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The Honorable George H. Mahon, Chairman
Committee on Appropriations
House of Representatives

Dear Mr. Chairman:

Your letter of January 13, 1975, requested our review of the propriety and legality of a proposal by the Department of Defense (DOD) to proceed with Navy shipbuilding programs as presently constituted in spite of predicted funding deficits.

The Navy shipbuilding programs were funded in a total amount of \$3,059 million, to remain available for five fiscal years, under the heading "Shipbuilding and Conversion, Navy" in title IV of the Department of Defense Appropriation Act, 1975, approved October 8, 1974, Pub. L. No. 93-437, 88 Stat. 1220. Individual programs under the Shipbuilding and Conversion, Navy heading were funded in 1975 as separate line items, in accordance with the Department of Defense Appropriation Authorization Act, 1975, approved August 5, 1974, Pub. L. No. 93-365, 88 Stat. 399, 400.

The problems existing with respect to the shipbuilding programs and DOD's proposed action are described in a letter to you from the Deputy Secretary of Defense dated January 9, 1975. The Deputy Secretary's letter indicates that there is a "predicted funding deficit" of \$2,269 million through the years during which ships will be under construction, resulting primarily from unexpected inflation, changed market conditions, and necessary program changes. Of the total predicted deficit, \$1,354 million applies to shipbuilding programs for fiscal year 1974 and prior years which are all under contract. As to this portion of the deficit, the Deputy Secretary states:

"According to practice, the funding problem on the Fiscal Year 1974 and prior programs will be budgeted in the Fiscal Year 1976 budget, with the Department requesting new appropriations to restore those ship programs to a fully funded status. This procedure, with some reprogramming of existing funds to insure proper allocation within line items, allows those programs with funding deficiencies to continue without disruption."

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The remaining \$915 million of the predicted deficit applies to the fiscal year 1975 programs, and is discussed in the Deputy Secretary's letter as follows:

"The funding deficit in the Fiscal Year 1975 program presents a somewhat different problem, inasmuch as only one ship from that program is currently under a contract - the Fleet Ballistic Missile Submarine Tender conversion. Unless allowed some departure from the practice of having all funds for predicted escalation and inflation in hand prior to contract award, the Navy would be unable to contract for the 22 badly needed new ships approved by the Congress in Fiscal Year 1975. Such a situation is highly undesirable from both a national defense and economic standpoint. An alternative which would reduce ship programs by allowing award of only so much program as each line item appropriation can support on a fully funded basis would also impact severely the Navy's urgently needed fleet modernization effort. It could also result in one contract default (DD 963, January 15, 1975) and would cause two missed contract options (DLGN 41/42, February 1, 1975 and TRIDENT, February 28, 1975). The resulting program disruption, cancelled ship procurements, legal implications on subsequent claims, and higher costs would not be in the government's best interest.

"It is imperative that we find a solution. I think you will agree that there is no alternative but to proceed with a plan that will maintain a viable shipbuilding program and avoid the penalties associated with loss of options or contract default. It has been our policy to have all required funding in hand, including estimates of inflation, prior to contract award. However, because of the extraordinary circumstances and the unforeseen inflation, we are contemplating a procedural adjustment which will permit the Department to proceed with construction of ships already authorized by the Congress. I intend therefore to keep you advised and take timely action to authorize the Navy to implement the Fiscal Year 1975 shipbuilding program requiring that each contract and obligational document be fully funded except for escalation estimates beyond Fiscal Year 1975. The additional funding requirements will be included in the Fiscal Year 1976 SCH budget."

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Your letter to us presents the following matters for consideration in terms of the DOD proposal:

"Of immediate concern to the Committee is the Secretary's proposal to award fiscal year 1975 contracts for certain ships, knowing full well that funds requested and made available by the Congress are insufficient by \$915 million. This proposal not only violates the full-funding concept, which has been in existence since fiscal year 1961, but it raises certain questions, which may be legally germane, as to the propriety of this action in light of the line item authorization and appropriation by Congress in the fiscal year 1975 Shipbuilding and Conversion, Navy, program. The purpose of the line item approach was to bring greater Congressional control over funds authorized and appropriated for the Navy shipbuilding program. This is the only Defense program which has received line item authorization and appropriation.

