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EXTENSION OF RENEGOTIATION ACT OF 1951

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Mr. LONG of Louisiana, from the Committee on Finance, submitted the following

REPORT

[To accompany H.R. 13431]

The Committee on Finance, to which was referred the bill (H.R. 13431) to extend the Renegotiation Act of 1951, having considered the same, reports favorably thereon without amendment and recommends that the bill do pass.

I. SUMMARY

The Renegotiation Act of 1951, as amended, which authorizes the Government to recapture excessive profits on certain Government contracts and subcontracts expires as of June 30, 1966. H.R. 13431 extends the act for 2 years, or until June 30, 1968.

II. GENERAL STATEMENT

Present law.—The Renegotiation Act of 1951, in general, provides that the Renegotiation Board is to review the total profit derived by a contractor during a year from all of his renegotiable contracts and subcontracts in order to determine whether or not this profit is excessive. The Board is empowered to eliminate those profits found to be excessive in accordance with certain statutory factors. Thus, the renegotiation occurs not with with respect to individual contracts but with respect to all renegotiable contracts and subcontracts of a contractor during a year. These contracts vary in form from cost-plus-fixed-fee to firm fixed-price contracts. Some may be prime contracts, while others are subcontracts, and they may be concerned with many different services and products. With respect to any given year they may also reflect only partial payments made on the contracts.

For purposes of renegotiation, profits generally are defined and determined in much the same way as for tax purposes. This similar-

ity is also reflected in that provision is made in renegotiation for a 5-year loss carryforward, as well as the offsetting of losses and profits on different contracts within the year.

The act provides, in general terms, that the Renegotiation Board in determining whether profits are excessive is to give favorable recognition to the efficiency of the contractor with particular regard to attainment of quantity and quality products, reduction of costs and economy. The Board must also consider the reasonableness of costs and profits, the net worth (with particular regard to the amount and source of public and private capital employed), the extent of the risk assumed, the nature and extent of the contribution to the defense effort, and the character of the business. Thus, in effect, the Board in its judgment must consider all of these factors, and the producer, where these factors are present to the greatest extent (e.g., is most efficient or makes the greatest contribution to the defense effort), is permitted to retain more profit than the producer who satisfies these factors to a lesser extent. This gives assurance that the act will not impede the cost reduction program of the Defense Department with its emphasis on the use of incentive contracts.

Various types of contracts are excluded from the act; some on a mandatory and others on a permissive basis. The mandatory exemptions include contracts with a State, local, or foreign government, those dealing with certain agricultural commodities, those dealing with mineral and related products, those with certain regulated common carriers, and receipts and accruals for standard commercial articles or services.

Reasons for extension.—Under existing world conditions, the continuation of the Renegotiation Act is in the national interest. The deterrent effects of renegotiation on overpricing have long been recognized. Not to continue renegotiation at this time would encourage price rises and larger Government spending in the area of defense contracts. This is a result which none of us desires.

The renegotiation process has saved large amounts for the Government. In the fiscal year 1965 alone, directly or indirectly renegotiation resulted in refunds or price reductions of over $32 million and since the inception of the Renegotiation Board in 1951 has resulted in savings of over $2 billion. Of course, in addition to this savings, the renegotiation process has had a deterrent effect on overpricing on Government contracts because of the realization that renegotiation is backstopping the allowable profits. The savings referred to above include both refunds made as the result of determinations of excessive profits by the Renegotiation Board and also voluntary refunds and price adjustments made, or justified, by the companies because of the existence of renegotiation. The breakdown between these two categories is as follows:

[In millions]

	Fiscal year 1965	Cumulative total from 1961 through 1965
1. Refunds arising from determinations of excessive profits made by Renegotiation Board	$16.1	$911.9
2. Voluntary refunds and price reductions reported by contractors	16.4	1,246.6
3. Total	32.5	2,158.5

The bulk of military procurements must, under present conditions of necessity, be made on the basis of negotiated prices, since the product or service being procured usually does not have a market price to guide the negotiators. Thus, renegotiation is essential, in the absence of competitive norms which make it possible to assess in advance the probably profit outcome.

