an increasing majority of contract awards). In addition, the average earned profits do not reflect the deduction of "unallowable/nonrecoverable costs," as do the data for defense business in table 2. If this had been done, the average earned profit in table 4 would have been "reasonabl comparable" with profits by type of contract pricing in table 2.²⁴ In both cases, however, fixed-price incentive contracts had the highest profit rates. Furthermore, data on earned profit rates in table 4 are limited by the fact that they, as the studies mentioned previously, are averages; thus, they do not reflect variations among different business.

²⁴ LMI, p. 34.

TABLE 4.—DOD PROFIT REVIEW: REALIZED PROFIT RATES (BEFORE TAXES) ON COMPLETED CONTRACTS¹

Type of contract	Number of contracts	Total costs (millions)	Average negotiated profit-percent of cost	Sales	Average earned profit-percent of cost	Sales
Firm fixed-price.....	(²)	-----	-----	-----	-----	-----
Fixed redetermination.....	351	\$12,346	9.3	8.5	8.6	7.9
Fixed-price incentive fee.....	311	3,883	9.3	8.5	9.2	8.4
Cost-plus-incentive-fee.....	75	331	6.4	6.0	7.2	6.7
Cost-plus-fixed-fee.....	1,105	4,689	6.4	6.0	6.1	5.7
Total contracts reported.....	1,842	11,249	-----	-----	-----	-----

¹ Contracts awarded July 1, 1958–Dec. 31, 1963 (preweighted guidelines). Also, "Contracting officers have not yet submitted sufficient data on completed contracts which were placed under the weighted guidelines (1964–67) to permit a meaningful analysis."

² No data.

Source: LMI, p. 37.

In order to relate the DOD profit review system to the LMI profit study, "the LMI profit study task will require an increase in its analysis of the consolidated [DOD] 1499 and 1500 Forms data as those data expand. An improved understanding of the relationship between the data collected under the DOD system and the data received from contractors participating in this [LMI] study should result."²⁵

In view of the limitations of the various profitability studies discussed above (LMI, Renegotiation Board data, Professor Weidenbaum, and the DOD profit review system), it is apparent that a continuing and more refined analysis of the profitability of defense business and comparable commercial business is necessary for an adequate evaluation of the effects of recent changes in Defense Department procurement and profit review policies.

²⁵ LMI, p. 35.

SECTION 4. CONSIDERATIONS IN EXTENDING THE RENEGOTIATION ACT

A. SHOULD RENEGOTIATION BE CONTINUED?

There are a number of factors which should be taken into account in considering whether renegotiation should be continued. The more important of these are presented below.

1. The policy of renegotiation

The policy underlying renegotiation is that contractors doing business with the Government in the defense and space programs should not be allowed to obtain excessive profits on that work. Another relevant policy is that the goods and services needed by the Government should be secured at a fair and reasonable price. As is discussed more fully below, it is difficult at the present time to judge the effectiveness of new procurement policies and methods, especially during the procurement buildup associated with the Vietnam conflict, in obtaining Government procurements at proper prices and also in limiting excessive profits on these procurements. It is also difficult to judge whether renegotiation supplements these procurement policies and methods, including the role assigned to the profit motive, or whether it detracts from their full implementation and effectiveness. In this connection it should be noted that the Department of Defense feels the Renegotiation Act should be continued at this time.

2. The results of renegotiation

Renegotiation has recovered for the Government more than the amounts expended by the Renegotiation Board for its activities. In analyzing this aspect of renegotiation, it does not appear appropriate to consider the Board's activities from its inception to the present time. The effect of looking back to 1951 is to attribute in part to the present time amounts recovered during a period characterized by crash procurement and substantially less sophisticated procurement methods. The procurement framework of the present time is quite different in terms both of the methods employed and the circumstances in which procurement must take place. Accordingly, the past 5 years have been used for purposes of analysis as more representative of current conditions.

Actual determinations of excessive profits by the Renegotiation Board for the fiscal years 1963 through 1967 averaged about \$18.2 million a year (before the Federal tax credit), resulting in an average net recovery by the Government of \$9.4 million a year. In view of the normal timelag between the time a contract is awarded by a procurement agency and the time a determination is made by the Renegotiation Board with respect to amounts received under that contract, the determinations of excessive profits mentioned above (including those in 1967) resulted, generally, from contracts awarded in a period of relatively stable procurement; that is, a period which does not

include the acceleration in procurement resulting from the Vietnam conflict.

It would appear that renegotiation also may limit excessive profits through voluntary refunds and price reductions which are made by contractors. For the fiscal years 1963 through 1967, contractors reported to the Renegotiation Board voluntary refunds and price reductions which averaged over \$27.8 million a year. This probably resulted in an average net recovery by the Government of about \$14.5 million a year (assuming the portion of refunds and price reductions recovered is about the same as the portion of excessive profits recovered). These voluntary refunds and price reductions, which are made to procurement agencies and higher tier contractors, are not required by a contract provision. It would appear, therefore, reasonable to assume that the existence of renegotiation is at least one of the motivating factors behind the making of these refunds and price reductions.

It is also possible that renegotiation limits excessive profits by exerting a deterrent effect on the determination of the contract price at the time a contract is awarded. Although this effect is not measurable, it appears reasonable to assume that the existence of renegotiation may have a restraining effect on contract pricing.

Thus, the measurable effect of renegotiation in controlling excessive profits has averaged somewhere between \$9.5 and \$24 million a year during the past 5 years, depending on the extent to which voluntary refunds and price reductions are attributable to renegotiation. When the immeasurable effect which the existence of renegotiation probably has on contract pricing is also taken into account, it is apparent that renegotiation has resulted in recoveries to the Government which exceed the comparatively small amounts expended by the Renegotiation Board for its activities (approximately \$2.5 million a year over the past 5 years).

On the other hand, the impact of renegotiation within the overall procurement context is relatively insignificant. In 1967, the excessive profits determinations by the Renegotiation Board amounted to only one-twentieth of 1 percent of the amount of renegotiable sales reported in filings with the Renegotiation Board.

Another indication of the relatively small magnitude of the recoveries attributable to renegotiation is shown by the fact that the amount of profits which the Renegotiation Board determined to be excessive from fiscal year 1963 to fiscal year 1967 averaged 1.3 percent of total renegotiable profits. Moreover, the amount actually recovered by the Government with respect to these determinations of excessive profits (i.e., after allowance of the credit for Federal income taxes previously paid on the excessive profits) amounted to 0.7 percent of the total net profits on renegotiable sales.

If the voluntary refunds and price reductions which are made to procurement agencies and higher tier contractors are considered to be a result of the existence of renegotiation, the magnitude of the savings resulting from renegotiation would be increased somewhat.

In addition to the fact that recoveries pursuant to the Renegotiation Act are relatively insignificant in magnitude, it should also be noted that contractors incur costs in complying with the requirements of the Renegotiation Act, both in preparing the necessary reports and in the actual renegotiation of a case. However, the magnitude of the costs incurred solely by reason of renegotiation is not ascertainable.

These costs in addition to being deductible for Federal income tax purposes are probably passed on at least in part to the Government in future contracts.

3. Renegotiation and procurement

The structural environment within which defense and space procurement takes place is characterized by uncertainties. Large amounts are being spent in the defense and space effort for products with respect to which there is little or no production or cost experience available. The steadily rising pace of technological change and innovation has made available, and the rising sophistication of the defense and space programs have required, new and extremely complex products, materials, applications, and systems. These various factors produce an environment characterized by uncertainty and lack of cost and production experience.

In order to insure fair and proper prices on military purchases by the Government within this environment, and also to reduce the cost of these purchases to the Government, the Department of Defense has significantly revised its procurement methods in recent years. A cost reduction program was adopted, procurement emphasis was shifted from cost-plus-fixed-fee contracts to fixed price and incentive contracts, the amount of competitive procurement was increased, contract review and auditing procedures have been expanded, and the Truth in Negotiations Act has been implemented. A significant percentage in terms of value of Defense Department contracts, over 56 percent in 1967, were firm fixed-price contracts. In addition, over 83 percent of the 229,357 contracts awarded (over \$10,000) by the Defense Department in 1967 were firm fixed-price contracts. Firm fixed-price contracts are not used in the circumstances usually cited as requiring renegotiation; namely, where there is a lack of adequate cost and production experience. Moreover, an additional 30 percent in terms of value of contract awards by the Department of Defense in 1967 included a price adjustment feature (i.e., incentive escalation, or redeterminable). In other words, 86 percent of the value and 93 percent of the number of contract awards (over \$10,000) were either firm-fixed price or included a price adjustment feature.

Although substantial and significant changes have been made by the Department of Defense in its procurement methods in recent years to make those procurement methods more effective, it appears that there is a need to further assess those methods before their effectiveness can be judged, especially with respect to adequately insuring against excessive profits. The amount of excessive profits on procurement occurring during the Vietnam buildup (fiscal years 1966 and 1967) will be reflected in Renegotiation Board determinations during the next few years. The level of these determinations will afford some indication of the effectiveness of procurement methods during recent years.

The overall review of military procurement policies, practices, and procedures begun last August by the Special Investigations Subcommittee of the House Armed Services Committee, which it is not contemplated will be completed for some time, has resulted in two interim reports indicating some deficiencies in procurement practices regarding implementation of the Truth-in-Negotiations Act and also regarding small purchases.

The studies in recent years of the General Accounting Office, the Federal Procurement and Regulation Subcommittee and the Economy in Government Subcommittee of the Joint Economic Committee have also indicated some shortcomings in procurement practices.

At the present time, studies also are being made of the level of profits in defense work with a view to determining the effectiveness of the Department of Defense profit policy in terms of the overall goals of securing the goods and services needed by the Government at reasonable prices and of encouraging the growth of efficient and innovative suppliers.

4. *The recent procurement buildup*

It appears that the amounts subject to the renegotiation process will increase substantially in the next few years. Amounts received under contracts awarded during the buildup in procurement associated with the Vietnam conflict are just beginning to be reflected in contractor filings with the Renegotiation Board. The number of filings with the Board, the amount of renegotiable sales reported in those filings, and the number of cases assigned to regional boards increased substantially in fiscal 1967 and are expected to do so in fiscal 1968 and 1969. Although the procurement buildup associated with Vietnam has been less rapid and more orderly than the Korean conflict procurement buildup, the Vietnam buildup has reached a higher absolute dollar level of expenditures. It also should be noted that the percentage of negotiated procurements by the Department of Defense reversed a downward trend in fiscal 1966 and began rising again. Moreover, the percentage of negotiated procurements by the National Aeronautics and Space Administration and the Atomic Energy Commission, which together with the Department of Defense account for the bulk of renegotiable sales, have in recent years consistently stayed at a high level. In addition, the portion of Department of Defense procurement which is considered by the department to be price competitive accounted for only 43 percent of total procurement in fiscal 1967, a slight decrease from fiscal 1966, and almost half of price competitive procurement occurred in the category of "negotiated price competition."

On the other hand, the procurement buildup associated with Vietnam does not appear to have been of a type which would impair the basic effectiveness of procurement methods. The Vietnam buildup, unlike the Korean buildup, has occurred at a relatively slow pace. The Department of Defense military prime contract awards increased 675 percent from fiscal 1950 to fiscal 1952 (\$5.4 billion to \$41.5 billion). On the other hand, these same awards increased by only 57 percent from fiscal 1965 to fiscal 1967 (\$25.3 billion to \$39.8 billion). Moreover, the increase in procurement associated with Vietnam did not occur primarily with respect to those types of items for which renegotiation is usually said to be necessary; i.e., those items for which there is little prior cost and production experience available. Approximately 39 percent of the \$14.5 billion increase in the Department of Defense procurement from fiscal 1965 to fiscal 1967 occurred in items such as aircraft, missile and space systems, ships, and electronics and communications equipment. The bulk of the increase, however, occurred in such common items as ammunition, tank and automotive products, subsistence, and textiles, clothing and equipage. In other words, the Vietnam procurement buildup does not appear to have

been of the type which would significantly impair the effectiveness of procurement methods.

B. SHOULD RENEGOTIATION BE MADE PERMANENT?

1. *Administration's request for an indefinite extension*

As indicated in section 2, the Renegotiation Board has requested that the Renegotiation Act be continued for an indefinite period. The basic reason advanced for making the act permanent is that the conditions presently necessitating the act will continue for the foreseeable future.

The Board elaborated on its request for an indefinite extension in the following manner. There will be continuing large purchases of novel and complex military and space products for which market-tested prices or reliable cost experience data do not exist. These items must be procured on the basis of negotiated prices determined with reference to uncertain cost estimates. Improved procurement techniques cannot alter these basic characteristics of military and space procurement. Moreover, the only means for insuring that the profit outcome of procurement is reasonable is through the overall, after-the-fact review provided by renegotiation. The Board also noted that its ability to recruit skilled personnel and to otherwise administer the act would be greatly improved by an indefinite extension. Finally, the Board noted that in 1960 the Special Subcommittee on Procurement Practices of the Department of Defense, of the House Committee on Armed Services, recommended that the Renegotiation Act be made permanent law. (H. Rept. No. 1959, 86th Cong., 2d sess. 38 (1960)).

2. *Considerations for a limited extension*

In addition to the considerations which may be advanced for making the Renegotiation Act a permanent feature of the law, there are also considerations involving the nature of renegotiation and the effectiveness of procurement methods which support a limited extension.

In both principle and operation, renegotiation is a process which warrants periodic review by Congress. The underlying principle of renegotiation is profit control, and in operation, a significant portion of the control effected through the renegotiation process is dependent on the subjective application of the general standards set forth in the statute. It would seem desirable that there be a periodic assessment of the need for governmentally imposed profit controls. To the extent it is determined that it is necessary and desirable to limit profits in the manner of the renegotiation process, it would also seem appropriate that the implementation of the limitation be periodically reviewed.

Although it may not be possible for procurement methods to completely eliminate the occurrence of excessive profits on Government contracts, it is conceivable that procurement methods could reduce the incidence of excessive profits to a level which would be considered insignificant. Because of the timelag between contract awards and determinations by the Renegotiation Board of excessive profits, the full impact of the procurement changes which have been instituted in recent years on the need for renegotiation is not clear at this time. It is also difficult to judge at this time the effect of the increase in procurement associated with the Vietnam conflict on procurement

methods and practices and on the incidence of excessive profits on defense and space program work. At the present time, moreover, procurement policies, practices and methods are being reviewed by congressional committees and the General Accounting Office. Studies of the profitability of defense work are in process to determine whether the Defense Department profit policy is adequately implemented. The results of these studies and the experience with renegotiation in the next few years will be of substantial assistance in evaluating the need for renegotiation and the interrelationship of renegotiation and procurement policies and methods.

SECTION 5. COVERAGE OF THE ACT

A. RECEIPTS AND ACCRUALS AND COVERED DEPARTMENTS

Except for those receipts and accruals attributable to contracts or subcontracts exempt from the act under section 106 (providing certain "mandatory" and "permissive" exemptions), and those which are not renegotiable under section 105(f) because they are below the minimum amount subject to renegotiation (the "floor"), the Renegotiation Act applies to all amounts received or accrued on or after January 1, 1951, under contracts with the departments named in the act, or under related subcontracts.

Section 103(a) of the act specifies several departments of the Government and provides that a contract is not subject to the act unless it is with one of those departments or with a department designated by the President. The named departments at the present time are the Department of Defense, the Departments of the Army, Navy, and the Air Force, the Maritime Administration, the Federal Maritime Board, the General Services Administration, the National Aeronautics and Space Administration, the Atomic Energy Commission, and the Federal Aviation Agency.

The Board is required by the act to exercise its powers with respect to the aggregate of the amounts received or accrued during the fiscal year (or such other period as may be fixed by mutual agreement) by a contractor or subcontractor under contracts with the departments and subcontracts, and not separately with respect to amounts received or accrued under separate contracts with the departments or subcontracts. The reference to contracts applies to those with the departments named in the act and which are not exempt under section 106. The reference to subcontracts applies to contracts or arrangements defined by section 103(g) as "subcontracts."

Section 103(g) broadly defines "subcontract" to include three different classes of subcontracts. The first class comprises "any purchase order or agreement * * * to perform all or any part of the work, or to make or furnish any materials, required for the performance of any other contract or subcontract," but "does not include any purchase order or agreement to furnish office supplies." The second class comprises "any contract or arrangement covering the right to use any patented or secret method, formula, or device for the performance of a contract or subcontract." The third class comprises "any contract or arrangement * * * under which—(A) any amount payable is contingent upon the procurement" of any renegotiable contract or subcontract, or (B) "any amount payable is determined with reference to the amount" of a renegotiable contract or subcontract, "or (C) any part of the services performed or to be performed consists of the soliciting, attempting to procure, or procuring" a renegotiable contract or subcontract.

B. EXEMPTIONS

Section 106 provides 10 "mandatory" exemptions, five "permissive" exemptions, and a "cost allowance" which has the effect of an exemption for integrated producers of certain agricultural products and raw materials.

1. *Mandatory exemptions*

The mandatory exemptions are as follows:

1. Any contract by a department with any territory, possession, or State, or any agency or political subdivision thereof, or with any foreign government or any agency thereof.

2. Any contract or subcontract for an agricultural commodity in its raw or natural state, or if the commodity is not customarily sold or has not an established market in its raw or natural state, in the first form or state, beyond the raw or natural state, in which it is customarily sold or in which it has an established market.

3. Any contract or subcontract for the product of a mine, oil or gas well, or other mineral or natural deposit, or timber, which has not been processed, refined, or treated beyond the first form or state suitable for industrial use.

4. Any contract or subcontract with a common carrier for transportation or with a public utility for gas, electric energy, water, communications, or transportation, when made in either case at rates not in excess of unregulated rates of such a public utility which are substantially as favorable to users and consumers as are regulated rates.

5. Contracts or subcontracts with organizations, which are tax exempt charitable, religious, or educational institutions.

6. Any contract which the Board determines does not have a direct and immediate connection with the national defense.

7. Subcontracts directly or indirectly under contracts or subcontracts which are exempt.

8. Any contract, awarded as a result of competitive bidding, for the construction of any building, structure, improvement, or facility, other than a contract for the construction of housing, financed with a mortgage or mortgages insured under the provisions of title VIII of the National Housing Act.

9. Certain receipts and accruals from contracts or subcontracts for "durable productive equipment."

10. Certain receipts and accruals from contracts or subcontracts for "standard commercial articles" or "standard commercial services."

2. *Exemption for standard commercial articles and services*

(a) *Present law*

The standard commercial article exemption provided by section 106(e) exempts amounts received or accrued in a fiscal year under any contract or subcontract for any one of the following categories:

1. A standard commercial article.

2. An article which is "identical in every material respect" with a standard commercial article.

3. A standard commercial service.

4. A service which is "reasonably comparable" with a standard commercial service.

5. Any article in a standard commercial class of articles.

For the exemption to be applicable to an article or service in any one of the above five categories, the item must meet what may be referred to as the 35 percent rule, as well as other tests prescribed by the act. The 35 percent rule requires, in the case of a standard commercial article, that at least 35 percent of the contractor's sales of the item be nonrenegotiable during the fiscal year under review or, alternatively, at least 35 percent of the aggregate sales for such year and the preceding fiscal year. In other words, at least 35 percent of the contractor's sales of the item must be commercial sales or sales to Government departments and agencies not covered by the act. In the case of the other four categories, the rule requires that at least 35 percent of the sales for the year under review be nonrenegotiable.

Certain other tests must also be met with respect to each category. Thus, for an article to qualify as a standard commercial article, it must be one which is either "customarily maintained in stock" by the contractor or is "offered for sale in accordance with a price schedule regularly maintained" by the contractor. If an article is to be exempt as being identical in every material respect with a standard commercial article, it must be of the "same kind and manufactured of the same or substitute materials * * * as a standard commercial article," and it must be sold at a price which is "reasonably comparable with the price of such standard commercial article."

For a service to be exempt as a standard commercial service, it need meet only the 35-percent test and be a "service" as defined by the statute. And, for a service to be exempt as "reasonably comparable with a standard commercial service", it must be of the "same or a similar kind, performed with the same or similar materials, and" have "the same or a similar result * * * as a standard commercial service."

For an article to be exempt as an article in a standard commercial class of articles, the class in which it is grouped must be a "standard commercial class." This means, under the statute, the class must consist of two or more articles with respect to which three conditions are met: (1) "at least one of such articles either is customarily maintained in stock by the contractor . . . or is offered for sale in accordance with a price schedule regularly maintained by the contractor," (2) "all of such articles are of the same kind and manufactured of the same or substitute materials," and (3) "all of such articles are sold at reasonably comparable prices."

A contractor may waive the exemption for sales of any one or all of the five categories discussed above for any fiscal year under certain prescribed conditions. In waiving the exemption with respect to any particular article or service, the contractor will not necessarily waive the exemption for any other article or service. The exemption for sales of a standard commercial article is "self-executing," in that it may be applied by the contractor without the filing of any application therefor. However, exemptions for sales of articles or services in any of the other four categories can be obtained only if the contractor files an application with the Board.

The following list indicates some of the types of items which are regarded by the Board as qualifying for the standard commercial article exemption:

Abrasives, steel shot, grit	Drugs—Continued
Adhesive tape	Stelazine
Aircraft	Thorayine
Aluminum ingots, sheets, bars and other standard mill forms	Fabrics, polyester, and nylon
Antennas	Fans and blowers
Antifreeze	Frequency and time measuring equipment
Boilers, oil and gas fired	Fuel and lubricants, automobile and aircraft
Boots	Gases, industrial and medical
Broadcloth	Governors
Bushings	Insecticides
Cases, frozen food display cases	Memory systems and components
Chemicals	Microwave instruments and components
Coffee	Nails
Computers and related equipment	Nuts
Cotton greige goods	"O" rings
Cylinders, gas	Paints and thinner
Digital equipment and components	Potentiometers
Drills, counterbores, countersinks, and boring bars	Recorders, video and audio
Drugs:	Sheets and pillowcases
Actifed	Shoes
Colymycin	Tacks
Deramyl	Tools, taps, gages
Lanoxin	Vegetables and fruit, canned
Mandelamine	Ventilators
Pyridium	Wire screen cloth

In each year, an unknown number of contractors self-apply the standard commercial article exemption and do not inform the Board. The Board is of the belief that millions of dollars of sales are thus exempted, but it has stated that it has no way of knowing or estimating the amount involved. However, for the fiscal years 1963 through 1967, the amounts involved in self-applications of exemptions which were reported to the Board are as follows:

Fiscal year:	<i>Reported amounts of self-applications</i>	<i>Millions</i>
1963-----		\$623
1964-----		603
1965-----		561
1966-----		439
1967-----		773

The applications received by the Board for fiscal years 1963 through 1967 for exemptions under the provisions of the standard commercial article exemption which are not self-executing (i.e., identical articles, standard commercial services, identical services, and classes of articles) showed the following:

APPLICATIONS FOR STANDARD COMMERCIAL ARTICLE EXEMPTION

(Dollar amounts in thousands)

Fiscal year	Number of applications	Amount of exemptions		
		Applied for	Approved	Denied
1963.....	218	\$515,564	\$479,074	\$36,490
1964.....	230	566,445	556,589	9,856
1965.....	244	485,958	457,922	28,036
1966.....	264	545,733	527,667	18,066
1967.....	251	671,901	636,611	35,290

(b) Administration's recommendation

In identical letters dated February 23, 1968, to the President of the Senate and to the Speaker of the House, the Renegotiation Board recommended that exemption for standard commercial articles and services be eliminated in its entirety. The Renegotiation Board made the following statement on this matter:

Forwarded herewith and recommended for enactment is a draft of legislation "To extend the Renegotiation Act of 1951, and for other purposes."

The Bureau of the Budget has advised that enactment of this legislation is in accord with the program of the President.

The proposed legislation would amend section 102(c) of the Renegotiation Act of 1951, as amended (50 U.S.C. App., sec. 1212(c)) by striking out the renegotiation termination date; would repeal the exemption of standard commercial articles and services provided in Section 106(e) in its entirety; and would modify the profit limitation suspension in Section 102(e) by eliminating the reference to Section 106(e).

* * * * *

2. *Elimination of commercial exemption.*—The exemption of commercial articles and services in Section 106(e) of the Act should be repealed in its entirety.

The exemption of individual articles provided in Section 106(e) may be self-applied by the contractor if, among other things, his sales of an article in a fiscal year, or in such fiscal year and the preceding fiscal year, are at least 35 per cent nonrenegotiable.

Section 106(e) also provides exemption for an article which is identical in every material respect with a standard commercial article; for an article in a standard commercial class of articles; for a standard commercial service; and for a service which is reasonably comparable with a standard commercial service. In these four categories, the contractor must make application for the exemption and the 35 per cent requirement is limited to sales in the fiscal year.

The contractor is entitled by the Act to waive these exemptions, in whole or in part.

The commercial exemption assumes that excessive profits will not result when at least 35 per cent of the sales of an article which the contractor either maintains in stock or offers for sale from a price schedule are nonrenegotiable.

This assumption is not valid because what is a fair price in commercial sales may be clearly excessive for large Government contracts. The assumption is particularly untenable when the volume of Government purchasing is expanded and accelerated by the threat or fact of war.

There is an additional ground for objection to the class exemption. Under this exemption only one article in a class need be maintained in stock or offered for sale in accordance with a price schedule. Other articles which are of the same kind and content and are sold at reasonably comparable prices may be included in the class, and all are exempt, provided only that 35 percent of the aggregate sales of the articles in the class are nonrenegotiable. This exemption has been applied to a wide variety of articles, many of which are sold exclusively or predominantly to the military departments.

Sincerely yours,

(Signed) Lawrence E. Hartwig
LAWRENCE E. HARTWIG,
Chairman.

A BILL To amend the Renegotiation Act of 1951, and for other purposes

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled, That this Act may be cited as the "Renegotiation Amendments Act of 1968".

* * * * *

MODIFICATION OF PROFIT LIMITATIONS SUSPENSION

SEC. 3. (a) Subsection (e) of section 102 of such Act (50 U.S.C. App., 1212(e)) is amended by striking out "or would be subject to this title except for the provisions of section 106(e)" wherever such words appear therein.

(b) The amendment made by subsection (a) shall apply to contracts with the departments and subcontracts only to the extent of the amounts received or accrued by a contractor or subcontractor after June 30, 1968.

ELIMINATION OF COMMERCIAL EXEMPTION

SEC. 4. (a) Section 106 of such Act (50 U.S.C. App., 1216) is amended by striking out subsection (e) thereof.

(b) The amendment made by subsection (a) shall apply to contracts with the departments and subcontracts only to the extent of the amounts received or accrued by a contractor or subcontractor after June 30, 1968.

(c) *Discussion*

In addition to the Renegotiation Board, some Members of Congress have recommended in bills introduced by them that the exemption for standard commercial articles and services be eliminated.

It should be noted that it is difficult to estimate the impact of repealing the standard commercial articles exemption in terms of additional filings and renegotiable sales, especially in view of the

fact that the Renegotiation Board is not notified of a significant portion of the instances in which it is applied. Accordingly, the estimate by the Board of the effect of eliminating this exemption must be viewed in light of the data and forecasting difficulties involved. The Board has estimated that the repeal of the exemption for standard commercial articles and services would result in 600 additional contractor filings with the Board and additional renegotiable sales of \$2.1 billion in fiscal 1969. This would increase estimated renegotiable sales in fiscal 1969 to \$46.6 billion, an increase of 4.7 percent.

A number of interested individuals and organizations submitted comments setting forth their reasons in opposition to the proposed repeal of the exemption for standard commercial articles and services. The reasons advanced are as follows:

The exemption has been in the act since 1954 and was given further consideration by Congress in 1955 and again in 1956 on the basis of experience under the act. Moreover, the exemption was carefully considered by Congress when enacted and also when revised. In essence, Congress factually concluded that in the case of standard commercial articles and services there was no basis or need for renegotiation since cost and pricing experience had already been acquired and prices made in a competitive market. The exemption was designed to recognize the fact that prices on commercial items are made in a competitive market and accordingly can be assumed to be reasonable.

In other words, Congress adopted a minimum exemption to prevent the unreasonable and unnecessary renegotiation of commercial articles that find a fair price in the competition of the marketplace. In addition, the marketplace for standard commercial articles and services is more competitive today than it was in 1956 when the exemption took its present form. Moreover, the exemption presently requires that a company, before it can avail itself of the exemption, must itself have a commercial market and established price for the article or service in question. Under these conditions there are no circumstances in which Congress can justify subjecting the receipts from commercial articles or services to renegotiation since the effect of this would be to allow the Government to indirectly pay less through the working of renegotiation for standard articles or services than commercial purchasers would have to pay.

It is difficult to evaluate the exemption for standard commercial articles because of the incomplete nature of the information regarding the exemption. The extent of the application of the exemption is not known. Moreover, there is little indication of whether the incidence of excessive profits on articles qualifying for the exemption is higher or lower than the incidence of excessive profits on renegotiable sales generally. Also, the effect of the procurement buildup associated with the Vietnam conflict on the incidence of excessive profits on commercial items is not ascertainable at this time. Some tangible evidence with respect to this exemption resulted from the recent investigation of the Special Investigations Subcommittee of the House Armed Services Committee into small purchases practices which revealed situations in which the Government was significantly over-

charged for commercial items. This study indicated deficiencies in procurement procedures for small purchases, although the overall extent of overcharging is not clear.

The premise underlying the exemption for standard commercial articles and services is that the competitive market which exists for these items insures against excessive profits. It is suggested that a competitive market generally is not characterized by uncertainties regarding cost, production, or price experience which may give rise to excessive profits.

In its request for an indefinite extension of the Renegotiation Act, the Renegotiation Board primarily justified the continued need for renegotiation on the basis that market-tested prices do not exist for novel and complex military and space products which accordingly must be procured on the basis of negotiated prices and uncertain cost estimates. By implication, this would appear to corroborate the basic premise of the standard commercial articles exemption.

The primary reason advanced by the Board for removing the standard commercial article exemption was: "The commercial exemption assumes that excessive profits will not result when at least 35 percent of the sales of an article which the contractor either maintains in stock or offers for sale from a price schedule are nonrenegotiable. This assumption is not valid because what is a fair price in commercial sales may be clearly excessive for large Government contracts." In effect, the Board appears to be suggesting that the volume discounts received by the Government on commercial items may not be large enough. Substantial questions may be raised as to whether this is a proper concern of renegotiation. The failure to obtain a proper volume discount would appear to indicate either inadequate implementation of procurement practices by contracting officials or an otherwise crucial defect in procurement methods. This is quite different than the premise on which renegotiation is based; namely, that uncertainties at the time of the procurement of certain types of items requires the after-the-fact review provided by renegotiation.

It would seem that a more fundamental question with respect to the standard commercial articles exemption would be whether the exemption's underlying premise is adequately implemented through the statutory definition. Prior to 1956, the exemption did not apply unless the Board made a specific finding that competitive conditions affecting the sale of an article were such as would reasonably prevent excessive profits. This manner of implementing the premise of the exemption was abandoned in 1956 because of the great burden it placed on the Board and the considerable expense it involved for industry. Instead, it was decided that the underlying premise of the exemption could be implemented by looking at the individual contractor concerned, rather than at an entire industry. In place of the "competitive conditions" test, it was provided that the exemption would apply if at least 35 percent of a contractor's sales during the year of an item or class of items were nonrenegotiable. It was recognized that the substitution of the 35-percent test for the "competitive conditions" test was a considerable liberalization of the exemption then available.

In addition, the exemption for a class of articles was adopted because of the substantial difficulties which would be encountered by

contractors in identifying to whom many similar articles were sold. Contractors' records often do not disclose on a product-by-product basis the buyers of similar products.

Although there is a lack of specific information regarding various aspects of the exemption for standard commercial articles, there are certain factors which suggest it might be desirable to make changes in the exemption. The procurement buildup associated with the Vietnam conflict, although not a crash procurement, may well have put substantial strains on certain markets. In addition, the recent disclosures of overpricing on certain commercial items suggests a higher incidence of excessive profits on these items than the exemption contemplates.

There are three changes which the staff believes the committee might want to see made in the exemption in order to give more assurance that items qualifying for the exemption are commercial products. First, the ratio between renegotiable and nonrenegotiable sales which presently is a prerequisite to application of the exemption would appear to be lower than is appropriate. The commercial nature of an item would be more certain if at least 50 percent of the sales of the item (and the items in a class) were not subject to renegotiation. A similar change regarding services would also be appropriate. Second, it would appear desirable to require contractors who self-apply the exemption to report the self-application and its basis to the Renegotiation Board. This would provide a better indication of the extent to which the exemption is used and also would tend to make contractors more careful in applying the exemption. Third, the investigation by the Special Investigations Subcommittee of the House Armed Services Committee indicates that items maintained in stock or items for which a price schedule is maintained may, in fact, be sold to the Government at prices which are greatly in excess of the prices on a comparable order for a commercial purchaser. This type of price differentiation was not contemplated when the present exemption for standard commercial articles was adopted. Accordingly, it would appear to be appropriate to prescribe an additional requirement which must be met for an article (or service) to qualify as a standard commercial article (or service): namely, that the price at which the article (or service) is sold to the Government must be reasonably comparable to the price charged a commercial purchaser for an order of similar quantity.

Although it is true that a particular product qualifying for the class exemption may be sold entirely to the Government, it does not appear appropriate to make any changes in this aspect of the exemption, other than raising the required percentage of nonrenegotiable sales to 50 percent. The statutory requirements regarding the items which may be included within a class would appear to be adequate to insure a substantial degree of substitutability between the items included in the class. This substantially negates the implications regarding the non-existence of a competitive market which might otherwise be considered to result from the fact that an item included in an exempt class may be sold solely to the Government. Moreover, the basic reason for adopting the class exemption in 1956—the difficulty of identifying sales of similar articles—would appear to be equally valid today.

3. *Permissive exemptions*

Under the "permissive" exemptions provision of section 106 (d) of the act, the Board is authorized, in its discretion, to exempt from some or all of the provisions of the act:

1. Any contract or subcontract to be performed outside of the territorial limits of the continental United States or in Alaska.

2. Any contracts or subcontracts under which, in the opinion of the Board, the profits can be determined with reasonable certainty when the contract price is established.

3. Any contract or subcontract or performance thereunder during a specified period or periods if, in the opinion of the Board, the provisions of the contract are otherwise adequate to prevent excessive profits.

4. Any contract or subcontract the renegotiation of which would jeopardize secrecy required in the public interest.

5. Any subcontract or group of subcontracts not otherwise exempt if, in the opinion of the Board, it is not administratively feasible in the case of such subcontract or in the case of such group of subcontracts to determine and segregate the profits attributable thereto from the profits attributable to activities not subject to renegotiation.

The Board is not permitted to delegate its power to grant permissive exemptions, and it may exercise its power to grant permissive exemptions both individually and by general classes or types of contracts.

Under the last of the permissive exemptions enumerated above the Board is authorized to provide an exemption when in its opinion it is not administratively feasible to determine and segregate the profits described therein. This is known as the "stock item" exemption; it has been in effect throughout the life of the act, and it generally applies to sales made to replenish stock customarily maintained by a purchaser. The Board's regulations (section 1455.6(b)) state that under the exemption it will exempt from the act amounts received or accrued from "all subcontracts subject to the act which are for materials (including maintenance, repair and operating supplies) customarily purchased for stock in the normal course of the purchaser's business, except when such materials are specifically purchased for use in performing one or more prime contracts or higher tier subcontracts subject to the act."

C. THE STATUTORY MINIMUM OR "FLOOR"

1. *Present law*

With one exception, the Renegotiation Act provides that if the aggregate of renegotiable amounts received or accrued during a fiscal year ending after June 30, 1956, by a contractor or subcontractor, is not more than \$1 million, such receipts and accruals shall not be subject to renegotiation. In addition, if the aggregate of the amounts received or accrued is more than \$1 million, no determination of excessive profits may be made in an amount greater than the amount by which the aggregate exceeds \$1 million. The minimum amount subject to renegotiation is referred to as the floor. It was originally \$250,000, was later raised to \$500,000, and, in 1956, was raised to the present \$1 million. For purposes of applying the floor, amounts received or accrued by persons controlling, under the control of, or under common control with, a contractor or subcontractor are combined with the

receipts or accruals of the contractor or subcontractor. Thus, a business may not be fragmented to avoid renegotiation.

The one exception referred to above (respecting the amount of the floor) is contained in section 103(g)(3) of the act, describing certain contracts with brokers, manufacturer's representatives, etc. In those situations, the act provides that the applicable floor is \$25,000, regardless of the year involved. If the aggregate of the amounts received or accrued during a fiscal year from such contracts is more than \$25,000, no determination of excessive profits with respect to such contracts may be made in an amount greater than the amount by which such aggregate exceeds \$25,000.

A contractor who is subject to the act, must file an annual financial statement with the Board if the aggregate of his renegotiable sales exceeds the statutory floor. If his renegotiable sales do not exceed that amount, the contractor may at his election file a statement (of nonapplicability) for the fiscal year with the Board.

2. Suggested changes in the "floor"

A number of proposals have been made to change the present statutory minimum, or floor. It has been recommended that the floor be lowered to \$250,000. It also has been recommended that the floor be raised to \$5 million or to \$10 million. In the past, it has been recommended that the floor be raised to \$2 million.

3. Discussion

At the request of the staff, the Renegotiation Board prepared estimates of the effects of changing the floor to various levels. As is true in the case of the estimates regarding the impact of repealing the standard commercial article exemption, the estimates of the effects of changing the floor must be viewed in light of the forecasting difficulties involved.

The Board estimated that if the floor remained at \$1 million, it would receive 4,800 filings involving renegotiable sales of \$44,500,000 in fiscal 1969. The changes in the amount of filings and renegotiable sales which would result from raising or lowering the floor to various levels, as well as the absolute amount of filings and renegotiable sales which would result if the floor was set at the various levels are indicated in the following table:

ESTIMATED IMPACT OF PROPOSED FLOOR CHANGES, FISCAL 1969

[Dollar amounts of sales in millions]

Amount of floor	Number of filings	Increase or (decrease) in number of filings	Renegotiable sales which would be reported	Increase or (decrease) in reported renegotiable sales
\$5,000,000	2,300	(2,500)	\$40,300	(\$4,200)
2,000,000	3,700	(1,100)	43,300	(1,200)
1,000,000	4,800	0	44,500	0
500,000	7,800	3,000	46,700	2,200
250,000	12,400	7,600	48,400	3,900

Various considerations may be advanced in support of changing the level of the floor. The considerations which support lowering the floor include the following. The present \$1 million floor allows appreciable amounts of renegotiable sales, and presumably excessive profits, to escape the renegotiation process. Moreover, the firms with renegotiable sales of less than \$1 million are in many cases not small business con-

cerns, but rather are large companies whose renegotiable sales comprise a relatively small portion of their total sales. To the extent contractors with less than \$1 million of renegotiable sales are small business concerns, it should be noted that the recent trend in military procurement toward granting a higher percentage of contract awards to small business firms indicates that a significant portion of military procurement awards goes to firms which are not subject to renegotiation because of the present floor. In addition, lowering the floor might increase the amount of voluntary refunds and price reductions made by contractors.

On the other hand there are a number of considerations which support the view that the floor should be maintained at its present level or in fact raised to a higher level. These considerations include the following. Proposals to lower the floor do not appear to take account of the reasons which convinced Congress in 1956 that it should raise the floor to its present level (S. Rept. No. 2624, 84th Cong., 2d sess., 1956):

Because of the substantial compliance cost, renegotiation is a serious burden on small business firms. Another consideration supporting this increase in the statutory floor is the fact that only a small portion of the renegotiation recoveries comes from firms that would be affected by the amendment. This change in the statutory floor will be a substantial aid to small businesses. It will in addition enable the Board to concentrate on the larger cases.

