

DOCUMENT RESUME

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National Academy of Sciences: Applicability of Armed Services Procurement Regulations to Independent Research and Development Reimbursement. B-58911. August 1, 1977. 7 pp.

Decision re: President, Trans Country Van Lines, Inc.; by Robert F. Keller, Deputy Comptroller General.

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Contact: Office of the General Counsel: General Government Matters.

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Authority: National Academy of Sciences Charter Act, sec. 3 (36 U.S.C. 253). Economy Act (31 U.S.C. 686, 686(a)). B-4252 (1939). B-19556 (1941). 39 Comp. Gen. 71. 39 Comp. Gen. 391, 392. 56 Comp. Gen. 275. A.S.P.R., sec. XV, part 3. A.S.P.R. 7-103.12. A.S.P.R. 15-205.35. A.S.F.R. 15-205.35(d) (1-2).

The President of the National Academy of Sciences requested a decision on the recoverability of independent research and development costs incurred in its contract work for the Navy. Such expenses are recoverable to the full extent compatible with Federal procurement policies to which the Academy agreed to be bound. (Author/DJM)

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DECISION



**THE COMPTROLLER GENERAL
OF THE UNITED STATES**
WASHINGTON, D. C. 20548

FILE: B-58911

DATE: August 1, 1977

MATTER OF: National Academy of Sciences--Applicability
of Armed Services Procurement Regulations
to Independent Research and Development

DIGEST: Reimbursement.

National Academy of Sciences is entitled to recovery from Office of Naval Research, Department of Defense, of independent research and development (IR&D) costs to full extent compatible with Armed Services Procurement Regulations to which it agreed by contract to be bound. Section 3 of Academy's Charter Act, 36 U.S.C. § 253, requiring recovery of actual expenses, does not preempt Federal procurement requirements so as to permit open-ended recovery of IR&D costs by the Academy.

This decision is in response to a request from the President, National Academy of Sciences (NAS) for our consideration of certain problems which have arisen concerning the treatment of "independent research and development" (IR&D) costs incurred by the NAS in relation to its Government contract work in fiscal year 1975.

The Office of Naval Research (ONR), Department of the Navy, contracted with the NAS on February 1, 1976, (Basic Agreement # N00014-76-A-0013) for certain basic and applied research, studies, and analysis on a cost reimbursement basis. The contract incorporated by reference or set forth in full all the clauses usual in Government procurements. Among these is clause A-29 which specifies that the allowability of costs is to be determined by the terms of the contract and Part 3 of Section XV of the Armed Services Procurement Regulations (ASPR) in effect on the date of the contract. Also incorporated by reference into the contract is the standard "disputes clause" required by Section 7-103.12 of ASPR, which provides for resolution of questions of fact arising under the contract by the contracting officer, subject to the right of the contractor to appeal to the agency head or his representative.

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(Appendix A of ASPR establishes the Armed Services Board of Contract Appeals (Board) as the designated representative).

Under Armed Services Procurement Regulation § 15-205.35, which governs the allowability of IR&D costs under contracts subject to ASPR, contractors which received IR&D (and bidding and proposal expense) payments from the Defense Department in excess of \$2 million for the prior fiscal year are required to negotiate advance agreements which establish a ceiling for allowability of IR&D costs for the following fiscal year. ASPR § 15-205.35(d)(1). For contractors which did not receive such payments in excess of \$2 million, ASPR § 15-205.35(d)(2) provides for application of a formula to place a ceiling on allowable IR&D costs. However, it is further provided that, in lieu of applying the formula:

"* * * at the discretion of the contracting officer, an advance agreement may be negotiated when the contractor can demonstrate that the formula would produce a clearly unequitable cost recovery. The requirements of (d)(1) above [for contractors having prior year payments exceeding \$2 million] are not mandatory for such agreements." Id.

Apparently the Academy's IR&D costs for fiscal year 1975 qualified for the formula specified in ASPR § 15-205.35(d)(2) and were not determined by the contracting officer to be subject to an advance agreement for modification of the formula. Application of the formula was accomplished through an audit determination by the Defense Contract Audit Agency, and resulted in a disallowance of \$93,800 of the Academy's total of \$156,837 in IR&D costs incurred for fiscal year 1975.

In a July 8, 1976, letter commenting on the audit findings, the Academy's Comptroller expressed "no difficulty with the mathematics and the application of the formula to the numbers for our fiscal year ended June 30, 1975." However, he stated the Academy's position that it "should not be bound by the formula as it is described in ASPR." This position was further elaborated in the instant NAS submission as follows:

"* * * the procurement regulations were designed primarily to guide the Government's arrangements with industrial contractors that have histories of extended cost experience for IR&D and concerning which the Government's concern is to limit, by formula, the build-up of such costs. With no record of a historical base of such activities on which to build, the Academy finds itself hampered by these

formula restrictions. And since the Academy operates without fee or profit, there are no accumulated reserves from which such costs can be paid, or retroactive disallowances absorbed.