In addition, price competition in substantial areas of Government procurement under present conditions is weak or nonexistent, since in the procurement of large weapons and space systems the contractor winning a research and development contract is usually the only one capable of performing on follow-up contracts. There are a number of other factors also which recommend the desirability of continuing the Renegotiation Act under present conditions. Many of the major Government contractors work with Government plant, equipment, and progress payments which makes it difficult to evaluate the prices which should be paid to them in view of their extensive use of Government capital. Moreover, in the case of many new products and systems, cost estimates involve a high degree of uncertainty and, in many other cases, negotiated prices may be affected by the relative negotiating skill of the Government and private negotiators. The greater knowledge of technology involved in this area tends to give the private negotiators an advantage in this respect.

In addition, since Government contracts are negotiated on a contract-by-contract basis with many of these contracts extending over several years, negotiators cannot be certain that the profits of a contractor in any particular year will be reasonable, except through the renegotiation process.

Your committee agrees with the Committee on Ways and Means of the House that in view of the extent of our defense effort at the present time, the Renegotiation Act should be extended for a 2-year period, from June 30, 1966, to June 30, 1968. This is in place of the 6-year period initially recommended by the administration. The Renegotiation Board has advised the Committee on Finance that in the interest of speedy passage of this bill it approves the 2-year extension. The 2-year extension will accord Congress the opportunity to reexamine the need for the renegotiation process in the relatively near future.

III. APPENDIX—STATISTICAL DATA WITH RESPECT TO OPERATION OF RENEGOTIATION BOARD

In fiscal 1965, 3,315 filings of contractors, other than brokers or manufacturers' agents, were screened These filings represented $34.8 billion of renegotiable sales. The comparable figure for fiscal 1964 was $39.3 billion.

The composition of renegotiable sales, as disclosed in contractors' filings, is set forth below:

Renegotiable sales reviewed in fiscal 1965, by contract type

[In millions of dollars]

	Total		Cost plus fixed fee		Fixed price		Other	
	Amount	Percent	Amount	Percent	Amount	Percent	Amount	Percent
Prime contracts	$26,311	75.6	$8,635	32.8	$8,679	33.0	$8,996	34.2
Subcontracts	8,462	24.3	1,491	17.6	6,203	73.3	767	9.1
Management fees, etc	25	0.1	4	16.0	10	40.0	11	44.0
Total	34,798	100.0	10,130	29.1	14,893	42.8	9,774	28.1

NOTE: Details do not add to totals because of rounding.

Of the 3,315 nonagent contractors whose filings were reviewed in fiscal 1965, 2,291, with renegotiable sales of $30 billion, showed a profit of $1.3 billion; and 1,024, with renegotiable sales of $4.8 billion, showed a loss of $291 million. Details are given in the tables below:

TABLE 1.—*Sales and profits of companies reporting net renegotiable profits*

[In millions of dollars]

	Renegotiable sales		Renegotiable profits	
	Amount	Percent of total	Amount	Percent of total
Cost plus fixed fee	$9,373	31.3	$296	22.2
Fixed price	11,322	37.8	559	41.9
Other	9,258	30.9	478	35.9
Total	29,953	100.0	1,333	100.0

TABLE 2.—*Sales and profits of companies reporting net renegotiation losses*

[In millions of dollars]

	Renegotiable sales		Renegotiation losses	
	Amount	Percent of total	Amount	Percent of total
Cost-plus-fixed-fee	$758	15.6	$12	4.1
Fixed price	3,571	73.7	254	87.3
Other	516	10.7	25	8.6
Total	4,845	100.0	291	100.0

It should be noted that profit and loss figures in the above tables are net figures, reflecting the presence of both profitable and loss contracts in individual cases. Such figures are based on cost allowances

required for renegotiation purposes, which differ in significant respects from costs allowable for procurement purposes.

In fiscal 1965 the Board made 52 determinations of excessive profits totaling $16,146,803; and, as of June 30, 1965, the Board had also made, but had not yet incorporated in agreements or orders, additional refund determinations in the amount of $3,369,697. From its inception through June 30, 1965, the Board made 3,716 determinations of excessive profits totaling $911,941,861.

Also in fiscal 1965, contractors reported to the Board voluntary refunds and price reductions in the amount of $16,402,517. This brought the total of such refunds and price reductions reported since the inception of the Board to $1,246,553,691. These refunds and price reductions are wholly voluntary, and are to be distinguished from price reductions made under the terms of price-redeterminable contracts.