Reducing the floor would complicate administration of the act. Moreover, a lower floor would put a substantial burden on small businesses in terms of the costs of, and personnel needed to, comply with the act. The amount of small companies which do not do business with the Government at present because of the difficulties involved might increase, if in addition these companies were required to cope with the difficulties and expenses of the renegotiation process. In other words, lowering the floor might cause small companies to participate to a lesser degree in defense procurement. This appears to conflict with established Government policy toward small business, as indicated by the increasing amount of military procurement being awarded to small business concerns and also by programs of the Small Business Administration. Moreover, the amount of excessive profits which would be recovered by reason of lowering the floor would in all probability be less than the additional funds which the Renegotiation Board would require to administer the substantially increased number of filings it would receive and be required to process. If the rate of excessive profits actually recovered by the Government (i.e., excessive profits minus the credit for Federal income taxes) on the estimated additional renegotiable sales resulting from a lower floor was the same as the average rate of recoveries on total renegotiable sales for the past 5 years, a \$500,000 floor would result in additional recoveries by the Government of approximately \$620,000 and a \$250,000 floor would result in additional recoveries of \$1.1 million. The Board has informed the staff that its additional expenses would be \$1 million to \$1.5 million if the floor were lowered to \$500,000 and \$3.2 million to \$3.7 million if the floor were lowered to \$250,000. It is difficult to know whether lowering the floor would also increase the amount of voluntary refunds and price reductions.

It also can be argued that even the present floor imposes hardships on small and medium-size companies, and accordingly, the floor should be raised to eliminate this hardship and to bring the renegotiation process into accord with the general Government policy toward small business concerns. Moreover, it has been 12 years since the floor was increased. In view of the increase in the general price level during that period, it can be argued that it is necessary to raise the floor merely to make the relationship of the act to the present economic conditions the same as the relationship which existed when the floor was increased in 1956. The price rise, reflected by the implicit price deflator for the gross national product, suggests that prices at the end of 1967 were 126.5 percent of 1956 prices. In effect, this price rise has lowered the \$1 million floor to about \$790,000 in terms of 1956 prices.

SECTION 6. DETERMINING EXCESSIVE PROFITS

The procedures prescribed by the act for determining excessive profits require that several other determinations first be made. These involve determinations of—

(1) The contractor or subcontractor to be renegotiated.

(2) The fiscal year (or other accounting period) and the method of accounting to be used for renegotiation.

(3) The segregation of the contractor's sales, costs, and profits for the fiscal year between renegotiable and nonrenegotiable business.

After these determinations have been made, the statutory factors enumerated in section 103(e) of the act are applied in order to determine the amount of renegotiable profits which constitute "excessive profits."

A. DETERMINATION OF CONTRACTOR OR SUBCONTRACTOR

Section 105(a) requires the Board to exercise its powers with respect to amounts received or accrued by a "contractor or subcontractor," but that term is not defined in the act. However, section 103(j) does define "person" to include "an individual, firm, corporation, association, partnership, and any organized group of persons whether or not incorporated." And, the Board's regulations provide that the term "contractor" generally includes "subcontractor," and that a joint venture will be treated as a contractor or subcontractor within the meaning of the act.

Section 105(a) of the act requires renegotiation to be conducted on a consolidated basis with a parent and its subsidiary corporations which constitute an "affiliated group" under the provisions of the Internal Revenue Code, if all the corporations within the group request renegotiation on that basis and consent to certain regulations of the Board. This section of the act also authorizes the Board in its discretion, and by agreement with the contractor, to conduct renegotiation on a consolidated basis "in order properly to reflect excessive profits of two or more related contractors or subcontractors."

B. DETERMINATION OF THE CONTRACTOR'S FISCAL YEAR AND ACCOUNTING METHOD

Section 105(a) of the act provides that renegotiation is to be conducted "with respect to the aggregate of the amounts received or accrued during the fiscal year (or such other period as may be fixed by mutual agreement)" and "not separately with respect to amounts received or accrued under separate contracts." (However, the Board may conduct renegotiation with respect to one or more separate contracts at the request of the contractor or subcontractor.) The fiscal year referred to in the act is the contractor's taxable year for Federal income tax purposes.

The Board's most recent annual report to Congress expressed the following views regarding the fact that renegotiation is conducted on a fiscal year basis:

The contracts may vary in form from cost-plus-a-fixed-fee to firm fixed-price; they may be prime contracts or subcontracts; and they may relate to a variety of products and services. Also, they may be performed over differing periods: some may be completed within the contractor's particular fiscal year, while the performance of others may extend beyond such year. Accordingly, aggregate renegotiable profits during any fiscal year of a given contractor will often reflect the performance of different contracts in different stages of completion, and may result from an offset of losses or low profits on some contracts against high or even excessive profits on others. Thus fiscal year renegotiation, which deals with aggregate profits, is entirely different from price adjustment or redetermination of individual contract prices pursuant to contract provisions.

Sections 103 (f) and (i) of the act provide that receipts and accruals and costs are to be determined in accordance with the method of accounting regularly employed by the contractor in keeping his records; however, if such a method of accounting does not, in the Board's opinion, properly reflect the contractor's receipts, accruals, or costs, then these items are to be determined in accordance with the method which does, in the opinion of the Board, properly reflect the items. The Board's regulations require the use of the method of accounting employed for Federal income tax purposes, but also provide for special accounting agreements in writing, between the contractor and the Board, if the tax method is "manifestly unsuitable for the purpose of renegotiation because it does not clearly reflect" renegotiable profits, and the method to be adopted does clearly reflect such profits. Such an agreement may change the contractor's entire method of accounting, or it may provide only for the treatment of a particular item of cost. In addition, a change may be permitted to the "completed contract method" in the case of certain contracts; for example, contracts for the construction of major facilities or major units (such as a vessel), etc.

C. DETERMINATION OF RENEGOTIABLE SALES, COSTS, AND PROFITS

For purposes of segregating renegotiable sales and costs, the Board's regulations provide that the terms "renegotiable business" and "renegotiable sales" mean the aggregate business of a contractor or subcontractor under subject prime contracts and subcontracts which are not exempt, and that the term "nonrenegotiable business" means any business of a contractor or subcontractor other than renegotiable business. The regulations note that the report which a contractor files with the Board requires a statement of the amount of his renegotiable sales and for an explanation of the methods used in determining that amount. They also state that "The contractor has the primary responsibility for determining which of its sales are subject to renegotiation," and that his segregation of such sales must be satisfactory to the Board.

Section 103(f) of the act defines the term "profits derived from contracts with the Departments and subcontracts" to mean "the excess of the amount received or accrued under such contracts and subcontracts over the cost paid or incurred with respect thereto and determined to be allocable thereto." That same provision provides generally, that all items estimated to be allowed as deductions and exclusions under the Internal Revenue Code shall, to the extent allocable to such contracts and subcontracts, be allowed as items of cost.

D. THE STATUTORY FACTORS

Section 103(e) of the act provides that in determining "excessive profits" the Board must give favorable recognition to the efficiency of a contractor or subcontractor, and that it give particular consideration to the attainment of quantity and quality production, reduction of costs, and economy in the use of materials, facilities, and manpower. In addition, the following factors set forth in that section (commonly referred to as the "statutory factors") are to be taken into account in determining excessive profits:

(1) Reasonableness of costs and profits, with particular regard to volume of production, normal earnings, and comparison of war and peacetime products.

(2) The net worth, with particular regard to the amount and source of public and private capital employed.

(3) Extent of risk assumed, including the risk incident to reasonable pricing policies.

(4) Nature and extent of contribution to the defense effort, including inventive and developmental contribution and co-operation with the Government and other contractors in supplying technical assistance.

(5) Character of business, including source and nature of materials, complexity of manufacturing technique, character and extent of subcontracting, and rate of turnover.

(6) Such other factors the consideration of which the public interest and fair and equitable dealing may require, which factors shall be published in the regulations of the Board from time to time as adopted.

The determination of excessive profits may also be affected by renegotiation losses in a year prior to the year under review. Section 103(m)(4) of the act provides that a renegotiation loss for any fiscal year (the "loss year") ending on or after December 31, 1956, shall be a renegotiation loss carry forward to each of the 5-fiscal years following the loss year. The act does not provide for a carryback of such losses.

Section 105(a) of the act provides as follows:

Whenever the Board makes a determination with respect to the amount of excessive profits, and such determination is made by order, it shall, at the request of the contractor or subcontractor, as the case may be, prepare and furnish such contractor or subcontractor with a statement of such determination, of the facts used as a basis therefor, and of its reasons for such determination. Such statement shall not be used in The Tax Court of the United States as proof of the facts or conclusions stated therein.

In its last annual report to the Congress, the Board commented as follows upon the statutory factors contained in section 103(e) of the act:

It is apparent from the statutory language that no formulae or preestablished rates can be used to determine whether the profits are, or are not, excessive in any given case. Rather, the determination in each instance must reflect the judgment of the Board on the application of each of the statutory factors * * * to the facts of the specific case.

These statutory factors have been viewed by others, however, as too general to provide any realistic basis for determining whether profits in a specific case are excessive.

It is difficult, of course, to formulate a prescribed set of standards to determine the reasonableness of a business concern's profits which is both specific enough to be implemented and general enough to take account of the varieties and multiplicity of situations to which it must be applicable.

It would appear that the application of the statutory factors to reach a determination of whether profits in a given case are excessive in view of the attendant factors and circumstances will essentially involve a process of economic evaluation and comparison. In other words, if, for investment purposes, a business concern was being evaluated to determine its financial position and the degree of its profitability, the process would basically involve an economic analysis of the concern through the use of the various analytical tools available and then a comparison of the results of that analysis with the results of analyses of other similarly situated business concerns.

In evaluating a business, various ratios may be developed to determine the company's financial position. Thus, ratios which relate net income after taxes to sales, various items of expense to sales, net profit after taxes to total sales, and net profit after taxes to stockholders equity may be used to measure a concern's profitability. Other ratios may be used to measure the concern's use of assets, such as the relationship of sales to inventories, cost of goods sold to inventories, net investment in plant to sales, and receivables to sales. A concern's liquidity may be measured by ratios such as the following: the relationship of current assets to current liabilities; the ratio of cash, marketable securities, and receivables to current liabilities; and the relationship of cash and marketable securities to average daily cash payments. Of course, numerous other ratios are available to take into account the varying factors in specific types of situations.

After an economic analysis of a concern's financial position has been developed, comparisons are necessary in order to evaluate the results of the analysis. Thus, the concern could be compared with other concerns in the same type of business or with similar product lines and with other concerns of the same relative size. The results of the economic analysis for the year could be compared with other years' analyses. These comparisons, by indicating the relative position of the concern, would provide the basis for an overall judgment of the concern.

In essence, the renegotiation process would appear to involve procedures very similar to those employed in analyzing a company's financial position for investment purposes. In other words, the various

analytical ratios would be developed, including those necessitated by the nature of defense and space program work, and the various relevant comparisons made. The product of this analysis would be an indication of the degree to which the profits of the business concern were substantially above a reasonable, competitive norm; in other words, the extent to which the profits were excessive. The present statutory definition would appear to be a fair statement of the process of economic evaluation and comparison which is the essence of renegotiation.

Concern has been expressed, however, regarding the manner in which the statutory factors are applied by the Renegotiation Board in various types of situations. One specific area of concern has been the treatment of incentive contracts. In the last several years, greater use has been made of incentive-type contracts in procurement, and concern has been expressed by some regarding the treatment which the Board would accord profits realized from this type of contracting. In order to state its position, the Board issued release No. 3-62 on April 17, 1962. It contained the following views regarding the treatment of incentive contracts:

The Renegotiation Board has followed with interest the formulation of the [Defense] Department's incentive program, and recognizes its objectives. The Board understands that the new program represents an expansion and modification of past incentive arrangements. The Board is aware that the Department hopes to achieve its aim of greatly reducing the cost of new weapons, improving their quality and speeding their development, by encouraging and rewarding performance efficiency and by penalizing inefficiency. The Board believes that the Renegotiation Act does not impede the proper accomplishment of these objectives.

Under the Renegotiation Act and regulations, the Renegotiation Board rewards demonstrated efficiency by according it "favorable recognition" in determining whether and the extent to which the contractor's total profits, from all its contracts in a fiscal year, are excessive in the light of the several factors prescribed in the Renegotiation Act. The Board's determination is not earmarked to the profits on any particular contract, or any particular portion of a contract. Bonus profits realized under an incentive-type contract, and the performance facts that gave rise to them, are a part, but only a part, of the total renegotiation case.

The regulations of the Board state that particular attention will be given, under the statutory factor of efficiency, to the nature and objectives of incentive contracts and the extent to which any differences between estimated costs and actual costs are the result of the efficiency of the contractor. The regulations also state that the Board will consider and give due regard to the views of the contracting agencies on such differences and reasons therefor. It is believed that these and other provisions of the regulations are adequate to enable the Board, as an independent agency, to give fair and proper consideration to performance excellence in the context of the whole case under all the factors prescribed in the renegotiation law.

In the 6 years which have elapsed since the Board stated its position on incentive contracts, the use of incentive contracts has increased substantially. This is particularly true in the case of the National Aeronautics and Space Administration: the relative use of incentive contracts in NASA procurement increased from less than 2 percent in fiscal 1962 to 68 percent in fiscal 1967. In addition, there have been significant improvements during this period in cost analysis and certification procedures and in profit review and control techniques. The Renegotiation Board does not appear to have officially indicated in its regulations or rulings, however, whether it has reevaluated its 1962 position on the treatment of amounts received under incentive contracts in light of the intervening procurement changes.

The need for reconsideration of the manner of treating incentive contracts in renegotiation is suggested not only by the fact that there does not appear to have been an indication of a change in policy in this regard since 1962, but also by the comments of the National Aeronautics and Space Administration on this matter. NASA stated that it does not believe the Renegotiation Board has given full recognition to the difficult performance requirements of NASA's major research and development programs and the role which incentive contracts have been given within this framework. In other words, in order to obtain the best contractor performance in its programs, NASA relies on a combination of extensive management and technical program reviews and incentive contract arrangements which relate a contractor's profit to the quality of his work and his ability to meet program requirements. NASA believes the result of this combination is a thoughtful control of profit, on the one hand, and high performance stimulated by incentives, on the other hand.

If the Renegotiation Board has not already done so, it is believed the Board should reevaluate the manner in which incentive contracts are taken into account for purposes of renegotiation and report to the committee the results of this reevaluation. Such a report might include a detailed discussion of the specific manner in which the Board implements the statutory command that “* * * favorable recognition must be given to the efficiency of the contractor or subcontractor * * *” When it considers incentive contracts. The report might also indicate specifically the manner in which incentive contracts awarded by NASA are taken into account. In other words, the Board might indicate how it takes into account the procurement difficulties with which NASA is faced and the contracting arrangements and review programs NASA has instituted to deal with these difficulties in determining whether profits realized on NASA incentive contracts are “excessive.”

SECTION 7. STAFF RECOMMENDATIONS

A. EXTENSION OF THE RENEGOTIATION ACT

It is recommended that the act be extended for 2 years, or until June 30, 1970.

It appears appropriate to continue the act for this period in view of a number of factors which have been discussed more fully above. One of these factors is the substantial increase in procurement by the departments and agencies subject to the act in the last 2 years. The normal timelag between the time of contract awards and the time of determinations under the Renegotiation Act indicates that amounts received under contracts awarded during the Vietnam buildup will be reported in filings with the Renegotiation Board during at least the next 2 years.

Although substantial changes have been made in the Department of Defense procurement practices in recent years, it appears there is a need to further assess the effectiveness of these practices in insuring that excessive profits will not be obtained on Government defense business, especially in light of the possible impact on these practices of the increase in procurement associated with Vietnam.

On the other hand, it is possible that further time and study will demonstrate that effective procurement practices can achieve normal competitive profits on Government work, or at least reduce the incidence of excessive profits on defense and space work to an insignificant level. In addition, the nature of renegotiation in principle, and its substantial reliance on human judgment in operation, make it a process which should be periodically reviewed. These factors lead to the conclusion that the Renegotiation Act should not be made a permanent feature of the law. In other words, the nature of the renegotiation process, and the many and changing variables of the overall framework within which renegotiation functions, demonstrate the need for a continuing and periodic review of the Renegotiation Act by Congress.

Although a 2-year extension of the act is recommended by the staff, it should be noted that present circumstances would also appear to justify a 4-year extension. The primary factor in this regard is the consideration that it will probably require more than 2 years to adequately determine the effectiveness of new procurement methods in limiting excessive profits. In addition, the application of the renegotiation process to amounts received under contracts awarded during the Vietnam buildup will continue for more than 2 years. Noting that a 4-year extension of renegotiation would appear justified is not to suggest that Congress should not continue to exercise a periodic and continuing review of the Renegotiation Act, but rather to say that present circumstances and past experience with the act suggest that it might be appropriate for Congress to wait 4 years, instead of 2 years, to exercise that review.

B. EXEMPTION FOR STANDARD COMMERCIAL ARTICLES

The committee may wish to give consideration to revising the exemption for standard commercial articles and services in order to more adequately insure that goods and services qualifying for the exemption are, in fact, commercial items. If the committee desires to take action on this area, the staff recommends three modifications in the exemption. First, the percentage of the sales of an article or service (or class of articles) which must be nonrenegotiable for the exemption to apply could be raised to 50 percent. Second, contractors who self-apply the exemption for a standard commercial article could be required to report the application, and its basis, to the Board. Third, it could be provided that for the exemption to apply, a standard commercial article (or service) must be sold to the Government at a price which is reasonably comparable to the price charged a commercial purchaser for an order of similar quantity. These recommendations are discussed in greater detail in section 5 of the report.

C. ADDITIONAL DATA REQUIRED FOR EVALUATION OF RENEGOTIATION

In the course of its present study of renegotiation, the staff found that needed information was not available with respect to a number of the aspects of the renegotiation process. The lack of this information prevented adequate analysis of some of the more fundamental questions raised with respect to renegotiation, such as: What types of contracts have produced "excessive profits"; whether "excessive profits" are more prevalent in certain industries; whether "excessive profits" occur more frequently with respect to firms of a given size; and the relationship between procurement policies and the method of their implementation, on the one hand, and the policy of renegotiation and the manner of its implementation, on the other hand (e.g., whether the Defense Department profit policy and the renegotiation process are in conflict).

In order to make the needed information available for purposes of future evaluations of the renegotiation process, the staff recommends that the Renegotiation Board develop and maintain the following types of information:

(1) A more detailed breakdown of renegotiable sales and profits by type of contract for contractors reporting net profits on their renegotiable sales as well as for those reporting net losses. (In other words, data for cost-plus-incentive-fee contracts and fixed-price incentive contracts, in addition to the presently available data for (firm) fixed-price and cost-plus-fixed-fee contracts.)

(2) Renegotiable sales and profits by type of industry and size of contractor (asset size and amount of sales); in addition, data on nonrenegotiable sales and profits for these same firms.

(3) Renegotiable profits (before and after renegotiation) as a percent of contractor net worth (including reporting of amounts of Government supplied capital and equipment).

(4) Data analyses of firms determined to have excessive profits: types of industries, sales and profits by types of contracts, percentage distribution of their renegotiable contracts by types, contractor net worth, and amounts of Government supplied capital.

D. TREATMENT OF INCENTIVE CONTRACTS

In 1962, the Renegotiation Board stated its position on the treatment in renegotiation of amounts received under incentive contracts. Since that time, the use of incentive contracts has increased significantly and substantial developments have occurred in the area of cost control and review procedures. In addition, the National Aeronautics and Space Administration stated its belief that inadequate recognition has been given by the Renegotiation Board to NASA incentive contracts and the reasons underlying their use. These factors suggest the need for a reconsideration of the manner in which incentive contracts are taken into account for renegotiation purposes.

The staff recommends that the Renegotiation Board reevaluate its treatment of incentive contracts, and report the results of this reevaluation to the committee. The report might include a detailed discussion of the specific manner in which incentive contracts are taken into account in the renegotiation process. Moreover, the report might place particular emphasis on the specific manner in which the Board takes NASA's procurement difficulties, programs, and contracting arrangements into account in determining whether profits realized on NASA incentive contracts are "excessive."

Appendix A

SUGGESTED CHANGES IN THE RENEGOTIATION ACT

Various changes in the Renegotiation Act have been suggested in bills introduced by Members of Congress and in comments of interested individuals and organizations which were submitted to the Committee on Ways and Means and made available to the staff of the Joint Committee on Internal Revenue Taxation. The proposed changes concerning the length of the extension of the act (i.e., whether renegotiation should be made permanent), the statutory floor, and the exemption for standard commercial articles have been discussed in earlier parts of this report. The other changes which were suggested are summarized below:

A. DEPARTMENTS COVERED BY THE ACT

It was suggested that the act be made applicable to the Tennessee Valley Authority. (H.R. 6792, Mr. Gonzalez; H.R. 14678, Mr. Vanik; H.R. 14697, Mr. Feighan; H.R. 14999, Mr. Minshall; H.R. 15341, Mr. Evins.)

It was also suggested that certain "fringe" agencies be eliminated from the application of the act; namely, the General Services Administration, purchases in connection with the civil works functions of the Army Corps of Engineers, and the nonmilitary procurements of the Atomic Energy Commission. (Machinery and Allied Products Institute, Charles Stewart, president.)

B. EXEMPTIONS

It was suggested that amounts received under arm's-length bona fide competitive bid subcontracts for a sum of less than \$1 million be exempted from renegotiation, if the subcontractor is not affiliated with the prime contractor. (H.R. 3100, Mr. Multer.)

It was suggested that the existing partial mandatory exemption for new durable productive equipment be limited in its application to subcontracts where the equipment does not become a part of either an end product acquired by the Government or of an article incorporated in such an end product. (H.R. 6792, Mr. Gonzalez; H.R. 1467, Mr. Vanik; H.R. 14697, Mr. Feighan; H.R. 14999, Mr. Minshall; H.R. 15341, Mr. Evins.)

It was suggested that the existing exemption for competitive bid contracts for the construction of any building, structure, improvement, or facility be eliminated. (H.R. 6792, Mr. Gonzalez; H.R. 14678, Mr. Vanik; H.R. 14697, Mr. Feighan; H.R. 14999, Mr. Minshall; H.R. 15341, Mr. Evins.)

It was suggested that an exemption be added for all formally advertised competitive bid supply contracts. (Machinery and Allied Products Institute, Charles Stewart, president.)

It was suggested that cost-plus-fixed-fee contracts be exempted from renegotiation. (Winzen Research, Inc., D. R. Williams, vice president.)

It was suggested that contracts in which incentive and competitive elements have been introduced be exempted from renegotiation. (National Association of Manufacturers.)

It was suggested that all contracts with a value of less than \$5 million be exempted from renegotiation. (National Association of Manufacturers.)

C. FISCAL YEAR BASIS OF RENEGOTIATION

It was suggested that the provisions of the Renegotiation Act which allow a 5-year carry forward of losses on renegotiable sales be amended to also allow a 3-year loss carryback. It also was suggested that a 5-year loss carryback be allowed. It was further suggested that a carry forward and carryback of inadequate profits be allowed. (Machinery and Allied Products Institute, Charles Stewart, president, and National Association of Manufacturers.)

D. OTHER

It was suggested that amounts received under competitive bid subcontracts should not be taken into account for purposes of applying the statutory floor, if three or more competitive bidders took part in the bidding and the subcontractor is not affiliated with the prime contractor. (H.R. 3100, Mr. Multer.)

It was suggested that some form of relief should be extended to companies whose business generally consists of competitive bid subcontracts. (Mr. Donald A. Holmes, Minneapolis, Minn.)

It was suggested that the act be made inapplicable to contractors whose renegotiable sales amount to 5 percent or less of their total sales. (Machinery and Allied Products Institute, Charles Stewart, president.)

It was suggested that cost allowances consistent with those allowed by the Internal Revenue Service be allowed for purposes of renegotiation, including allowances for contributions, interest, advertising new securities issues, and expenses for corporate organizations. (National Association of Manufacturers.)

It was suggested that the Renegotiation Board in determining excessive profits be required to give favorable recognition to economies achieved through contracting with small business concerns. It also was suggested that in determining excessive profits a contractor or subcontractor who achieves economies through governmental programs to increase the share of small business concerns in procurement be allowed incentive rewards with fair profit allowances. (H.R. 3100, Mr. Multer.)

It was suggested that the act be amended to provide for the revocation of any excessive profits determination if the amount of "excessive profits" is employed directly by the contractor to conduct reconversion planning, to undertake new commercial product research and development, to conduct market surveys on products not connected with Government work, or otherwise to be used in reconverting to civilian activity company facilities now devoted to defense work. (Machinery and Allied Products Institute, Charles Stewart, president.)

Various changes regarding the organization and procedures of the Renegotiation Board were suggested; namely, that minority party representation be required on the Board; that appointees to the Board be required to be "qualified and experienced in financial or logistical activities"; that the Board be required to establish and maintain a regional office in the south-central area of the country; and that the Board be required, prior to arriving at a settlement agreement with, or issuing a unilateral order against, a contractor to make available to the contractor the reports, documents, etc., which the Board has prepared or obtained regarding the contractor's performance. It was further suggested that a corps of hearing examiners be established within the Board's structure to adjudicate appeals by contractors and subcontractors aggrieved by an order of the Board determining an amount of excessive profits. (Ives, Whitehead & Co., Inc., W. S. Whitehead, president.)

It was suggested that the flat rate profit limitations contained in the Vinson-Trammel Act of 1934 and the Merchant Marine Act of 1936 be repealed. (Machinery and Allied Products Institute, Charles Stewart, president; National Security Industrial Association, J. M. Lyle, president.)

It was also suggested that these flat rate profit limitations be repealed if renegotiation is made permanent (Shipbuilders Council of America, Edwin M. Hood, president).

Appendix B

PROCUREMENT TRENDS, METHODS, AND POLICIES

A. RECENT TRENDS IN DEFENSE AND SPACE RELATED PROCUREMENT

In examining the renegotiation process, and in order to put renegotiation into context, it is useful to look at the procurement activities of the Government agencies covered by the Renegotiation Act; namely, the Department of Defense (DOD), the National Aeronautics and Space Administration (NASA), the Atomic Energy Commission (AEC), the General Services Administration (GSA), the Maritime Administration and Maritime Subsidy Board (formerly Federal Maritime Board) (MAMSB), and the Federal Aviation Agency (FAA) which has been a covered agency since the beginning of fiscal year 1965. In this part of the report, various aspects of the procurement activities of these departments and agencies are considered. The major emphasis is focused, of course, upon the Department of Defense in view of the relative magnitude of its procurement activities within the overall framework of defense and space related procurement.

1. Trends in total defense related procurement

The historical trend in total DOD military procurement (including intragovernmental and overseas purchases) from fiscal years 1951 to 1967 is shown in table 1. The peak year for total military procurement prior to 1967 was the Korean conflict year of 1952, \$43.6 billion, as compared to \$44.6 billion in 1967. Following the low year of 1954 of \$13.3 billion, total military procurement increased steadily (except for a decline in 1960) until reaching a 1963 total of \$29.4 billion. In 1964 and 1965 there were slight declines in total military procurement before the 1966 and 1967 Vietnam conflict expenditure increases.

TABLE 1.—TOTAL DEPARTMENT OF DEFENSE MILITARY PROCUREMENT, FISCAL YEARS 1951-67

[Amounts in millions]

<i>Fiscal year:</i>	<i>Total procurement</i> ¹
1951	\$32,649
1952	43,569
1953	31,812
1954	13,279
1955	16,582
1956	19,590
1957	21,458
1958	24,197
1959	25,312
1960	23,689
1961	25,584
1962	29,254
1963	29,379
1964	28,796
1965	27,997
1966	38,243
1967	44,632

¹ Includes intragovernmental procurement and purchases outside the United States.

Source: Office of the Secretary of Defense, "Military Prime Contract Awards and Subcontracts or Commitments, July 1966 to June 1967," and "July 1961 to June 1962."

(a) *Korean versus Vietnam military procurement buildup*

Data for total military procurement (including intragovernmental purchases and purchases outside the United States) are not indicated in Defense Department statistics for years prior to fiscal 1951; however, comparable figures for the net value of military contract awards to business firms for work within the United States indicate a rapid expansion from \$5.4 billion in 1950 to \$30.8 billion in 1951 (almost a sixfold increase) due to the sudden nature of the involvement in the military conflict (and a further increase of \$10.7 billion in 1952). On the other hand, the Vietnam buildup was more gradual, with the greatest increase occurring in 1966 (an \$8.7 billion increase, or 34.6 percent). The 2-year (1965-67) buildup (again, on the basis of procurement with business firms within the United States) was \$14.5 billion, or 57.5 percent (see table 6 for the historical trend in military contract awards to business firms in the United States, 1948-67). The amount of procurement with business firms within the United States was \$34.0 billion in 1966 and \$39.8 billion in 1967.

On the basis of total military procurement (table 2), the 1965-1967 buildup was \$16.6 billion, or 59.4 percent. The 1965-67 increase, excluding intragovernmental, was \$16.0 billion, or 58.4 percent.

(b) *Changes in military procurement, 1960-67*

(i) *Total DOD contract awards.*—Most of the statistical data for DOD military procurement in this report covers fiscal years 1960-1967. On the total procurement basis, military contracts increased \$20.9 billion from \$23.7 billion in 1960 to \$44.6 billion in 1967, or 88.4 percent.

Total procurement, excluding intragovernmental, rose from \$22.9 billion in 1960 to \$43.4 billion in 1967, or 89.4 percent; at the same time, contract awards to business firms in the United States increased from \$21.3 billion in 1960 to \$39.8 billion in 1967, or 86.7 percent.

(ii) *Small business awards.*—During the same period, military prime contract awards to "small business" grew by 134.7 percent, from \$3.4 billion to \$8.1 billion. Small business awards as a percent of total business awards ranged from a low of 15.9 percent in 1961 to a high of 21.4 percent in 1966, with a slight decline to 20.3 percent in 1967.¹

¹ A small business concern is a firm as defined by the Small Business Administration in the Federal Register (title 13, chap. I, pt. 121). The definition also is published in the Armed Services Procurement Regulation (1-701). Generally, a small business concern is one that is independently owned and operated, is not dominant in its field of operations, and with its affiliates does not employ more than a specified number of employees (usually not more than 500, 750, or 1,000) depending on the type of product called for by the contract. For construction and some service industries, the criterion is a specified annual dollar volume of sales or receipts instead of employment.

TABLE 2.—COMPARISONS IN MILITARY PROCUREMENT, FISCAL YEARS 1960-1967

[Dollar amounts in millions]

Fiscal year	Total procurement	Total excluding intragovernmental	Total to all business firms in the United States	Small business	
				Amount	Percent
1960.....	\$23,689	\$22,908	\$21,302	\$3,440	16.1
1961.....	25,584	24,703	22,992	3,657	15.9
1962.....	29,254	28,099	26,147	4,622	17.7
1963.....	29,379	29,032	27,143	4,301	15.8
1964.....	28,796	28,234	26,221	4,519	17.2
1965.....	27,997	27,385	25,281	4,943	19.6
1966.....	38,243	37,229	34,026	7,269	21.4
1967.....	44,632	43,381	39,809	8,073	20.3
Amount increase 1960-67.....	20,943	20,473	18,507	4,633	-----
Percent increase 1960-67.....	88.4	89.4	86.9	134.7	14.2

¹ Percentage points increase.

Source: Office of the Secretary of Defense, "Military Prime Contract Awards and Subcontracts or Commitments, July 1966 to June 1967," and "July 1961 to June 1962."

(iii) *DOD subcontracting awards*.—Total subcontracting in DOD military contracts indicated a fluctuating picture: \$9.7 billion in 1960; a slight decline in 1961; up to \$11.4 billion in 1963; down again to \$8.5 billion in 1965; with a sharp rise to \$15.5 billion in 1967.

The small business share of total subcontracting, however, maintained a steady climb from 37.1 percent in 1960 to 43.3 percent in 1967. Thus, small business firms received total military contract awards (prime and subcontracts) of \$7.0 billion in 1960, with an increase to \$14.8 billion in 1967, or 110.2 percent. These small business totals represented an average of one-third of the total military awards to business firms in the United States during 1960-67.

TABLE 3.—DEFENSE DEPARTMENT MILITARY SUBCONTRACTING PROGRAM, FISCAL YEARS 1960-67

[Dollar amounts in millions]

Fiscal year	Total subcontracting ¹	Small business subcontracting		Small business total—prime and subcontracting	
		Amount ²	Percent	Amount	Percent of total prime business awards
1960.....	\$9,666	\$3,587	37.1	\$7,027	33.0
1961.....	9,407	3,495	37.2	7,152	31.1
1962.....	10,560	4,011	38.0	8,633	33.0
1963.....	11,411	4,341	38.0	8,642	31.8
1964.....	9,278	3,629	39.1	8,148	31.1
1965.....	8,518	3,534	41.5	8,477	33.5
1966.....	12,163	5,102	41.9	12,371	36.4
1967.....	15,472	6,697	43.3	14,770	37.1

¹ Represents commitments starting with fiscal year 1964 and payments for prior years. Subcontract amounts relate to the year subcontracting is awarded; therefore, the amounts may or may not coincide with the year of the prime contract award.

² Represents subcontracting from "large" business military prime contractors only; however, the amount of subcontracting received by small business includes an insignificant amount of DOD civil subcontracts (e.g., Corps of Engineers contracts). The total amount of DOD civil contracts for all business in the United States was only \$800,000,000 in fiscal year 1967; \$288,000,000 of this amount went to small business concerns as prime civil contracts.

Small business concerns are not required by the DOD to report amounts subcontracted by them. Large firms are required to report any subcontracting on any prime contract of \$500,000 or more (DOD administrative policy).

Source: Office of the Secretary of Defense, "Military Prime Contract Awards and Subcontracts or Commitments, July 1966 to June 1967," and "July 1961 to June 1962."

(c) *DOD military procurement awards by program, 1960-67*

(i) *Changes in program procurement, 1960-67.*—A comparison of DOD military procurement awards by programs for 1960-67 to business firms for work in the United States is shown in table 3A. "Large" contract awards (over \$10,000) for "hard goods" accounted for over 70 percent of military procurement amounts during 1960-67. These contract awards were for the sizable items typical of major military equipment: for example, aircraft, missiles, ships, tanks, weapons, electronic equipment, ammunition, and so forth. Total procurement of these hard goods increased from \$15.7 billion in 1960 to a pre-Vietnam high of \$20.2 billion in 1963. A decrease to \$17.5 billion in 1965 was followed by an increase to \$28.5 billion in 1967, which was 81 percent over the 1960 level. Procurement for services, soft goods, and actions of less than \$10,000, however, more than doubled: from \$5.6 billion in 1960 to \$11.3 billion in 1967.

Procurement of military items commonly characterized as "costly, novel, and complex" (for example, aircraft, missile and space systems, ships, and electronics and communications equipment) increased from \$13.8 billion in 1960 to \$20.2 billion in 1967, or 46 percent. At the same time, other less costly (per unit), more standardized, and less complete military hard goods (for example, tank-automotive, weapons, ammunition, and miscellaneous) increased from \$1.9 billion to \$8.3 billion, or 331 percent.

Procurement awards for (a) standard military soft goods such as subsistence and textiles, clothing, and equipage and (b) for all contract actions of less than \$10,000 increased from \$2.2 billion in 1960 to \$6.1 billion in 1967, or 179 percent. Thus, procurement of the more standardized and less costly (per unit) hard and soft goods (as well as all awards of less than \$10,000) increased by \$10.3 billion from 1960 to 1967. On the other hand, there was only a \$6.4 billion increase in the more "costly, novel, and complex" military items.

(ii) *Vietnam military program buildup, 1965-67.*—Of the \$18.5 billion increase in military procurement, 1960-67, \$14.5 billion occurred during the Vietnam military buildup, 1965-67. Procurement for total hard goods rose by \$11.0 billion. The remaining \$3.5 billion of the increase was for services and soft goods.

Within the hard goods category, the more "costly, novel, and complex" items (aircraft, missile and space systems, ships, and electronics and communications equipment) increased by \$5.7 billion, or 40 percent.

Procurement of other "less costly (per unit) and less complex" hard goods rose by \$5.2 billion, or 72 percent. Ammunition procurement showed the greatest percentage buildup during 1965-67: an increase from \$0.8 billion in 1965 to \$3.6 billion in 1967, or 368 percent (more than 4½ times the 1965 level).

Contract awards for "services" increased by \$1.2 billion, or 70 percent. At the same time, procurement of (a) such standard soft goods as subsistence and textiles, clothing, etc. and (b) all awards of less than \$10,000 rose by \$2.3 billion, or 60 percent. Thus, the "less costly and less complex" hard goods, soft goods, services, and the smaller contract awards of less than \$10,000, accounted for the greatest part of the 1965-67 buildup.

Table 3A

MILITARY PROCUREMENT AWARDS BY PROGRAM, TO BUSINESS FIRMS FOR WORK IN THE UNITED STATES

[Amounts in millions of dollars]

Major program	1960	1961	1962	1963	1964	1965	1966	1967
Total, business firms in the United States.....	21,301	22,992	26,147	27,144	26,221	25,281	34,026	39,809
Hard goods.....	15,726	17,499	19,862	20,176	18,721	17,524	24,025	28,497
Aircraft.....	4,788	4,936	5,104	5,479	6,067	5,781	7,510	9,677
Missile and space systems.....	4,984	5,884	6,690	6,689	5,579	4,233	4,124	4,333
Ships.....	1,010	1,366	1,475	1,683	1,485	1,691	1,316	2,048
Tank-automotive.....	404	579	1,044	1,032	745	851	1,555	1,438
Weapons.....	121	143	220	214	211	299	500	617
Ammunition.....	476	552	921	886	661	759	2,830	3,554
Electronics and communications equipment.....	3,026	3,154	3,306	3,061	2,918	2,778	3,602	4,160
Miscellaneous hard goods.....	918	886	1,101	1,133	1,054	1,132	2,588	2,671
Services.....	1,321	1,090	1,090	1,504	1,800	1,740	2,290	2,950
All other.....	4,255	4,402	5,196	5,464	5,700	6,017	7,711	8,361
Subsistence.....	469	469	575	586	579	647	1,046	1,125
Textiles, clothing, and equipage.....	177	264	408	259	262	301	1,246	1,141
Fuels and lubricants.....	859	818	883	877	788	818	908	1,059
Construction.....	1,207	1,186	1,214	1,132	1,360	1,325	2,588	1,185
All actions of less than \$10,000.....	1,543	1,665	2,117	2,610	2,710	2,855	3,481	3,852

Source: Office of the Secretary of Defense, "Military Prime Contract Awards and Subcontract Payments or Commitments, July 1966-June 1967," and "July 1965-June 1966."

(d) Changes in nondefense agency procurement, 1961-67

Procurement contract awards to covered agencies, other than the Defense Department, are summarized in table 4 for fiscal years 1961-67. Space related procurement by NASA and atomic energy contracts by AEC accounted for the majority of nondefense procurement awards. The peak procurement year for NASA was 1965, \$4.1 billion, which was almost a tenfold increase over 1961; whereas, the 1967 total was \$3.8 billion. The high year for AEC was 1962, \$2.7 billion, which was followed by declining procurement to \$2.3 billion in 1967. On the other hand, GSA procurement more than doubled from \$0.9 billion in 1961 to \$1.9 billion in 1967. Combined nondefense covered agency procurement rose from \$4.3 billion in 1961 to \$8.3 billion in 1967, or 92.6 percent.

TABLE 4.—COMPARISONS OF NONDEFENSE AGENCY PROCUREMENT FISCAL YEARS 1961-67

[In millions of dollars]

Fiscal year	Combined total	NASA	AEC	GSA ¹	MAMSB ²	FAA ³
1961.....	4,330.7	\$423.3	\$2,611.5	\$892.7	\$320.4	\$82.8
1962.....	5,056.3	1,030.1	2,737.7	1,034.1	133.9	120.5
1963.....	6,444.4	2,261.7	2,601.1	1,179.2	255.9	146.5
1964.....	7,848.5	3,521.1	2,616.4	1,386.8	159.2	165.0
1965.....	8,341.2	4,141.4	2,474.4	1,434.1	189.5	101.8
1966.....	8,494.5	4,087.7	2,364.2	1,515.6	319.0	208.0
1967.....	8,342.0	3,864.1	2,321.0	1,867.1	72.7	217.1

¹ Total of Federal Supply Service and Property Management and Disposal Service contracts; excludes Public Building Service contracts.