"If we follow the Department's proposal, our Committee would be in effect committing Congress in advance to authorize and appropriate \$915 million in fiscal year 1976 in order to complete the funding of fiscal year 1975 ships. The only other alternative available to Congress in fiscal year 1976 would be to cancel certain fiscal year 1975 ships already awarded on contracts and partially built, increasing the funding deficit by the additional termination costs attendant thereto, in order to fully fund the highest priority ships in the fiscal year 1975 program."

Since receipt of your letter we have on several occasions informally discussed the DOD proposal, and possible legal issues in connection therewith, with officials of that Department and the Navy Department. In the brief time period available for our response, we have not attempted to undertake a detailed factual review of the DOD proposal or the presumably numerous and varied procurement actions which it would entail. Accordingly, our response is necessarily limited to a general conceptual analysis of the proposal on the basis of the Deputy Secretary's letter to you and additional representations made to us in the course of our informal discussions with DOD and Navy officials.

As you point out and the Deputy Secretary specifically states, the DOD proposal would constitute a departure from the "full funding

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policy" applicable to military procurement programs such as Navy shipbuilding. The premise of the full funding policy, as developed by DOD and congressional committees, is that funding for procurement programs should be requested and provided at the initial stage of procurement actions on the basis of the entire estimated cost of the procurement, irrespective of the anticipated fiscal year timing and rate of obligations. Full funding is to be distinguished from an "incremental funding" approach whereby appropriations for long-term undertakings are requested and provided in fiscal year installments limited in amount to the anticipated obligations necessary during particular fiscal years. See our report to your Committee dated February 17, 1969, B-165069, entitled "Application of the Full Funding Concept and Analysis of the Unobligated and Unexpended Balances in Selected Appropriations," at 3-14. The full funding policy is the subject of DOD Directive No. 7200.4 (October 30, 1969), and is described in section III-A thereof, in part, as follows:

"General. Full funding is the term used to describe the principle which has been applied by the Congress in providing funds for the Department of Defense programs which are covered within the Procurement title of the yearly appropriation acts. * * * The objective is to provide funds at the outset for the total estimated cost of a given item so that the Congress and the public can clearly see and have a complete knowledge of the full dimensions and cost when it is first presented for an appropriation. In practice, it means that each annual appropriation request must contain the funds estimated to be required to cover the total cost to be incurred in completing delivery of a given quantity of usable end items, such as aircraft, missiles, ships, vehicles, ammunition, and all other items of equipment. This policy is also a requirement of the Bureau of the Budget as expressed in their Circular No. A-11, "Preparation and Submission of annual budget estimates."

The Deputy Secretary's letter to you states that application of the full funding policy to the 1975 shipbuilding programs here involved would preclude contracting for 22 ships in view of the current predicted costs for escalation and inflation. It is proposed, therefore, to proceed with the 1975 programs as scheduled without requiring that contracts and obligational documents be full funded for escalation estimates beyond fiscal year 1975. Additional funding would then be requested for fiscal year 1976 to meet increased costs for future fiscal years.

As suggested in your letter, implementation of the DOD proposal would, as a practical matter, limit congressional options. Nevertheless, we do not believe that this proposed departure from full funding is legally objectionable as such. The determinative factor here, in our view, is that the full funding policy does not constitute a statutory requirement. It is, instead, a policy developed between DOD and congressional committees and formalized by a DOD Directive. The full funding policy is in this regard similar to formalized but nonstatutory policies which govern reprogramming actions within appropriations for the military departments. Moreover, section V of DOD Directive 7200.4 in effect provides for exceptions from the full funding policy upon specific approval by the Secretary of Defense. We do not, of course, question the validity or appropriateness of the full funding policy; nor does the Deputy Secretary's letter to you indicate any objection to or abandonment of this policy except as stated in the instant proposal. Rather, the thrust of his letter, and of informal representations made to us, is that a dilemma exists with respect to the shipbuilding programs in which a departure from full funding is the least objectionable alternative.