The determinations of excessive profits in the amount of $911,941,861 are after State income tax adjustments but before the deduction of credits for Federal income and excess profits taxes. As of June 30, 1965, total net recoveries by the Government after such tax adjustments and credits amounted to $348,083,095. Of this amount, the sum of $8,823,865 resulted from determinations made during fiscal 1965. Net recoveries by the Government arising from determinations of excessive profits are covered into the Treasury as miscellaneous receipts. They do not revert to departmental funds.

Of the 52 determinations of excessive profits made by the Board during fiscal 1965, 41 resulted in agreements between the Board and the contractors involved; 11 resulted in the issuance of unilateral orders. As the table below indicates, the Board made 3,716 determinations of excessive profits through June 30, 1965, and 3,346, or 90.0 percent of such determinations, were agreed to by contractors. These agreements accounted for $674 million, or 73.9 percent, of the total amount of excessive profits determined. Details are as follows:

REFUND DETERMINATIONS: AGREEMENTS AND UNILATERAL ORDERS

TABLE 3.—*Number of determinations*

	Total	By agreement	Percent of total	By order	Percent of total
Through June 30, 1964	3,664	3,305	90.2	359	9.8
Fiscal year 1965	52	41	78.8	11	21.2
Total	3,716	3,346	90.0	370	10.0

TABLE 4.—*Amount of determinations*

[In millions of dollars]

	Total	By agreement	Percent of total	By order	Percent of total
Through June 30, 1964	$895.79	$663.27	74.0	$232.52	26.0
Fiscal year 1965	16.15	10.69	66.2	5.45	33.8
Total	911.94	673.97	73.9	237.97	26.1

NOTE.—Details do not add to totals because of rounding.

When a contractor does not agree with a determination of excessive profits, the Board issues a unilateral order directing the contractor to refund to the Government the amount of excessive profits involved.

Of the 52 determinations of excessive profits made by the Board during fiscal 1965, 11 resulted in unilateral orders. Under the act, contractors have a right to petition the Tax Court of the United States forre a determination. Three of the eleven unilateral orders issued by the Board during the fiscal year were appealed to the court and, as of June 30, 1965, the time for appealing two orders had not expired.

From the inception of the Board through June 30, 1965, 136 of the 370 unilateral orders issued by the Board were appealed to the Tax Court. Details are set forth in the following table:

Refund determinations taken to the Tax Court as of June 30, 1965

Fiscal year of Board determination	Number of determinations	Amount of determinations	Fiscal year of Board determination	Number of determinations	Amount of determinations
1953	0	0	1961	10	$8,497,330
1954	7	$310,119	1962	3	344,172
1955	12	5,610,285	1963	8	5,372,151
1956	16	12,678,321	1964	5	8,979,225
1957	25	36,693,939	1965	3	1,946,447
1958	17	31,506,588			
1959	11	18,743,297	Total	136	157,934,303
1960	19	27,252,429			

During fiscal 1965, the Tax Court disposed of 19 cases. As is shown below, as of June 30, 1965, the court had disposed of a total of 91 cases, leaving 45 pending on that date.

Renegotiation cases in the Tax Court

	Total filed	Dismissed	Closed by stipulation	Closed by redetermination	Pending
Through June 30, 1964	133	32	19	21	61
Fiscal year 1965	3	7	10	2	(16)
Total as of June 30, 1965	136	39	29	23	45

The aggregate amount of refund determinations involved in the 45 pending cases is $40,890,663.

The 91 cases concluded in the Tax Court as of June 30, 1965, involved Board determinations of excessive profits in the amount of $134 million. The court upheld the Board's determination in 51 of the 91 cases reviewed; in 5 cases the determinations were increased and in 35 they were decreased.

IV. CHANGES IN EXISTING LAW

In compliance with subsection 4 of rule XXIX of the Standing Rules of the Senate, changes in existing law made by the bill are shown as follows (existing law proposed to be omitted is enclosed in black brackets, new matter is printed in italic; existing law in which no change is proposed is shown in roman):

RENEGOTIATION ACT OF 1951

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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.

(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 subcontractor 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, 1966] *June 30, 1968.*

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