² Maritime Administration and Maritime Subsidy Board (formerly, Federal Maritime Board); excludes contracts of less than \$10,000, which amounts to approximately \$4,000,000 annually; "with respect to procurements under the Merchant Marine Act of 1936, as amended, Government expenditure amounted to approximately 51 percent of the total [new ship construction and ship conversion] contract expenditures. The balance is paid by the owner"; therefore, to obtain the actual Government expenditures, the above amounts for MAMSB would be reduced by approximately \$153,900,000 for 1961, \$53,100,000 for 1962, \$123,000,000 for 1963, \$76,400,000 for 1964, \$91,400,000 for 1965, \$132,600,000 for 1966, and \$8,100,000 for 1967; in addition, amounts for 1966 and 1967 are based on sampling of incomplete data, and are preliminary.

³ Includes intragovernmental purchases, and all procurement awards over \$100 to U.S. business firms.

Source: Agencies concerned.

2. Methods of procurement placement

Basically, Department of Defense procurement methods may be divided into two major categories: formal advertisement and negotiation. (See appendix C for a description of the formal advertisement and negotiation processes and the statutorily specified situations in which a contract may be negotiated.)

(a) Formal advertisement versus negotiation in DOD military contracts

(i) *Generally.*—The percentage of total military contracts (excluding intragovernmental) awarded by formal advertisement for the years 1954 to 1967 is presented in table 5: it increased from 14.2 percent in 1954 to 16.3 percent in 1957; then decreased to a low of 11.9 percent in 1961; steadily rose again to a high of 17.6 percent in 1965; and then declined again to 13.4 percent in 1967.

The percentage comparisons for 1948–67 for contracts to all business firms for work within the United States are shown in table 6. The pattern within this category is similar to that for total military contracts (excluding intragovernmental) after 1954; however, the highest percentage of formal advertisement on the contracts with business firms for work in the U.S. category occurred in 1949 prior to the Korean conflict—29.8 percent. A sharp reduction occurred during the Korean conflict reaching the lowest point in 1952—10.8 percent; thereafter, the percentage of formally advertised contracts to business firms for work in the United States was slightly higher (less than one percentage point) than the percentage of total military contracts (excluding intragovernmental) obtained by formal advertisement.

TABLE 5.—VALUE OF FORMALLY ADVERTISED AND NEGOTIATED MILITARY CONTRACTS (TOTAL, EXCLUDING INTRAGOVERNMENTAL), FISCAL YEARS 1951–67

[Dollar amounts in millions]

Fiscal year	Total value	Formally advertised		Negotiated	
		Amount	Percent	Amount	Percent
1951.....	\$31, 585	(1)	(1)	(1)	(1)
1952.....	42, 801	(1)	(1)	(1)	(1)
1953.....	31, 240	(1)	(1)	(1)	(1)
1954.....	12, 859	\$1, 822	14.2	\$11, 037	85. 8
1955.....	16, 041	2, 401	15. 0	13, 640	85. 0
1956.....	19, 156	2, 902	15. 1	16, 254	84. 9
1957.....	20, 996	3, 423	16. 3	17, 573	83. 7
1958.....	23, 666	3, 282	13. 9	20, 384	86. 1
1959.....	24, 554	3, 256	13. 3	21, 298	86. 7
1960.....	22, 908	3, 170	13. 8	19, 738	86. 2
1961.....	24, 703	2, 932	11. 9	21, 771	88. 1
1962.....	28, 099	3, 545	12. 6	24, 554	87. 4
1963.....	29, 032	3, 678	12. 7	25, 354	87. 3
1964.....	28, 234	4, 072	14. 4	24, 163	85. 6
1965.....	27, 385	4, 817	17. 6	22, 568	82. 4
1966.....	37, 229	5, 283	14. 2	31, 945	85. 8
1967.....	43, 381	5, 792	13. 4	37, 589	86. 6

¹ Not available.

Source: Office of the Secretary of Defense, "Military Prime Contract Awards and Subcontract Payments or Commitments, July 1966–June 1967," and July 1961–June 1962."

TABLE 6.—VALUE OF FORMALLY ADVERTISED AND NEGOTIATED MILITARY CONTRACTS (WITH BUSINESS FIRMS FOR WORK IN THE UNITED STATES), FISCAL YEARS 1948-67

Fiscal year	Total value (millions)	Formally advertised		Negotiated	
		Amount (millions)	Percent	Amount (millions)	Percent
1948	\$1,456	\$196	13.5	\$1,260	86.5
1949	5,463	1,626	29.8	3,837	70.2
1950	5,355	1,461	27.3	3,894	72.7
1951	30,823	3,720	12.1	27,103	87.9
1952	41,482	4,479	10.8	37,003	89.2
1953	27,822	3,089	11.1	24,733	88.9
1954	11,448	1,789	15.6	9,659	84.4
1955	14,930	2,386	16.0	12,544	84.0
1956	17,750	2,815	15.9	14,935	84.1
1957	19,133	3,321	17.4	15,812	82.6
1958	21,827	3,115	14.3	18,712	85.7
1959	22,744	3,089	13.6	19,655	86.4
1960	21,302	2,978	14.0	18,324	86.0
1961	22,992	2,770	12.0	20,222	88.0
1962	26,147	3,412	13.1	22,735	86.9
1963	27,143	3,538	13.0	23,605	87.0
1964	26,221	3,889	14.8	22,332	85.2
1965	25,281	4,660	18.4	20,621	81.6
1966	34,026	5,147	15.1	28,879	84.9
1967	39,809	5,621	14.1	34,188	85.9

Source: Office of the Secretary of Defense, "Military Prime Contract Awards and Subcontract Payments or Commitments, July 1966-June 1967", and "July 1961-June 1962."

(ii) *Small business versus large business firms.*—The amount of contracts obtained by formal advertisement and by negotiation for "small" business and "large" business firms are indicated in tables 7 and 8. Small business data reveal a sharp decline from a high of 52.2 percent formally advertised contracts in 1957 to a low of 20.2 percent in 1963; 1964 and 1967 were only slightly higher at 20.6 percent. On the other hand, "large" business firms had an upward trend in the percentage of formally advertised contracts from a low of 4.5 percent in 1953 to a 1965 high of 17.7 percent; 1966 and 1967, however, reversed this trend with 13.5 and 12.5 percent, respectively.

TABLE 7.—VALUE OF FORMALLY ADVERTISED AND NEGOTIATED MILITARY CONTRACTS, TO SMALL BUSINESS FIRMS IN UNITED STATES, FISCAL YEARS 1951-67

Fiscal year	Total value (millions)	Small business as a percent of total business	Formally advertised		Negotiated	
			Amount (millions)	Percent	Amount (millions)	Percent
1951	\$6,436	20.9	\$1,799	28.0	\$4,637	72.0
1952	7,066	17.0	2,545	36.0	4,521	64.0
1953	4,608	16.6	2,035	44.2	2,573	55.8
1954	2,902	25.3	1,150	39.6	1,752	60.4
1955	3,214	21.5	1,501	46.7	1,713	53.3
1956	3,475	19.6	1,750	50.4	1,725	49.6
1957	3,783	19.8	1,973	52.2	1,810	47.8
1958	3,729	17.1	1,794	48.1	1,935	51.9
1959	3,783	17.6	1,466	38.8	2,317	61.2
1960	3,440	16.1	1,175	34.2	2,265	65.8
1961	3,657	15.9	1,008	27.6	2,649	72.4
1962	4,622	17.7	1,089	23.6	3,533	76.4
1963	4,301	15.8	867	20.2	3,434	79.8
1964	4,519	17.2	930	20.6	3,589	79.4
1965	4,943	19.6	1,058	21.4	3,885	78.6
1966	7,269	21.4	1,530	21.0	5,739	79.0
1967	8,073	20.3	1,663	20.6	6,410	79.4

Source: See table 6.

TABLE 8.—VALUE OF FORMALLY ADVERTISED AND NEGOTIATED MILITARY CONTRACTS TO LARGE BUSINESS FIRMS IN UNITED STATES, FISCAL YEARS 1951-67

Fiscal year	Total value (millions)	Large firms as a percent of all business	Formally advertised		Negotiated	
			Amount (millions)	Percent	Amount (millions)	Percent
1951	\$24,387	80.1	\$1,921	7.9	\$22,466	92.1
1952	34,416	83.0	1,934	5.6	32,482	94.4
1953	23,214	83.4	1,054	4.5	22,160	95.5
1954	8,546	74.7	639	7.5	7,907	92.5
1955	11,716	78.5	885	7.6	10,831	92.4
1956	14,275	80.4	1,065	7.5	13,210	92.5
1957	15,350	80.2	1,348	8.8	14,002	91.2
1958	18,098	82.9	1,321	7.3	16,777	92.7
1959	18,961	82.4	1,623	8.6	17,338	91.4
1960	17,862	83.9	1,803	10.1	16,059	89.9
1961	19,335	84.1	1,762	9.1	17,573	90.9
1962	21,525	82.3	2,323	10.8	19,202	89.2
1963	22,842	84.2	2,671	12.6	20,171	87.4
1964	21,702	82.8	2,959	13.6	18,743	86.4
1965	20,338	80.4	3,602	17.7	16,736	82.3
1966	26,757	78.6	3,617	13.5	23,140	86.5
1967	31,736	79.7	3,958	12.5	27,778	87.5

Source: See table 6.

(b) *Formal advertisement versus negotiation in nondefense agency contracts*

Data on formally advertised contract procurement in nondefense agencies reveal a wide variation of experience between agencies. Table 9 portrays the comparative percentages.

Of the nondefense agencies, NASA and AEC had the lowest percentages of formally advertised procurement. NASA's formally advertised contracts declined from 9.1 percent of total procurement in 1961 to a low of 2.7 percent in 1966, and rose again to 3.0 percent in 1967. Formally advertised awards for AEC remained relatively stable: 2.5 percent of total procurement in 1961 and 2.7 percent in 1967. Reported data for GSA indicated 35.0 percent of procurement was formally advertised in 1961; advertised procurement rose to a high of 44.7 percent in 1965, and declined to 34.2 percent in 1967. Procurement for the Maritime Administration (MAMSB) was reported as almost entirely formally advertised, except for a sharp drop to 64.9 percent in 1967 due to the reduction reported for ship construction contracts, which are usually advertised. FAA's formally advertised procurement declined from 54.6 percent of total procurement in 1961 to 12.2 percent in 1967.

TABLE 9.—COMPARISONS OF NON-DEFENSE-AGENCY PROCUREMENT METHODS: FORMALLY ADVERTISED VERSUS NEGOTIATED CONTRACTS, FISCAL YEARS 1961-67

[In percent]

Fiscal year	NASA		AEC		GSA ¹		MAMSB ²		FAA	
	Advertised	Negotiated	Advertised	Negotiated	Advertised	Negotiated	Advertised	Negotiated	Advertised	Negotiated
1961	9.1	90.9	2.5	97.5	35.0	65.0	98.3	1.7	54.6	45.4
1962	6.2	93.8	2.6	97.4	36.7	63.3	97.2	2.8	39.9	60.1
1963	4.7	95.3	2.2	97.8	36.4	63.6	98.7	1.3	17.5	81.5
1964	3.8	96.2	2.7	97.3	32.3	67.7	98.6	1.4	12.1	87.9
1965	4.1	95.9	2.1	97.9	44.7	55.3	98.9	1.1	17.4	81.6
1966	2.7	97.3	2.2	97.8	39.4	60.6	93.0	7.0	8.9	91.1
1967	3.0	97.0	2.7	97.3	34.2	65.8	94.9	35.1	12.2	87.8

¹ Excludes public buildings service contracts for GSA.² Maritime Administration and Maritime Subsidy Board (formerly Federal Maritime Board); excludes contracts less than \$10,000, which amounts to approximately \$4,000,000 annually; 1966 and 1967 are based upon incomplete sampling data.

Source: Agencies concerned.

(c) *Competition in DOD procurement placement*

In determining the degree of price "competition" which exists in its procurement placement, the Department of Defense considers price competition to be present when a contract is awarded by formal advertisement and also in certain situations when a contract is awarded by negotiation.

(i) *Price competition in DOD military procurement.*—The components of "price" competition in DOD military procurement, 1960-67 are summarized in table 10. Total price competition increased from \$6.9 billion in 1960 to \$18.6 billion in 1967, or 170.8 percent; at the same time, total military procurement (excluding intragovernmental) rose by 89.4 percent. Contracts awarded under price competition (as a percent of total procurement) increased from 30.0 percent in 1960 to 44.4 percent in 1966, with a slight decline to 42.9 percent in 1967.

Certain categories of negotiated contracts are considered by the DOD to be price competitive: "set-asides" restricted to bidding by small business firms (which utilize the sealed bid procedures utilized for unrestricted formal advertising);² "set-asides" for labor surplus areas;³ and "open market purchases of \$2,500 or less within the United States."

The largest component of price competition is what has been termed "negotiated" price competition—purchases other than the three above categories, in which two or more solicitations are made by the DOD procurement agency. As indicated in table 10, "negotiated price competition" has increased rapidly since 1960 in dollar amount and as a percent of total procurement: 9.3 percent in 1960, 13.4 percent in 1961, 15.2 percent in 1963, 20.9 percent in 1966, and 20.8 percent in 1967. Thus, "negotiated" price competition represented almost one-half of price competition in 1966 and 1967.

² "Set-asides" for small business may be made for any individual item procurement, a class of items, a part of a class, or a total procurement. These "set-asides" are for the exclusive participation of small business concerns and are made upon the recommendation of the Department Small Business Specialist or the contracting officer (if there is "reasonable expectation that bids or proposals will be obtained from a sufficient number of responsible small business concerns so that awards will be made at reasonable prices.") (ASPR, §§ 1-706.1 and 1-706.5).

³ It is the policy of the DOD to place contract awards in "labor surplus" areas whenever possible, provided a comparable price is obtainable. This policy takes precedence over small business set-asides; thus, the first priority would be given to "persistent labor surplus area concerns which are also small business concerns." (ASPR, § 1-802).

TABLE 10.—PRICE COMPETITION IN MILITARY PROCUREMENT CONTRACTS, FISCAL YEARS 1960-67

Type of price competition	1960	1961	1962	1963	1964	1965	1966	1967
	Amount (millions)							
Total, price competition.....	\$6,875	\$8,127	\$10,003	\$10,764	\$11,031	\$11,884	\$16,539	\$18,616
Formally advertised.....	3,170	2,932	3,545	3,678	4,072	4,817	5,283	5,792
Small business and labor surplus area set-asides.....	736	983	1,422	1,382	1,539	1,622	1,751	1,936
Open market purchases of \$2,500 or less (within the United States) ¹	825	919	1,069	1,280	1,338	1,393	1,705	1,841
Negotiated price competition.....	2,144	3,293	3,966	4,423	4,084	4,051	7,800	9,047
Total, nonprice competition.....	16,033	16,576	18,096	18,269	17,203	15,501	20,689	24,765
	Percentage distribution							
Price competition.....	30.0	32.9	35.6	37.1	39.1	43.4	44.4	42.9
Formally advertised.....	13.8	11.9	12.6	12.7	14.4	17.6	14.2	13.4
Small business and labor surplus area set-asides.....	3.3	3.9	5.1	4.8	5.5	5.9	4.7	4.5
Open market purchases of \$2,500 or less (within the United States) ¹	3.6	3.7	3.8	4.4	4.7	5.1	4.6	4.2
Negotiated price competition.....	9.3	13.4	14.1	15.2	14.5	14.8	20.9	20.8
Nonprice competition.....	70.0	67.1	64.4	62.9	60.9	56.6	55.6	57.1

¹ "Price competition required on actions of \$250 or more," as defined by DOD regulations in effect during the above years.

Source: Office of the Secretary of Defense, "Military Prime Contract Awards and Subcontract Payments of Commitments, July 1966-June 1967", "July 1961-June 1962", "and July 1960-June 1961."

Among the 17 categories of allowable contract negotiation (all procurement other than formally advertised), "price" competition was considered present in 26.3 percent in 1962, 31.3 percent in 1965, 35.2 percent in 1966, and 34.1 percent in 1967. This, of course, includes the categories listed as 100-percent price competitive: (a) small business and labor surplus area set-asides and (b) open market purchases of \$2,500 or less within the United States. Small business and labor surplus area set-asides are included within "national emergency" as listed in table 11.

Price competition in negotiated contracts for 1967 ranged from 0.6 percent in "services of educational institutions" to 99.2 percent for "national emergency" as indicated in table 11 (see above for primary explanation).

TABLE II.—PRICE COMPETITION IN NEGOTIATED MILITARY PROCUREMENT CONTRACTS, BY TYPE OF STATUTORY AUTHORITY, FISCAL YEARS 1962-67¹
 [As a percent of total amount of each negotiated type]

	1962	1963	1964	1965	1966	1967
Statutory authority negotiated procurement						
National emergency.....	78.8	94.1	96.3	98.6	98.6	99.2
Public exigency.....	27.1	28.2	21.4	28.2	47.4	36.2
Purchases outside United States.....	51.0	52.9	50.7	52.6	38.6	37.5
Perishable or nonperishable subsistence.....	99.1	92.8	92.0	91.2	91.1	90.6
Impractical to secure competition by formal advertising.....	25.0	23.3	24.1	22.6	22.8	33.2
Experimental, developmental, test, or research.....	4.3	3.6	2.3	3.9	3.3	2.3
Technical or specialized supplies requiring substantial initial investment or extended period of preparation for manufacture.....	7.6	8.0	9.9	8.7	4.9	1.9
Purchases to keep facilities available in interest of national defense or industrial mobilization.....	80.7	84.1	86.7	93.7	46.0	34.9
Classified purchases.....	43.5	35.4	46.5	53.6	47.3	41.4
Services of educational institutions.....	3.5	3.7	1.1	1.1	1.3	.6
Other (miscellaneous) authority.....	(²)	(²)	(²)	(²)	57.4	60.3

¹ Not available for 1960 and 1961.

² Not available.

Sources: Office of the Secretary of Defense, "Military Prime Contract Awards and Subcontract Payments or Commitments," each fiscal year.

(ii) *Definitional problems in price competition—GAO and DOD.*—Certain differences of opinion concerning classification of procurement as having “price competition” have occurred as a result of audits of Defense Department contracting by the General Accounting Office (GAO). Testimony by the GAO at the Joint Economic Committee hearings, May 1967, challenged certain aspects of DOD statistical definitions on price competition by stating:

A large percentage of the actions which were classified and reported to higher management levels within the Department of Defense as competitive procurements, in our opinion, were in fact made without competition.

The primary cause for misclassifying procurements as having been awarded on the basis of price competition appears to stem from the criteria in the Armed Services Procurement Regulation. The regulation permits a contract award to be classified as competitively priced, even when only one response is received, as long as two or more proposals were solicited and the accepted proposal meets certain other evaluation tests.

In addition, the Armed Services Procurement Regulation permits purchases of \$2,500 and under to be reported as competitive even though many are not. The four locations we visited reported in the fiscal year 1966 a total of about \$80 million in procurement actions of \$2,500 and under as being awarded on the basis of price competition. Of the total amount, however, an estimated \$55 million, or 69 percent, represented noncompetitive procurements.

We are proposing changes in the Armed Services Procurement Regulation to provide additional guidance to contracting officers for classifying and reporting of negotiated contracts.⁴

The GAO did not indicate (other than the example of the \$55 million of “under \$2,500” purchases) a number for the “large percentage” of competitive actions that “were in fact made without competition.” Furthermore, the \$80 million of purchases surveyed represented a sample of only 4.7 percent of the total procurements in the category “open market purchases of \$2,500 or less.” On the other hand, the \$55 million judged “noncompetitive” by the GAO did indicate the necessity of refining the definition of “price competition” and requiring the receipt of at least two responsive bids, not just the sending of two or more solicitations.

Following the GAO recommendations, the Assistant Secretary of Defense (Installations and Logistics) issued a memorandum on August 18, 1967, regarding the DOD rules on price competition which reads in part as follows:⁵

We do not interpret either the GAO or the Joint Economic Committee position as suggesting any change in our current reporting rules for formal advertising. With respect to negotiated procurements however, I have determined that

⁴ Joint Economic Committee, hearings, “Economy in Government,” May 8, 9, 10, 16, 1967, pt. 1, p. 9.

⁵ Joint Economic Committee, hearings, “Economy in Government Procurement and Property Management,” Nov. 27-30 and Dec. 8, 1967, vol. I, pp. 77-78.

statistical accuracy will be best attained by adoption of rules substantially as follows:

1. A contract shall be reported as price competitive if offers were solicited and received from at least two responsible offerors capable of satisfying the Government's requirements wholly or partially and the award or awards were made to the offeror or offerors submitting the lowest evaluated prices. However, price competition may exist even though only one offer is received when the offers are solicited from at least two responsible offerors who normally contend for contracts for the same or similar items.

2. Procurements shall not be reported as competitive where only one responsive offer was received and the solicitation was restricted to a prime contractor for contracts for the same or similar items.

3. Multiple awards in such areas as subsistence, clothing and equipage, and other commodities where several awards normally result from one solicitation may be recorded as competitive, even though the total quantity of the solicitation is not awarded, if in the judgment of the contracting officer there are sufficient facts to support a valid finding of price competition.

4. Transactions shall not be recorded as price competitive solely on the basis of the number of solicitations made. Contracting officers shall consider the content of the responses to solicitations, the procurement history of the items procured, and other relevant information and shall exercise sound judgment in the recording of transactions as competitive.

5. Purchase orders in amounts less than \$250 shall be reported as noncompetitive. With regard to orders of \$250 or over, but not exceeding \$2,500, contracting officers shall determine on an individual transaction basis which actions should be recorded as competitive and which noncompetitive. However, where it is not economically feasible to do this, these actions will be recorded as noncompetitive.

These instructions shall become effective upon publication in a DPC, in approximately two weeks.

(Signed) PAUL R. IGNATIUS,
Assistant Secretary of Defense
(Installations and Logistics).

The Assistant Secretary testified in the November 1967 Joint Economic Committee hearings that had these new classification rules (which the GAO has approved) been in effect for defining "price competition," the 1961-67 percentage of price competition would have been reduced by 2 to 3 percentage points; for example, instead of 32.9 percent for 1961, approximately 30 percent would have been classified as "price competition"; also, instead of 42.9 percent for 1967, it would have been approximately 40 percent.⁶ The percentage of price competition in military procurement would still be increased by a significant one-third.

⁶ *Ibid.*, p. 79.

3. *Types of contract pricing provisions*

(a) *Basic principles in DOD procurement*

The basic principle behind DOD procurement actions is that the business profit motive should be utilized effectively in order to achieve economical contract performance. The DOD procurement policy may be summarized as follows. To achieve efficient contract performance, it is necessary to negotiate sound performance (cost) standards and realistic targets (prices).⁷ If effective price competition is present, it may be assumed that the contract price represents a sound procurement in terms of both cost and price. Thus, comparable cost experience is probably available, and the profit margin is more likely to be reasonable (i.e., not out of line with others in the industry).⁸

Contracts awarded through formal advertisement must have reasonably definite design or performance specifications available; otherwise, they could not be advertised in such a manner. Therefore, these contracts primarily utilize "fixed price" contracts (mostly "firm fixed price," with some as "fixed price" with an escalation clause).⁹

Where effective price competition is not present or design or performance specifications are not reasonably definite, it is the policy of the DOD to utilize the type of contract pricing that will closely associate realized profits to the contractor's efficiency in cost, quality, and delivery performance. To make effective use of the profit motive in private business, the contractor should be given cost responsibility as soon as possible and to the maximum extent possible in the contract process. Therefore, some variation of the fixed-price contract is preferred by the DOD.¹⁰

(b) *Fixed-price versus cost-reimbursement contracts*

(i) *DOD experience.*—In light of the advantages of the fixed-price contract in placing greater cost responsibility upon the contractor, the DOD policy and practice since 1960 has been a gradual trend toward greater reliance upon fixed-price contracts, and a corresponding decline in reliance upon cost-reimbursement contracts.

The percentage use of fixed-price contracts (as indicated in table 12) increased from 57.4 percent in 1960 to 78.9 percent in 1967, an increase of 21.5 percentage points; 1966 was the peak year with 79.2 percent. Prior to 1960, the trend was down: from 82.1 percent in 1952 to 59.1 percent in 1959.

As a percent of the number of contract actions, fixed-price contracts showed a gradual year by year increase: from 82.8 percent in 1960 to 91.0 percent in 1967; correspondingly, use of cost-reimbursement contracts declined from 17.2 percent in 1960 to 9.0 percent in 1967. (See table 15 at p. 91.)

⁷ See ASPR, sec. 3-808.5.

⁸ See ASPR, sec. 3-807.2.

⁹ ASPR, sec. 2-104.1.

¹⁰ See ASPR, sec. 3-402.

TABLE 12.—VALUE OF MILITARY FIXED PRICE AND COST REIMBURSEMENT TYPE CONTRACTS,
FISCAL YEARS 1952-67

[Dollar amounts in millions]

Fiscal year	Total †	Fixed-price contract		Cost-reimbursement contract	
		Amount	Percent	Amount	Percent
1952.....	\$34,028	\$27,954	82.1	\$6,074	17.9
1953.....	29,285	23,358	79.8	5,927	20.2
1954.....	10,942	7,708	70.5	3,234	29.5
1955.....	13,661	10,366	75.9	3,295	24.1
1956.....	16,102	11,221	69.7	4,881	30.3
1957.....	17,997	11,995	66.6	6,002	33.4
1958.....	22,162	13,389	60.4	8,773	39.6
1959.....	22,873	13,520	59.1	9,353	40.9
1960.....	21,181	12,160	57.4	9,022	42.6
1961.....	22,857	13,243	57.9	9,614	42.1
1962.....	25,780	15,667	60.8	10,113	39.2
1963.....	26,225	17,013	64.9	9,212	35.1
1964.....	25,328	18,029	71.2	7,299	28.8
1965.....	24,331	18,619	76.5	5,711	23.5
1966.....	33,515	26,551	79.2	6,964	20.8
1967.....	39,249	30,974	78.9	8,276	21.1

† Excludes intragovernmental procurement and actions of less than \$10,000.

Source: Office of the Secretary of Defense, "Military Prime Contract Awards and Subcontract Payments or Commitments, July 1966-June 1967," and "July 1961-June 1962."

(ii) *Experience of nondefense agencies.*—A comparison of nondefense agency experience with fixed-price versus cost-type contracts in terms of the value of contracts awarded is presented in table 13. The data indicate a wide variation between the covered agencies, which is a reflection of the diverse nature of items procured.

The comparative use of fixed-price versus cost-type contracts by NASA remained relatively stable during 1961-1967. Fixed-price contracts accounted for 15.6 percent of contract awards classified by pricing provisions in 1961; the use of fixed-price contracts declined to 12.3 percent in 1964, rose again to 14.9 percent in 1965, dropped to a low of 12.2 percent in 1966, and climbed back to 14.0 percent for 1967.

Fixed-price contract data for the Atomic Energy Commission reveal a relatively stable picture after the rapid drop of more than one-half from 44.8 percent of total contract awards in 1961 to 20.4 percent in 1963; thereafter, the percentage of fixed-price contracts increased slightly to 24.5 percent in 1965, before reaching a level of 23.0 percent for 1967.

Fixed-price contracts for the General Services Administration averaged almost 100 percent of procurement for the period, 1961-1967. The Maritime Administration & Board (MAMSB) also had a very high constant percentage, over 98 percent, of fixed-price procurement. Data for the Federal Aviation Administration indicate a fluctuating use of fixed-price contracts: 91.4 percent of awards in 1964, 23.6 percent in 1966, and 88.8 percent in 1967. (See footnote 8, table 18, for an explanation of the sharp drop in 1966.)

TABLE 13.—COMPARISONS OF FIXED PRICE AND COST TYPE CONTRACTS OF NONDEFENSE AGENCIES, FISCAL YEARS 1961-67
 [In percent]

Fiscal year	NASA		AEC		GSA		MAMSB		FAA	
	Fixed price	Cost type								
1961.....	15.6	84.4	44.8	55.2	99.9	0.1	98.6	1.4	(2)	(2)
1962.....	14.2	85.8	32.3	67.7	100.0	-----	97.4	2.6	(2)	(2)
1963.....	12.4	87.6	20.4	79.6	100.0	(1)	98.8	1.2	(2)	(2)
1964.....	12.3	87.7	21.9	78.1	99.9	.1	98.9	1.1	91.4	8.6
1965.....	14.9	85.1	24.5	75.5	100.0	-----	99.6	1.4	65.5	34.5
1966.....	12.2	87.8	21.4	78.6	99.9	-----	100.0	(1)	23.6	76.4
1967.....	14.0	86.0	23.0	77.0	100.0	(1)	98.2	1.8	88.8	11.2

1 Less than 0.05 percent.

2 Not available.

Source: Tables 16 and 17, and Agencies concerned.

(c) *Specific types of contract pricing—DOD*¹¹

(i) *Fixed-price contracts.*—Fixed-price contracts may be characterized under four major types: (1) firm, (2) redeterminable, (3) incentive, and (4) escalation.

Firm fixed-price.—The firm fixed-price contract (FFP) provides for a price which is not subject to adjustment. This is due to the availability of adequate cost experience, as was discussed above concerning contract pricing in “formerly advertised” procurement. According to the DOD: “The firm-fixed-price contract is the preferred contract type under most conditions. Under the firm-fixed-price contracts, the contractor assumes full cost responsibility and guarantees to deliver a product meeting our specifications—this is, in effect, the best form of incentive contract, with the contractor assuming responsibility for all costs under or over target at the start of the contract period.”¹²

The use of firm fixed-price contracts (as a percentage of the total value of contracts, excluding intragovernmental and actions of less than \$10,000) has increased from 31.4 percent and 31.5 percent in 1960 and 1961, respectively, to 57.5 percent and 56.3 percent in 1966 and 1967, respectively (see tables 14 and 15 for a detailed summary of DOD contract pricing provisions, 1960–67). As a percentage of the number of military contracts, firm fixed-price contracts have increased steadily from 71.8 percent in 1960 to 83.8 percent in 1967.

Price redeterminable.—A second type of fixed-price contract is referred to as “price redeterminable”: (a) with “prospective price redetermination at a stated time or times during performance of the contract” (price redetermination may be upward or downward, after an initial period of performance or delivery of a certain quantity under the original fixed-price contract); and (b) with “retroactive price redetermination” after completion of the contract, which includes the setting of a ceiling price. The use of this type of contract is limited to research and development contracts of less than \$100,000 with contractors that have an adequate accounting system for price redetermination purposes.

Price redeterminable contracts have declined in use in terms of value from a peak of \$2,403 million (10.5 percent of the total) in 1961 to \$688 million (1.8 percent of the total) in 1967. As a percentage of the number of contract actions, fixed-price redeterminable contracts have declined from 2.8 percent in 1960 to 1.1 percent in 1967.

Fixed-price incentive.—Fixed-price incentive (FPIF) contracts, which represent the second largest aggregate and percentage amounts within the fixed-price group, may be divided into the following types:

(a) “Fixed-price incentive with a firm target”—A target cost, a target profit, and a price ceiling are negotiated at the outset of the contract (along with a formula for determining the final profit and price). The Government and the contractor share, within the set price ceiling, the responsibility for the difference between the original and the final negotiated cost. If the final cost is greater than the target cost, the final profit will be less than the target profit; conversely, if final costs are less than target costs, the final profit will be greater. The formula, thus, “should reflect the relative risks involved in contract performance.”

¹¹ This discussion of contracts by type of pricing provision is based on ASPR, sec. III, pt. 4—Types of Contracts.

¹² Memorandum of the Assistant Secretary of Defense (Installation and Logistics), Oct. 10, 1966, as cited in Joint Economic Committee, Staff Report, “Background Material on Economy in Government—1967,” (April 1967), p. 107. Also, ASPR, sec. 3-402 (b).

(b) "Fixed-price incentive with successive targets"—This category of contracts is similar to category (a) except that a production point is selected at which time the negotiated profit formula is initiated. At the selected production point, a firm fixed-price may be negotiated, or another formula may be negotiated for establishing a final profit and price, based upon consideration of the "experienced cost and all other pertinent factors."

Fixed-price incentive contracts are not to be used in price negotiations unless the contractor's system of accounting is "adequate for price revision purposes and permits satisfactory application of the profit and price adjustment formulas."

The use of incentive fixed-price contract provisions increased from \$2,554 million in 1961 (11.2 percent of the total) to \$7,001 million in 1967 (17.8 percent of the total). As a percentage of the number of contract actions, FPIF contracts showed a slight decline from 4.7 percent in 1960 to 3.7 percent in 1967.

Fixed-price-escalation.—A fourth type of fixed-price contract contains an "escalation" clause. This type of contract is similar to the firm fixed-price contract, with the addition of a provision for an upward or downward adjustment of the contract price. The adjustments are dependent upon certain contingencies which are specifically defined in the original contract; e.g., in cases of unstable market conditions in prices of materials or wage rates.

The use of fixed-price-escalation contracts has remained relatively stable in dollar amounts: \$1,075 million in 1961 and \$1,193 million in 1967. The relative use of escalation-type provisions has declined from 6.3 percent and 4.7 percent in 1960 and 1961, respectively, to 3 percent in 1967. The percentage of contract actions using fixed-price-escalation contracts has declined from 3.5 percent in 1960 to 2.4 percent in 1967.

(ii) *Cost-reimbursement contracts.*—As indicated in table 12, the relative use of cost-type pricing in terms of value has declined since 1961: from 42.1 percent to 20.8 percent and 21.1 percent in 1966 and 1967, respectively. The dollar amount of cost reimbursement contracts declined from \$10,113 million in 1962 to \$5,711 million in 1965, but rose again to \$8,276 million in 1967.

As mentioned previously, the use of fixed-price contracts is conditioned upon the availability of adequate and reliable cost and pricing data, including the use of a reliable cost accounting system by the contractor, and upon adequate Government surveillance of cost performance. Cost reimbursement contracts are primarily used where estimated costs are \$100,000 or more. Cost-type contracts are segmented into: (a) no fee—including cost-sharing, (b) fixed fee, (c) incentive fee, and (d) time and materials—including labor-hour contracts.

Cost-no fee, cost-sharing.—Cost contracts with "no fee" are utilized primarily for research and development contracts with nonprofit organizations and for facilities contracts. The amount of "no fee" cost contracts has increased from \$467 million in 1960 (2.2 percent of the total) to \$752 million in 1967 (1.9 percent of the total). "Cost-no fee" contracts have declined as a percentage of the number of procurement actions from 3.4 percent in 1960 to 1.9 percent in 1967.

"Cost-sharing" contracts provide for reimbursement of an agreed portion of the contractor's allowable costs and are utilized only for research and development contracts. This type of cost contract is

reported separately for some of the covered nondefense agencies, but not for the DOD.

Cost-plus-fixed-fee.—“Cost-plus-fixed-fee” (CPFF) contracts provide for the reimbursement of a contractor’s actual costs, plus a fixed fee. This type of contract does not offer adequate incentives for the contractor to reduce costs; accordingly, the use of cost-plus-fixed-fee contracts has been discouraged by the DOD. This type of contract is primarily used for research or preliminary study, where the degree of work required is not known.

The fee in CPFF contracts generally is limited to 10 percent of the estimated cost, exclusive of the fee; however, 15 percent is the limit for “experimental, developmental, or research work,” and 6 percent is the limit for architectural or engineering services for public works or utility projects (10 U.S.C. 2306 (d)).

The program of reducing DOD reliance on CPFF contracts resulted in a steady decline in the relative use of CPFF contracts in terms of value from 36.8 percent of the total in 1960 to 9.4 percent in 1965. However, the relative use increased in 1966 and 1967 to 9.9 percent and 10.4 percent, respectively. The dollar amount of CPFF contracts declined from a high of \$8,385 million in 1962 to a low of \$2,289 million in 1965, and rose again to \$4,069 million in 1967. As a percentage of the number of contract actions, CPFF contracts dropped sharply from 12.1 percent in 1960 to 4.5 percent in 1967.

Cost-plus-incentive-fee.—Under cost-plus-incentive-fee (CPIF) contracts, the fee is adjusted by a formula relating to the allowable cost and the target cost. The final fee is calculated according to the adjustment formula after the completion of the contract. If the final allowable costs are less than the targeted costs, the final fee will be larger (within limits); conversely, the final fee will be less if the allowable costs exceed the targeted costs.

The cost-plus-incentive-fee contract is particularly suitable for development and test procurement where a target fee and an adjustment formula can be negotiated to provide an effective profit incentive for cost management. CPIF contracts may be used in conjunction with certain performance incentives which provide for increased fees or profits if performance targets are improved.

The use of CPIF contracts increased sharply from \$673 million in 1960 to \$3,580 million in 1964 (with a corresponding increase as a percentage of the total from 3.2 percent in 1960 to 14.1 percent in 1964). In 1965 and 1966, CPIF contracts declined slightly to \$2,721 million and \$2,763 million, respectively (the 1966 amount was 8.3 percent of the total); in 1967, they increased to \$3,277 million, but remained at 8.3 percent of the total. CPIF contracts increased as a percentage of the number of contract actions from 0.6 percent in 1960 to a peak of 2.4 percent in 1965, but dropped to 1.5 percent in 1967.

Cost time and materials.—The final form of cost-contracts, “time and materials” (including labor-hour contracts, in which materials are not supplied by the contractor) provides for payment at specified hourly rates, and for materials at cost. Time and materials contracts are very minor in importance, representing only 0.5 percent of the total value of contracts in 1967, as compared to 0.4 percent in 1960. These contracts also maintained a stable percentage of the number of total procurement actions: 1.1 percent in 1960 and 1967.

TABLE 14.—MILITARY PROCUREMENT AWARDS, BY TYPE OF CONTRACT, PRICING PROVISION, FISCAL YEARS 1960-67

Type of pricing provision	1960	1961	1962	1963	1964	1965	1966	1967
	Amounts (millions)							
Total ¹	\$21,181	\$22,857	\$25,780	\$26,225	\$25,328	\$24,331	\$33,515	\$39,249
Fixed price.....	12,160	13,243	15,667	17,013	18,029	18,619	26,551	30,974
Firm.....	6,646	7,211	9,795	10,886	11,730	12,857	19,277	22,082
Redeterminable.....	1,298	2,403	1,898	981	612	536	766	688
Incentive.....	2,879	2,554	3,097	4,137	4,685	4,040	5,327	7,001
Escalation.....	1,337	1,075	877	1,007	1,001	1,187	1,181	1,193
Cost reimbursement.....	9,022	9,614	10,113	9,212	7,299	5,711	6,964	8,276
No fee.....	467	467	595	621	582	578	734	752
Fixed fee.....	7,803	8,362	8,385	5,439	3,035	2,289	3,328	4,069
Incentive fee.....	673	724	1,061	3,062	3,580	2,721	2,763	3,277
Time and materials ²	79	61	72	90	101	123	140	178
	Percentage distribution							
Total.....	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0
Fixed price.....	57.4	57.9	60.8	64.9	71.2	76.5	79.2	78.9
Firm.....	31.4	31.5	38.0	41.5	46.3	52.8	57.5	56.3
Redeterminable.....	6.1	10.5	7.4	3.7	2.4	2.2	2.3	1.8
Incentive.....	13.6	11.2	12.0	15.8	18.5	16.6	15.9	17.8
Escalation.....	6.3	4.7	3.4	3.9	4.0	4.9	3.5	3.0
Cost reimbursement.....	42.6	42.1	39.2	35.1	28.8	23.5	20.8	21.1
No fee.....	2.2	2.0	2.3	2.4	2.3	2.4	2.2	1.9
Fixed fee.....	36.8	36.6	32.5	20.7	12.0	9.4	9.9	10.4
Incentive fee.....	3.2	3.2	4.1	11.7	14.1	11.2	8.3	8.3
Time and materials ².....	.4	.3	.3	.3	.4	.5	.4	.5

¹ Excludes intragovernmental and actions of less than \$10,000.