As noted previously, we assume that under the DOD proposal a number of procurement actions would be initiated in fiscal year 1975 pursuant to the various line item shipbuilding programs. Procurements for certain program elements might still be capable of completion within the limits of appropriations now available, although the total cost of the entire program is not fully funded under current estimates. While initiation of such procurement actions would depart from the full funding policy, this result is not, in our view, legally objectionable for the reasons stated above. However, we believe that serious legal issues would arise to the extent that the DOD proposal might include initiation of procurement actions during fiscal year 1975 which of themselves involve predicted funding deficits. This would be the case with respect to any procurement action which, under current estimates for escalation and inflation, would cause the Government to incur obligations exceeding the amount of appropriations now available for such procurement. Of concern here is the so-called "Antideficiency Act," R.S. § 3679, as amended, 31 U.S.C. § 665(a) (1970), which provides:

"No officer or employee of the United States shall make or authorize an expenditure from or create or authorize an obligation under any appropriation or fund in excess of the amount available therein; nor shall any such officer or employee involve the Government in any contract or other obligation, for the payment of money for any purpose, in advance of appropriations made for such purpose, unless such contract or obligation is authorized by law."

Also of concern is R.S. § 3732, as amended, 41 U.S.C. § 11 (1970), which provides, with exceptions not here relevant:

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"(a) No contract or purchase on behalf of the United States shall be made, unless the same is authorized by law or is under an appropriation adequate to its fulfillment * * *."

Our informal discussions with DOD and Navy officials concerning the applicability of the cited statutory provisions to the instant proposal have focused upon the nature and extent of obligations under the procurement actions to be initiated in fiscal year 1975. It is our understanding that some of these procurement actions are in the nature of fixed price incentive contracts, having negotiated "target" and "ceiling" prices but providing for subsequent determination of actual costs and price. See ASPR § 3-404.4 (1 July 1974). We have also been advised that in the case of such procurement actions the target price would be the amount recorded against the applicable appropriation for purposes of section 1311 of the Supplemental Appropriation Act, 1955, as amended, 31 U.S.C. § 200 (1970), which provides in part:

"(a) * * * no amount shall be recorded as an obligation of the Government of the United States unless it is supported by documentary evidence of--

"(1) a binding agreement in writing between the parties thereto, including Government agencies, in a manner and form and for a purpose authorized by law, executed before the expiration of the period of availability for obligation of the appropriation or fund concerned for specific goods to be delivered, real property to be purchased or leased, or work or services to be performed * * *."

The position taken by DOD officials in our informal discussions is that, since the amount of recorded obligations on a "target price" basis would not exceed the amount of appropriations currently available, the initiation of such proposed procurement actions will not violate either 31 U.S.C. § 665(a) or 41 U.S.C. § 11(a), supra, which statutory provisions are viewed as substantively the same. Moreover, it is said that no violation of 31 U.S.C. § 665(a) will occur in the future because if Congress appropriates the additional funds to be requested, the deficits now predicted for future fiscal years will be made up. If, on the other hand, the Congress fails to provide additional funding, procurements would be terminated before predicted deficits accrue.

In a 1955 decision to the Secretary of Defense, 34 Comp. Gen. 418, we approved the recording of obligations under contracts of the type

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described above on a target price or similar basis for purposes of section 1311 of the Supplemental Appropriation Act, supra. We observed with reference to a proposed DOD Directive to this effect, 34 Comp. Gen. at 420¹21:

"* * * Subsection (b) [of the proposed Directive] provides that under fixed-price contracts with escalation, price redetermination, or incentive provisions, obligations shall be recorded for the amount of the fixed price stated in the contract, or the target or billing price in the case of a contract with an incentive clause, and that the amount so recorded shall be increased or decreased to reflect price revisions at the time that such revisions are made or determined pursuant to provisions of the contract. It is assumed that none of these contracts with incentive clauses will have both a target price and a billing price. While we have no objection to the recording of obligations upon that basis, such practice might well result in a violation of section 3679, Revised Statutes, as amended, 31 U.S.C. 665, unless appropriate safeguards are provided either in this proposed Directive or in the administrative regulations issued under the latter act with the concurrence of the Director of the Bureau of the Budget. Such safeguards normally would consist of administrative reservations of sufficient funds to cover at least the excess of the estimated increases over the decreases."