² Includes labor-hour contracts.

Source: Office of the Secretary of Defense, "Military Prime Contract Awards and Subcontract Payments or Commitments, July 1966-June 1967."

TABLE 15.—NUMBER OF MILITARY PROCUREMENT ACTIONS, BY TYPE OF CONTRACT PRICING PROVISION, FISCAL YEARS 1960-67

Type of pricing provision	Number							
	1960	1961	1962	1963	1964	1965	1966	1967
Total ¹	117,990	122,306	141,460	149,740	146,157	156,787	206,068	229,357
Fixed price.....	97,735	101,784	118,852	126,143	125,188	137,156	186,289	208,746
Firm.....	84,690	89,601	105,719	113,998	111,682	124,950	171,012	192,189
Redeterminable.....	3,320	2,971	3,408	2,617	2,278	1,668	2,225	2,562
Incentive.....	3,968	5,213	4,735	4,711	6,780	6,529	7,487	8,418
Escalation.....	4,156	3,999	4,990	4,817	4,448	4,009	5,565	5,557
Cost reimbursement.....	20,255	20,522	22,608	23,597	20,969	19,631	19,779	20,611
No fee.....	4,011	3,600	3,722	4,020	4,064	3,924	4,171	4,249
Fixed fee.....	14,278	14,823	16,131	15,577	11,931	9,850	9,567	10,429
Incentive fee.....	674	893	1,316	2,512	3,364	3,803	3,615	3,386
Time and materials ²	1,292	1,206	1,439	1,488	1,610	2,054	2,426	2,547
Total ¹	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0
Fixed price.....	82.8	83.2	84.0	84.2	85.7	87.5	90.4	91.0
Firm.....	71.8	73.3	74.7	76.1	76.4	79.7	83.0	83.8
Redeterminable.....	2.8	2.4	2.4	1.8	1.6	1.1	1.1	1.1
Incentive.....	4.7	4.3	3.4	3.1	4.6	4.2	3.7	3.7
Escalation.....	3.5	3.2	3.5	3.2	3.1	2.5	2.7	2.4
Cost reimbursement.....	17.2	16.8	16.0	15.8	14.3	12.5	9.6	9.0
No fee.....	3.4	3.0	2.6	2.7	2.8	2.5	2.0	1.9
Fixed fee.....	12.1	12.1	11.4	10.4	8.1	6.3	4.6	4.5
Incentive fee.....	.6	.7	.9	1.7	2.3	2.4	1.8	1.5
Time and materials ²	1.1	1.0	1.1	1.0	1.1	1.3	1.2	1.1

¹ Excludes intragovernmental and actions of less than \$10,000.

² Includes labor-hour contracts.

Source: Office of the Secretary of Defense, "Military Prime Contract Awards and Subcontract Payments or Commitments, July 1966-June 1967," and other fiscal years.

(d) *Specific types of contract pricing—nondefense agencies*

(i) *Fixed-price contracts.*—Of the agencies listed in tables 16 and 17, only NASA and FAA segmented their fixed-price contracts into “firm,” “incentive,” and “redeterminable.”

Firm fixed-price contracts for NASA increased in magnitude from \$55 million in 1961 (or 15.3 percent of total contract pricing) to a high of \$492 million in 1965 (12.3 percent of the total); this dropped to a low of 10.1 percent in 1966, before increasing slightly to \$410 million in 1967 (or 10.8 percent).

Use of fixed-price incentive contracts (FPIF) by NASA expanded rapidly from \$4 million in 1962 (or 0.4 percent of the total) to \$117 million in 1967 (or 3.1 percent). Fixed-price redeterminable and escalation represented only very minor amounts and percentages.

The greatest amount and percentage of FAA’s total contracts (as listed by pricing provision) have been firm fixed price, except in 1966: FFP contracts accounted for 75.5 percent of total contract pricing awards in 1964; this dropped to 21.9 percent in 1966, before rising to 85.9 percent in 1967. FAA fixed-price incentive contracts (FPIF) have declined from 13.8 percent of the total in 1964 to 2.2 percent in 1967.

(ii) *Cost-type contracts.*—NASA and FAA also listed cost contracts by type of classification. In addition, the MAMSB reported cost-plus-fixed-fee and cost (no fee) contracts; however, only in 1961 and 1967 did they have cost (no fee) contracts. Cost-plus-fixed-fee contracts represented only a small percentage of total MAMSB procurement: 1.0 percent in 1961, 2.6 percent in 1962, and 1.6 percent in 1967.

Cost-plus-fixed-fee (CPFF) contracts accounted for the majority of NASA contracts in 1961, \$300 million, or 82.7 percent of the total. The absolute magnitude of CPFF contracts increased to a high of \$2,841 million in 1965, but this represented only 71.2 percent of the total amount. Since 1965, NASA’s use of CPFF contracts has declined considerably: \$1,591 million in 1966, or 40.3 percent of total contract pricing, to \$775 million in 1967, or only 20.5 percent.

The biggest change in NASA procurement policy has occurred in the rapid increase in the use of cost-plus-incentive-fee (CPIF) contracts. This increased from \$9 million in 1962 (or 1.0 percent of the total), to \$502 million in 1965 (or 12.6 percent), to \$1,849 million in 1966 (or 46.8 percent), and to \$2,450 million in 1967 (or 64.9 percent). Other types of cost contracts: cost-no fee, cost sharing, and cost-time and materials, accounted for a declining minority of total NASA contract pricing.

The large amount and percentage for FAA under the cost (no fee and cost sharing) category for 1966 was attributed to a \$151.7 million cost sharing award for the supersonic transport (SST).

(e) *Shifting from cost-plus-fixed-fee to fixed-price and incentive contracts.*

(i) *DOD experience.*—A percentage comparison of “cost-plus-fixed-fee” contracts to fixed-price (less incentive) and incentive (fixed and cost) type contract pricing from 1952 to 1967 is presented in table 18. As mentioned previously, CPFF contracts reached a peak percentage of 36.8 percent in 1960 and a low of 9.4 percent in 1965. Total fixed-price (less incentive) contracts declined from 70.1 percent in

1952 to 41.2 percent in 1958, and gradually rose to its recent peak of 63.3 percent in 1966.

Incentive-type contracts (FPIF and CPIF) showed a decline from 27.7 percent in 1954 to a low of 14.4 percent in 1961; this was followed by a rapid rise to a high of 32.6 percent in 1964, and a decline to 26.1 percent in 1967.

TABLE 16.—NONDEFENSE AGENCY PROCUREMENT AWARDS,¹ BY TYPE OF CONTRACT PRICING PROVISION, FISCAL YEARS 1961-1967
 [In millions of dollars]

Agency and type of contract pricing	1961	1962	1963	1964	1965	1966	1967
NASA:²							
Fixed-price type.....	56.4	129.2	262.0	415.6	593.1	480.7	528.4
Firm.....	55.4	125.0	247.5	387.0	492.0	399.2	403.5
Redeterminable.....	0.9	0.4	4.1	1.4	0.3	1.3	1.2
Incentive.....	0.1	3.8	10.2	27.2	100.6	73.6	117.1
Escalation.....			0.2		0.2	6.6	0.6
Cost-type.....	306.1	779.2	1,851.8	2,964.0	3,399.9	3,470.5	3,247.0
No fee and cost sharing.....	0.5	11.6	74.5	48.7	44.2	21.1	6.1
Fixed fee.....	299.9	748.6	1,618.0	2,664.9	2,841.3	1,531.0	771.6
Incentive fee.....		9.3	152.5	242.1	501.6	1,848.9	2,450.5
Time and materials ³	5.7	9.7	6.8	8.3	12.8	9.5	15.8
AEC:							
Fixed-price type.....	1,169.2	884.2	529.9	573.6	605.7	505.2	534.3
Cost-type.....	1,442.3	1,853.5	2,071.2	2,042.8	1,868.7	1,899.0	1,786.7
GSA:⁴							
Firm fixed-price.....	891.9	1,034.1	1,178.9	1,386.1	1,434.1	1,514.3	1,867.0
Cost-type.....	.8		.3	.7		1.3	.1
MAMSB:							
Fixed-price.....	315.8	130.5	252.9	157.4	188.7	319.0	71.4
CPFF.....	3.1	3.4	3.0	1.8	.8	.2	
Cost-no fee.....	1.5						.1
Fixed-price.....	(⁵)	(⁵)	(⁵)	124.8	68.6	49.5	105.9
FAA:⁶							
Firm.....				103.1	64.2	46.1	102.4
Incentive.....				18.9	4.2	2.8	2.6
Redeterminable and escalation.....				2.8	.1	.7	.8
Cost-type.....	(⁵)	(⁵)	(⁵)	11.8	36.1	160.5	13.4
No fee and cost sharing.....				.5	26.3	7151.9	6.6
Incentive.....				2.8	1.1	.4	.8
Fixed fee.....				7.5	7.8	7.5	5.3
Time and materials ³				1.0	.9	.8	.7

¹ Amounts of contract awards that are classified by type of pricing; agency totals may not equal total procurement amounts reported in table 4.
² Represents awards on research and development contracts over \$10,000 and all other contracts not reported in table 4.
³ Includes wage-hour contracts.
⁴ Total for Federal Supply Service and Property Management and Disposal Service contracts; excludes Public Buildings Service contracts.
⁵ Not available.
⁶ Primarily 1966 award for SST program, \$151,700,000 (cost sharing).
 Source: Agencies concerned.

⁷ Totals for FAA do not include intragovernmental procurement awards; awards under \$100, nor cash purchase orders (standard form 44 operation); thus, these totals do not equal total procurement reported in table 4.

TABLE 17.—NONDEFENSE AGENCY PROCUREMENT AWARDS¹ BY TYPE OF CONTRACT PRICING PROVISION, FISCAL YEARS 1961-67
[In percent]

Agency and type of contract pricing	1961	1962	1963	1964	1965	1966	1967
NASA: ²							
Fixed-price type:							
Firm.....	15.3	13.8	11.7	11.5	12.3	10.1	10.8
Redeterminable.....	.2	(3)	.2	(3)	(3)	(3)	(3)
Incentive.....	(3)	.4	.5	.8	2.5	1.9	3.1
Escalation.....			(3)		(3)	.2	(3)
Cost type:							
No fee and cost sharing.....	1	1.3	3.5	1.4	1.1	.5	2
Fixed fee.....	82.7	82.4	76.5	78.8	71.2	40.3	20.5
Incentive fee.....		1.0	7.2	7.2	12.6	46.8	64.9
Time and materials ⁴	1.6	1.1	.3	.2	.3	.3	.4
AEC:							
Fixed-price type.....	44.8	32.3	20.4	21.9	24.5	21.4	23.0
Cost type.....	55.2	67.7	79.6	78.1	78.5	78.6	77.0
GSA: ⁵							
Firm fixed price.....	99.9	100.0	100.0	99.9	100.0	99.0	100.0
Cost type.....	.1		(3)	.1		.1	(3)
MAMSB:							
Fixed price.....	98.6	97.4	98.8	98.9	99.6	100.0	98.2
CPFF.....	1.0	2.6	1.2	1.1	.4	(3)	1.6
Cost, no fee.....	.4						.2
FAA: ⁶							
Fixed price.....							
Firm.....				75.5	61.3	21.9	85.9
Incentive.....				13.8	4.0	1.1	2.2
Redeterminable and escalation.....				2.1	.2	.6	.7
Cost type.....							
No fee and cost sharing.....				.4	25.1	772.3	5.5
Incentive.....				2.0	1.1	1	.7
Fixed fee.....				5.5	7.5	3.6	4.4
Time and materials ⁴.....				.7	.8	.4	.6

¹ Amounts of contract awards that are classified by type of pricing; agency totals may not equal total procurement amounts reported in table 4.

² Represents awards on research and development contracts over \$10,000 and all other contracts of \$25,000 and over.

³ Less than 0.05 percent.

⁴ Includes wage-hour contracts.

⁵ Total for Federal Supply Service and Property Management and Disposal Service contracts; excludes Public Buildings Service contracts.

⁶ Totals for FAA do not include intragovernmental procurement awards, awards under \$100, nor cash purchase orders (standard form No. 44 operation); thus, these totals do not equal total procurement reported in table 4.

⁷ Primarily 1966 award for SST program, \$151,700,000 (cost sharing).

Source: Agencies concerned.

TABLE 18.—COST-PLUS-FIXED-FEE CONTRACTS IN RELATION TO FIXED PRICE AND INCENTIVE TYPES OF MILITARY PROCUREMENT PRICING, FISCAL YEARS 1952-67

[In percent]

Fiscal year	Total	Fixed-price-less-incentive type			Incentive type			Other	
		Cost plus fixed fee	Firm	Redeterminable	Escalation	Total	FPIF		CPIF	Total
1952	100.0	13.3	29.8	38.5	1.8	70.1	12.0	-----	12.0
1953	100.0	16.3	31.8	21.8	2.2	55.8	24.0	2.2	26.2
1954	100.0	23.8	38.0	5.9	1.4	45.3	25.2	2.5	27.7
1955	100.0	19.7	39.7	12.5	8	53.0	22.9	1.4	24.3
1956	100.0	24.1	36.4	9.9	4.2	50.5	19.2	1.9	21.1
1957	100.0	29.9	35.3	8.6	4.9	48.8	17.8	1.2	19.0
1958	100.0	33.2	27.8	7.4	6.0	41.2	19.2	3.2	22.4
1959	100.0	34.3	32.8	4.7	6.3	43.8	15.3	3.2	18.5
1960	100.0	36.8	31.4	6.1	6.3	43.8	13.6	3.2	16.8
1961	100.0	36.6	31.5	7.4	4.7	46.7	11.2	3.2	14.4
1962	100.0	32.5	38.0	10.5	3.4	48.8	12.0	4.1	16.1
1963	100.0	20.7	41.5	3.7	3.9	49.1	15.8	11.7	27.5
1964	100.0	12.0	46.3	2.4	4.0	52.7	18.5	14.1	32.6
1965	100.0	9.4	52.8	2.2	4.9	59.9	16.6	11.2	27.8
1966	100.0	9.9	57.5	2.3	3.5	63.3	15.9	8.3	24.2
1967	100.0	10.4	56.3	1.8	3.0	61.1	17.8	8.3	26.1

Note: Details may not add to totals because of rounding.

Source: Office of the Secretary of Defense, "Military Prime Contract Awards and Subcontract Payments or Commitments, July 1966-June 1967," and July 1961-June 1962."

On the basis of the number of military contract actions (see table 15), the relative use of CPFF contracts declined from 12.1 percent of total military contract actions over \$10,000 each (excluding intra-governmental) in 1960 to 4.5 percent in 1967. On the other hand the number of fixed-price (less incentive) contracts increased from 78.1 percent of procurement actions in 1960 to 87.3 percent in 1967. The relative use of incentive contracts (fixed and cost) rose from 5.3 percent of procurement actions in 1960 to a peak of 6.9 percent in 1964, and then declined to 5.2 percent in 1967.

(ii) *Experience of nondefense agencies.*—As previously discussed, the greatest shift from CPFF contract pricing to either fixed-price or incentive contracts in nondefense agency procurement has taken place in NASA procurement. CPFF contracts, as a percent of total contract amounts, declined steadily from 82.7 percent in 1961 to 71.2 percent in 1965; thereafter, 1966 and 1967 revealed a substantial drop to 40.3 percent and 20.5 percent, respectively.

The shift in NASA procurement was to cost-plus-incentive-fee contract pricing: from 1 percent in 1962, to 7.2 percent in 1964, to 12.6 percent in 1965, to 46.8 percent in 1966, and to 64.9 percent in 1967. This shift was due to the NASA policy of using profit incentives to encourage industry to undertake the research and development type contracts prevalent in the space industry, which involve greater uncertainties in accurately estimating costs over the life of the contract.

4. Summary of DOD cost reduction program

The DOD has stated that savings from shifting from noncompetitive procurement averages about 25 percent.¹³ The shift from noncompetitive to competitive procurement is a part of the overall DOD cost reduction program initiated during fiscal 1962. The major areas involved are as follows (see table 19 for a detailed summary):

1. Buying only what we need.
2. Buying at the lowest sound price.
3. Reducing operating costs.
4. Military assistance program.

(a) *Buying at the lowest sound price*

Shifting from noncompetitive to competitive procurement represents the largest subtotal of "savings" within category (2) "Buying at the lowest sound price." A few examples given by the DOD of savings achieved from price competition were as follows:¹⁴

Items	Noncompetitive unit price	Competitive unit price	Percent reduction	Savings
Electron tube.....	\$2,538	\$1,745	31.2	\$396,400
Radio set.....	15,123	7,260	52.0	3,985,162
Night vision sight.....	1,573	984	37.4	884,130
Cluster bomb dispenser and container.....	710	310	56.3	7,276,056
Multiplexer equipment.....	4,806	2,808	41.6	272,700
Energy absorbers.....	24,557	9,926	59.6	1,020,459

¹³ See Joint Economic Committee Staff Report, "Background Material on Economic Impact of Federal Procurement—196" (March 1966), app. 1, p. 41. Also, Joint Economic Committee hearings, "Economy in Government, Procurement and Property Management" (Nov. 27–30, and Dec. 3, 1967), p. 80.

¹⁴ Joint Economic Committee, Staff Report, "Economy in Government—1967: Updated Background Material," (November 1967), p. 52.

Examples given as illustrative of the savings realized from a second program under category (2), "direct purchase breakout," were:¹⁵

Items	Prime contractor's price	Manufacturers' price	Percent reduction	Savings
90 spare parts.....	\$8,500,000	\$5,000,000	41	\$3,500,000
Compensator, machine trim.....	2,500	1,801	28	244,500
Modification kit, radar scope.....	624	177	72	116,900

Savings were estimated at 10 percent per dollar converted from Cost-Plus-Fixed-Fee (CPFF) contract pricing to Fixed or Incentive price contracts during fiscal years 1962-66. The estimated value of contracts converted from CPFF and from noncompetitive to price competitive (1963-66) were as follows:¹⁶

[In billions of dollars]

Fiscal year	Value of contracts converted from—	
	CPFF to fixed or incentive	Noncompetitive to price competitive
1963.....	\$4.3	\$0.9
1964.....	6.2	1.8
1965.....	6.3	2.6
1966.....	7.8	2.2

A fourth program under "Buying at the lowest sound price" has been the "multiyear procurement procedure," in lieu of awarding a separate contract each year. Lower contract prices obtainable via multiyear procurement are illustrated by the following fiscal 1967 examples:¹⁷

Department	Unit price		Percent reduction	Fiscal 1967 net savings
	Single year	Multiyear		
Army:				
Image intensifier assembly.....	\$2,060	\$1,795	12.9	\$795,000
Radio set AN/PRC-77.....	985	937	4.8	258,336
Radio set AN/GRC-106.....	7,119	6,897	3.1	166,955
Rocket motors, M-30A2.....	1,755	1,703	3.0	113,672
Navy:				
Navigational sets (AN/ARN-52V).....	6,531	5,060	22.5	287,000
3 coordinate radar.....	1,415,029	1,188,977	16.0	1,808,416
Mechanical time fuze, MK-349 model O.....	31	30	3.2	262,970
Air operation centrals.....	8,696,800	8,000,000	8.0	1,393,600
Air Force: Aircraft engine, TF-41.....	354,090	342,904	3.2	973,182

(b) Changes in DOD reporting policy

The detailed "savings" in the DOD cost reduction program for fiscal years 1962-69 are summarized in table 19. Fiscal years 1962-66 composed the original 5-year cost reduction program. The basis of determining cost savings for this period was to include recurring savings from the base year, 1961, and to continue with each year's own savings plus recurring savings from prior years back to 1961. "Recurring savings" were those, for example, that were counted over the life (within the 5-year period) of a contract in which an

¹⁵ *Ibid.*

¹⁶ Joint Economic Committee Staff Report, "Background Material on Economy in Government—1967" (April 1967), pp. 104, 106.

¹⁷ Joint Economic Committee Staff Report (Nov. 1967), p. 53.

initial savings occurred (e.g., some permanent cost reduction continuing as long as a particular item was procured or serviced). Another example of a recurring saving would be the partial or complete closing of a military base or depot.

The goal of the DOD 5-year cost reduction program was to achieve at least a \$3 billion continuing annual "rate of savings." This was surpassed during both 1965 and 1966. At the end of the 5-year period, the DOD adopted new reporting criteria which would measure savings only on an annual basis (i.e., savings achieved through current fiscal cost improvements that are realized during the current fiscal year). As operations proceeded further away from the previous 1961 base year, the allocated "recurring savings" became less realistic. Therefore, the annual savings during 1962-66 are not comparable to the annual savings reported for 1967 and estimated for 1968 and 1969. It is contemplated by the DOD that certain of these savings programs realized or authorized during the year will continue or be realized during later fiscal years when the cost reduction program is fully implemented.

TABLE 19.—DEPARTMENT OF DEFENSE COST REDUCTION PROGRAM, FISCAL YEARS 1962-69¹
[In millions of dollars]

Area	1962	1963	1964	1965	1966	1967 ²	1968 ³	1969 ³
A. Buying only what we need.....	412	860	1,521	2,555	1,665	685	638	637
1. Refining requirement calculations.....	348	769	1,374	2,087	1,096	293	313	311
2. Increased use of excess equipment and inventory in lieu of new procurement.....	64	19	71	181	163	50	60	61
3. Eliminating "goldplating" (value engineering).....	---	72	76	204	324	339	265	265
4. Inventory item reduction.....	---	---	---	83	82	3	---	---
B. Buying at the lowest sound price.....	160	237	553	1,150	1,235	70	93	95
1. Shift to competitive procurement.....	160	237	448	641	551	30	43	44
2. Shift from CPFF to fixed or incentive price contracts.....	---	---	100	436	600	---	---	---
3. Direct purchase breakout.....	---	---	5	6	14	11	17	17
4. Multiyear procurement.....	---	---	---	67	70	29	33	34
C. Reducing operating costs.....	178	289	757	1,119	1,560	281	303	249
1. Terminate unnecessary operations.....	---	123	334	484	794	7	---	---
2. Consolidations and standardizations.....	31	31	137	245	295	135	137	143
3. Increasing efficiencies of operations.....	147	135	286	390	471	139	166	106
D. Military assistance program.....	---	---	---	19	3	16	8	8
Total program.....	750	1,386	2,831	4,843	4,463	1,052	1,042	989

¹ Original 5-year program including savings realized during and recurring from prior years' actions, for 1962-66.

³ Estimated goals.

² New reporting criteria for fiscal year 1967 and thereafter measures savings on an annual basis only.
Source: Office of the Secretary of Defense "Statement by Secretary of Defense Robert S. McNamara: The Fiscal Year 1969-73 Defense Program and the 1969 Defense Budget," p. 218.

B. RENEGOTIATION AND PROCUREMENT

It is important to note that the discussion of profitability contained in this part of the report, and the ratios used for purposes of discussion, are presented only for purposes of indicating comparative profitability in the various situations described. No implications as to the absolute profitability of various types of contracts or the absolute profitability in other situations are intended. The ratio generally used in the discussion, that of profit to sales, is only one indicator of profitability. Moreover, the Renegotiation Board data from which some of the ratios have been derived are on an aggregate basis and are subject to substantial limitations: For example, different size companies and companies with varying proportions of defense and space business are included; profitable contracts and loss contracts are included; and the effect of the use of Government property and facilities is not known.

1. Renegotiable sales and profits—By type of contract pricing

The Renegotiation Board has reported renegotiable sales, profits, and losses by type of contract pricing for 1963–67. The pricing categories data are stated separately for those companies reporting net profits and for those companies reporting net losses for the fiscal year (i.e., for each company, profits and losses under individual contracts are netted). The contracting pricing types are: (1) "Firm" fixed-price (FFP), (2) cost-plus-fixed-fee (CPFF), and (3) "Other." At the request of the staff, the "other" category was segregated further by the Renegotiation Board for 1965 and later years into: (a) fixed price-incentive fee (FPIF), (b) cost-plus-incentive-fee (CPIF), and (c) "other." The second "other" category includes price redeterminable and time and materials contracts. The more detailed classification for 1965–67, however, combines those contractors reporting net profits for the year with those reporting net losses.

(a) Renegotiable sales—Combined profits and losses

As indicated in table 20, total renegotiable sales (profitable and loss sales) increased from \$31.2 billion in 1963 to \$39.3 billion in 1964, then declined to \$31.8 billion in 1966 and \$33.1 billion in 1967.

As a percent of renegotiable sales, firm fixed-price contracts declined from 46.1 percent in 1963 to 41.0 percent in 1964 and 42.8 percent in 1965; however, it rose again in 1966 and 1967 to 52.2 percent in 1967. CPFF contracts, on the other hand, declined from 35.4 percent and 36.0 percent in 1963 and 1964, respectively, to a low of 18.2 percent in 1967. This is a reflection of the changing trend in DOD military procurement: The use of FFP procurement increased from 31.5 percent in 1961 to 52.8 percent in 1965 and 56.3 percent in 1967; at the same time, CPFF procurement declined sharply from 36.6 percent in 1961 to 9.4 percent in 1965 and 10.4 percent in 1967.

Incentive-type contract pricing was segregated by the Renegotiation Board for 1965–67 (FPIF and CPIF). These two incentive-types increased from 17.7 percent of renegotiable sales in 1965 to 25.4 percent in 1966 and 23.6 percent in 1967. CPIF contracts showed the greatest rise: from 5.7 percent in 1956 to 12.4 percent in 1967.

Since the renegotiable sales reported in the Board's annual reports are the result of prior year's procurement policies, it is understandable to note the sharp rise in CPIF contracts because of the rapid increase in the use of CPIF contracts in military procurement from 1962 to 1965: 4.1 percent of military procurement in 1962, 11.7 percent in

1963, 14.1 percent in 1964, and 11.2 percent in 1965. Thereafter, CPIF contracts dropped to 8.3 percent of military procurement in both 1966 and 1967 (see table 14). Thus, the noticeable rise indicated in table 20 for CPIF contracts in renegotiable sales may level off or decline in the next few years. Total military incentive contracts (FPIF and CPIF) have also declined as a percent of total military procurement: from a peak of 32.6 percent in 1964 to 24.2 percent and 26.1 percent in 1966 and 1967, respectively.

(b) *Renegotiable sales—Net profits and net losses*

Sections (B) and (C) of table 20 also give a percentage breakdown for renegotiable sales (net profit sales and net loss sales) by the three major contract pricing categories: FFP, CPFF, and other. The distribution between these types of contract pricing for firms reporting net profits is approximately the same as in section (A) of table 20, the combined profit and loss totals.

Renegotiable sales of firms reporting net losses remained relatively stable from 1963 to 1966: ranging from \$4.8 to \$5.2 billion, before declining to \$4.2 billion in 1967. As a percent of total renegotiable sales reported, however, "net loss" sales decreased from 16.1 percent in 1963 to 13.3 percent in 1964, increased again to 15.5 percent in 1966, and then decreased to 12.7 percent in 1967.

The greatest share of "net loss" contracts was accounted for by FFP contracts: ranging from 67.9 percent to 75.2 percent of total "net loss" sales during 1963-67.

TABLE 20.—RENEGOTIABLE SALES REVIEWED BY RENEGOTIATION BOARD, BY CONTRACT TYPE, FISCAL YEARS 1963-67

(Dollar amounts in millions)

Contract type	1963		1964		1965		1966		1967	
	Amount	Percent	Amount	Percent	Amount	Percent	Amount	Percent	Amount	Percent
A. Total, profit and loss combined.....	\$31,228	100.0	\$39,283	100.0	\$34,798	100.0	\$31,841	100.0	\$33,124	100.0
Firm fixed price.....	14,389	46.1	16,109	41.0	14,893	42.8	14,437	45.0	17,288	52.2
Cost plus fixed fee.....	11,052	35.4	14,135	36.0	10,131	29.1	7,820	24.6	6,020	18.2
Other.....	5,787	18.5	9,039	23.0	9,774	28.1	9,585	30.1	9,817	29.6
Fixed price incentive fee.....	(2)	-----	(2)	-----	4,176	12.0	4,461	14.0	3,792	11.4
Cost plus incentive fee.....	(2)	-----	(2)	-----	1,986	5.7	3,630	11.4	4,048	12.2
Other ³	(2)	-----	(2)	-----	3,612	10.4	1,494	4.7	1,976	6.0
B. Total, net profit.....	26,208	100.0	34,073	100.0	29,953	100.0	26,915	100.0	28,914	100.0
Firm fixed price.....	10,978	41.9	12,190	35.8	11,322	37.8	11,051	41.0	14,156	49.0
Cost-plus-fixed fee.....	10,361	39.5	13,254	38.9	9,373	31.3	6,865	25.9	5,332	18.4
Other.....	4,869	18.6	8,629	25.3	9,258	30.9	8,999	33.1	9,426	32.6
C. Total, net loss.....	5,020	100.0	5,210	100.0	4,845	100.0	4,926	100.0	4,210	100.0
Firm fixed price.....	3,411	67.9	3,919	75.2	3,571	73.7	3,386	68.7	3,132	74.4
Cost-plus-fixed fee.....	691	13.8	881	16.9	758	15.6	855	17.3	688	16.3
Other.....	918	18.3	410	7.9	516	10.7	686	13.9	391	9.3

¹ 1965 was first year of breakdown of data into "FPF, CPIF, and Other"; therefore, division

between categories may not be completely accurate.

² Not available.³ Price redeterminable and time and materials contracts.

Source: Renegotiation Board.

(c) Renegotiable profits—Combined profits and losses

As FFP contracts composed the greatest sector of "net loss" renegotiable sales, FFP contracts conversely indicated the lowest profit to sales ratio when total profits and losses are combined. The following tabulation compares the profits to sales ratios of FFP, CPFF, and other contracts:

TABLE 21.—COMBINED PROFITS (NET OF LOSSES) AS A PERCENT OF RENEGOTIABLE SALES, FISCAL YEARS 1963-67

Fiscal year	Total	Contract type		
		FFP	CPFF	Other ¹
1963.....	2.9	2.1	3.1	4.5
1964.....	2.9	2.1	2.9	4.2
1965.....	3.0	2.0	2.8	4.6
1966.....	3.0	2.0	2.5	4.9
1967.....	3.5	3.0	2.5	5.0

¹ Includes FPIF, CPIF, price redeterminable, and time and materials contracts, not reported separately (except for FPIF and CPIF in table 20).

The combined profit (net of losses) to sales ratio varied only slightly from 1963 to 1966's 3.0 percent, before rising to 3.5 percent in 1967. The major cause of this jump was an increase from the low of 2.0 percent in 1965 and 1966 for FFP contracts to 3.0 percent in 1967. CPFF contracts, on the other hand, showed a decline from 3.1 percent in 1963 to 2.5 percent in 1966 and 1967. "Other" contract pricing showed an increase from 4.2 percent in 1964 to 5.0 percent in 1967.

A more detailed comparison of combined renegotiable profits to sales ratios for 1965-67 is presented in table 22. As presented, one comparison may be made between fixed-price type (FFP and FPIF) and cost reimbursement type (CPFF and CPIF) contracts. This reveals little difference in ratios; the slight gap of 0.2 percentage points in 1965 is closed to an even 3.5 percent in 1967.

Incentive type contracts (FPIF and CPIF), however, have significantly greater ratios: FPIF increased from 5.4 percent in 1965 to 5.9 percent in 1967, and CPIF rose from 3.9 percent in 1965 to 5 percent in 1967. Within the "fixed" and "cost" categories, incentive contracts enjoyed about a two to one edge in ratios in 1967 (5.0/2.5 for CPIF/CPFF and 5.9/3.0 for FPIF/FFP).

(d) Renegotiable profits—Net profits and net losses

Net renegotiable profits (for firms reporting net profits) fluctuated during 1963-67: from \$1,250 million in 1963 to a high of \$1,492 million in 1964; profits then declined to a low of \$1,245 million in 1966; and they climbed again in 1967 to \$1,443 million, or an increase of 15.4 percent over the 1963 level. Total reported net renegotiable losses, on the other hand, declined steadily from a high of \$359 million in 1964 to a low of \$272 million in 1967 (see app. E for details on net renegotiable profits and losses, by major contract types).

Firm fixed-price (FFP) contracts accounted for a majority of reported net renegotiable profits: ranging from a low of 41.9 percent of profits in 1965 to a high of 54.4 percent in 1967. Cost-plus-fixed-fee (CPFF) contracts represented a declining portion of net renegotiable profits: from 28.4 percent in 1963 to a low of 10.6 percent in 1967. "Other" contracts (primarily fixed-price and cost incentive) increased from 22.0 percent of reported profits in 1963 to 37.8 percent in 1966, and 35.0 percent in 1967.

FFP contracts also accounted for most of the reported renegotiable losses: averaging over 90 percent of net losses. CPFF contracts, however, represented only a very insignificant percent of losses, e.g., 2.0 percent in 1963 and 0 percent in 1967.

Net renegotiable profits as a percentage of renegotiable sales (with net profits) ranged slightly higher than combined profits to combined sales (profit and loss sales) during 1963-1967. As portrayed in table 23, the profit/sales ratio ranged from 4.4 percent in 1964 to 5.0 percent in 1967, or approximately 40 percent greater than when renegotiable losses were "netted" against renegotiable profits.

Whereas FFP contracts had the lowest profit/sales ratios in table 21 (combined sales and profits), these same type contracts revealed the highest ratio (in most cases) in table 23. The picture changed so markedly for FFP contracts because these contracts had the largest share of net renegotiable losses; these losses ranged from 7.1 percent to 9.1 percent of renegotiable sales during 1963-67. At the same time, CPFF contracts had the lowest profit/sales ratios in table 23; they also had the lowest loss/sales ratios on reported net renegotiable losses.

TABLE 23.—RENEGOTIABLE PROFITS AND LOSSES AS A PERCENT OF SALES BY CONTRACT TYPE, FISCAL YEARS 1963-67

Contract type	1963	1964	1965	1966	1967
A. Reported net renegotiable profits.....	4.5	4.4	4.8	4.6	5.0
Firm fixed price.....	4.9	5.4	5.7	5.2	5.5
Cost plus fixed fee.....	3.2	3.2	3.4	2.9	2.9
Other ¹	5.2	4.7	5.6	5.3	5.4
B. Reported net renegotiable losses.....	6.0	6.9	6.6	5.7	6.4
Firm fixed price.....	7.1	8.1	9.1	8.3	8.2
Cost plus fixed fee.....	1.6	1.7	1.0	.8	0
Other ¹	4.8	6.8	1.7	(?)	2.8

¹ Includes fixed price incentive fee, cost plus incentive fee, price redeterminable, and time and materials.

² Profit reported.

Source: Renegotiation Board.

2. Renegotiable sales and profits, and excessive profits determinations

The Renegotiation Board did not provide a data breakdown of renegotiable sales and profits by type of contract pricing for those contractors with respect to which there were excessive profits determinations, as it did for total renegotiable sales, profits, and losses. These data would be helpful in analyzing the type of procurement most likely to result in "excessive profits." In addition, it would help in ascertaining whether or not new or strengthened procurement policies were increasing competitive pricing in contract awards, thus reducing the potential for occurrences of profits which are out of line with those in the particular industry. The available data, however, do afford some indication of the relative magnitude of excessive profits within the overall framework of renegotiation. In addition, some indications are provided of the relative profitability of those contractors with respect to which excessive profits determinations were made.

(a) Excessive profits determinations

Excessive profits determinations, as a percent of total renegotiable sales, ranged from a low of 0.03 percent (three one-hundredths of 1 percent) in 1962 and 1963 to a high of 0.08 percent in 1966, and back down to 0.05 percent in 1967. Excessive profits as a percent of renegotiable sales with a net profit ranged slightly higher: From 0.04 percent in 1963 to 0.09 percent in 1966 (see table 24).

TABLE 24.—EXCESSIVE PROFIT DETERMINATIONS AS A PERCENT OF RENEGOTIABLE SALES, FISCAL YEARS 1961-67

[Dollar amounts in millions]

Fiscal year	Total renegotiable sales	Profitable renegotiable sales	Excessive profits		
			Amount	Percent of total sales	Percent of profitable sales
1961-----	\$25,084	(1)	\$17.2	0.07	-----
1962-----	29,262	(1)	7.8	.03	-----
1963-----	31,228	\$26,208	10.4	.03	0.04
1964-----	39,283	34,073	24.2	.06	.07
1865-----	34,798	29,953	16.1	.05	.05
1966-----	31,841	26,915	24.5	.08	.09
1967-----	33,124	28,914	16.0	.05	.06

¹ Not available.

Source: Renegotiation Board.

Excessive profits determinations (before adjustment for the Federal income tax credit), as a percent of total reported renegotiable profits during 1963-67, ranged from a low of 0.8 percent in 1963 to a high of 1.9 percent in 1966, with a decline to 1.1 percent of profits in 1967. The 5-year average was 1.3 percent:

Fiscal year	Total renegotiable profits (millions)	Excessive profits	
		Amount (millions)	Percent
1963-----	\$1,250	\$10.1	0.8
1964-----	1,492	24.2	1.6
1965-----	1,333	16.1	1.2
1966-----	1,245	24.5	1.9
1967-----	1,443	16.0	1.1
5-year total-----	6,763	90.9	
5-year average-----	1,353	18.2	1.3

(b) *Net excessive profits refunded (after Federal income tax adjustment)*

Net excessive profits returned to the Federal Government (after adjustment for Federal income taxes) fluctuated considerably every other year from 1963 to 1967: \$5.0 million in 1963, up to \$12.3 million in 1964, down to \$8.8 million in 1965, up again to \$12.6 million in 1966, and back to \$8.3 million in 1967. The 5-year annual average amounted to \$9.4 million per year. The net excessive profits, as a percent of reported renegotiable profits, ranged from a low of 0.4 percent in 1963 to a high of 1.0 percent in 1966, before dropping to 0.6 percent in 1967.

Fiscal year	Total renegotiable profits (millions)	Net excessive profits refunded (after Federal income tax adjustment)	
		Amount (millions)	Percent
1963.....	\$1,250	\$5.0	0.4
1964.....	1,492	12.3	0.8
1965.....	1,333	8.8	0.7
1966.....	1,245	12.6	1.0
1967.....	1,443	8.3	0.6
5-year total.....	6,763	47.0	-----
5-year average..	1,353	9.4	0.7

¹ Revised

(c) *Renegotiable sales and profits of firms determined by the Board to have excessive profits*

The Renegotiation Board provided the staff with aggregate annual data for renegotiable sales and profits before Federal income taxes for those firms (contractors and subcontractors) with respect to which excessive profits determinations were made. Renegotiable profits (before refund) as a percent of renegotiable sales increased from 8.8 percent in 1963 to 16.0 percent in 1967 (see table 25). Profit/sales ratios after renegotiation ranged from 7.3 percent to 13.8 percent for the same period. The renegotiable profit/renegotiable sales ratio for these firms contrasts with the profit/sales ratios reported previously in table 23 for total renegotiable profits and sale of all firms filing reports with the Board:

Fiscal year	Profit/sales ratios, before renegotiation	
	Firms with excess profit determinations ¹	All reported renegotiable profits ²
1963.....	8.8	4.5
1964.....	12.8	4.4
1965.....	15.2	4.8
1966.....	13.6	4.6
1967.....	16.0	5.0

¹ See table 25.

² See table 23.

Excessive profits determinations, as a percent of the renegotiable sales of these firms, ranged from 1.2 percent in 1964 to 2.3 percent in 1966, and 2.1 percent in 1967. For net excessive profits refunded (after Federal income tax adjustments), the profits refunded/sales ratio for these firms varied from 0.6 percent in 1964 to 1.2 percent in 1966, and 1.1 percent in 1967.

TABLE 25.—RENEGOTIABLE SALES AND PROFITS OF FIRMS DETERMINED TO HAVE EXCESSIVE PROFITS, FISCAL YEARS 1963-67

[Dollar amounts in millions]

Fiscal year	Before renegotiation			Excessive profit determination				After renegotiation ¹		
	Sales	Profits		After State tax credit		Net of Federal taxes		Sales	Profits	
		Amount	Percent of sales	Amount	Percent of sales	Amount	Percent of sales		Amount	Percent of sales
1963.....	\$717.2	\$62.9	8.77	\$10.1	1.41	\$5.0	0.70	\$705.7	\$51.4	7.28
1964.....	2,046.1	261.0	12.76	24.2	1.18	12.3	.60	2,014.4	229.3	11.33
1965.....	1,304.8	198.7	15.23	16.1	1.23	8.8	.67	1,282.9	176.7	13.77
1966.....	1,079.1	146.6	13.59	24.5	2.27	12.6	1.17	1,050.6	118.7	11.30
1967.....	776.6	124.2	15.99	16.0	2.06	8.3	1.07	756.8	104.4	13.79

¹ Renegotiable sales and profits after excess profit determination are adjusted by the gross amount of the excess profit (before State tax credits).

Source: Based on data supplied by Renegotiation Board.

Data on renegotiable sales and profits of firms determined to have excessive profits by the Renegotiation Board indicate that these firms represent a declining portion of total renegotiable sales and profits over the past 4 years, 1964-67. As portrayed in the following tabulation, renegotiable sales of these firms, as a percent of total renegotiable sales, have declined from the high of 5.2 percent in 1964 to 2.3 percent in 1967. As a percent of profitable renegotiable sales, the decline has been from 6 percent in 1964 to 2.7 percent in 1967:

TABLE 25A.—RENEGOTIABLE SALES OF FIRMS DETERMINED TO HAVE EXCESSIVE PROFITS, FISCAL YEARS 1963-67

Fiscal year	As a percent of —	
	Total renegotiable sales	Profitable renegotiable sales
1963.....	2.3	2.7
1964.....	5.2	6.0
1965.....	3.8	4.4
1966.....	3.4	4.0
1967.....	2.3	2.7

In addition, renegotiable profits of firms with excessive profits determinations have declined absolutely and as a percent of total renegotiable profits reported: from \$261 million, or 17.5 percent of total renegotiable profits in 1964, to \$127 million, or 8.6 percent in 1967:

*Renegotiable profits of firms determined to have excessive profits, fiscal years, 1963-67—
As a percent of total renegotiable profits*

Fiscal year:	
1963.....	5.0
1964.....	17.5
1965.....	14.9
1966.....	11.8
1967.....	8.6

The profit/sales ratios on the nonrenegotiable business (all other sales of the firm—commercial and nonrenegotiable governmental) of the firms having excessive profits determinations were much higher than the profit/sales ratios on the renegotiable business of these firms for 1964-67 (see table 26). This ratio increased from 19.9 percent in 1964 to 31.4 percent in 1967, as compared to the increase from 12.8 percent to 16.0 percent for the ratio on renegotiable sales during the

same period. Overall profit/sales ratios for these firms ranged from 8.2 percent in 1963 to 29.2 percent in 1967.

Although the renegotiable sales of these firms declined substantially from 1964 to 1967, nonrenegotiable sales for 1967 were only slightly below the 1964 level after reaching a low point in 1966. Profits on nonrenegotiable sales rose from \$987 million in 1964 to \$1,484 million in 1967.

TABLE 26.—PROFITS AS A PERCENT OF SALES, NONRENEGOTIABLE VERSUS RENEGOTIABLE SALES OF FIRMS DETERMINED TO HAVE EXCESSIVE PROFITS, FISCAL YEARS 1963-67

[Amounts in millions]

Fiscal year	Total			Nonrenegotiable			Renegotiable ¹	
	Sales	Profits		Sales	Profits		Profits	
		Amount	Percent of sales		Amount	Percent of sales	Amount	Percent of sales
1963.....	\$1,913.8	\$157.1	8.21	\$1,196.6	\$94.2	7.87	\$62.9	8.77
1964.....	7,010.1	1,248.3	17.81	4,964.0	987.3	19.89	261.0	12.76
1965.....	5,630.9	1,341.9	23.83	4,326.1	1,143.2	26.43	198.7	15.23
1966.....	4,370.4	932.2	21.33	3,291.3	785.6	23.87	146.6	13.59
1967.....	5,507.1	1,608.6	29.21	4,730.5	1,484.4	31.38	124.2	15.99

¹ See table 25 for renegotiable sales before renegotiation.

Source: Based on data supplied by the Renegotiation Board.

The annual profit/sales ratios in tables 25 and 26 represent the average of all the firms with respect to which excessive profits determinations were made; thus, an analysis of the variation between firms is not possible. The Renegotiation Board did not supply data on a case-by-case basis. Moreover, the comparability or noncomparability of the renegotiable and nonrenegotiable business of these firms was not indicated. In addition, data were also not provided for a comparison of profits as a percent of net worth. Therefore, the above comparisons of average profit/sales ratios are based on only one indicator of corporate profitability, and the validity of the comparisons also is limited by the aggregate nature of the data.

Appendix C

ADDITIONAL INFORMATION ON DEPARTMENT OF DEFENSE PROCUREMENT

A. FORMAL ADVERTISEMENT VERSUS NEGOTIATION IN DOD CONTRACT POLICY

The term "formal advertisement" suggests that the nature of the procedure is formal and legalistic, with strict and clear specifications to be followed by both Government and industry participants. The "Government Invitation for Bid" is distributed to prospective bidders as well as being announced publicly. Sealed bids are submitted, publicly opened, and the contract is awarded "to that responsible bidder whose bid, * * * will be most advantageous to the Government, price and other factors considered."¹ Thus, if clear-cut specifications are not available for the proposed contract (e.g., research and development contract) or cost experience data are not accurately determinable (e.g., new weaponry systems), then the contract must be awarded on some type of negotiated basis.

Under a negotiation procedure, a request for proposals or quotations accompanied by adequate supporting cost or price data is made. Following review and analysis (and sometimes audit verification), negotiations are conducted with "all responsible offerors who submit proposals within a competitive range, price and other factors considered."² In order to justify the use of negotiations, a contract may not be negotiated unless it comes within one of 17 statutorily authorized categories (10 U.S.C. 2304(a)):

(1) necessarily in the public interest during a period of "national emergency"—this includes (a) labor surplus area and industry set-asides, (b) small business set-asides, and (c) balance-of-payments program;

(2) if the "public exigency" does not allow the delay present in advertising;

(3) if the total contract purchase price does not exceed \$2,500;

(4) contracts for personal or professional services;

(5) services of educational institutions;

(6) supplies or services purchased and used outside the United States;

(7) medicine or medical supplies;

(8) supplies purchased for authorized resale;

(9) perishable or nonperishable subsistence supplies;

(10) if it is "impractical to secure competition by formal advertising" (includes items obtainable from only one source, where patent rights preclude competition, where formal advertisement has not resulted in a "responsive" bid, etc.);

¹ASPR, sec. 2-101.

²ASPR, sec. 3-102.

- (11) "experimental, developmental, test, or research" contracts;
- (12) purchases involving security classified items;
- (13) determination that "standardization of technical equipment and interchangeability of parts" is necessary;
- (14) determination of "technical or specialized supplies requiring substantial initial investment or extended period of preparation for manufacture";
- (15) where formally advertised bids are not reasonable or have not been arrived at independently in open competition;
- (16) purchases from a supplier in order to "keep facilities available in the interest of national defense or industrial mobilization"; or
- (17) otherwise authorized by specific laws or statutes.

B. NEGOTIATED AUTHORITY—DOD MILITARY CONTRACTS

As previously mentioned, contracts may be negotiated only if they may be categorized within one of the 17 statutory authorizations. A comparative summary for 11 of the major statutory categories is presented in tables A and B. Contract awards under "public exigency" have shown the greatest absolute and percentage increases from 1960 to 1967: (1) an increase from \$144 million in 1960 to \$6,029 million in 1967, and (2) a rise from 0.6 percent of total awards (excluding intragovernmental) in 1960 to 13.9 percent of such awards in 1967. The next greatest increase in dollar magnitude was in the category of contracts determined to be "impractical to secure by formal advertising": (1) from \$3,327 million in 1960 to \$7,521 million in 1967; and (2) an increase from 14.5 percent of the total in 1960 to 17.3 percent in 1967.

Negotiated purchases from a supplier in order to "keep facilities available in the interest of national defense or industrial mobilization" also increased sharply: (1) first, declining from \$924 million in 1960 to a low of \$328 million in 1964 and, second, rising to a new high of \$3,293 in 1967; and (2) as a percent of total purchases, declining from 4.2 percent in 1960 to 1.2 percent in 1964, then rising rapidly to 7.6 percent in 1967.

The two categories previously representing the largest share of negotiated procurement were (a) "experimental, developmental, test, or research" and (b) "technical or specialized supplies requiring substantial initial investment or extended period of preparation for manufacture." These two categories accounted for 20.4 percent and 26.4 percent respectively in 1960; category (b) increased to 29.2 percent in 1962, and thereafter declined to 15 percent in 1967; while category (a) increased to 21.4 percent in 1961, and steadily decreased to 11.2 percent of total defense procurement in 1967. The absolute amounts for each category in 1967 were about the same as they were in 1960, after increases during the intervening years. Thus, the above four major categories (each over 10 percent) of negotiated contracts (all those mentioned except the category of purchases to keep facilities available) accounted for 57.5 percent of total procurement in 1966 and 57.4 percent in 1967. These same four categories accounted for 61.9 percent of procurement in 1960 and 64.4 percent in 1961.

TABLE A.—VALUE OF DEPARTMENT OF DEFENSE MILITARY CONTRACT AWARDS BY MAJOR STATUTORY AUTHORITY, FISCAL YEARS 1960-67¹
 [In millions of dollars]

Statutory authority	1960	1961	1962	1963	1964	1965	1966	1967
Total, excluding intragovernmental.....	22,908	24,703	28,099	29,032	28,235	27,385	37,229	43,381
Formally advertised.....	3,170	2,932	3,545	3,678	4,072	4,817	5,283	5,792
“Other” authority.....	19,738	21,772	24,554	25,354	24,163	22,567	31,945	37,589
“Other” authority (major categories):								
National emergency.....	769	941	1,430	1,397	1,544	1,639	1,857	2,114
Public exigency.....	144	126	417	562	586	1,104	5,082	6,029
Purchases not over \$2,500.....	825	919	1,069	1,280	1,338	1,393	1,705	1,841
Purchases outside United States.....	940	1,014	1,194	962	958	1,037	1,934	2,263
Perishable or nonperishable subsistence.....	442	436	485	536	685	802	1,088	1,178
Impractical to secure by formal advertising.....	3,324	3,513	3,906	4,487	4,690	3,929	5,747	7,521
Experimental, developmental, test, or research.....	4,680	5,279	5,764	5,585	5,017	4,557	4,496	4,848
Technical or specialized supplies requiring substantial initial investment or extended period of preparation for manufacturing.....	6,034	6,992	8,194	8,069	8,016	6,284	6,039	6,501
Purchases to keep facilities available in the interest of national defense or industrial mobilization.....	974	671	670	819	328	337	2,172	3,293
Classified purchases.....	964	1,259	772	420	217	115	123	129
Services of educational institutions.....	299	310	295	446	412	431	384	454
Other (miscellaneous) authority.....	343	312	358	790	974	938	1,320	1,418

¹ Details may not add to totals because of rounding.

Source: Office of the Secretary of Defense, “Military prime contract awards and subcontract payments or commitments, July 1966-June 1967,” and “July 1961-June 1962.”

TABLE B.—VALUE OF DEPARTMENT OF DEFENSE MILITARY CONTRACT AWARDS BY MAJOR STATUTORY AUTHORITY, FISCAL YEARS 1960-67¹

[Percentage distribution]

	1960	1961	1962	1963	1964	1965	1966	1967
Statutory authority								
Total, excluding intragovernmental.....	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0
Formally advertised.....	13.8	11.9	12.6	12.7	14.4	17.6	14.2	13.4
"Other" authority.....	86.2	88.1	87.4	87.3	85.6	82.4	85.8	86.6
"Other" authority (major categories):								
National emergency.....	3.4	3.8	5.1	4.8	4.5	6.0	5.0	4.9
Public exigency.....	0.6	0.5	1.5	1.9	2.1	4.0	13.7	13.9
Purchases not over \$2,500.....	3.6	3.7	3.8	4.4	4.7	5.1	4.6	4.2
Purchases outside United States.....	4.1	4.1	4.3	3.3	3.4	3.8	5.2	5.2
Perishable or nonperishable subsistence.....	1.9	1.8	1.7	1.9	2.4	2.9	2.9	2.7
Impractical to secure by formal advertising.....	14.5	14.2	13.9	13.5	14.5	14.4	13.5	17.3
Experimental, developmental, test, or research.....	20.4	21.4	20.5	19.2	17.8	16.6	12.1	11.2
Technical or specialized supplies requiring substantial initial investment or extended period of preparation for manufacturing.....	24.6	28.3	29.2	27.8	28.4	23.0	16.2	15.0
Purchases to keep facilities available in the interest of national defense or industrial mobilization.....	4.2	2.7	2.4	2.8	1.2	1.2	5.8	7.6
Classified purchases.....	4.2	5.1	2.7	1.4	0.8	0.4	0.3	0.3
Services of educational institutions.....	1.3	1.3	1.1	1.5	1.5	1.6	1.0	1.1
Other (miscellaneous) authority.....	1.6	1.2	1.2	2.8	3.4	3.4	3.5	3.2

Details may not add to totals because of rounding.

Source: Table A.

Appendix D

SECRETARY NITZE'S MEMO OF SEPTEMBER 29, 1967, AND VIEWS THEREON BY THE COMPTROLLER GENERAL, RE- GARDING POSTAWARD AUDITS

THE SECRETARY OF DEFENSE,
Washington, September 29, 1967.

Memorandum for: Secretaries of the Military Departments.
Assistant Secretary of Defense (Comptroller).
Assistant Secretary of Defense (I. & L.).
Directors of Defense agencies.

Subject: Access to cost performance records on noncompetitive firm fixed-price contracts.

I have given careful consideration to the arguments for and against access to contractor postaward cost performance records on noncompetitive firm fixed-price contracts, for the purpose of determining the degree of contractor compliance with Public Law 87-653. Clearly, it has been and remains our policy that in firm fixed-price contracts the cost and profit consequences are the full responsibility of the contractor since he assumes all the risk of performing in accordance with the contract. Likewise, it is our policy that such contracts be used only where there exists a reliable basis for judging reasonableness of contractor cost estimates. Where such a basis does not exist, other contract forms should be used.

The Department of Defense is required to conduct a program of review and audit sufficient to ascertain that the cost or pricing data submitted by contractors in connection with the negotiation of noncompetitive firm fixed-price contracts were current, accurate, and complete as required by Public Law 87-653. It is our policy to make such audits, as fully as possible, prior to completing the negotiation of the contract. However, when it is necessary to provide assurance that defective cost or pricing data were not submitted, audits should also be conducted of actual costs incurred after contracts are consummated. To assure that such postaward audits may be conducted when deemed appropriate, action shall be taken to include in all noncompetitive firm fixed-price contracts involving certified costs or pricing data, a contractual right to have access to the contractor's actual performance records.

Circumstances which may dictate the use of a postaward cost performance audit include such cases as those where: (1) factors of urgency in placing the initial procurement were clearly present; (2) material costs are a significant portion of the contractor's total cost estimate; (3) a substantial portion of the contract is proposed for subcontracting; or (4) there was a substantial interval between completion of the precontract cost evaluation and agreement on price.

In directing this action, I wish to make it clear that the purpose of any postaward cost performance audit, as provided herein, is limited

to the single purpose of determining whether or not defective cost or pricing data were submitted. Access to a contractor's records shall not be for the purpose of evaluating profit-cost relationships, nor shall any repricing of such contracts be made because the realized profit was greater than was forecast, or because some contingency cited by the contractor in his submission failed to materialize—unless the audit reveals that the cost and pricing data certified by the contractor were, in fact, defective.

I desire that the Assistant Secretary of Defense (Installations and Logistics) and the Assistant Secretary of Defense (Comptroller) issue implementing instructions to place the above policies into effect.

PAUL H. NITZE.

COMPTROLLER GENERAL OF THE UNITED STATES,
Washington, D.C., October 30, 1967.

HON. WILLIAM PROXMIRE,
U.S. Senate.

DEAR SENATOR PROXMIRE: In view of your interest in the implementation of Public Law 87-653 by the Department of Defense, we are offering our views on a memorandum issued by the Deputy Secretary of Defense dated September 29, 1967, on access to cost performance records on noncompetitive firm fixed-price contracts.

The memorandum is addressed to the Secretary of the Military Departments, the Assistant Secretaries of Defense (Comptroller) and (Installations and Logistics) and Directors of Defense agencies. It contains statements on contracting and auditing policies of the Department of Defense and directs the Assistant Secretaries of Defense to issue implementing instructions to place the policies, summarized below, into effect.

Noncompetitive firm fixed-price contracts shall be used only where there exists a reliable basis for judging reasonableness of contractor cost estimates; where such a basis does not exist, other contract forms shall be used.

A program shall be conducted for review and audits sufficient to ascertain that the cost or pricing data submitted by contractors in connection with the negotiation of noncompetitive firm fixed-price contracts were current, accurate, and complete as required by Public Law 87-653. Such audits shall be made, as fully as possible, prior to completing the negotiation of the contract.

When it is necessary to provide assurance that defective cost or pricing data were not submitted, audits should be conducted of actual costs incurred after contracts are consummated. To assure that such postaward audits may be conducted, action shall be taken to include, in all noncompetitive firm fixed-price contracts involving certified cost or pricing data, a contractual right to have access to the contractor's actual performance records.

The memorandum also lists circumstances which may indicate the need for postaward audits of performance costs.

With respect to access to contractors' records, we believe that the memorandum would accomplish by administrative action what would be accomplished by enactment of the bill, S. 1913, submitted by you on June 6, 1967, except that the Deputy Secretary's memorandum is

silent on the matter of the agency's right of access to subcontractors' performance records which was specifically provided for in your bill. We, therefore, spoke to Department of Defense officials responsible for drafting regulations to implement the memorandum about this apparent omission.

We were advised that consideration would be given, in drafting the implementing regulations, to requiring prime contractors to include clauses in subcontracts giving agency representatives the right to have access to subcontractors' records of performance. As soon as we have had an opportunity to review the Department of Defense regulations on this matter we will advise you.

Sincerely yours,

ELMER B. STAATS,
Comptroller General of the United States.

Appendix E

RENEGOTIABLE PROFITS AND LOSSES

RENEGOTIABLE PROFITS AND LOSSES REVIEWED BY RENEGOTIATION BOARD, BY CONTRACT TYPE, FISCAL YEARS 1963-67

A—REPORTED NET RENEGOTIABLE PROFITS

[Amounts in millions of dollars]

Fiscal year	Amounts			Percent			
	Total	Firm-fixed price	CPFF	Other ¹	Firm-fixed price	CPFF	Other ¹
1963	\$1,250	\$620	\$355	\$275	49.6	28.8	22.0
1964	1,492	658	430	404	44.1	28.2	27.1
1965	1,333	559	296	478	41.9	22.2	35.9
1966	1,245	574	200	471	46.1	16.1	37.8
1967	1,443	785	153	505	54.4	10.6	35.0

B—REPORTED NET RENEGOTIABLE LOSSES

1963	\$333	\$311	\$7	\$16	93.4	2.0	4.7
1964	359	316	15	28	88.0	4.1	7.9
1965	291	254	12	25	87.3	4.1	8.6
1966	283	281	7	² (4)	99.2	2.3	² (1.5)
1967	272	261	0	11	96.0	0.0	4.0

¹ Includes Fixed-Price Incentive Fee (FP/IF), Cost Plus Incentive Fee (CP/IF), Price Redeterminable, Source: Renegotiation board.
and Time and Materials Contracts.

² Profit figure.

Appendix F

INFORMATION RELATING TO NATIONAL AERONAUTICS AND SPACE ADMINISTRATION CONTRACTS

NATIONAL AERONAUTICS AND SPACE ADMINISTRATION,
Washington, D.C., March 13, 1968.

HON. WILBUR D. MILLS,
*Chairman, Joint Committee on Internal Revenue Taxation, House
of Representatives, Washington, D.C.*

DEAR MR. CHAIRMAN: This is in reply to Mr. Woodworth's letter of February 13, 1968, requesting information about NASA contracts for use in a report on the Renegotiation Act of 1951. The requested data is an attachment to this letter.

Mr. Woodworth also solicits our views on the application of the act to NASA contracts, and I appreciate the opportunity to comment on this subject.

As I understand it, the determination of excessive profits must, in each instance, reflect the judgment of the Board of the application of each of the statutory factors enumerated in section 103 of the Renegotiation Act. Among these factors is subparagraph (6) which reads in part: "Such other factors the consideration of which the public interest and fair and equitable dealing may require * * *."

We believe that the Renegotiation Board might well give added weight to special factors involved in performing work under NASA contracts. We believe that it should be recognized that NASA's work involves complex, long leadtime, advanced research, and development in which progress, development plans, and costs cannot always be laid out with assurance of meeting every goal established. Every effort is made to plan the work in such a way that potential problems are anticipated and so that guidance is given to contractors by the Government to assure that the work proceeds as satisfactorily as possible. These circumstances require close monitoring of contractor activities by NASA laboratories having a strong technical interface with the contractor. Through our laboratory competence we must provide constructive criticism all through the program, rather than waiting for demonstration of successful achievement of program goals only when the end product is delivered and flown. Nevertheless, the final test of the success of the development program and of the work aimed at solving and reducing the number of problems encountered through the course of the development program is in the final flight operations of the aeronautical or space system involved.

While we are aware that the Board under its regulation and policy pronouncements recognizes the objectives of incentive contracts, we believe the Board has not given full recognition to the difficult performance requirements of our major research and development programs. NASA has relied on extensive management and technical program reviews, as well as innovative contractual arrangements, to

assure that the Government receives the result it is seeking through the expenditures of Government funds. These reviews, and the incentive contract arrangements wherein the contractor's profit is based on evaluation of the quality of his work and his ability to achieve specified program requirements, provide for a thoughtful control of the profit paid to the contractor. This control considers the difficulty of the job, the risk of the contractor's reputation and financial status, the investment made by the contractor in undertaking the work, including his financial and management commitment to the job, and the overall management responsibility that he assumes for the work that he directly performs or that his subcontractors perform. In our effort to get the best possible performance and in recognition of these various factors, our incentive fee contract arrangements are so established that added profit goes with high performance by the contractor.

In summary, then we believe that the complexity of our work, its public visibility, and the long time required for completion of any individual part of it argue for some special consideration when the reasonableness of the fees we have paid are rejudged. We do believe, however, that the Renegotiation Act of 1951 should have continuing effect. We support legislation removing the provision of that act which limits to June 30, 1968, the contracts subject to renegotiation under that act.

Because of the urgency of your committee's most recent request, this report has not been submitted to the Bureau of the Budget for advice as to its relationship to the program of the President.

Sincerely,

JAMES E. WEBB, *Administrator.*

DISCUSSION OF NASA'S METHODS OF PROCUREMENT AND SELECTION OF TYPES OF CONTRACTS

The attached table 1 shows NASA awards to business firms by method of placement for the period fiscal years 1961-67. This table includes all awards to business firms regardless of the dollar value of the individual award.

Table 2 shows NASA awards to business firms by type of contract for the period fiscal years 1961-67. The data in this table include only awards on research and development contracts of \$10,000 and over and on other contracts of \$25,000 and over. However, the dollar value of these larger awards account for more than 90 percent of the dollar value of the total awards. Conversely, in terms of numbers of actions, the larger contracts account generally for less than 10 percent of the total number of actions.

NASA's extensive use of negotiation procedures, which is evidenced in table 2, reflects the fact that most of our procurements are for experimental, development, or research work. Specifications for these procurements can rarely be established to the degree necessary for firm-fixed-price contracts and formal advertising.

With respect to the negotiated procurements, NASA utilizes a wide range of contract types from which we select, for a given procurement, that type most practical and advantageous to the Government. In major research and development projects, NASA employs "Phased Project Planning." This procedure provides for the conduct of the

projects in an appropriate number of sequential phases and the most advantageous type of procurement is utilized for each phase.

As may be noted from table 2, NASA has been utilizing, to an increasing degree, incentive-type contracts. These employ various types of incentive arrangements from which are selected those most suitable for the specific procurements. The various types in effect as of December 31, 1967, and their aggregate target values are shown in table 3. It will be noted that the majority of the dollars represent cost-plus-incentive-fee contracts. These contracts utilize formulas against which performances may be measured objectively. The second and third largest groups are the cost-plus-award-fee and the combined cost-plus-incentive-fee/cost-plus-award-fee contracts which are primarily for support services and which require subjective evaluation of contract performance.

Generally the range in confidence in negotiated target costs is within plus or minus 15 to 25 percent. This range becomes smaller as we gain experience in space age products and are better able to define our requirements.

Information about overruns and underruns of estimated costs is not regularly maintained in our procurement data bank and is not immediately available. It could be gathered from procuring centers, if required. We would, of course, have to carefully define these terms since cost growth in a research and development program has multiple causes.

TABLE 1.—NASA AWARDS TO BUSINESS FIRMS¹ BY METHOD OF PLACEMENT, FISCAL YEARS 1961-67

Method of placement	1961	1962	1963	1964	1965	1966	1967
Net value of awards (millions) ¹							
Total.....	\$423.3	\$1,030.1	\$2,261.7	\$3,521.1	\$4,141.4	\$4,087.7	\$3,864.1
Total, competitive.....	276.8	565.8	1,302.0	2,119.5	2,630.1	2,692.5	2,698.4
Advertised.....	38.6	64.1	106.6	134.4	169.2	111.0	81.1
Negotiated.....	238.2	501.7	1,195.4	1,985.1	2,460.9	2,581.5	2,617.3
Total, noncompetitive.....	146.5	464.3	959.7	1,401.6	1,511.3	1,395.2	1,165.7
Follow-on after competition.....	(²)	(²)	³ 255.7	³ 494.8	³ 503.6	³ 372.7	³ 346.9
Other noncompetitive.....	146.5	464.3	704.0	906.8	1,007.7	1,022.5	818.8
Number of contract actions ¹							
Total.....	82,700	109,600	176,600	237,100	235,100	216,600	212,100
Total, competitive.....	32,000	36,700	72,800	88,200	101,200	97,300	91,000
Advertised.....	4,000	3,700	9,900	15,600	15,500	13,200	11,400
Negotiated.....	28,000	33,000	62,900	72,600	85,700	84,100	79,600
Total, noncompetitive.....	50,700	72,900	103,800	148,900	133,900	119,300	121,100
Follow-on after competition.....	(²)	(²)	³ 100	³ 200	³ 100	³ 100	³ 200
Other noncompetitive.....	50,700	72,900	103,700	148,700	133,800	119,200	120,900

¹ Total awards to business firms.

² Data included in other noncompetitive procurements.

³ Follow-on after competition procurements of less than \$25,000 are included in other noncompetitive procurements

TABLE 2.—NASA AWARDS TO BUSINESS FIRMS¹ BY TYPE OF CONTRACT, FISCAL YEARS 1961-67

[Net value of awards (millions) †]

Type of contract	Fiscal year 1961	Fiscal year 1962	Fiscal year 1963	Fiscal year 1964	Fiscal year 1965	Fiscal year 1966	Fiscal year 1967
Total.....	\$362.5	\$908.4	\$2,113.8	\$3,379.6	\$3,993.0	\$3,951.2	\$3,775.4
Incentive.....	.1	13.1	162.7	269.3	602.2	1,922.5	2,567.6
Fixed price.....	.1	3.8	10.2	27.2	100.6	73.6	117.1
Cost reimbursable.....		9.3	152.5	242.1	501.6	1,848.9	2,450.5
Other fixed price.....	56.3	125.4	251.8	388.4	492.5	407.1	411.3
Firm.....	55.4	125.0	247.5	387.0	492.0	399.2	409.5
Redeterminable.....	.9	.4	4.1	1.4	.3	1.3	1.2
Escalation.....			.2		.2	6.6	.6
Other cost reimbursable.....	300.4	760.2	1,692.5	2,713.6	2,885.5	1,612.1	780.7
Cost no fee.....	.3	11.1	71.4	46.5	42.9	20.8	5.6
Cost plus fixed fee.....	299.9	748.6	1,618.0	2,664.9	2,841.3	1,591.0	774.6
Cost sharing.....	.2	.5	3.1	2.2	1.3	.3	.5
Labor hour.....		.2	1.3	1.7	2.0	.1	.7
Time and materials.....	5.7	9.5	5.5	6.6	10.8	9.4	15.1
Number of contract actions ¹							
Total.....	1,270	2,438	4,295	7,544	11,716	12,029	11,623
Incentive.....	1	10	68	237	602	956	1,265
Fixed price.....	1	4	5	48	99	110	145
Cost reimbursable.....		6	63	189	503	846	1,120
Other fixed price.....	551	984	1,965	3,565	6,279	6,785	5,870
Firm.....	541	979	1,941	3,550	6,262	6,740	5,844
Redeterminable.....	10	5	22	15	15	10	13
Escalation.....			2		2	35	13
Other cost reimbursable.....	669	1,361	2,185	3,626	4,689	4,077	4,216
Cost no fee.....	5	26	80	95	190	198	164
Cost plus fixed fee.....	662	1,332	2,096	3,515	4,484	3,872	4,039
Cost sharing.....	2	3	9	16	15	7	13
Labor hour.....		3	14	28	31	8	6
Time and materials.....	49	80	63	88	115	203	266

¹ Awards on R. & D. contracts of \$10,000 and over and on all other contracts of \$25,000 and over.

TABLE 3.—NASA INCENTIVE CONTRACTS—BY TYPE AS OF DEC. 31, 1967

Type of contract	Number of contracts	Target value (millions)
Cost-plus-incentive-fee.....	117	\$3,848.3
Cost-plus-award-fee.....	77	848.1
Cost-plus-incentive-fee/award-fee.....	45	1,026.7
Fixed-price-incentive.....	30	342.1
Fixed-price-incentive/award-fee.....	3	131.6
Cost contribution.....	1	6.4
Total.....	273	6,203.2

Appendix G

INFORMATION RELATING TO ATOMIC ENERGY COMMISSION CONTRACTS

U.S. ATOMIC ENERGY COMMISSION,
Washington, D.C., February 26, 1968.

MR. LAURENCE N. WOODWORTH,
*Chief of Staff, Joint Committee on Internal Revenue Taxation,
Congress of the United States.*

DEAR MR. WOODWORTH: In response to your letter of February 13, 1968, addressed to Chairman Glenn T. Seaborg, I am enclosing herewith procurement statistics in the form of summary of procurement actions for the fiscal years 1961 through 1967. Prime contracts are broken down to show method of placement; i.e., advertised or negotiated. Since subcontracts are not subject to the formal advertising statutory requirements that apply to prime contracts, we do not have this same breakdown with respect to method of placement. However, our cost-type contractors who operate AEC plants and laboratories have established procurement and contracting procedures which provide for the placing of subcontracts wherever possible on a competitive basis. The enclosed statistics also show for both prime contracts and subcontracts a breakdown as to type of work, source of supply, and type of procurement.

You will note that there was a substantial decline in the percentage of dollars awarded under fixed-price contracts after fiscal year 1962. This was due to a significant reduction in the program for the purchase of uranium ore.

Our cost contracts are basically all either cost-plus-a-fixed-fee or, in the case of educational institutions and nonprofit organizations, straight cost contracts. In the case of our cost-plus-a-fixed-fee contracts, we have adopted declining fee curves which are based upon the scope, character, and estimated cost of the work to be performed by the contractor and which provides for fees which we feel are fair and reasonable.

Expenditures under our cost contracts are closely controlled by established cost principles, periodic audits, establishment of approved procurement and contracting procedures for subcontracting and purchasing, and specific approval of subcontracts over a specified dollar amount. We do not have readily available information as to overruns and underruns of estimated cost. In the case of cost-plus-a-fixed-fee contracts, the fee, which includes the contractor's profit, of course would not change because of overruns or underruns of estimated cost.

While our contracts cover the entire range from off-the-shelf items to first-of-a-kind production items to basic research, the major part of our prime contracting is carried on under cost or cost-plus-a-fixed-fee operating contracts, which provide little, if any, opportunity for

excessive profits; therefore, the Renegotiation Act has a limited impact on our program. However, in view of the possibility that there may be some direct fixed-price procurements for which there is relatively little cost and production experience available and for fixed-price procurements by our cost-type contractors, we believe the Renegotiation Act may be a deterrent to excessive pricing and provides a measure of insurance against excessive profits. We do not have any specific suggestions for improvement in the act.

If there is any further or additional information that you desire, we shall be happy to furnish it to you.

Sincerely yours,

JOSEPH L. SMITH,
Director, Division of Contracts.

PROCUREMENT STATISTICS—SUMMARY OF PROCUREMENT ACTIONS,¹ FISCAL YEAR 1961

[Dollars in millions]

	Actions	Amount	Percent	
I. Advertised versus negotiated (15,752 prime actions):				
Advertised.....	1,388	\$65.5	2.5	
Negotiated.....	14,364	2,546.0	97.5	
Total.....	15,752	2,611.5	100.0	
	Prime actions	Percent	Subactions	Percent
II. Type of work:				
Construction and A-E.....	\$151.3		\$54.3	
Materials, supplies, and equipment (for construction)	3.8		65.3	
Materials, supplies, and equipment (other than construction)	830.3		474.9	
Research and development.....	524.3		20.6	
Plant operation and other.....	1,101.8		54.1	
Total.....	2,611.5		669.2	
III. Source of supply:				
Big business.....	1,762.0	67.5	377.2	56.4
Small business.....	190.4	7.3	277.4	41.4
Government agency.....	273.5	10.5	7.2	1.1
Educational and other nonprofit organizations.....	385.6	14.7	7.4	1.1
Total.....	2,611.5	100.0	669.2	100.0
IV. Type of procurement:				
Fixed-price.....	1,169.2	44.8	587.6	87.8
Cost-type.....	1,442.3	55.2	81.6	12.2
Total.....	2,611.5	100.0	669.2	100.0

¹ Actions are \$25 and over and include original contract (or subcontract) modifications, amendments, and supplemental agreements.

PROCUREMENT STATISTICS—SUMMARY OF PROCUREMENT ACTIONS,¹ FISCAL YEAR 1962

[Dollars in millions]

	Actions	Amount	Percent	
I. Advertised versus negotiated (16,494 prime actions):				
Advertised.....	1,138	70.2	2.6	
Negotiated.....	15,356	2,667.5	97.4	
Total.....	16,494	2,737.7	100.0	
	Prime actions	Percent	Subactions	Percent
II. Type of work:				
Construction and A-E.....	\$163.3		\$29.1	
Materials, supplies, and equipment (for construction).....	6.3		100.8	
Materials, supplies, and equipment (other than for construction).....	570.1		511.0	
Research and development.....	692.2		24.1	
Plant operation and other.....	1,305.8		61.0	
Total.....	2,737.7		736.0	
III. Source of supply:				
Big business.....	1,797.2	65.6	382.0	51.9
Small business.....	191.5	7.0	338.0	45.9
Government agency.....	275.1	10.1	10.2	1.4
Educational and other nonprofit organizations.....	473.9	17.3	5.8	0.8
Total.....	2,737.7	100.0	736.0	100.0
IV. Type of procurement:				
Fixed-price.....	884.2	32.3	639.9	86.9
Cost-type.....	1,853.5	67.7	96.1	13.1
Total.....	2,737.7	100.0	736.0	100.0

¹ Actions are \$25 and over and include original contract (or subcontract) modifications, amendments, and supplemental agreements.

PROCUREMENT STATISTICS—SUMMARY OF PROCUREMENT ACTIONS¹ FISCAL YEAR 1963

[Dollars in millions]

	Actions	Amount	Percent	
I. Advertised versus negotiated (15,419 prime actions):				
Advertised.....	968	\$58.5	2.2	
Negotiated.....	14,451	2,542.6	97.8	
Total.....	15,419	2,601.1	100.0	
	Prime actions	Percent	Subactions	Percent
II. Type of work:				
Construction and A-E.....	\$181.3		\$38.9	
Materials, supplies, and equipment (for construction).....	4.3		67.2	
Materials, supplies, and equipment (other than for construction).....	198.4		549.3	
Research and development.....	732.8		27.1	
Plant and operation and other.....	1,484.3		62.0	
Total.....	2,601.1		744.5	
III. Source of supply:				
Big business.....	1,754.2	67.4	391.9	52.6
Small business.....	83.5	3.2	334.9	45.0
Government agency.....	248.5	9.6	10.8	1.4
Educational and other nonprofit organizations.....	514.9	19.8	6.9	1.0
Total.....	2,601.1	100.0	744.5	100.0
IV. Type of procurement:				
Fixed-price.....	529.9	20.4	645.8	86.7
Cost-type.....	2,071.2	79.6	98.7	13.3
Total.....	2,601.1	100.0	744.5	100.0

¹ Actions are \$25 and over and include original contract (or subcontract) modifications, amendments, and supplemental agreements.

PROCUREMENT STATISTICS—SUMMARY OF PROCUREMENT ACTIONS¹ FISCAL YEAR 1964

[Dollars in millions]

	Actions	Amount	Percent	
I. Advertised versus negotiated (16,670 prime actions):				
Advertised.....	932	\$71.7	2.7	
Negotiated.....	15,738	2,544.7	97.3	
Total.....	16,670	2,616.4	100.0	
	Prime actions	Percent	Subactions	Percent
II. Type of work:				
Construction and A-E.....	\$133.3		\$40.6	
Materials, supplies, and equipment (for construction).....	1.4		86.4	
Materials, supplies, and equipment (other than for construction).....	177.5		565.1	
Research and development.....	848.2		21.8	
Plant operation and other.....	1,456.0		58.9	
Total.....	2,616.4		772.8	
III. Source of supply:				
Big business.....	1,745.9	66.7	388.0	50.2
Small business.....	60.7	2.3	364.9	47.2
Government agency.....	225.8	8.7	13.7	1.8
Educational and other nonprofit organizations.....	584.0	22.3	6.2	.8
Total.....	2,616.4	100.0	772.8	100.0
IV. Type of procurement:				
Fixed-price.....	573.6	21.9	682.0	88.3
Cost-type.....	2,042.8	78.1	90.8	11.7
Total.....	2,616.4	100.0	772.8	100.0

¹ Actions are \$25 and over and include original contract (or subcontract) modifications, amendments, and supplemental agreements.

PROCUREMENT STATISTICS—SUMMARY OF PROCUREMENT ACTIONS¹ FISCAL YEAR 1965

[Dollars in millions]

	Actions	Amount	Percent	
I. Advertised versus negotiated (16,494 prime actions):				
Advertised.....	830	\$50.5	2.1	
Negotiated.....	15,664	2,423.9	97.9	
Total.....	16,494	2,474.4	100.0	
	Prime actions	Percent	Subactions	Percent
II. Type of work:				
Construction and A-E.....	\$122.8		\$34.0	
Materials, supplies, and equipment (for construction).....	9.9		76.2	
Materials, supplies, and equipment (other than for construction).....	264.4		474.3	
Research and development.....	824.1		19.7	
Plant operation and other.....	1,253.2		73.1	
Total.....	2,474.4		677.3	
III. Source of supply:				
Big business.....	1,599.5	64.6	341.0	50.3
Small business.....	67.5	2.7	312.3	46.2
Government agency.....	234.5	9.5	14.9	2.2
Educational and other nonprofit organizations.....	572.9	23.2	9.1	1.3
Total.....	2,474.4	100.0	677.3	100.0
IV. Type of procurement:				
Fixed-price.....	605.7	24.5	611.3	90.3
Cost-type.....	1,868.7	75.5	66.0	9.7
Total.....	2,474.4	100.0	677.3	100.0

¹ Actions are \$25 and over and include original contract (or subcontract) modifications, amendments, and supplemental agreements.