In view of our 1955 decision, we do not here question the DOD practice of recording obligations on a "target price" or similar basis in order to comply with section 1311. However, consistent with the clear implication in the above-quoted excerpt from our decision, we do not believe that the proper recording of obligations under section 1311 is sufficient of itself to foreclose possible violation of 31 U.S.C. § 665(a) and 41 U.S.C. § 11. Accordingly, it is still necessary to examine procurement actions of the type described above in terms of the latter statutes.

We have on many occasions recited the generally accepted purport of 31 U.S.C. § 665(a) and 41 U.S.C. § 11. For example, we stated in Part, at 42 Comp. Gen. 272, 275 (1962):

"These statutes evidence a plain intent on the part of the Congress to prohibit executive officers, unless otherwise authorized by law, from making contracts

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involving the Government in obligations for expenditures or liabilities beyond those contemplated and authorized for the period of availability of and within the amount of the appropriation under which they are made; to keep all the departments of the Government in the matter of incurring obligations for expenditures, within the limits and purposes of appropriations annually provided for conducting their lawful functions, and to prohibit any officer or employee of the Government from involving the Government in any contract or other obligation for the payment of money for any purpose, in advance of appropriations made for such purpose; * * *

"In 21 Op. Atty. Gen. 244, 248, the Attorney General pointed out that the object of these statutes was to prevent executive officers from involving the Government in expenditures or liabilities beyond those contemplated and authorized by the law-making power. * * *"

As noted previously, DOD officials maintain (1) that the recording of section 1311 obligations in the amount of a target or similar price, where applicable, would be the only transaction now relevant with respect to 31 U.S.C. § 665(a) and (2) that any potential for future deficits subject to the statutory prohibition would be avoided whether or not additional funds are provided. In 42 Comp. Gen. 272, *supra*, we considered a position somewhat similar to DOD's first argument, involving in that case a contract by the Air Force Department to procure services extending beyond the one-year appropriation under which the contract was made but providing for the furnishing of services only as orders were placed. We stated in that case, *id.* at 277:7

"The Department justifies the continuing liability terms of the contract on the basis that such liability does not result in appropriation obligations within the meaning of section 1311 unless and until orders are issued under future available appropriations. Conceding that the integrity of the available appropriations would be maintained, there is to be considered the fact that the applicable restrictions of the Revised Statutes prohibit contractual agreements under fiscal year appropriations which involve the Government beyond such period of availability not only in appropriation obligations, but any other obligation or liability which may arise thereunder and ultimately require the expenditure of funds. * * *"

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FROM: ASSISTANT
COMPTROLLER
GENERAL
OF THE UNITED STATES

TO: ASSISTANT
COMPTROLLER
GENERAL
OF THE UNITED STATES

These observations seem applicable as well to fixed price incentive or similar procurement actions under the instant DOD proposal. However, even assuming arguendo that such procurement actions might not involve present transactions prohibited by 31 U.S.C. § 665(a), they would appear to be inconsistent with 41 U.S.C. § 11, which by its terms prohibits, inter alia, the making of a contract under an appropriation which is not adequate to its fulfillment. We perceive of no reason why current agency cost estimates would not constitute an appropriate standard for determining the applicability of 41 U.S.C. § 11.

For the reasons stated, we believe that the instant DOD proposal is technically subject to legal objection if, and to the extent that, procurement actions initiated during fiscal year 1975 involve, by current estimates, costs exceeding amounts presently available therefor. We again point out that our analysis of the DOD proposal is largely conceptual. Thus we do not know whether or to what extent procurement actions of the type described would actually take place. Also, it should be recognized that the legal problem which we point out does not in any event relate to actual expenditures in excess of appropriations, since we understand that sufficient funds are presently available to cover termination costs should termination of the contracts involved become necessary after congressional action on the appropriation request. In view of these considerations, and the fact that the DOD proposal has been presented to cognizant congressional committees, our Office would not take exception to implementation of the Department's proposal.

We hope that the foregoing analysis will be of assistance in your consideration of the DOD proposal.

Sincerely yours,

(SIGNED) ELMER B. STAATE

Comptroller General
of the United States

FROM: ASSISTANT
COMPTROLLER
GENERAL
OF THE UNITED STATES

TO: ASSISTANT
COMPTROLLER
GENERAL
OF THE UNITED STATES