PROCUREMENT STATISTICS—SUMMARY OF PROCUREMENT ACTIONS¹ FISCAL YEAR 1966

[Dollars in millions]

	Actions	Amount	Percent	
I. Advertised versus negotiated (14,800 prime actions):				
Advertised.....	721	\$52.0	2.2	
Negotiated.....	14,079	2,312.2	97.8	
Total.....	14,800	2,364.2	100.0	
	Prime actions	Percent	Subactions	Percent
II. Type of work:				
Construction and A-E.....	\$84.1		\$36.2	
Materials, supplies, and equipment (for construction).....	22.1		55.4	
Materials, supplies, and equipment (other than for construction).....	171.2		478.2	
Research and development.....	834.5		19.2	
Plant operation and other.....	1,252.3		61.9	
Total.....	2,364.2		650.9	
III. Source of supply:				
Big business.....	1,510.2	63.9	315.5	48.5
Small business.....	58.5	2.5	312.9	48.1
Government agency.....	182.6	7.7	13.1	2.0
Educational and other nonprofit organizations.....	612.9	25.9	9.4	1.4
Total.....	2,364.2	100.0	650.9	100.0
IV. Type of procurement:				
Fixed-price.....	505.2	21.4	590.0	90.6
Cost-type.....	1,859.0	78.6	60.9	9.4
Total.....	2,364.2	100.0	650.9	100.0

¹ Actions are \$25 and over and include original contract (or subcontract) modifications, amendments, and supplemental agreements.

PROCUREMENT STATISTICS—SUMMARY OF PROCUREMENT ACTIONS,¹ FISCAL YEAR 1967

[Dollars in millions]

	Actions	Amount	Percent	
I. Advertised versus negotiated (14,288 prime actions):				
Advertised.....	692	\$62.0	2.7	
Negotiated.....	13,596	2,259.0	97.3	
Total.....	14,288	2,321.0	100.0	
	Prime actions	Percent	Subactions	Percent
II. Type of work:				
Construction and A-E.....	\$85.3		\$30.8	
Materials, supplies, and equipment (for construction).....	.5		29.3	
Materials, supplies, and equipment (other than for construction).....	88.5		484.5	
Research and development.....	657.5		21.4	
Plant operation and other.....	1,489.2		77.5	
Total.....	2,321.0		643.5	
III. Source of supply:				
Big business.....	1,656.0	71.3	337.3	52.4
Small business.....	55.8	2.4	280.0	43.5
Government agency.....	117.3	5.1	15.6	2.4
Educational and other nonprofit organizations.....	491.9	21.2	10.6	1.7
Total.....	2,321.0	100.0	643.5	100.0
IV. Type of procurement:				
Fixed-price.....	534.3	23.0	572.8	89.0
Cost-type.....	1,786.7	77.0	70.7	11.0
Total.....	2,321.0	100.0	643.5	100.0

¹ Actions are \$25 and over and include original contract (or subcontract) modifications, amendments, and supplemental agreements.

Appendix H

INFORMATION RELATING TO MARITIME ADMINISTRATION AND MARITIME SUBSIDY BOARD (SUCCESSOR TO FED- ERAL MARITIME BOARD) CONTRACTS

OFFICE OF THE ADMINISTRATOR,
U.S. DEPARTMENT OF COMMERCE,
MARITIME ADMINISTRATION,
Washington, D.C., March 1, 1968.

Mr. LAURENCE N. WOODWORTH,
*Chief of Staff, Joint Committee on Internal Revenue Taxation, Congress
of the United States, Washington, D.C.*

DEAR MR. WOODWORTH: By your letter of February 13, 1968, you asked for certain statistical data with respect to contracts entered into by the Maritime Administration and the Maritime Subsidy Board, or its predecessor, the Federal Maritime Board, during the fiscal years 1961 through 1967. Attached to this letter for each of the referred to fiscal years is a tabulation of the number and dollar value of the agency's contracts (excluding contracts of \$10,000 or less) by method of procurement, type of contract, and type of product and service.

You have asked about the extent of overrun or underrun of estimated costs employed in initial pricing. Overruns or underruns arise primarily in connection with the administration's research and development cost reimbursable contracts. An analysis of the research and development contracts completed during fiscal years 1961 through 1967 indicates that overruns and underruns have not been in excessive amounts. As the attached tabulation shows, however, in fiscal year 1967, there was a 20-percent overrun in a ship construction contract.

The procurements of the Maritime Administration (Maritime Subsidy Board) are of ships employed in the foreign commerce of the United States, under the Merchant Marine Act of 1936, as amended. Under these three-party contracts the owner, the ship operator, pays to the contractor a sum equal to the Maritime Subsidy Board's estimate of the cost of building the vessel of the owner to similar plans and specifications in a foreign shipyard. The Board pays the difference between the estimated foreign cost and the domestic price. The Maritime Administration also enters into ship construction contracts with shipbuilders on the basis of orders placed by other Federal agencies under the Economy Act of 1932, as amended.

The dollar values shown for new ship construction and ship conversion do not represent, in the entirety, Government expenditures in the indicated amounts. With respect to procurements under the Merchant Marine Act of 1936, as amended, Government expenditures amounted to approximately 51 percent of the total contract expenditures. The balance is paid by the owner. Of course, under the Economy Act contracts, the Government is responsible for the total price.

The maintenance and repair contracts noted in the attached tabulation represent specific job orders awarded on the basis of competitive bid or negotiation, and are referable to master lump-sum repair contracts entered into by the Maritime Administration with shipyards in the several coastal regions. A ship, undergoing maintenance and repair after each voyage, will have a considerable number of job orders to be performed. Because of the magnitude of the number of maintenance and repair job orders brought about by the increased activity due to the Southeast Asian conflict, currently involving approximately 650 voyages each year, estimates of the total number of contracts, and the total dollars connected therewith, are based upon sampling of ships and voyages as they relate to geographic and traffic factors. The sampling is necessary only for fiscal years 1966 and 1967. In the earlier fiscal years, the number of contracts and dollar amounts shown were based upon actual data.

We trust the above contains the information you desire. Please advise use of any further questions you may have.

Sincerely,

CARL C. DAVIS,
Acting Maritime Administrator.

CONTRACTS AWARDED BY MARITIME SUBSIDY BOARD/
MARITIME ADMINISTRATION

	Number	Amount
FISCAL YEAR 1961		
Method of placement:		
Advertised.....	35	\$315,117,546
Negotiated.....	32	5,242,284
		<u>320,359,830</u>
Compensation arrangement:		
Fixed price.....	55	315,789,661
Cost plus fixed fee.....	6	3,102,314
Cost.....	6	1,467,855
		<u>320,359,830</u>
Types of products and services:		
New ship construction.....	8	305,799,789
Ship conversion.....	1	8,193,300
Research and development.....	17	5,147,458
Supplies, services, and material ¹	19	¹ 1,055,818
Maintenance and repair.....	22	163,465
		<u>320,359,830</u>

CONTRACTS AWARDED BY MARITIME SUBSIDY BOARD/
MARITIME ADMINISTRATION—Continued

	Number	Amount
FISCAL YEAR 1962		
Method of placement:		
Advertised.....	56	\$130,170,792
Negotiated.....	42	3,711,570
		<u>133,882,362</u>
Compensation arrangement:		
Fixed price.....	88	130,455,479
Cost plus fixed fee.....	10	3,426,883
Cost.....		
		<u>133,882,362</u>
Types of products and services:		
New ship construction.....	4	128,855,000
Ship conversion.....		
Research and development.....	12	3,498,575
Supplies, services, and material ¹	7	¹ 1,169,348
Maintenance and repair.....	55	359,439
		<u>133,882,362</u>

See footnote at end of table, p. 133.

CONTRACTS AWARDED BY MARITIME SUBSIDY BOARD/
 MARITIME ADMINISTRATION—Continued

	Number	Amount
FISCAL YEAR 1963		
Method of placement:		
Advertised.....	56	\$252,521,123
Negotiated.....	40	3,374,539
		<u>255,895,662</u>
Compensation arrangement:		
Fixed price.....	87	252,917,847
Cost plus fixed fee.....	9	2,977,815
Cost.....		<u>255,895,662</u>
Types of products and services:		
New ship construction.....	8	242,307,538
Ship conversion.....	2	8,762,600
Research and development.....	10	2,997,798
Supplies, services, and material ¹	25	¹ 1,346,804
Maintenance and repair.....	51	480,922
		<u>255,895,662</u>
FISCAL YEAR 1964		
Method of placement:		
Advertised.....	53	157,040,310
Negotiated.....	38	2,199,302
		<u>159,239,612</u>
Compensation arrangement:		
Fixed price.....	48	137,422,058
Cost plus fixed fee.....	7	1,817,554
Cost.....		<u>159,239,612</u>
Types of products and services:		
New ship construction.....	5	155,999,087
Ship conversion.....	10	1,927,283
Research and development.....	25	¹ 992,588
Supplies, services, and material ¹	51	320,654
Maintenance and repair.....		<u>159,239,612</u>
FISCAL YEAR 1965		
Method of placement:		
Advertised.....	43	187,450,811
Negotiated.....	36	2,073,546
		<u>189,524,357</u>
Compensation arrangement:		
Fixed price.....	74	188,699,185
Cost plus fixed fee.....	5	825,172
Cost.....		<u>189,524,357</u>

 CONTRACTS AWARDED BY MARITIME SUBSIDY BOARD/
 MARITIME ADMINISTRATION—Continued

	Number	Amount
FISCAL YEAR 1965—Continued		
Types of products and services:		
New ship construction.....	7	\$186,547,377
Ship conversion.....	7	1,729,172
Research and development.....	23	¹ 946,344
Supplies, services, and material ¹	42	301,464
Maintenance and repair.....		<u>189,524,357</u>
FISCAL YEAR 1966		
Method of placement:		
Advertised.....	189	296,831,924
Negotiated.....	504	22,212,065
		<u>319,043,989</u>
Compensation arrangement:		
Fixed price.....	692	319,022,974
Cost plus fixed fee.....	1	21,015
Cost.....		<u>319,043,989</u>
Types of products and services:		
New ship construction.....	7	262,818,796
Ship conversion.....	2	7,779,000
Research and development.....	1	21,015
Supplies, services, and material ¹	31	¹ 1,248,082
Maintenance and repair.....	652	47,177,096
		<u>319,043,989</u>
FISCAL YEAR 1967		
Method of placement:		
Advertised.....	442	47,172,862
Negotiated.....	848	25,523,744
		<u>72,696,606</u>
Compensation arrangement:		
Fixed price.....	1,281	71,422,508
Cost plus fixed fee.....	6	1,164,098
Cost.....	3	110,000
		<u>72,696,606</u>
Types of products and services:		
New ship construction.....	2	16,540,450
Ship conversion.....	11	932,688
Research and development.....	43	¹ 3,202,376
Supplies, services, and material ¹	1,234	52,021,092
Maintenance and repair.....		<u>72,696,606</u>

¹ Due to the large number of purchase orders/contracts under \$10,000 placed by this agency each year for supplies, services, and materials, the analysis excludes approximately \$4,000,000 of such expenditures annually.

Appendix I

INFORMATION RELATING TO GENERAL SERVICES ADMINISTRATION CONTRACTS

GENERAL SERVICES ADMINISTRATION,
Washington, D.C., March 1, 1968.

Mr. LAURENCE N. WOODWORTH,
*Chief of Staff, Joint Committee on Internal Revenue Taxation, Congress
of the United States, Washington, D.C.*

DEAR MR. WOODWORTH: This is in further reply to your letter of February 13 requesting statistics and information for use in preparing a report on the Renegotiation Act of 1951.

The statistics requested are attached. Pursuant to discussion of February 19 between Mr. Holmead of this office and Mr. Bedell of your staff, wherein it was indicated that statistical information was not required on Public Buildings Service contracts, such data have not been included. Schedule I covers Federal Supply Service contracts for supplies and equipment and schedule II covers property management and disposal service contracts for servicing the various strategic and critical materials in the stockpile, together with contracts for upgrading basic materials to higher use form and for appraisals of real property. The only procurement by GSA of strategic and critical materials during the period covered was for jewel bearings from the Government-owned plant at Rolla, N. Dak. However, there were certain of these materials acquired through the Commodity Credit Corporation under its barter program and transferred to GSA.

The vast majority of the Federal Supply Service contracts are on a fixed-price basis and do not involve the problem of initial pricing and subsequent price redeterminations as in the case in cost-type contracts. We do encounter cases where there is little cost and production experience available for new items being introduced into the supply system; however, in most cases it is possible to extrapolate pricing data available with respect to similar supply items involving closely related types of cost and production. Variances in the products and services procured from year to year are experienced but the differences normally do not relate to commodity or service areas in which we have not had some prior experience. The footnotes shown on schedule II are self-explanatory regarding PMDS contracts.

Due to the nature of our programs and operations, the Renegotiation Act has limited application to contracts placed by this agency. The basic statutory exemptions in the act, particularly the one covering standard commercial articles and standard commercial services, are applicable to a wide range of our procurement activities. In addition, the Renegotiation Board has determined that major areas of GSA contracting do not have a direct and immediate connection with the national defense and, therefore, are exempt from re-

negotiation (see par. 5-53.804.1 of the attached copy of General Services Administration Procurement Regulations, Subpart 5-53.8).

With respect to the proposed amendments to the Renegotiation Act of 1951, GSA has no objection to the enactment of the Board's draft bill which was submitted to the Speaker of the House by letter dated February 23, 1968, from Mr. Lawrence E. Hartwig, Chairman of the Renegotiation Board.

If we can assist you further, please let us know.

Sincerely yours,

LAWSON B. KNOTT, Jr.,
Administrator.

PART 5-53 CONTRACT ADMINISTRATION

SUBPART 5-53.8 RENEGOTIATION

§ 5-53.801 General.

(a) The Renegotiation Act of 1951, as amended (50 U.S.C. App. 1211-1224), provides for recovery by the Government of contractors' excessive profits under certain contracts. GSA contracts are subject to renegotiation under the terms of the Renegotiation Act of 1951 unless exempted by the statute or by authorization of the Renegotiation Board.

(b) The Renegotiation Board, in its Regulations under the Renegotiation Act of 1951 (32 CFR Ch. XIV), prescribes definitions, sets forth mandatory and permissive exemptions, implements the statute with substantive rules, and provides procedures in connection with contracts subject to renegotiation.

§ 5-53.802 Contract clause.

(a) Contracts which are determined to be subject to the Renegotiation Act of 1951 shall contain the following clause:

RENEGOTIATION

The contract is subject to the Renegotiation Act of 1951, as amended, and shall be deemed to contain the provisions required by section 104 thereof. The extent of renegotiation will be determined in accordance with regulations under the Act. The Contractor agrees to include this Renegotiation clause (including this sentence) in each subcontract made to perform any part of the work or to furnish any materials required for this contract.

(b) When this clause is to be included in preprinted supplemental provisions, the clause set forth in (a), above, may be preceded by a preamble setting forth the basic exemptions applicable to the contracting programs for which the supplemental provisions form is generally used; for example:

The following Renegotiation clause shall apply unless the contract calls for delivery to a GSA supply depot or a Government agency not included in the Renegotiation Act of 1951.

§ 5-53.803 Exemptions by statute.

The Renegotiation Act of 1951 exempts the following:

(a) Any contract with any Territory, possession, or State, or any agency or political subdivision thereof, or with any foreign government or any agency thereof. (See Renegotiation Board Regulations 32 CFR 1453.1.)

(b) Any contract or subcontract for an agricultural commodity in its raw or natural state, or if the commodity is not customarily sold or has not an established market in its raw or natural state, in the first form or state, beyond the raw or natural state, in which it is customarily sold or in which it has an established market. The term "agricultural commodity" includes but is not limited to (see 32 CFR 1453.2):

(1) Commodities resulting from the cultivation of the soil, such as grains of all kinds, fruits, nuts, vegetables, hay, straw, cotton, tobacco, sugarcane, and sugar beets.

(2) Natural resins, saps, and gums of trees.

(3) Animals, such as cattle, hogs, poultry, and sheep, fish and other marine life, and the produce of live animals, such as wool, eggs, milk, and cream.

(c) Any contract or subcontract for the product of a mine, oil, or gas well, or other mineral or natural deposit, or timber, which has not been processed, refined, or treated beyond the first form or state suitable for industrial use. (See 32 CFR 1453.2(b).)

(d) Any contract or subcontract with a common carrier for transportation, or with a public utility for gas, electric energy, water, communications, or transportation, when made in either case at rates not in excess of published rates or charges filed with, fixed, approved, or regulated by a public regulatory body, State, Federal, or local, or at rates not in excess of unregulated rates of such a public utility which are substantially as favorable to users and consumers as are regulated rates. In the case of the furnishing or sale of transportation by common carrier by water, this paragraph shall apply only to such furnishing or sale which is subject to the jurisdiction of the Interstate Commerce Commission under Part III of the Interstate Commerce Act or subject to the jurisdiction of the Federal Maritime Board under the Intercoastal Shipping Act, 1933, and to such furnishing or sale in any case in which the Renegotiation Board finds that the regulatory aspects of rates for such furnishing or sale, or the type and nature of the contract for such furnishing or sale, are such as to indicate, in the opinion of the Renegotiation Board, that excessive profits are improbable. (See 32 CFR 1453.3.)

(e) Any contract or subcontract with an organization exempt from taxation under section 501(c)(3) of the Internal Revenue Code of 1954, but only if the income from such contract or subcontract is not includible under section 512 of such Code in computing the unrelated business taxable income of such organization. (See 32 CFR 1453.4.)

(f) Any contract which the Renegotiation Board determines does not have a direct and immediate connection with the national defense. In designating those classes and types of contracts which shall be exempt and in exempting any individual contract under this paragraph, the Board considered as not having a direct or immediate connection with national defense any contract for the furnishing of materials

or services to be used by the United States, a Department or agency thereof, in the manufacture and sale of synthetic rubbers to a private person or to private persons which are to be used for nondefense purposes. (See 32 CFR 1453.5.)

(g) Any subcontract directly or indirectly under a contract or subcontract already exempt in accordance with paragraph (b), (c), (d), (f), or (h) of this § 5-53.803. (See 32 CFR 1453.6.)

(h) Any contract, awarded as a result of competitive bidding, for the construction of any building, structure, improvement, or facility other than a contract for the construction of housing financed with a mortgage or mortgages insured under the provisions of Title VIII of the National Housing Act, as now or hereafter amended. (See 32 CFR 1453.7.)

(i) Any contract or subcontract which the Renegotiation Board exempts, as provided in § 5-53.805.

(j) Contracts and subcontracts for standard commercial articles and standard commercial services (and "like" articles and services) exempt from renegotiation in accordance with section 106(e) of the Renegotiation Act of 1951. The exemption on standard commercial articles only is self-executing; the other require application to the Renegotiation Board.

§ 5-53.804 National defense considerations.

§ 5-53.804-1 Determinations by the Renegotiation Board.

Subject to § 1453.5(c) of the Renegotiation Board's Regulations, the Renegotiation Board has determined that the following contracts do not have a direct and immediate connection with the national defense and, therefore, are exempt from renegotiation:

(a) All contracts of the Public Buildings Service and the National Archives and Records Service.

(b) All stores stock contracts for delivery to GSA supply depots.

(c) All Federal Supply Schedule contracts and consolidated direct delivery contracts with respect to deliveries made to Government agencies other than the Department of Defense (including the military departments), Atomic Energy Commission, and National Aeronautics and Space Administration.

(d) Contracts for maintenance and repair of buildings and structures.

(e) Contracts to the extent they obligate funds of, or are reimbursed by, another Department named in section 103 of the Renegotiation Act of 1951 as exercising functions having a direct and immediate connection with the national defense, if the contracts would be exempt if made by such other Department. Contractors should be informed that funds of other Departments are being used. (See 32 CFR 1453.5(b)(2).) The Departments named in section 103 are the Department of Defense, the Department of the Army, the Department of the Navy, the Department of the Air Force, the Maritime Administration, the Federal Maritime Board, the General Services Administration, the National Aeronautics and Space Administration, and the Atomic Energy Commission. (See 32 CFR 1451.14(b).)

(f) Contracts to the extent they obligate funds of another agency of the Government, other than a Department named in or designated in section 103 of the Renegotiation Act of 1951, or to the extent that GSA is to be reimbursed by such other Government agency or other person. Contractors should be informed that funds of other De-

partments are being used. Those contracts obligating funds for military assistance in connection with foreign aid programs are not exempt from renegotiation under this paragraph. (See 32 CFR 1453.5(b)(3)(ii).)

(g) Contracts for the purchase of materials for authorized resale except contracts for the purchase of materials to be issued or sold under the monetary clothing allowance system of the armed services. (See 32 CFR 1453.5(b)(4).)

(h) Contracts for the removal of waste materials. (See 32 CFR 1453.5(b)(5).)

(i) Contracts for laundry, cleaning, and pressing services. (See 32 CFR 1453.5(b)(6).)

§ 5-53.804-2 Determinations by GSA.

(a) Notwithstanding the determination set forth in § 5-53.804-1, individual contracts will be subject to renegotiation when the Head of the appropriate Service or Staff Office, or any of his designees, determines that such individual contract does have a direct and immediate connection with the national defense. This determination shall be set forth in the contract as follows:

For the purpose of the Renegotiation Act of 1951, as amended, it has been determined that this contract has a direct and immediate connection with the national defense. (See 32 CFR 1453.5(c).)

(b) In considering whether a specific contract does have a direct and immediate connection with the national defense, the Renegotiation Board requested that such determination be made in any case in which:

(1) The language of the appropriation act making funds available, enabling legislation, or the legislative history, is such that it is evident that the project was presented to, and approved by, the Congress because of its importance to the national defense.

(2) Award of the contract cannot be made without a certification, determination, or comparable prior action that the procurement is essential or necessary in the interest of the national defense. Such certification, determination, or comparable prior action would normally be made by the General Services Administration, but could be made by any agency of the Government which is competent to act in such manner.

(3) The contract is to be made under a War Powers Act—such as Public Law 85-804 (50 U.S.C. 1431-1435).

(4) Loans or advances are to be made to the contractor under the Defense Production Act of 1950 in order to facilitate performance of the contract.

(5) For other reasons, it is believed that the contract has a direct and immediate connection with the national defense.

§ 5-53.804-3 Individual prime contracts.

Individual prime contracts may be determined not to have a direct and immediate connection with the national defense by the Renegotiation Board on application of the prime contractor through GSA.

§ 5-53.805 Exemptions by the Renegotiation Board.

§ 5-53.805-1 Exempted classes of contracts.

In the exercise of its discretion as authorized by the Renegotiation Act of 1951, the Renegotiation Board has exempted the following classes of contracts from renegotiation:

(a) All prime contracts and subcontracts wholly performed outside the United States by any person who is not engaged in a trade or business in the United States and is (1) an individual who is not a national of the United States; (2) a partnership or joint venture in which individuals who are not nationals of the United States or corporations which are not domestic corporations are entitled to more than 50 percent of the profits; or (3) a corporation (other than a domestic corporation) more than 50 percent of the voting stock of which is owned directly or indirectly by persons described in subdivisions (1) and (2) of this paragraph. (See 32 CFR 1455.2(c), (c-1).)

For the purposes of this paragraph, the term "United States", when used in a geographical sense, includes the Territories and possessions of the United States, the Commonwealth of Puerto Rico, and the Canal Zone; and the term "domestic corporation" means a corporation organized under the laws of the United States or of any State, any Territory or possession of the United States, the District of Columbia, the Commonwealth of Puerto Rico, or the Canal Zone. (See 32 CFR 1455.2(c), (c-1).)

(b) Individual prime contracts or subcontracts, or the prime contracts or subcontracts related to a particular authorized procurement program, when such prime contracts or subcontracts are to be performed outside the territorial limits of the continental United States or in Alaska, and when it is established to the satisfaction of the Board that (1) the prime contracts or subcontracts involved in the request are to be placed with foreign nationals or foreign corporations whom it is not practicable to subject to renegotiation; (2) the provisions of the prime contracts or subcontracts are otherwise sufficient to prevent excessive profits; (3) the program is of direct and immediate concern to the defense of the United States and refusal to grant the exemption would jeopardize the success of the program; or (4) the contract or group of contracts should be exempted for any combination of the foregoing reasons or for any other reason. (See 32 CFR 1455.2(d).)

(c) Contracts or subcontracts under which, in the opinion of the Board, the profits can be determined with reasonable certainty when the contract price is established. On this basis, the Board has exempted the following:

(1) All prime contracts with natural persons (not partnerships, joint ventures, or corporations) which call for performance of personal or professional services by the individual contractor in person under the supervision of the Government, and which are paid for on a time basis. (See 32 CFR 1455.3(b)(1).)

(2) Prime contracts for the sale or rental of any interest in existing real estate. (See 32 CFR 1455.3(b)(2).)

(3) Prime contracts and subcontracts for the sale or exchange of tangible property used in the trade or business of the vendor

with respect to which depreciation is allowable under section 167 of the Internal Revenue Code of 1954. (This exemption extends only to contracts under which the price is a fixed or determinable amount at the time the contract is entered into, and does not apply to any contract under which the price, at the time the contract is entered into, is contingent upon a subsequent event or is thereafter to be determined by reference to a variable element.) (See 32 CFR 1455.3(b)(3).)

(4) Prime contracts and subcontracts for perishable subsistence supplies. (See 32 CFR 1455.3(b)(4).)

(5) Prime contracts where the aggregate amount does not exceed \$1,000 and the period of performance is not in excess of 30 days. (See 32 CFR 1455.3(b)(5).)

(6) Subcontracts for architectural, design, or engineering services as provided in the Renegotiation Board's Regulations §1455.3(b)(6).

(7) Contracts entered into with a non-profit-making agency for the blind pursuant to the program for the purchase of blind-made products. (See 32 CFR 1455.3(b)(7).)

§ 5-53.805-2 Contracts exempt subject to prescribed conditions.

The following contracts or subcontracts may be exempted on an individual contract basis on application to the Renegotiation Board by GSA:

(a) Contracts or subcontracts where the profits thereunder can be determined with reasonable certainty when the contract price is established. (See 32 CFR 1455.3(c).)

(b) Contracts or subcontracts where the contract provisions are otherwise adequate to prevent excessive profits. (See 32 CFR 1455.4(c).)

(c) Contracts or subcontracts the renegotiation of which would jeopardize secrecy required in the public interest. (See 32 CFR 1455.5(b).)

§ 5-53.805-3 Subcontracts exempted by the Renegotiation Board.

(a) Stock item exemption. Amounts received or accrued prior to January 1, 1964 on subcontracts and groups of subcontracts subject to the Act for materials (including maintenance, repair, and operating supplies) customarily purchased for stock in the normal course of the purchaser's business, except when such materials are specially purchased for use in performing one or more prime contracts or higher tier subcontracts subject to the Act. (See 32 CFR 1455.6.)

(b) Subcontracts related to exempt prime contracts and subcontracts except those performed outside the United States (see § 5-53.805-1(a)) and other subcontracts, when the Board, in exempting prime contracts or subcontracts, determined that the exemption will not extend to some or all of the subcontracts related to such prime contracts or subcontracts. (See 32 CFR 1455.7.)

SCHEDULE I.—FEDERAL SUPPLY SERVICE CONTRACTS FOR SUPPLIES AND EQUIPMENT FOR FISCAL YEARS 1961 THROUGH 1967

Fiscal Year	Number of term contracts		Dollar value of term contracts		Number of definite quantity		Dollar value of definite quantity		Summary of number of term and definite quantity		Summary of dollar value for term and definite quantity	
	Advertised	Negotiated	Advertised	Negotiated	Advertised	Negotiated	Advertised	Negotiated	Advertised	Negotiated	Advertised	Negotiated
1961	6,425	3,159	207,745,433	555,849,669	3,933	1,882	102,262,908	22,022,883	10,358	5,041	310,008,341	577,872,552
1962	6,280	3,564	239,136,069	611,113,842	4,314	2,320	138,379,603	40,299,454	10,594	5,884	377,515,672	651,413,296
1963	6,474	3,984	295,884,454	698,417,633	4,416	2,837	131,965,595	46,510,263	10,890	6,821	427,850,049	744,927,896
1964	6,642	4,304	301,966,279	881,811,915	6,578	3,285	143,925,590	54,329,938	13,220	7,589	445,891,869	936,141,853
1965	8,074	7,200	491,680,159	730,028,107	6,037	3,874	146,388,328	60,099,367	14,111	11,074	638,068,487	790,127,574
1966	8,590	5,883	455,970,483	911,851,815	4,585	4,807	137,850,468	103,267,047	13,175	10,690	593,830,951	1,015,118,862
1967	8,307	6,875	476,388,265	1,085,957,198	3,051	4,192	160,401,788	137,652,944	11,358	11,067	636,790,053	1,223,610,142
CONTRACTS NEGOTIATED WITH SINGLE SOURCE INCLUDED IN ABOVE ³												
1967	15		11,796,728		399		17,678,972		414		29,475,700	

¹ Over 90 percent of this total consists of small business set-asides and multiple-award Federal supply schedule contracts (term contracts under which using agencies select the lowest priced items meeting their particular needs and order direct from contractor).

² This includes small business and surplus labor area set-asides, emergency purchases, and other purchases which are exempt from formal advertising.

³ Information on contracts which were negotiated with a single source as contrasted to those contracts negotiated with 2 or more bidders is not available as a separate record. A case-by-case review of

negotiated contracts made by the Central Office of the Federal Supply Service for fiscal year 1967 was performed. The contracts negotiated with a single source are indicated above. Such contracts include automotive vehicles, trucks and equipment for use in remote foreign locations where standardization is desired for spare parts and maintenance purposes; proprietary items of equipment and supplies not available from other sources; security cabinets and locks where limited number of qualified manufacturers have been approved; certain business machines and other items of equipment which are in excess of the maximum order limitations of the Federal Supply Schedules.

Schedule II

SUMMARY OF PMDS PROCUREMENTS

Fiscal year and offices	Firm price contracts				Cost-type contracts			
	Advertised		Negotiated		Advertised		Negotiated	
	Number of contracts	Dollar value	Number of contracts	Dollar value	Number of contracts	Dollar value	Number of contracts	Dollar value
1961								
Central office.....	15	300,075	80	1,002,671	-----	-----	2	800,000
Regional offices.....	55	1,661,852	300	1,836,787	-----	-----	-----	-----
Total.....	70	1,961,927	380	2,839,458	-----	-----	2	800,000
1962								
Central office.....	7	193,171	94	1,506,831	-----	-----	-----	-----
Regional offices.....	86	1,282,528	527	2,143,034	-----	-----	-----	-----
Total.....	93	1,475,699	621	3,649,865	-----	-----	-----	-----
1963								
Central office.....	11	230,230	75	2,893,747	-----	-----	1	300,000
Regional offices.....	46	1,017,457	643	2,250,779	-----	-----	-----	-----
Total.....	57	1,247,687	718	5,144,526	-----	-----	-----	-----
1964								
Central office.....	21	482,432	85	1,935,499	-----	-----	2	700,000
Regional offices.....	60	916,171	1,024	1,422,200	-----	-----	-----	-----
Total.....	81	1,398,603	1,109	3,357,699	-----	-----	2	700,000
1965								
Central office.....	17	1,794,731	57	1,924,857	-----	-----	-----	-----
Regional offices.....	91	934,570	881	1,266,980	-----	-----	-----	-----
Total.....	108	2,729,301	938	3,191,837	-----	-----	-----	-----
1966								
Central office.....	19	2,153,082	28	197,695	-----	-----	6	1,281,689
Regional offices.....	134	1,229,108	780	1,738,563	-----	-----	-----	-----
Total.....	153	3,382,190	808	1,936,258	-----	-----	6	1,281,689
1967								
Central office.....	12	775,428	38	3,133,576	-----	-----	5	101,759
Regional offices.....	159	1,746,087	550	1,017,891	-----	-----	-----	-----
Total.....	171	2,521,515	588	4,151,467	-----	-----	5	101,759

Note: The firm price contracts are recurring fixed-price type for services and supplies required in the receipt, and/or removal, storage, maintenance, protection, and quality control of the various stockpile materials. Also included in this category are contracts for upgrading basic stockpile materials to higher use form and contracts for appraisal of real property. Prior experience in these types of contracting enables us to determine proper charges. The cost-type contracts include economic studies of certain stockpile materials and could be considered labor-hour type contracts. These contracts do not lend themselves to standardization for cost purposes as the scope and complexities of each commodity study will vary depending on the depth of investigation required. A contract with the Bulova Watch Co., which was entered into in June 1958, for operating the Government-owned plant at Rolla, N. Dak., is also included in the cost-type category. This contract is considered as a cost-plus-fixed-fee type. The contract has been extended from year to year and the figures include only the amended portion applicable to each fiscal year.

Approximately 85 percent of the dollar value of contracts negotiated by PMDS for fiscal years 1961 through 1967 were as the result of competitive negotiations (2 or more bids).

The balance of negotiated contracts for which competition could not be obtained were in instances where (1) a particular item or service was required to fit a particular need for which there was only one source, (2) there was urgent need for the item or service, and (3) competition was not available for services needed in remote areas.

SCHEDULE III.—FEDERAL SUPPLY SERVICE CONTRACTS FOR SUPPLIES AND EQUIPMENT FOR FISCAL YEARS 1961
THROUGH 1967, MULTIPLE AWARD SCHEDULES

Fiscal year	Number of multiple award contracts negotiated	Dollar value of multiple award contracts negotiated
1961	3, 023	551, 285, 541
1962	3, 199	595, 982, 634
1963	3, 250	668, 592, 960
1964	3, 511	839, 411, 910
1965	3, 677	665, 941, 284
1966	3, 664	820, 014, 309
1967	3, 406	947, 584, 227

Note: Multiple-award Federal Supply Schedule contracts are those contracts made for items where it is not practicable to have formal standards or specifications permitting formal advertised procurement. These are indefinite quantity term contracts negotiated with more than 1 supplier for comparable items at either the same or different prices for delivery to the same geographical area and are designed to provide effective utilization of industry production and distribution facilities. Examples of the type items procured by this method of contracting are office machines, including typewriters, adding machines, computing machines, and dictating machines; laboratory equipment; data processing equipment; etc. Using agencies submit their purchase orders direct to the supplier and delivery is made direct to the using agency or point of use. Under Federal Procurement Management Regulations, each ordering agency placing an order under a schedule contract is required to purchase the lowest delivered priced item that will satisfy the agency's minimum needs unless purchase of a higher priced item can be fully justified, subject to review by the General Accounting Office.

Appendix J

INFORMATION RELATING TO FEDERAL AVIATION ADMINISTRATION CONTRACTS

DEPARTMENT OF TRANSPORTATION,
FEDERAL AVIATION ADMINISTRATION,
OFFICE OF THE ADMINISTRATOR,
Washington, D.C., March 1, 1968.

HON. RUSSELL B. LONG,
*Chairman, Joint Committee on Internal Revenue Taxation,
U.S. Senate, Washington, D.C.*

DEAR MR. CHAIRMAN: Reference is made to Mr. Laurence N. Woodworth's letter dated February 13, 1968, requesting contract information between the years 1961 and 1967.

A portion of the information requested is readily available and is as follows:

Enclosure 1 lists the method of procurement for the fiscal years 1961 through 1967.

Enclosure 2 lists for the fiscal years 1964 through 1967 the variety of cost and fixed-price-type contracts. This information has been accumulated only since 1964.

Enclosure 3 is a list of the contracts for fiscal years 1965 through 1967 that have been reported to the Renegotiation Board. This was not requested in the referenced letter but is being furnished as a result of a telephone call with a member of Mr. Woodworth's staff. [Enclosure 3 is not reproduced.]

The Federal Aviation Administration does not record the accumulated overrun or underrun dollars except on an individual contract basis.

The materials/services procured by this agency cover a wide range of cost type study, design, or design and initial production of hardware. The fixed price type contracts cover production or performance type specifications, follow on supply type of procurement, and the bulk of our construction contracting. To illustrate this point, our current active contracts list contains 479 contracts that are not completed for a variety of reasons. A breakdown of the 479 contracts is as follows: Fixed price, 256 (53 percent); cost type, 147 (30 percent); issued to other government agencies, 48 (10 percent); labor hour and time and materiel [sic], 28 (7 percent). Many of our contracts are entered into for which there is no previous cost or production experience. We find that there is little change in the variety of supplies and services that are procured from year to year.

At this time the FAA has no particular comment to make as to the merits of any proposed extension of the Renegotiation Act. It is expected that the Office of the Secretary will in the future be making one comment on the effects of such legislation on all elements of the Department of Transportation.

The data being furnished as enclosures 1 through 3 was discussed in a telephone conversation between Mr. Erwin Ames of our Logistics Service and Mr. Dennis P. Bedell, a member of Mr. Woodworth's staff. Mr. Bedell suggested that the data be submitted and if additional information was required, it would be requested.

Sincerely,

D. D. THOMAS, *Acting Administrator.*

SUMMARY OF FAA PROCUREMENT ACTIVITY BY METHOD—FORMAL ADVERTISING AND NEGOTIATION

Fiscal year	Actions ¹					Dollar value (millions) ²				
	Advertised	Percent advertised	Negotiated	Percent negotiated	Total	Advertised	Percent advertised	Negotiated	Percent negotiated	Total
1961.....	6,275	19	26,780	81	33,055	45.2	55	37.6	45	82.8
1962.....	8,941	22	32,411	78	41,352	48.1	40	72.4	60	120.5
1963.....	(³)	(³)	(³)	(³)	(³)	27.1	18	119.4	82	146.5
1964.....	2,213	60	1,485	40	3,698	19.9	12	145.1	88	165.0
1965.....	742	31	1,676	69	2,418	18.7	18	83.1	82	101.8
1966.....	717	31	1,569	69	2,286	18.6	11	189.4	89	208.0
1967.....	1,000	41	1,430	59	2,430	26.6	13	190.4	87	217.1

¹ For fiscal year 1961 and fiscal year 1962 these data include all procurement awards over \$100 from all sources for fiscal year 1964 through fiscal year 1967 these data include all procurement awards over \$2,500 to U.S. business firms only, including new contracts, modifications, and other follow-on actions involving monetary changes to the contract.

² These data include all procurement awards over \$100 to U.S. business firms and through established sources; i.e., under other agency's contracts.

³ No data available.

SUMMARY OF FEDERAL AVIATION ADMINISTRATION CONTRACT ACTIONS BY CONTRACT TYPE

[Dollar amounts in millions]

Contract type	Fiscal year 1964	Percent	Fiscal year 1965	Percent	Fiscal year 1966	Percent	Fiscal year 1967	Percent
FIXED PRICE								
Firm fixed price.....	\$103.14	82.65	\$64.24	93.72	\$46.09	93.07	\$102.37	96.70
Fixed price incentive.....	18.89	15.14	4.22	6.11	2.77	5.60	2.65	2.51
Fixed price redetermination.....	1.99	1.61	.05	.07	.61	1.23	.78	.74
Fixed price escalation.....	.76	.60	.07	.10	.05	.10	.06	.05
Subtotal.....	124.78	100.0	68.58	100.00	49.52	100.00	105.86	100.00
COST								
Cost contract.....	.35	2.97	.53	1.47	.20	.12	2.74	20.51
Cost-plus-incentive.....	2.83	23.98	1.11	3.08	.39	.24	.75	5.61
Cost-plus-fixed-fee.....	7.48	63.39	7.79	21.58	7.46	4.65	5.30	39.67
Cost sharing.....	.17	1.44	25.81	71.50	151.67	94.48	3.85	28.84
Labor hours.....	.49	4.15	.16	.44	.13	.08	.10	.74
Time and materials.....	.48	4.07	.70	1.93	.69	.43	.62	4.63
Subtotal.....	11.80	100.00	36.10	100.00	160.54	100.00	13.36	100.00
Grand total.....	136.58		104.68		210.06		119.22	

Appendix K

RENEGOTIATION ACT OF 1951 AS AMENDED TO DATE

[Public Law 9, 82d Cong., approved March 23, 1951, as amended by Public Law 764, 83d Cong., approved September 1, 1954; Public Law 216, 84th Cong., approved August 3, 1955; Public Law 870, 84th Cong., approved August 1, 1956; Public Law 85-930, 85th Cong., approved September 6, 1958; Public Law 86-89, 86th Cong., approved July 13, 1959; Public Law 87-520, 87th Cong., approved July 3, 1962; Public Law 88-339, 88th Cong., approved June 30, 1964; and Public Law 89-480, 89th Cong., approved June 30, 1966]

To provide for the renegotiation of contracts, and for other purposes.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled, That this Act may be cited as the "Renegotiation Act of 1951".

TITLE I—RENEGOTIATION OF CONTRACTS

SEC. 101. DECLARATION OF POLICY.

It is hereby recognized and declared that the Congress has made available for the execution of the national defense program extensive funds, by appropriation and otherwise, for the procurement of property, processes, and services, and the construction of facilities necessary for the national defense; that sound execution of the national defense program requires the elimination of excessive profits from contracts made with the United States, and from related subcontracts, in the course of said program; and that the considered policy of the Congress, in the interests of the national defense and the general welfare of the Nation, requires that such excessive profits be eliminated as provided in this title.

SEC. 102. CONTRACTS SUBJECT TO RENEGOTIATION.

(a) IN GENERAL.—The provisions of this title shall be applicable (1) to all contracts with the Departments specifically named in section 103(a), and related subcontracts, to the extent of the amounts received or accrued by a contractor or subcontractor on or after the first day of January 1951, whether such contracts or subcontracts were made on, before, or after such first day, and (2) to all contracts with the Departments designated by the President under section 103(a), and related subcontracts, to the extent of the amounts received or accrued by a contractor or subcontractor on or after the first day of the first month beginning after the date of such designation, whether such contracts or subcontracts were made on, before, or after such first day.¹

(b) PERFORMANCE PRIOR TO JULY 1, 1950.—Notwithstanding the provisions of subsection (a), the provisions of this title shall not apply to contracts with the Departments, or related subcontracts, to the extent of the amounts received or accrued by a contractor or sub-

¹ Pub. Law 870, 84th Cong., approved August 1, 1956, struck out at this point "; but provisions of this title shall not be applicable to receipts or accruals attributable to performance, under contracts, or subcontracts, after December 31, 1956". The last date was changed from "1953" to "1954" by Pub. Law 76483d Cong., approved September 1, 1954, and changed to "1956" by Pub. Law 216, 84th Cong., approved August 3, 1955.

contractor on or after the 1st day of January 1951, which are attributable to performance, under such contracts or subcontracts, prior to July 1, 1950. This subsection shall have no application in the case of contracts, or related subcontracts, which, but for subsection (c), would be subject to the Renegotiation Act of 1948.

(c) *TERMINATION.*—

(1) *IN GENERAL.*—*The provisions of this title shall apply only with respect to receipts and accruals, under contracts with the Departments and related subcontracts, which are determined under regulations prescribed by the Board to be reasonably attributable to performance prior to the close of the termination date. Notwithstanding the method of accounting employed by the contractor or subcontractor in keeping his records, receipts or accruals determined to be so attributable, even if received or accrued after the termination date, shall be considered as having been received or accrued not later than the termination date. For the purposes of this title, the term "termination date" means June 30, 1968.*

(2) *TERMINATION OF STATUS AS DEPARTMENT.*—*When the status of any agency of the Government as a Department within the meaning of section 103 (a) is terminated, the provisions of this title shall apply only with respect to receipts and accruals, under contracts with such agency and related subcontracts, which are determined under regulations prescribed by the Board to be reasonably attributable to performance prior to the close of the status termination date. Notwithstanding the method of accounting employed by the contractor or subcontractor in keeping his records, receipts or accruals determined to be so attributable, even if received or accrued after the status termination date, shall be considered as having been received or accrued not later than the status termination date. For the purposes of this paragraph, the term "status termination date" means with respect to any agency, the date on which the status of such agency as a Department within the meaning of section 103 (a) is terminated.²*

(d) *RENEGOTIATION ACT OF 1948.*—*The Renegotiation Act of 1948 shall not be applicable to any contract or subcontract to the extent of the amounts received or accrued by a contractor or subcontractor on or after the 1st day of January 1951, whether such contract or subcontract was made on, before, or after such first day. In the case of a fiscal year beginning in 1950 and ending in 1951, if a contractor or subcontractor has receipts or accruals prior to January 1, 1951, from contracts or subcontracts subject to the Renegotiation Act of 1948, and also has receipts or accruals after December 31, 1950, to which the provisions of this title are applicable, the provisions of this title shall, notwithstanding subsection (a), apply to such receipts and accruals prior to January 1, 1951, if the Board and such contractor or subcontractor agree to such application of this title; and in the case of such an agreement the provisions of the Renegotiation Act of 1948 shall not apply to any of the receipts or accruals for such fiscal year.*

² Subsection (c) of section 102 was added by Pub. Law 870, 84th Cong., approved August 1, 1956, which also relettered former subsections (c) and (d) as (d) and (e), respectively. The "termination date" in paragraph (1) of such subsection (c) was changed by Pub. Law 85-930, 85th Cong., approved September 6, 1958, from December 31, 1958 to June 30, 1959. By Pub. Law 86-89, 86th Cong., approved July 13, 1959. "June 30, 1959" was changed to "June 30, 1962". By Pub. Law 87-520, 87th Cong., approved July 3, 1962. "June 30, 1962" was changed to "June 30, 1964". By Pub. Law 88-339, 88th Cong., approved June 30, 1964. "June 30, 1964" was changed to "June 30, 1966". By Pub. Law 89-430, 89th Cong., approved June 30, 1966. "June 30, 1966" was changed to "June 30, 1968."

(e) **SUSPENSION OF CERTAIN PROFIT LIMITATIONS.**—Notwithstanding any agreement to the contrary, the profit-limitation provisions of the Act of March 27, 1934 (48 Stat. 503, 505), as amended and supplemented, and of section 505 (b) of the Merchant Marine Act, 1936, as amended and supplemented (46 U.S.C. 1155 (b)), shall not apply, in the case of such Act of March 27, 1934, to any contract or subcontract if any of the receipts or accruals therefrom are subject to this title or *would be subject to this title except for the provisions of section 106 (e)*, and, in the case of the Merchant Marine Act, 1936, to any contract or subcontract entered into after December 31, 1950, if any of the receipts or accruals therefrom are subject to this title or *would be subject to this title except for the provisions of section 106 (e)*.³

SEC. 103. DEFINITIONS.

For the purposes of this title—

(a) **DEPARTMENT.**—*The term "Department" means the Department of Defense, the Department of the Army, the Department of the Navy, the Department of the Air Force, the Maritime Administration, the Federal Maritime Board, the General Services Administration, the National Aeronautics and Space Administration, the Federal Aviation Agency, and the Atomic Energy Commission. Such term also includes any other agency of the Government exercising functions having a direct and immediate connection with the national defense which is designated by the President during a national emergency proclaimed by the President, or declared by the Congress, after the date of the enactment of the Renegotiation Amendments Act of 1956; but such designation shall cease to be in effect on the last day of the month during which such national emergency is terminated.*⁴

(b) **SECRETARY.**—*The term "Secretary" means the Secretary of Defense, the Secretary of the Army, the Secretary of the Navy, the Secretary of the Air Force, the Secretary of Commerce (with respect to the Maritime Administration), the Federal Maritime Board, the Administrator of General Services, the Administrator of the National Aeronautics and Space Administration, the Administrator of the Federal Aviation Agency, the Atomic Energy Commission, and the head of any other agency of the Government which the President shall designate as a Department pursuant to subsection (a) of this section.*⁵

³ Matter in italics in section 102 (e) was added by Pub. Law 216, 84th Cong., approved August 3, 1955, as amended by Pub. Law 870, 84th Cong., approved August 1, 1956, and applies only to the extent of amounts received or accrued after December 31, 1953. Pub. Law 870 changed "section 106 (a) (8)" to "section 106 (e)" with respect to fiscal years ending after June 30, 1956.

⁴ Section 103 (a) was amended by Pub. Law 870, 84th Cong., approved August 1, 1956, which struck out, effective December 31, 1956, the Department of Commerce, the Reconstruction Finance Corporation, the Canal Zone Government, the Panama Canal Company, the Housing and Home Finance Agency, and such other agencies of the Government as were designated by the President under the former subsection (a). Federal Civil Defense Administration, National Advisory Committee for Aeronautics, Tennessee Valley Authority, and U.S. Coast Guard were designated by Executive Order 10260, dated June 27, 1951; Defense Materials Procurement Agency, Bureau of Mines, and (United States) Geological Survey by Executive Order 10294, September 23, 1951; Bonneville Power Administration by Executive Order 10299, October 31, 1951; Bureau of Reclamation by Executive Order 10369, June 30, 1952; and Federal Facilities Corporation by Executive Order 10567, September 29, 1954. Section 103 (a) was further amended by Pub. Law 85-930, 85th Cong., approved September 6, 1958, which added the National Aeronautics and Space Administration and which made section 103 (a) applicable to contracts entered into by such Administration and to contracts transferred to such Administration from a Department under section 301 or 302 of the National Aeronautics and Space Act of 1958, and to related subcontracts; and by Pub. Law 88-339, 88th Cong., approved June 30, 1964, which added the Federal Aviation Agency and which made section 103 (a) applicable to contracts with such Agency, and related subcontracts, to the extent of the amounts received or accrued by a contractor or subcontractor after June 30, 1964.

⁵ Matter in italics in section 103 (b), except the references to the Administrator of the National Aeronautics and Space Administration and the Administration of the Federal Aviation Agency, was added by Pub. Law 870, 84th Cong., approved August 1, 1956, which also changed "the Chairman of the Atomic Energy Commission" to "the Atomic Energy Commission" and struck out the Board of Directors of the Reconstruction Finance Corporation, the Governor of the Canal Zone, the President of the Panama Canal Company, and the Housing and Home Finance Administrator, all effective on December 31, 1956. The Administrator of the National Aeronautics and Space Administration was added by Pub. Law 85-930, 85th Cong., approved September 6, 1958. The Administrator of the Federal Aviation Agency was added by Pub. Law 88-339, 88th Cong., approved June 30, 1964.

(c) BOARD.—The term “Board” means the Renegotiation Board created by section 107(a) of this Act.

(d) RENEGOTIATE AND RENEGOTIATION.—The terms “renegotiate” and “renegotiation” include a determination by agreement or order under this title of the amount of any excessive profits.

(e) EXCESSIVE PROFITS.—The term “excessive profits” means the portion of the profits derived from contracts with the Departments and subcontracts which is determined in accordance with this title to be excessive. In determining excessive profits favorable recognition must be given to the efficiency of the contractor or subcontractor, with particular regard to attainment of quantity and quality production, reduction of costs, and economy in the use of materials, facilities, and manpower; and in addition, there shall be taken into consideration the following factors:

(1) Reasonableness of costs and profits, with particular regard to volume of production, normal earnings, and comparison of war and peacetime products;

(2) The net worth, with particular regard to the amount and source of public and private capital employed;

(3) Extent of risk assumed, including the risk incident to reasonable pricing policies;

(4) Nature and extent of contribution to the defense effort, including inventive and developmental contribution and cooperation with the Government and other contractors in supplying technical assistance;

(5) Character of business, including source and nature of materials, complexity of manufacturing technique, character and extent of subcontracting, and rate of turn-over;

(6) Such other factors the consideration of which the public interest and fair and equitable dealing may require, which factors shall be published in the regulations of the Board from time to time as adopted.

(f) PROFITS DERIVED FROM CONTRACTS WITH THE DEPARTMENTS AND SUBCONTRACTS.—The term “profits derived from contracts with the Departments and subcontracts” means the excess of the amount received or accrued under such contracts and subcontracts over the costs paid or incurred with respect thereto and determined to be allocable thereto. All items estimated to be allowed as deductions and exclusions under chapter 1 of the Internal Revenue Code (excluding taxes measured by income) shall, to the extent allocable to such contracts and subcontracts, be allowed as items of cost, except that no amount shall be allowed as an item of cost by reason of the application of a carry-over or carry-back. Notwithstanding any other provision of this section, there shall be allowed as an item of cost in any fiscal year *ending before December 31, 1956*,⁶ subject to regulations of the Board, an amount equal to the excess, if any, of costs (computed without the application of this sentence) paid or incurred in the preceding fiscal year with respect to receipts or accruals subject to the provisions of this title over the amount of receipts or accruals subject to the provisions of this title which were received or accrued in such preceding fiscal year, but only to the extent that such excess did not

⁶ Matter in italics in section 103(f) was added by Pub. Law 870, 84th Cong., approved August 1, 1956.

result from gross inefficiency of the contractor or subcontractor. For the purposes of the preceding sentence, the term "preceding fiscal year" does not include any fiscal year ending prior to January 1, 1951. Costs shall be determined in accordance with the method of accounting regularly employed by the contractor or subcontractor in keeping his records, but, if no such method of accounting has been employed, or if the method so employed does not, in the opinion of the Board, or, upon redetermination, in the opinion of The Tax Court of the United States, properly reflect such costs, such costs shall be determined in accordance with such method as in the opinion of the Board, or, upon redetermination, in the opinion of The Tax Court of the United States, does properly reflect such costs. In determining the amount of excessive profits to be eliminated, proper adjustment shall be made on account of the taxes measured by income, other than Federal taxes, which are attributable to the portion of the profits which are not excessive.

(g) **SUBCONTRACT.**—The term "subcontract" means—

(1) any purchase order or agreement (including purchase orders or agreements antedating the related prime contract or higher tier subcontract) to perform all or any part of the work, or to make or furnish any materials, required for the performance of any other contract or subcontract, but such term does not include any purchase order or agreement to furnish office supplies;

(2) any contract or arrangement covering the right to use any patented or secret method, formula, or device for the performance of a contract or subcontract; and

(3) any contract or arrangement (other than a contract or arrangement between two contracting parties, one of whom is found by the Board to be a bona fide executive officer, partner, or full-time employee of the other contracting party) under which—

(A) any amount payable is contingent upon the procurement of a contract or contracts with a Department or of a subcontract or subcontracts; or

(B) any amount payable is determined with reference to the amount of a contract or contracts with a Department or of a subcontract or subcontracts; or

(C) any part of the services performed or to be performed consists of the soliciting, attempting to procure, or procuring a contract or contracts with a Department or a subcontract or subcontracts.

Nothing in this subsection shall be construed (i) to affect in any way the validity or construction of provisions in any contract with a Department or any subcontract, heretofore at any time or hereafter made, prohibiting the payment of contingent fees or commissions; or (ii) to restrict in any way the authority of the Board to determine the nature or amount of selling expense under subcontracts as defined in this subsection, as a proper element of the contract price or as a reimbursable item of cost, under a contract with a Department or a subcontract.

(h) **FISCAL YEAR.**—The term "fiscal year" means the taxable year of the contractor or subcontractor under chapter 1 of the Internal Revenue Code, except that where any readjustment of interests occurs

in a partnership as defined in section 3797 (a) (2) of such code, the fiscal year of the partnership or partnerships involved in such readjustment shall be determined in accordance with regulations prescribed by the Board.

(i) RECEIVED OR ACCRUED AND PAID OR INCURRED.—The terms “received or accrued” and “paid or incurred” shall be construed according to the method of accounting employed by the contractor or subcontractor in keeping his records, but if no such method of accounting has been employed, or if the method so employed does not, in the opinion of the Board, or, upon redetermination, in the opinion of The Tax Court of the United States, properly reflect his receipts or accruals or payments or obligations, such receipts or accruals or such payments or obligations shall be determined in accordance with such method as in the opinion of the Board, or, upon redetermination, in the opinion of The Tax Court of the United States, does properly reflect such receipts or accruals or such payments or obligations.

(j) PERSON.—The term “person” shall include an individual, firm, corporation, association, partnership, and any organized group of persons whether or not incorporated.

(k) MATERIALS.—The term “materials” shall include raw materials, articles, commodities, parts, assemblies, products, machinery, equipment, supplies, components, technical data, processes, and other personal property.

(l) AGENCY OF THE GOVERNMENT.—The term “agency of the Government” means any part of the executive branch of the Government or any independent establishment of the Government or part thereof, including any department (whether or not a Department as defined in subsection (a) of this section), any corporation wholly or partly owned by the United States which is an instrumentality of the United States, or any board, bureau, division, service, office, officer, employee, authority, administration, or other establishment of the Government which is not a part of the legislative or judicial branches.

(m) RENEGOTIATION LOSS CARRYFORWARDS.—

(1) ALLOWANCE.—*Notwithstanding any other provision of this section, the renegotiation loss deduction for any fiscal year ending on or after December 31, 1956, shall be allowed as an item of cost in such fiscal year, under regulations of the Board.*

(2) DEFINITIONS.—*For the purposes of this subsection—*

(A) *The term “renegotiation loss deduction” means—*

(i) *for any fiscal year ending on or after December 31, 1956, and before January 1, 1959, the sum of the renegotiation loss carryforwards to such fiscal year from the preceding two fiscal years; and*

(ii) *for any fiscal year ending after December 31, 1958, the sum of the renegotiation loss carryforwards to such fiscal year from the preceding five fiscal years (excluding any fiscal year ending before December 31, 1956).*

(B) *The term “renegotiation loss” means, for any fiscal year, the excess, if any, of costs (computed without the application of this subsection and the third sentence of subsection (f)) paid or incurred in such fiscal year with respect to receipts or accruals subject to the provisions of this title over the amount of receipts or accruals subject to the provisions of*

this title which were received or accrued in such fiscal year, but only to the extent that such excess did not result from gross inefficiency of the contractor or subcontractor.

(3) AMOUNT OF CARRYFORWARDS TO 1956, 1957, AND 1958.—For the purposes of paragraph (2)(A)(i), a renegotiation loss for any fiscal year (hereinafter in this paragraph referred to as the "loss year") shall be a renegotiation loss carryforward to the first fiscal year succeeding the loss year. Such renegotiation loss, after being reduced (but not below zero) by the profits derived from contracts with the Departments and subcontracts in the first fiscal year succeeding the loss year, shall be a renegotiation loss carryforward to the second fiscal year succeeding the loss year. For the purposes of the preceding sentence, the profits derived from contracts with the Departments and subcontracts in the first fiscal year succeeding the loss year shall be computed as follows:

(A) If such first fiscal year ends on or after December 31, 1956, such profits shall be computed by determining the amount of the renegotiation loss deduction for such first fiscal year without regard to the renegotiation loss for the loss year,

(B) If such first fiscal year ends before December 31, 1956, such profits shall be computed without regard to any renegotiation loss for the loss year or any fiscal year preceding the loss year.

(4) AMOUNT OF CARRYFORWARDS TO FISCAL YEARS ENDING AFTER 1958.—For the purposes of paragraph (2)(A)(ii), a renegotiation loss for any fiscal year (hereinafter in this paragraph referred to as the "loss year") ending on or after December 31, 1956, shall be a renegotiation loss carryforward to each of the five fiscal years following the loss year. The entire amount of such loss shall be carried to the first fiscal year succeeding the loss year. The portion of such loss which shall be carried to each of the other four fiscal years shall be the excess, if any, of the amount of such loss over the sum of the profits derived from contracts with the Departments and subcontracts in each of the prior fiscal years to which such loss may be carried. For the purposes of the preceding sentence, the profits derived from contracts with the Departments and subcontracts in any such prior fiscal year shall be computed by determining the amount of the renegotiation loss deduction without regard to the renegotiation loss for the loss year or for any fiscal year thereafter, and the profits so computed shall not be considered to be less than zero.⁷

SEC. 104. RENEGOTIATION CLAUSE IN CONTRACTS.

Subject to section 106(a) the Secretary of each Department specifically named in section 103(a) shall insert in each contract made by such Department thirty days or more after date of the enactment of this Act, and the Secretary of each Department designated by the President under section 103(a) shall insert in each contract made by such Department thirty days or more after the date of such designation, a provision under which the contractor agrees—

(1) to the elimination of excessive profits through renegotiation;

⁷ Section 103(m) was added by Pub. Law 870, 84th Cong., approved August 1, 1956, and was amended by Pub. Law 80-89, 86th Cong., approved July 13, 1959.

(2) that there may be withheld by the United States from amounts otherwise due the contractor, or that he will repay to the United States, if paid to him, any excessive profits;

(3) that he will insert in each subcontract described in section 103(g) a provision under which the subcontractor agrees—

(A) to the elimination of excessive profits through renegotiation;

(B) that there may be withheld by the contractor for the United States from amounts otherwise due to the subcontractor, or that the subcontractor will repay to the United States, if paid to him, any excessive profits;

(C) that the contractor shall be relieved of all liability to the subcontractor on account of any amount so withheld, or so repaid by the subcontractor to the United States;

(D) that he will insert in each subcontract described in section 103(g) provisions corresponding to those of subparagraphs (A), (B), and (C), and to those of this subparagraph;

(4) that there may be withheld by the United States from amounts otherwise due the contractor, or that he will repay to the United States, as the Secretary may direct, any amounts which under section 105(b)(1)(C) the contractor is directed to withhold from a subcontractor and which are actually unpaid at the time the contractor receives such direction.

The obligations assumed by the contractor of subcontractor under paragraph (1) or (3)(A), as the case may be, agreeing to the elimination of excessive profits through renegotiation shall be binding on him only if the contract or subcontract, as the case may be, is subject to this title. A provision inserted in a contract or subcontract, which recites in substance that the contract or subcontract shall be deemed to contain all the provisions required by this section shall be sufficient compliance with this section. Whether or not the provisions specified in this section are inserted in a contract with a Department or subcontract, to which this title is applicable, such contract or subcontract, as the case may be, shall be considered as having been made subject to this title in the same manner and to the same extent as if such provisions had been inserted.

SEC. 105. RENEGOTIATION PROCEEDINGS.

(a) PROCEEDINGS BEFORE THE BOARD.—Renegotiation proceedings shall be commenced by the mailing of notice, to that effect, in such form as may be prescribed by regulation, by registered mail *or by certified mail* to the contractor or subcontractor. The Board shall endeavor to make an agreement with the contractor or subcontractor with respect to the elimination of excessive profits received or accrued, and with respect to such other matters relating thereto as the Board deems advisable. Any such agreement, if made, may, with the consent of the contractor or subcontractor, also include provisions with respect to the elimination of excessive profits likely to be received or accrued. If the Board does not make an agreement with respect to the elimination of excessive profits received or accrued, it shall issue and enter an order determining the amount, if any, of such excessive profits, and forthwith give notice thereof by registered mail *or by certified mail* to the contractor or subcontractor. In the absence of

the filing of a petition with The Tax Court of the United States under the provisions of and within the time limit prescribed in section 108, such order shall be final and conclusive and shall not be subject to review or redetermination by any court or other agency. The Board shall exercise its powers with respect to the aggregate of the amounts received or accrued during the fiscal year (or such other period as may be fixed by mutual agreement) by a contractor or subcontractor under contracts with the Departments and subcontracts, and not separately with respect to amounts received or accrued under separate contracts with the Departments or subcontracts, except that the Board may exercise such powers separately with respect to amounts received or accrued by the contractor or subcontractor under any one or more separate contracts with the Departments or subcontracts at the request of the contractor or subcontractor. By agreement with any contractor or subcontractor, and pursuant to regulations promulgated by it, the Board may in its discretion conduct renegotiation on a consolidated basis in order properly to reflect excessive profits of two or more related contractors or subcontractors. Renegotiation shall be conducted on a consolidated basis with a parent and its subsidiary corporations which constitute an affiliated group under section 141(d) of the Internal Revenue Code if all of the corporations included in such affiliated group request renegotiation on such basis and consent to such regulations as the Board shall prescribe with respect to (1) the determination and elimination of excessive profits of such affiliated group, and (2) the determination of the amount of the excessive profits of such affiliated group allocable, for the purposes of section 3806 of the Internal Revenue Code, to each corporation included in such affiliated group. Whenever the Board makes a determination with respect to the amount of excessive profits, and such determination is made by order, it shall, at the request of the contractor or subcontractor, as the case may be, prepare and furnish such contractor or subcontractor with a statement of such determination, of the facts used as a basis therefor, and of its reasons for such determination. Such statement shall not be used in The Tax Court of the United States as proof of the facts or conclusions stated therein.^{7a}

(b) METHODS OF ELIMINATING EXCESSIVE PROFITS.—

(1) IN GENERAL.—Upon the making of an agreement, or the entry of an order, under subsection (a) of this section by the Board, or the entry of an order under section 108 by The Tax Court of the United States, determining excessive profits, the Board shall forthwith authorize and direct the Secretaries or any of them to eliminate such excessive profits—

(A) by reductions in the amounts otherwise payable to the contractor under contracts with the Departments, or by other revision of their terms;

(B) by withholding from amounts otherwise due to the contractor any amount of such excessive profits;

(C) by directing any person having a contract with any agency of the Government, or any subcontractor thereunder, to withhold for the account of the United States from any amounts otherwise due from such person or such subcontractor to a contractor, or subcontractor, having excessive

^{7a} Matter in italics in section 105(a) was added by Pub. Law 86-507, 86th Cong., approved June 11, 1960

profits to be eliminated, and every such person or subcontractor receiving such direction shall withhold and pay over to the United States the amounts so required to be withheld;

(D) by recovery from the contractor or subcontractor, or from any person or subcontractor directed under subparagraph (C) to withhold for the account of the United States, through payment, repayment, credit, or suit any amount of such excessive profits realized by the contractor or subcontractor or directed under subparagraph (C) to be withheld for the account of the United States; or

(E) by any combination of these methods, as is deemed desirable.

(2) **INTEREST.**—Interest at the rate of 4 per centum per annum shall accrue and be paid on the amount of such excessive profits from the thirtieth day after the date of the order of the Board or from the date fixed for repayment by the agreement with the contractor or subcontractor to the date of repayment, and on amounts required to be withheld by any person or subcontractor for the account of the United States pursuant to paragraph (1) (C), from the date payment is demanded by the Secretaries or any of them to the date of payment. When The Tax Court of the United States, under section 108, redetermines the amount of excessive profits received or accrued by a contractor or subcontractor, interest at the rate of 4 per centum per annum shall accrue and be paid by such contractor or subcontractor as follows:

(A) When the amount of excessive profits determined by the Tax Court is greater than the amount determined by the Board, interest shall accrue and be paid on the amount determined by the Board from the thirtieth day after the date of the order of the Board to the date of repayment and, in addition thereto, interest shall accrue and be paid on the additional amount determined by the Tax Court from the date of its order determining such excessive profits to the date of repayment.

(B) When the amount of excessive profits determined by the Tax Court is equal to the amount determined by the Board, interest shall accrue and be paid on such amount from the thirtieth day after the date of the order of the Board to the date of repayment.

(C) When the amount of excessive profits determined by the Tax Court is less than the amount determined by the Board, interest shall accrue and be paid on such lesser amount from the thirtieth day after the date of the order of the Board to the date of repayment, except that no interest shall accrue or be payable on such lesser amount if such lesser amount is not in excess of an amount which the contractor or subcontractor tendered in payment prior to the issuance of the order of the Board.

[Notwithstanding the provisions of this paragraph, no interest shall accrue after three years from the date of filing a petition with the Tax Court pursuant to section 108 of this title in any case in which there has not been a final determination by the Tax Court

with respect to such petition within such three-year period.]^{7b}

(3) **SUITS FOR RECOVERY.**—Actions on behalf of the United States may be brought in the appropriate courts of the United States to recover, (A) from the contractor or subcontractor, any amount of such excessive profits and accrued interest not withheld or eliminated by some other method under this subsection, and (B) from any person or subcontractor who has been directed under paragraph (1)(C) of this subsection to withhold for the account of the United States, the amounts required to be withheld under such paragraph, together with accrued interest thereon.

(4) **SURETIES.**—The surety under a contract or subcontract shall not be liable for the repayment of any excessive profits thereon.

(5) **ASSIGNEES.**—Nothing herein contained shall be construed (A) to authorize any Department or agency of the Government, except to the extent provided in the Assignment of Claims Act of 1940, as now or hereafter amended, to withhold from any assignee referred to in said Act, any moneys due or to become due, or to recover any moneys paid, to such assignee under any contract with any Department or agency where such moneys have been assigned pursuant to such Act, or (B) to authorize any Department or agency of the Government to direct the withholding pursuant to this Act, or to recover pursuant to this Act, from any bank, trust company or other financing institution (including any Federal lending agency) which is an assignee under any subcontract, any moneys due or to become due or paid to any such assignee under such subcontract.

(6) **INDEMNIFICATION.**—Each person is hereby indemnified by the United States against all claims on account of amounts withheld by such person pursuant to this subsection from a contractor or subcontractor and paid over to the United States.

(7) **TREATMENT OF RECOVERIES.**—All money recovered by way of repayment or suit under this subsection shall be covered into the Treasury as miscellaneous receipts. Upon the withholding of any amount of excessive profits or the crediting of any amount of excessive profits against amounts otherwise due a contractor from appropriations from the Treasury, the Secretary shall certify the amount thereof to the Treasury and the appropriations of his Department shall be reduced by an amount equal to the amount so withheld or credited. The amount of such reductions shall be transferred to the surplus fund of the Treasury.

(8) **CREDIT FOR TAXES PAID.**—In eliminating excessive profits, the Secretary shall allow the contractor or subcontractor credit for Federal income and excess profits taxes as provided in section 3806 of the Internal Revenue Code.

(c) **PERIODS OF LIMITATIONS.**—*In the absence of fraud or malfeasance or willful misrepresentation of a material fact*, no proceeding to determine the amount of excessive profits for any fiscal year shall be commenced more than one year after *a financial statement* under subsection (e)(1) of this section is filed with the Board with respect to

^{7b} By Pub. Law 87-520, 87th Cong., approved July 3, 1962, the matter in brackets was made inapplicable with respect to petitions for redetermination filed with the Tax Court after July 3, 1962.

such year, and, *in the absence of fraud or malfeasance or willful misrepresentation of a material fact*, if such proceeding is not commenced prior to the expiration of one year following the date upon which such statement is so filed, all liabilities of the contractor or subcontractor for excessive profits received or accrued during such fiscal year shall thereupon be discharged. If an agreement or order determining the amount of excessive profits is not made within two years following the commencement of the renegotiation proceeding, then, *in the absence of fraud or malfeasance or willful misrepresentation of a material fact*, upon the expiration of such two years all liabilities of the contractor or subcontractor for excessive profits with respect to which such proceeding was commenced shall thereupon be discharged, except that (1) if an order is made within such two years pursuant to a delegation of authority under subsection (d) of section 107, such two-year limitation shall not apply to review of such order by the Board, and (2) such two-year period may be extended by mutual agreement.⁸

(d) AGREEMENTS TO ELIMINATE EXCESSIVE PROFITS.—For the purposes of this title the Board may make final or other agreements with a contractor or subcontractor for the elimination of excessive profits and for the discharge of any liability for excessive profits under this title. Such agreements may contain such terms and conditions as the Board deems advisable. Any such agreement shall be conclusive according to its terms; and, except upon a showing of fraud or malfeasance or a willful misrepresentation of a material fact, (1) such agreement shall not for the purposes of this title be reopened as to the matters agreed upon, and shall not be modified by any officer, employee, or agent of the United States, and (2) such agreement and any determination made in accordance therewith shall not be annulled, modified, set aside, or disregarded in any suit, action, or proceeding. Notwithstanding any other provisions of this title, however, the Board shall have the power, pursuant to regulations promulgated by it, to modify any agreement or order for the purpose of extending the time for payment of sums due under such agreement or order, *and shall also have the power to set aside and declare null and void any such agreement if, upon a request made to the Board within three years from the date of such agreement, the Board finds as a fact that the aggregate of the amounts received or accrued by the other party to such agreement during the fiscal year covered by such agreement was not more than the minimum amounts subject to renegotiation specified in section 105 (f) for such fiscal year.*⁹

(e) INFORMATION AVAILABLE TO BOARD.—

(1) FURNISHING OF FINANCIAL STATEMENTS, ETC.—Every person who holds contracts or subcontracts, to which the provisions of this title are applicable, shall, in such form and detail as the Board may by regulations prescribe, file with the Board, on or before the first day of the *fifth* calendar month following the close of his fiscal year, a financial statement setting forth such information as the Board may by regulations prescribe as necessary to carry out this title. *The preceding sentence shall not apply*

⁸ Matter in italics in section 105 (c) was added by Pub. Law 870, 84th Cong., approved August 1, 1956. The words "a financial statement" were substituted for "the statement required". These amendments apply only with respect to fiscal years ending after June 30, 1956.

⁹ Matter in italics in section 105 (d) was added by Pub. Law 764, 83d Cong., approved September 1, 1954. This amendment is effective as if it were a part of the Renegotiation Act of 1951 on the date of its enactment.

to any such person with respect to a fiscal year if the aggregate of the amounts received or accrued under such contracts and subcontracts during such fiscal year by him, and all persons under control of or controlling or under common control with him, is not more than the applicable amount prescribed in subsection (f) (1) or (2) of this section; but any person to whom this sentence applies may, if he so elects, file with the Board for such fiscal year a financial statement setting forth such information as the Board may by regulations prescribe as necessary to carry out this title. The Board may require any person who holds contracts or subcontracts to which the provisions of this title are applicable (whether or not such person has filed a financial statement under this paragraph) to furnish any information, records, or data which are determined by the Board to be necessary to carry out this title and which the Board specifically requests such person to furnish. Such information, records, or data may not be required with respect to any fiscal year after the date on which all liabilities of such person for excessive profits received or accrued during such fiscal year are discharged. Any person who willfully fails or refuses to furnish any statement, information, records, or data required of him under this subsection, or who knowingly furnishes any statement, information, records, or data pursuant to this subsection containing information which is false or misleading in any material respect, shall, upon conviction thereof, be punished by a fine of not more than \$10,000 or imprisonment for not more than one year, or both.¹⁰

(2) AUDIT OF BOOKS AND RECORDS.—For the purpose of this title, the Board shall have the right to audit the books and records of any contractor or subcontractor subject to this title. In the interest of economy and the avoidance of duplication of inspection and audit, the services of the Bureau of Internal Revenue shall, upon request of the Board and the approval of the Secretary of the Treasury, be made available to the extent determined by the Secretary of the Treasury for the purpose of making examinations and audits under this title.

(f) MINIMUM AMOUNTS SUBJECT TO RENEGOTIATION.—

(1) IN GENERAL.—If the aggregate of the amounts received or accrued during a fiscal year (and on or after the applicable effective date specified in section 102(a)) by a contractor or subcontractor, and all persons under control of or controlling or under common control with the contractor or subcontractor, under contracts with the Departments and subcontracts described in section 103(g) (1) and (2), is not more than \$250,000, *in the case of a fiscal year ending before June 30, 1953, or \$500,000, in the case of a fiscal year ending on or after June 30, 1953, or \$1,000,000, in the case of a fiscal year ending after June 30, 1956*, the receipts or accruals from such contracts and subcontracts shall not, for such fiscal year, be renegotiated under this title. If the aggregate of such amounts received or accrued during the fiscal year under such contracts and subcontracts is more than \$250,000, *in the case of a*

¹⁰ Matter in italics in section 105 (e)(1) was added by Pub. Law 870, 84th Cong., approved August 1, 1956, which also struck out the second and third sentences of the former paragraph (1). The word "fifth" was substituted for "fourth" in the first sentence. These amendments apply only with respect to fiscal years ending after June 30, 1956.

*fiscal year ending before June 30, 1953, or \$500,000, in the case of a fiscal year ending on or after June 30, 1953, or \$1,000,000, in the case of a fiscal year ending after June 30, 1956, no determination of excessive profits to be eliminated for such year with respect to such contracts and subcontracts shall be in an amount greater than the amount by which such aggregate exceeds \$250,000, in the case of a fiscal year ending before June 30, 1953, or \$500,000, in the case of a fiscal year ending on or after June 30, 1953, or \$1,000,000, in the case of a fiscal year ending after June 30, 1956.*¹¹

(2) SUBCONTRACTS DESCRIBED IN SECTION 103(g)(3).—If the aggregate of the amounts received or accrued during a fiscal year (and on or after the applicable effective date specified in section 102(a)) by a subcontractor, and all persons under control of or controlling or under common control with the subcontractor, under subcontracts described in section 103(g)(3) is not more than \$25,000, the receipts or accruals from such subcontracts shall not, for such fiscal year, be renegotiated under this title. If the aggregate of such amounts received or accrued during the fiscal year under such subcontracts is more than \$25,000, no determination of excessive profits to be eliminated for such year with respect to such subcontracts shall be in an amount greater than the amount by which such aggregate exceeds \$25,000.

(3) COMPUTATION.—In computing the aggregate of the amounts received or accrued during any fiscal year for the purposes of *paragraph (1)* of this subsection, there shall be eliminated all amounts received or accrued by a contractor or subcontractor from all persons under control of or controlling or under common control with the contractor or subcontractor and all amounts received or accrued by each such person from such contractor or subcontractor and from each other such person. If the fiscal year is a fractional part of twelve months, the \$250,000 amount, *the \$500,000 amount, the \$1,000,000 amount, and the \$25,000 amount* shall be reduced to the same fractional part thereof of the purposes of paragraphs (1) and (2). In the case of a fiscal year beginning in 1950 and ending in 1951, the \$250,000 amount and the \$25,000 amount shall be reduced to an amount which bears the same ratio to \$250,000 or \$25,000, as the case may be, as the number of days in such fiscal year after December 31, 1950, bears to 365, but this sentence shall have no application if the contractor or subcontractor has made an agreement with the Board pursuant to section 102(c) for the application of the provisions of this title to receipts or accruals prior to January 1, 1951, during such fiscal year. *In the case of a fiscal year beginning on or before the termination date and ending after the termination date, the \$1,000,000 amount and the \$25,000 amount shall be reduced to an amount which bears the same ratio to \$1,000,000 or \$25,000, as the case may be, as the number of days in such fiscal year before the close of the termination date bears to 365.*¹²

¹¹ Matter in italics in section 105(f)(1) was added by Pub. Law 764, 83d Cong., approved September 1, 1954, as amended by Pub. Law 870, 84th Cong., approved August 1, 1956. The latter amendment added the references to \$1,000,000 for fiscal years ending after June 30, 1956.

¹² Pub. Law 764, 83d Cong., approved September 1, 1954, added "the \$500,000 amount" in the second sentence of section 105(f)(3). Pub. Law 870, 84th Cong., approved August 1, 1956, substituted "paragraph (1)" for "paragraphs (1) and (2)" in the first sentence; added "the \$1,000,000 amount" in the second sentence; and added the last sentence. The amendment substituting "paragraph (1)" applies only to fiscal years ending on or after June 30, 1956.

SEC. 106. EXEMPTIONS.

(a) **MANDATORY EXEMPTIONS.**—The provisions of this title shall not apply to—

(1) any contract by a Department with any Territory, possession, or State, or any agency or political subdivision thereof, or with any foreign government or any agency thereof; or

(2) any contract or subcontract for an agricultural commodity in its raw or natural state, or if the commodity is not customarily sold or has not an established market in its raw or natural state, in the first form or state, beyond the raw or natural state, in which it is customarily sold or in which it has an established market. The term "agricultural commodity" as used herein shall include but shall not be limited to—

(A) commodities resulting from the cultivation of the soil such as grains of all kinds, fruits, nuts, vegetables, hay, straw, cotton, tobacco, sugarcane, and sugar beets;

(B) natural resins, saps, and gums of trees;

(C) animals, such as cattle, hogs, poultry, and sheep, fish and other marine life, and the produce of live animals, such as wool, eggs, milk and cream; or

(3) any contract or subcontract for the product of a mine, oil or gas well, or other mineral or natural deposit, or timber, which has not been processed, refined, or treated beyond the first form or state suitable for industrial use; or

(4) any contract or subcontract with a common carrier for transportation, or with a public utility for gas, electric energy, water, communications, or transportation, when made in either case at rates not in excess of published rates or charges filed with, fixed, approved, or regulated by a public regulatory body, State, Federal, or local, or at rates not in excess of unregulated rates of such a public utility which are substantially as favorable to users and consumers as are regulated rates. In the case of the furnishing or sale of transportation by common carrier by water, this paragraph shall apply only to such furnishing or sale which is subject to the jurisdiction of the Interstate Commerce Commission under Part III of the Interstate Commerce Act or subject to the jurisdiction of the Federal Maritime Board under the Intercoastal Shipping Act, 1933, *and to such furnishing or sale in any case in which the Board finds that the regulatory aspects of rates for such furnishing or sale, or the type and nature of the contract for such furnishing or sale, are such as to indicate, in the opinion of the Board, that excessive profits are improbable; or*¹³

(5) any contract or subcontract with an organization exempt from taxation under section 101 (6) of the Internal Revenue Code, but only if the income from such contract or subcontract is not includible under section 422 of such code in computing the unrelated business net income of such organization; or

(6) any contract which the Board determines does not have a direct and immediate connection with the national defense. The Board shall prescribe regulations designating those classes and types of contracts which shall be exempt under this paragraph;

¹³ Matter in italics in section 106 (a) (4) was added by Pub. Law 764, 83d Cong., approved September 1, 1954, and applies only with respect to fiscal years ending on or after December 31, 1953.

and the Board shall, in accordance with regulations prescribed by it, exempt any individual contract not falling within any such class or type if it determines that such contract does not have a direct and immediate connection with the national defense. *In designating those classes and types of contracts which shall be exempt and in exempting any individual contract under this paragraph, the Board shall consider as not having a direct or immediate connection with national defense any contract for the furnishing of materials or services to be used by the United States, a Department or agency thereof, in the manufacture and sale of synthetic rubbers to a private person or to private persons which are to be used for nondefense purposes. If the use by such private person or persons shall be partly for defense and partly for non-defense purposes, the Board shall consider as not having a direct or immediate connection with national defense that portion of the contract which is determined not to have been used for national defense purposes. The method used in making such determination shall be subject to approval by the Board.* Notwithstanding section 108 of this title, regulations prescribed by the Board under this paragraph, and any determination of the Board that a contract is or is not exempt under this paragraph, shall not be reviewed or redetermined by the Tax Court or by any other court or agency; or ¹⁴

(7) any subcontract directly or indirectly under a contract or subcontract to which this title does not apply by reason of *any paragraph, other than paragraph (1), (5), or (8), of this subsection; or* ¹⁵

[Applicable to fiscal years ending on or before June 30, 1956. See footnote 16.]

(8) *any contract or subcontract for the making or furnishing of a standard commercial article or a standard commercial service, unless the Board makes a specific finding that competitive conditions affecting the sale of such article or such service are such as will not reasonably prevent excessive profits. This paragraph shall apply to any such contract or subcontract only if (1) the contractor or subcontractor files, at such time and in such form and detail as the Board shall by regulations prescribe, such information and data as may be required by the Board under its regulations for the purpose of enabling it to reach a decision with respect to the making of specific finding under this paragraph, and (2) within a period of six months after the date of filing of such information and data, the Board fails to make a specific finding that competitive conditions affecting the sale of such article or such service are such as will not reasonably prevent excessive profits, or (3) within such six-month period, the Board makes a specific finding that competitive conditions affecting the sale of such article or such service are such as will reasonably prevent excessive profits. Any contractor or subcontractor may waive the exemption provided in this paragraph with respect to*

¹⁴ Matter in italics in section 106 (a) (6) was added by Pub. Law 764, 83d Cong., approved September 1, 1954. This amendment is effective as if it were a part of the Renegotiation Act of 1951 on the date of its enactment.

¹⁵ Matter in italics in section 106 (a) (7) was added by Pub. Law 764, 83d Cong., approved September 1, 1954, as amended by Pub. Law 870, 84th Cong., approved August 1, 1956. The former amendment limited the exclusion to paragraph (8) and applies only to the extent of amounts received or accrued after December 31, 1953. The latter amendment added the references to paragraphs (1) and (5), and applies only with respect to subcontracts made after June 30, 1956.

receipts or accruals in any fiscal year by including a statement to such effect in the financial statement filed by such contractor or subcontractor for such fiscal year pursuant to section 105(e)(1). Any specific finding of the Board under this paragraph shall not be reviewed or redetermined by any court or agency other than by the Tax Court of the United States in a proceeding for a redetermination of the amount of excessive profits determined by an order of the Board. For the purpose of this paragraph—

(A) the term "article" includes any material, part, component, assembly, machinery, equipment, or other personal property;

(B) the term "standard commercial article" means an article—

(1) which, in the normal course of business, is customarily manufactured for stock, and is customarily maintained in stock by the manufacturer or any dealer, distributor, or other commercial agency for the marketing of such article; or

(2) which is manufactured and sold by more than two persons for general civilian industrial or commercial use, or which is identical in every material respect with an article so manufactured and sold;

(C) the term "identical in every material respect" means of the same kind, manufactured of the same or substitute materials, and having the same industrial or commercial use or uses, without necessarily being of identical specifications;

(D) the term "service" means any processing or other operation performed by chemical, electrical, physical, or mechanical methods directly on materials owned by another person;

(E) the term "standard commercial service" means a service which is customarily performed by more than two persons for general civilian industrial or commercial requirements, or is reasonably comparable with a service so performed;

(F) the term "reasonably comparable" means of the same or a similar kind, performed with the same or similar materials, and having the same or a similar result, without necessarily involving identical operations; and

(G) the term "persons" does not include any person under control of, or controlling, or under common control with any other person considered for the purposes of subparagraph (B)(2) of this paragraph.¹⁶

(9) any contract, awarded as a result of competitive bidding, for the construction of any building, structure, improvement, or facility, other than a contract for the construction of housing financed with a mortgage or mortgages insured under the provisions of title VIII of the National Housing Act, as now or hereafter amended.¹⁷

¹⁶ Paragraph (6) of section 106(a) was added by Pub. Law 754, 83d Cong., approved September 1, 1954, as amended by Pub. Law 216, 84th Cong., approved August 3, 1955. The latter amendment added the references to standard commercial services. These amendments apply only to the extent of amounts received or accrued after December 31, 1953. Pub. Law 870, 84th Cong., approved August 1, 1956, struck out paragraph (8) with respect to fiscal years ending after June 30, 1956 and added section 106(e) with respect to such fiscal years. Therefore, section 106(a)(8) applies to contracts and subcontracts only to the extent of amounts received or accrued after December 31, 1953, in fiscal years ending on or before June 30, 1956.

¹⁷ Section 106(a)(9) was added by Pub. Law 216, 84th Cong., approved August 3, 1955, and applies only to contracts with the Departments made after December 31, 1954.

(b) **COST ALLOWANCE.**—In the case of a contractor or subcontractor who produces or acquires the product of a mine, oil or gas well, or other mineral or natural deposit, or timber, and processes, refines, or treats such a product to and beyond the first form or state suitable for industrial use, or who produces or acquires an agricultural product and processes, refines, or treats such a product to and beyond the first form or state in which it is customarily sold or in which it has an established market, the Board shall prescribe such regulations as may be necessary to give such contractor or subcontractor a cost allowance substantially equivalent to the amount which would have been realized by such contractor or subcontractor if he had sold such product at such first form or state. Notwithstanding any other provisions of this title, there shall be excluded from consideration in determining whether or not a contractor or subcontractor has received or accrued excessive profits that portion of the profits, derived from receipts and accruals subject to the provisions of this title, attributable to the increment in value of the excess inventory. For the purposes of this subsection the term "excess inventory" means inventory of products, hereinbefore described in this subsection, acquired by the contractor or subcontractor in the form or at the state in which contracts for such products on hand or on contract would be exempted from this title by subsection (a) (2) or (3) of this section, which is in excess of the inventory reasonably necessary to fulfill existing contracts or orders. That portion of the profits, derived from receipts and accruals subject to the provisions of this title, attributable to the increment in value of the excess inventory, and the method of excluding such portion of profits from consideration in determining whether or not the contractor or subcontractor has received or accrued excessive profits, shall be determined in accordance with regulations prescribed by the Board.

(c) **PARTIAL MANDATORY EXEMPTION FOR DURABLE PRODUCTIVE EQUIPMENT.**—

[Applicable to fiscal years ended before June 30, 1953. See footnote 18]

(1) **IN GENERAL.**—The provisions of this title shall not apply to receipts or accruals (other than rents) from subcontracts for new durable productive equipment, except to that part of such receipts or accruals which bears the same ratio to the total of such receipts or accruals as five years bears to the average useful life of such equipment as set forth in Bulletin F of the Bureau of Internal Revenue (1942 edition) or, if an average useful life is not so set forth, then as estimated by the Board.

(2) **DEFINITIONS.**—For the purpose of this subsection—

(A) the term "durable productive equipment" means machinery, tools, or other equipment which does not become a part of an end product acquired by any agency of the Government under a contract with a department, or of an article incorporated therein, and which has an average useful life of more than five years; and

(B) the term "subcontracts for new durable productive equipment" does not include subcontracts where the purchaser of such durable productive equipment has acquired such equipment for the account of the Government, but

includes pool orders and similar commitments placed in the first instance by a Department or other agency of the Government when title to the equipment is transferred on delivery thereof or within one year thereafter to a contractor or subcontractor.

[Applicable to fiscal years ending on or after June 30, 1953. See footnote 18]

(1) *IN GENERAL.*—The provisions of this title shall not apply to receipts or accruals (other than rents) from *contracts or subcontracts* for new durable productive equipment, except (A) to that part of such receipts or accruals which bears the same ratio to the total of such receipts or accruals as five years bears to the average useful life of such equipment as set forth in Bulletin F of the Bureau of Internal Revenue (1942 edition) or, if an average useful life is not so set forth, then as estimated by the Board and (B) *to receipts and accruals from contracts for new durable productive equipment in cases in which the Board finds that the new durable productive equipment covered by such contracts cannot be adapted, converted, or retooled for commercial use.*

(2) *DEFINITION.*—*For the purpose of this subsection, the term "durable productive equipment" means machinery, tools, or other productive equipment, which has an average useful life of more than five years.*¹⁸

(d) *PERMISSIVE EXEMPTIONS.*—The Board is authorized, in its discretion, to exempt from some or all of the provisions of this title—

(1) any contract or subcontract to be performed outside of the territorial limits of the continental United States or in Alaska;

(2) any contracts or subcontracts under which, in the opinion of the Board, the profits can be determined with reasonable certainty when the contract price is established, such as certain classes of (A) agreements for personal service or for the purchase of real property, perishable goods, or commodities the minimum price for the sale of which has been fixed by a public regulatory body, (B) leases and license agreements, and (C) agreements where the period of performance under such contract or subcontract will not be in excess of thirty days;

(3) any contract or subcontract or performance thereunder during a specified period or periods if, in the opinion of the Board, the provisions of the contract are otherwise adequate to prevent excessive profits;

(4) any contract or subcontract the renegotiation of which would jeopardize secrecy required in the public interest;

(5) any subcontract or group of subcontracts not otherwise exempt from the provisions of this section, if, in the opinion of the Board, it is not administratively feasible in the case of such subcontract or in the case of such group of subcontracts to determine and segregate the profits attributable to such subcontract or group of subcontracts from the profits attributable to activities not subject to renegotiation.

¹⁸ Matter in italics in paragraph 1 was added by Pub. Law 764, 83d Cong., approved September 1, 1954. Paragraph 2 was amended to read as shown in italics by Pub. Law 764, as amended by Pub. Law 216, 84th Cong., approved August 3, 1955. The latter amendment added "productive" between "other" and "equipment" and struck out "which does not become a part of an end product, or of an article incorporated therein, and" after "other equipment". These amendments apply only with respect to fiscal years ending on or after June 30, 1953.

The Board may so exempt contracts and subcontracts both individually and by general classes or types.

[Applicable to fiscal years ending after June 30, 1956]

(e) *MANDATORY EXEMPTION FOR STANDARD COMMERCIAL ARTICLES AND SERVICES.*—

(1) *ARTICLES AND SERVICES.*—*The provisions of this title shall not apply to amounts received or accrued in a fiscal year under any contract or subcontract for an article or service which (with respect to such fiscal year) is—*

(A) *a standard commercial article;*

(B) *an article which is identical in every material respect with a standard commercial article; or*

(C) *a service which is a standard commercial service or is reasonably comparable with a standard commercial service.*

(2) *CLASSES OF ARTICLES.*—*The provisions of this title shall not apply to amounts received or accrued in a fiscal year under any contract or subcontract for an article which (with respect to such fiscal year) is an article in a standard commercial class of articles.*

(3) *APPLICATIONS.*—*Paragraph (1) (B) or (C) and paragraph (2) shall apply to amounts received or accrued in a fiscal year under any contract or subcontract for an article or service only if—*

(A) *the contractor or subcontractor at his election files, at such time and in such form and detail as the Board shall by regulations prescribe, an application containing such information and data as may be required by the Board under its regulations for the purpose of enabling it to make a determination under the applicable paragraph, and*

(B) *the Board determines that such article or service is, or fails to determine that such article or service is not, an article or service to which such paragraph applies, within the following periods after the date of filing such application:*

(i) *in the case of paragraph (1) (B) or (C), three months;*

(ii) *in the case of paragraph (2), six months; or*

(iii) *in either case, any longer period stipulated by mutual agreement.*

(4) *DEFINITIONS.*—*For the purposes of this subsection—*

(A) *the term “article” includes any material, part, component, assembly, machinery, equipment, or other personal property;*

(B) *the term “standard commercial article” means, with respect to any fiscal year, an article—*

(i) *which either is customarily maintained in stock by the contractor or subcontractor or is offered for sale in accordance with a price schedule regularly maintained by the contractor or subcontractor, and*

(ii) *from the sales of which by the contractor or subcontractor at least 35 percent of the receipts or accruals in such fiscal year, or of the aggregate receipts or accruals in such fiscal year and the preceding fiscal year, are not*

(without regard to this subsection and subsection (c) of this section) subject to this title;

(C) an article is, with respect to any fiscal year, "identical in every material respect with a standard commercial article" only if—

(i) such article is of the same kind and manufactured of the same or substitute materials (without necessarily being of identical specifications) as a standard commercial article from sales of which the contractor or subcontractor has receipts or accruals in such fiscal year,

(ii) such article is sold at a price which is reasonably comparable with the price of such standard commercial article, and

(iii) at least 35 percent of the aggregate receipts or accruals in such fiscal year by the contractor or subcontractor from sales of such article and sales of such standard commercial article are not (without regard to this subsection and subsection (c) of this section) subject to this title;

(D) the term "service" means any processing or other operation performed by chemical, electrical, physical, or mechanical methods directly on materials owned by another person;

(E) the term "standard commercial service" means, with respect to any fiscal year, a service from the performance of which by the contractor or subcontractor at least 35 percent of the receipts or accruals in such fiscal year are not (without regard to this subsection) subject to this title;

(F) a service is, with respect to any fiscal year, "reasonably comparable with a standard commercial service" only if—

(i) such service is of the same or a similar kind, performed with the same or similar materials, and has the same or a similar result, without necessarily involving identical operations, as a standard commercial service from the performance of which the contractor or subcontractor has receipts or accruals in such fiscal year, and

(ii) at least 35 percent of the aggregate receipts or accruals in such fiscal year by the contractor or subcontractor from the performance of such service and such standard commercial service are not (without regard to this subsection) subject to this title; and

(G) the term "standard commercial class of articles" means, with respect to any fiscal year, two or more articles with respect to which the following conditions are met:

(i) at least one of such articles either is customarily maintained in stock by the contractor or subcontractor or is offered for sale in accordance with a price schedule regularly maintained by the contractor or subcontractor,

(ii) all of such articles are of the same kind and manufactured of the same or substitute materials (without necessarily being of identical specifications),

(iii) all of such articles are sold at reasonably comparable prices, and

(iv) at least 35 percent of the aggregate receipts or accruals in the fiscal year by the contractor or subcontractor from sales of all of such articles are not (without regard to this subsection and subsection (c) of this section) subject to this title.

(5) *WAIVER OF EXEMPTION.*—Any contractor or subcontractor may waive the exemption provided in paragraphs (1) and (2) with respect to his receipts or accruals in any fiscal year from sales of any article or service by including a statement to such effect in the financial statement filed by him for such fiscal year pursuant to section 105(e)(1), without necessarily waiving such exemption with respect to receipts or accruals in such fiscal year from sales of any other article or service. A waiver, if made, shall be unconditional, and no waiver may be made without the permission of the Board for any receipts or accruals with respect to which the contractor or subcontractor has previously filed an application under paragraph (3).

(6) *NONAPPLICABILITY DURING NATIONAL EMERGENCIES.*—Paragraphs (1) and (2) shall not apply to amounts received or accrued during a national emergency proclaimed by the President, or declared by the Congress, after the date of the enactment of the Renegotiation Amendments Act of 1956.¹⁹

SEC. 107. RENEGOTIATION BOARD.

(a) *CREATION OF BOARD.*—There is hereby created, as an independent establishment in the executive branch of the Government, a Renegotiation Board to be composed of five members to be appointed by the President, by and with the advice and consent of the Senate. The Secretaries of the Army, the Navy, and the Air Force, respectively, subject to the approval of the Secretary of Defense, and the Administrator of General Services shall each recommend to the President, for his consideration, one person from civilian life to serve as a member of the Board. The President shall, at the time of appointment, designate one member to serve as Chairman. The Chairman shall receive compensation at the rate of \$17,500 per annum, and the other members shall receive compensation at the rate of \$15,000 per annum.^{19a} No member shall actively engage in any business, vocation, or employment other than as a member of the Board. The Board shall have a seal which shall be judicially noticed.

(b) *PLACES OF MEETING AND QUORUM.*—The principal office of the Board shall be in the District of Columbia, but it or any division thereof may meet and exercise its powers at any other place. The Board may establish such number of offices as it deems necessary to expedite the work of the Board. Three members of the Board shall constitute a quorum, and any power, function, or duty of the Board may be exercised or performed by a majority of the members present if the members present constitute at least a quorum.

(c) *PERSONNEL.*—There shall be a General Counsel of the Renegotiation Board who shall be appointed by the Board without regard to the civil-service laws and regulations. The Board is authorized, subject

¹⁹ Section 106(e) was added by Pub. Law 870, 84th Cong., approved August 1, 1956, and applies only with respect to fiscal years ending after June 30, 1956.

^{19a} By Federal Executive Pay Act of 1956, Pub. Law 854, 84th Cong., approved July 31, 1956, compensation of Chairman and other members of Board was increased to \$20,500 and \$20,000, respectively. By Federal Executive Salary Act of 1964, Title III, Pub. Law 88-426, 88th Cong., approved August 14, 1964, compensation of Chairman and other members of Board was increased to \$26,000.

to the Classification Act of 1949 *and the civil-service laws and regulations*,²⁰ to employ and fix the compensation of such officers and employees as it deems necessary to assist it in carrying out its duties under this title. The Board may, with the consent of the head of the agency of the Government concerned, utilize the services of any officers or employees of the United States, and reimburse such agency for the services so utilized. Officers or employees whose services are so utilized shall not receive additional compensation for such services, but shall be allowed and paid necessary travel expenses and a per diem in lieu of subsistence in accordance with the Standardized Government Travel Regulations while away from their homes or official station on duties of the Board.

(d) DELEGATION OF POWERS.—The Board may delegate in whole or in part any function, power, or duty (other than its power to promulgate regulations and rules and other than its power to grant permissive exemptions under section 106(d)) to any agency of the Government, including any such agency established by the Board, and may authorize the successive redelegation, within limits specified by it, of any such function, power, or duty to any agency of the Government, including any such agency established by the Board. But no function, power, or duty shall be delegated or redelegated to any person pursuant to this subsection or subsection (f) unless the Board has determined that such person (other than the Secretary of a Department) is responsible directly to the Board or to the person making such delegation or redelegation and is not engaged on behalf of any Department in the making of contracts for the procurement of supplies or services, or in the supervision of such activity; and any delegation or redelegation of any function, power, or duty pursuant to this subsection or subsection (f) shall be revoked by the person making such delegation or redelegation (or by the Board if made by it) if the Board shall at any time thereafter determine that the person (other than the Secretary of a Department) to whom has been delegated or redelegated such function, power or duty is not responsible directly to the Board or to the person making such delegation or redelegation or is engaged on behalf of any Department in the making of contracts for the procurement of supplies or services, or in the supervision of such activity.

(e) ORGANIZATION AND OPERATION OF BOARD.—The Chairman of the Board may from time to time divide the Board into division of one or more members, assign the members of the Board thereto, and in case of a division of more than one member, designate the chief thereof. The Board may also, by regulations or otherwise, determine the character of cases to be conducted initially by the Board through an officer or officers of, or utilized by, the Board, the character of cases to be conducted initially by the various agencies of the Government authorized to exercise powers of the Board pursuant to subsection (d) of this section, the character of cases to be conducted initially by the various divisions of the Board, and the character of cases to be conducted initially by the Board itself. The Board may review any determination in any case not initially conducted by it, on its own motion or, in its discretion, at the request of any contractor or sub-

²⁰ First sentence of section 107(c) was added by Pub. Law 86-89, 86th Cong., approved July 13, 1959, as amended by Pub. Law 88-426, 88th Cong., approved August 14, 1964, which repealed that part of such sentence reading: “, and shall receive compensation at the rate of \$19,000 per annum”. Matter in italics in second sentence was substituted by Pub. Law 870, 84th Cong., approved August 1, 1956, for “(but without regard to the civil-service laws and regulations)”.

contractor aggrieved thereby. Unless the Board upon its own motion initiates a review of such determination within ninety days from the date of such determination, or at the request of the contractor or subcontractor made within ninety days from the date of such determination initiates a review of such determination within ninety days from the date of such request, such determination shall be deemed the determination of the Board. If such determination was made by an order with respect to which notice thereof was given by registered mail or by *certified mail* pursuant to section 105(a), the Board shall give notice by registered mail or by *certified mail* to the contractor or subcontractor of its decision not to review the case. If the Board reviews any determination in any case not initially conducted by it and does not make an agreement with the contractor or subcontractor with respect to the elimination of excessive profits, it shall issue and enter an order under section 105(a) determining the amount, if any, of excessive profits, and forthwith give notice thereof by registered mail or by *certified mail* to the contractor or subcontractor. The amount of excessive profits so determined upon review may be less than, equal to, or greater than, that determined by the agency of the Government whose action is so reviewed.^{20a}

(f) DELEGATION OF RENEGOTIATION FUNCTIONS TO BOARD.—The Board is hereby authorized and directed to accept and perform such renegotiation powers, duties, and functions as may be delegated to it under any other law requiring or permitting renegotiation, and the Board is further authorized to redelegate any such power, duty, or function to any agency of the Government and to authorize successive redelegations thereof, within limits specified by the Board. Notwithstanding any other provision of law, the Secretary of Defense is hereby authorized to delegate to the Board, in whole or in part, the powers, functions, and duties conferred upon him by any other renegotiation law.

SEC. 108. REVIEW BY THE TAX COURT.

Any contractor or subcontractor aggrieved by an order of the Board determining the amount of excessive profits received or accrued by such contractor or subcontractor may—

(a) if the case was conducted initially by the Board itself—within ninety days (not counting Sunday or a legal holiday in the District of Columbia as the last day) after the mailing under section 105(a) of the notice of such order, or

(b) if the case was not conducted initially by the Board itself—within ninety days (not counting Sunday or a legal holiday in the District of Columbia as the last day) after the mailing under section 107(e) of the notice of the decision of the Board not to review the case or the notice of the order of the Board determining the amount of excessive profits,

file a petition with The Tax Court of the United States for a redetermination thereof. Upon such filing such court shall have exclusive jurisdiction, by order, to [finally] determine the amount, if any, of such excessive profits received or accrued by the contractor or subcontractor, and such determination shall not be reviewed or redeter-

^{20a} Matter in italics in section 107(e) was added by Pub. Law 86-507, 86th Cong., approved June 11, 1960.

mined by any court or agency *except as provided in Section 108A.*^{20b} The court may determine as the amount of excessive profits an amount either less than, equal to, or greater than that determined by the Board. A proceeding before the Tax Court to finally determine the amount, if any, of excessive profits shall not be treated as a proceeding to review the determination of the Board, but shall be treated as a proceeding de novo. For the purposes of this section the court shall have the same powers and duties, insofar as applicable in respect of the contractor, the subcontractor, the Board, and the Secretary, and in respect of the attendance of witnesses and the production of papers, notice of hearings, hearings before divisions, review by the Tax Court of decisions of divisions, stenographic reporting, and reports of proceedings, as such court has under sections 1110, 1111, 1113, 1114, 1115(a), 1116, 1117(a), 1118, 1120, and 1121 of the Internal Revenue Code in the case of a proceeding to redetermine a deficiency. In the case of any witness for the Board, the fees and mileage, and the expenses of taking any deposition shall be paid out of appropriations of the Board available for that purpose, and in the case of any other witnesses shall be paid, subject to rules prescribed by the court, by the party at whose instance the witness appears or the deposition is taken. The filing of a petition under this section shall operate to stay the execution of the order of the Board under subsection (b) of section 105 *only*²¹ if within ten days after the filing of the petition the petitioner files with the Tax Court a good and sufficient bond, approved by such court, in such amount as may be fixed by the court. Any amount collected by the United States under an order of the Board in excess of the amount found to be due under a determination of excessive profits by the Tax Court shall be refunded to the contractor or subcontractor with interest thereon at the rate of 4 per centum per annum from the date of collection by the United States to the date of refund.

SEC. 108A. VENUE OF APPEALS FROM TAX COURT DECISIONS IN RENEGOTIATION CASES.

[Applicable with respect to petitions for redetermination filed with the Tax Court on or before July 3, 1962]

A decision of the Tax Court of the United States under section 108 of this Act may, to the extent subject to review, be reviewed by—

(1) *the United States Court of Appeals for the circuit in which is located the office to which the contractor or subcontractor made his Federal income-tax return for the taxable year which corresponds to the fiscal year with respect to which such decision of the Tax Court was made, or if no such return was made for such taxable year, then by the United States Court of Appeals for the District of Columbia, or*

(2) *any United States Court of Appeals designated by the Attorney General and the contractor or subcontractor by stipulation in writing.*²²

^{20b} By Pub. Law 87-520, 87th Cong., approved July 3, 1962, the word "finally" was made inapplicable with respect to petitions for redetermination filed with the Tax Court after July 3, 1962; and the matter in italics was added effective only with respect to petitions filed after such date.

²¹ Matter in italics in next to last sentence of section 108 was added by Pub. Law 870, 84th Cong., approved August 1, 1956. This amendment is effective as of the date of the enactment of the Renegotiation Act of 1951

²² Section 108A was added by Pub. Law 870, 84th Cong., approved August 1, 1956.

SEC. 108A. REVIEW OF TAX COURT DECISIONS IN RENEGOTIATION CASES.

[Applicable with respect to petitions filed with the Tax Court after July 3, 1962.
See footnote 22a]

(a) *JURISDICTION.*—*Except as provided in section 1254 of title 28 of the United States Code, the United States Courts of Appeals shall have exclusive jurisdiction to review decisions by the Tax Court of the United States under section 108 of this Act in the same manner and to the same extent as decisions of the district courts in civil actions tried without a jury, except as otherwise provided in this section. In no case shall the question of the existence of excessive profits, or the extent thereof, be reviewed, and findings of fact by the Tax Court shall be conclusive unless such findings are arbitrary or capricious. The judgment of any such court shall be final except that it shall be subject to review, under the limitations herein provided for, by the Supreme Court of the United States upon certiorari, in the manner provided in section 1254 of title 28 of the United States Code.*

(b) *POWERS.*—*Upon such review, such courts shall have only the power to affirm the decision of the Tax Court or to reverse such decision on questions of law and remand the case for such further action as justice may require, except that such court shall not reverse and remand the case for error of law which is immaterial to the decision of the Tax Court.*

(c) *VENUE OF APPEALS FROM TAX COURT DECISIONS IN RENEGOTIATION CASES.*—*A decision of the Tax Court of the United States under section 108 of this Act may, to the extent subject to review, be reviewed by—*

(1) *the United States Court of Appeals for the circuit in which is located the office to which the contractor or subcontractor made his Federal income tax return for the taxable year which corresponds to the fiscal year with respect to which such decision of the Tax Court was made, or if no such return was made for such taxable year, then by the United States Court of Appeals for the District of Columbia, or*

(2) *any United States Court of Appeals designated by the Attorney General and the contractor or subcontractor by stipulation in writing.*

SEC. 109. RULES AND REGULATIONS.

The Board may make such rules, regulations, and orders as it deems necessary or appropriate to carry out the provisions of this title.

SEC. 110. COMPLIANCE WITH REGULATIONS, ETC.

No person shall be held liable for damages or penalties for any act or failure to act resulting directly or indirectly from his compliance with a rule, regulation, or order issued pursuant to this title, notwithstanding that any such rule, regulation, or order shall thereafter be declared by judicial or other competent authority to be invalid.

SEC. 111. APPLICATION OF ADMINISTRATIVE PROCEDURE ACT.

The functions exercised under this title shall be excluded from the operation of the Administrative Procedure Act (60 Stat. 237) except as to the requirements of section 3 thereof.

^{22a} Section 108A was amended by Pub. Law 87-520, 87th Cong., approved July 3, 1962, to provide for review of Tax Court decisions for cases in which the petition for redetermination is filed with the Tax Court after July 3, 1962.

SEC. 112. APPROPRIATIONS.

There are hereby authorized to be appropriated such sums as may be necessary and appropriate for the carrying out of the provisions and purposes of this title. Funds made available for the purposes of this title may be allocated or transferred for any of the purposes of this title, with the approval of the Bureau of the Budget to any agency of the Government designated to assist in carrying out this title. Funds so allocated or transferred shall remain available for such period as may be specified in the Acts making such funds available.

SEC. 113. PROSECUTION OF CLAIMS AGAINST UNITED STATES BY FORMER PERSONNEL.

Nothing in title 18, United States Code, sections 281 and 283, or in section 190 of the Revised Statutes (U.S.C., title 5, sec. 99) shall be deemed to prevent any person by reason of service in a Department or the Board from acting as counsel, agent, or attorney for prosecuting any claim against the United States: *Provided*, That such person shall not prosecute any claim against the United States (1) involving any subject matter directly connected with which such person was so employed, or (2) during the period such person is engaged in employment in a Department of the Board.²³

SEC. 114. REPORTS TO CONGRESS.

The Board shall on or before January 1, 1957, and on or before January 1 of each year thereafter, submit to the Congress a complete report of its activities for the preceding year ending on June 30. Such report shall include—

(1) *the number of persons in the employment of the Board during such year, and the places of their employment;*

(2) *the administrative expenses incurred by the Board during such year;*

(3) *statistical data relating to filings during such year by contractors and subcontractors, and to the conduct and disposition during such year of proceedings with respect to such filings and filings made during previous years;*

(4) *an explanation of the principal changes made by the Board during such year in its regulations and operating procedures;*

(5) *the number of renegotiation cases disposed of by the Tax Court, each United States Court of Appeals, and the Supreme Court during such year, and the number of cases pending in each such court at the close of such year; and*

(6) *such other information as the Board deems appropriate.*²⁴

TITLE II—MISCELLANEOUS PROVISIONS**SEC. 201. FUNCTIONS UNDER WORLD WAR II RENEGOTIATION ACT.**

(a) **ABOLITION OF WAR CONTRACTS PRICE ADJUSTMENT BOARD.**—The War Contracts Price Adjustment Board, created by the Renegotiation Act, is hereby abolished.

²³ Section 113 was amended by Pub. Law 870, 84th Cong., approved August 1, 1956, by striking out "during the period (or a part thereof) beginning July 1, 1950, and ending December 31, 1953," before "from acting".

²⁴ Section 114 was added by Pub. Law 870, 84th Cong., approved August 1, 1956.

(b) TRANSFER OF FUNCTIONS IN GENERAL.—All powers, functions, and duties conferred upon the War Contracts Price Adjustment Board by the Renegotiation Act and not otherwise specifically dealt with in this section are transferred to the Renegotiation Board.

(c) AMENDMENT OF THE RENEGOTIATION ACT.—Subsection (a)(4)(D) of the Renegotiation Act is amended by inserting at the end thereof the following: "A net renegotiation rebate shall not be repaid unless a claim therefor has been filed with the Board on or before the date of its abolition, or unless a claim shall have been filed with the Administrator of General Services (i) on or before June 30, 1951,²⁵ or (ii) within ninety days after the making of an agreement or the entry of an order under subsection (c)(1) determining the amount of excessive profits, whichever is later. A claim shall be deemed to have been filed when received by the Board or the Administrator, whether or not accompanied by a statement of the Commissioner of Internal Revenue showing the amortization deduction allowed for the renegotiated year upon the recomputation made pursuant to section 124(d) of the Internal Revenue Code."

(d) TRANSFER OF CERTAIN FUNCTIONS.—All powers, functions, and duties conferred upon the War Contracts Price Adjustment board by subsection (a)(4)(D) of the Renegotiation Act, subject to the amendment thereof by subsection (c) of this section, are hereby transferred to the Administrator of General Services.

(e) FUNCTIONS AND RECORDS.—Each Secretary of a Department is authorized and directed to eliminate the excessive profits determined under all existing renegotiation agreements or orders by the methods enumerated in subsection (c)(2) of the Renegotiation Act in respect of all renegotiations conducted by his Department pursuant to delegations from the War Contracts Price Adjustment Board. The several Departments shall retain custody of the renegotiation case files covering renegotiations thus conducted for such time as the Secretary deems necessary for the purposes of this section, and thereafter they shall be made available to the Renegotiation Board for appropriate disposition. The renegotiation records of the War Contracts Price Adjustment Board shall become records of the Renegotiation Board on the effective date of this section.

(f) REFUNDS.—All refunds under subsection (a)(4)(D) of the Renegotiation Act (relating to the recomputation of the amortization deduction), all refunds under the last sentence of subsection (i)(3) of such Act (relating to excess inventories), and all amounts finally adjudged or determined to have been erroneously collected by the United States pursuant to a determination of excessive profits, with interest thereon in the last mentioned case at a rate not to exceed 4 per centum per annum as may be determined by the Administrator of General Services or his duly authorized representative computed to the date of certification to the Treasury Department for payment shall be certified by the Administrator of General Services or his duly authorized representative to the Treasury Department for payment from such appropriations as may be available therefor: *Provided*, That such refunds shall be based solely on the certificate of the Administrator of General Services or his duly authorized representative.

²⁵ Subsec. (a) (4) (D) of the Renegotiation Act was further amended by Public Law 143, 82d Cong., approved October 20, 1951, which changed "June 30, 1951" to "October 31, 1951," and by Public Law 576, 82d Cong., approved July 17, 1952, which changed "October 31, 1951" to "December 31, 1952."

(g) **EXISTING POLICIES, PROCEDURES, ETC., TO REMAIN IN EFFECT.**—All policies, procedures, directives, and delegations of authority prescribed or issued (1) by the War Contracts Price Adjustment Board, or (2) by any Secretary or other duly authorized officer of the Government, under the authority of the Renegotiation Act, in effect upon the effective date of this section and not inconsistent herewith, shall remain in full force and effect unless and until superseded, or except as they may be amended, under the authority of this section or any other appropriate authority. All functions, powers, and responsibilities transferred by this section shall be accompanied by the authority to issue appropriate regulations and procedures, or to modify existing procedures, in respect of such powers, functions, and responsibilities.

(h) **SAVINGS PROVISION.**—This section shall not be construed (1) to prohibit disbursements authorized by the War Contracts Price Adjustment Board and certified pursuant to its authority prior to the effective date of this section, (2) to affect the validity or finality of any agreement or order made or issued pursuant to law by the War Contracts Price Adjustment Board or pursuant to delegations of authority from it, or (3) to prejudice or to abate any action taken or any right accruing or accrued, or any suit or proceeding had or commenced in any civil cause; but any court having on its docket a case to which the War Contracts Price Adjustment Board is a party, on motion or supplemental petition filed at any time within *four years* after the effective date of this section, showing a necessity for the survival of such suit, action, or other proceeding to obtain a determination of the questions involved, may allow the same to be maintained by or against the United States. *If any such case has been dismissed by any court for failure to substitute for the War Contracts Price Adjustment Board prior to the effective date of this sentence, such case is hereby revived and reinstated in such court as if it had not been dismissed.*²⁸

(i) **RENEGOTIATION ACT NOT REPEALED.**—Except as by this Act specifically amended or modified, all provisions of the Renegotiation Act shall remain in full force and effect.

(j) **DEFINITIONS.**—The terms which are defined in the Renegotiation Act shall, when used in this section, have the same meaning as when used in the Renegotiation Act, except that where a renegotiation function has been transferred by or pursuant to law the terms “Secretary” or “Secretaries” and “Department” or “Departments” shall be understood to refer to the successors in function to those officers or offices specifically named in the Renegotiation Act.

(k) **EFFECTIVE DATE OF SECTION.**—This section shall take effect sixty days after the date of the enactment of this Act.

SEC. 202. PERIOD OF LIMITATIONS FOR RENEGOTIATION ACT OF 1948.

No proceeding under the Renegotiation Act of 1948 to determine the amount of excessive profits for any fiscal year shall be commenced more than one year after the mandatory statement required by the regulations issued pursuant to such Act is filed with respect to such year, or more than six months after the date of the enactment of this title, whichever is the later, and if such proceeding is not so commenced (in the manner provided by the regulations prescribed pur-

²⁸ Matter in italics in section 201 (h) was added by Pub. Law 764, 83d Cong., approved September 1, 1954.

suant to such Act), all liabilities of the contractor or subcontractor under such Act for excessive profits received or accrued during such fiscal year shall thereupon be discharged. If an agreement or order determining the amount of excessive profits under such Act is not made within two years following the commencement of the renegotiation proceeding, then upon the expiration of such two years all liabilities of the contractor or subcontractor for excessive profits with respect to which such proceeding was commenced shall thereupon be discharged, except that (1) such two-year period may be extended by mutual agreement, and (2) if within such two years such an order is duly issued pursuant to such Act, such two-year limitation shall not apply to the review of such order by any renegotiation board duly authorized to undertake such review.

SEC. 203. AMENDMENT OF SECTION 3806 OF THE INTERNAL REVENUE CODE.

Section 3806 (a) (1) of the Internal Revenue Code is hereby amended by striking out subparagraphs (A), (B), and (C) and inserting in lieu thereof the following:

“(A) The term ‘renegotiation’ includes any transaction which is a renegotiation within the meaning of the Federal renegotiation act applicable to such transaction, any modification of one or more contracts with the United States or any agency thereof, and any agreement with the United States or any agency thereof in respect of one or more such contracts or subcontracts thereunder.

“(B) The term ‘excessive profits’ includes any amount which constitutes excessive profits within the meaning assigned to such term by the applicable Federal renegotiation act, any part of the contract price of a contract with the United States or any agency thereof, any part of the subcontract price of a subcontract under such a contract, and any profits derived from one or more such contracts or subcontracts.

“(C) The term ‘subcontract’ includes any purchase order or agreement which is a subcontract within the meaning assigned to such term by the applicable Federal renegotiation act.

“(D) The term ‘Federal renegotiation act’ includes section 403 of the Sixth Supplemental National Defense Appropriation Act (Public 528, 77th Cong., 2d Sess.), as amended or supplemented, the Renegotiation Act of 1948, as amended or supplemented, and the Renegotiation Act of 1951, as amended or supplemented.”

SEC. 204. SEPARABILITY PROVISION.

If any provision of this Act or the application of any provision to any person or circumstance is held invalid, the validity of the remainder of the Act and of the application of its provisions to other persons and circumstances shall not be affected thereby.