"The service of the Academy to the Government over the years has amply proved the soundness and wisdom of the concept that led to the establishment of the Academy in 1863. Its independence, financial and intellectual, must be maintained if the Academy is to continue to render the objective evaluations and responses that the legislative and executive branches of our Government are calling for on an ever increasing scale. We believe that the Congressional Charter authorized the Academy to recover all of its costs, without regard to any formula in the procurement regulations designed for application to contractors of quite different character provided, of course, that such costs are reasonable, necessary and appropriate for the performance of the Academy's services to the Government. The Academy has not requested and does not now request any sum in excess of its actual costs. But the Academy does believe that the concept of actual costs properly includes those aspects of its activities which are related to maintaining its readiness to respond fully, effectively and expeditiously to its Government."

The NAS suggests that the Federal procurement requirements concerning recovery of IR&D costs should not apply to the Academy in view of the provision for reimbursement of "actual expense[s]" contained in section 3 of the Academy's Charter Act, 36 U.S.C. § 253 (1970). Section 3 provides in this regard that the Academy--

"* * * shall, whenever called upon by any department of the Government, investigate, examine, experiment, and report upon any subject of science or art, the actual expense of such investigations, examinations, experiments, and reports, to be paid from appropriations which may be made for the purpose, but the academy shall receive no compensation whatever for any services to the Government of the United States."

In other words, NAS asks that we recognize the unique charter of the Academy "by affirming its right to recover full legitimate costs without regard to the limitations imposed by formula in current procurement regulations."

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There appears to be no substantial question of fact which, of course, would be for resolution in accordance with the procedures agreed to by both parties under the Disputes Clause. The sole question with which this Office is concerned is whether the contract provision for determination of questions pertaining to allowability of costs in accordance with ASPR regulations--a provision to which both parties also agreed--should be set aside as unenforceable because it is contrary to law.

Several decisions of our Office have addressed the "actual expense" provision of section 3 of the Academy's Charter Act. In B-4252, June 21, 1939, we held that Federal agencies cannot contract with the Academy for a fixed consideration which is not necessarily confined to reimbursement of actual expenses. On the other hand, our decisions at 39 Comp. Gen. 71 and 391 (1959) allowed the Academy's claim for recovery of costs exceeding the amount of a fixed price contract where the contract price was insufficient to cover the Academy's actual costs. We suggested that future contracts should "limit the consideration to be paid thereunder to reimbursement of the Academy's actual expenses, with a limitation if desired, on the maximum amount payable under the contracts." 39 Comp. Gen. at 392.

We have also recognized that section 3 of the Charter Act contemplates in appropriate cases recovery by the Academy of "travel, subsistence, stenographic assistance, employment of experts, and incidental expenses." Thus our decision at B-19556, August 28, 1941, concluded that the Academy could not impose a flat 10 percent surcharge on its Government contracts for such expenses, but went on to observe:

"The law referred to apparently contemplated that the Academy would be reimbursed for such extra expenses, as distinguished from regular or normal expenses to which the Academy is subjected by reason of making investigations, etc., for the Government. In other words, the apparent intent of the law is that the funds of the Academy are not to bear an additional burden solely because of the performance of services for some department or establishment of the Government. Obviously, there is no authority for reimbursing the Academy for any part of its normal or regular expenses merely because it was doing work for a department or establishment of the Government which work necessarily participated in the benefits derived from such expenses. However, where it can be shown that the work called for under an agreement

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with a department or establishment of the Government required the Academy to increase its normal overhead or other general expenses. The amount of such increase would constitute a part of the actual expense apparently contemplated by the law herein considered and for which the Academy is entitled to reimbursement. It is realized that in some cases it may not be possible to ascertain with exactness the amount of the increase which resulted solely from the work for the Government and in such cases a reasonable approximation of the amount may be accepted as a basis for reimbursement provided it be clearly established that some increase in such overhead or other general expenses actually and necessarily did result solely from the work for the Government. * * *

We have also addressed the concept of actual cost reimbursement in the somewhat analogous context of the so-called "Economy Act," 31 U.S.C. § 686 (1970), which applies generally to intra- and inter-agency transactions for the provision of goods or services. Under 31 U.S.C. § 686(a), such transactions are to be reimbursed "on the basis of the actual cost * * * as may be agreed upon by the departments, establishments, bureaus, or offices concerned * * *." In 56 Comp. Gen. 275 (1977), we held that the Economy Act requirement for "actual cost" reimbursement--

"* * * is only achieved when all significant elements of cost are recognized and recovered in any transaction under that section. If overhead expense is significant, then like other elements of costs it should be recognized and recovered. The recognition of these costs is necessary so that the performing agency and the ordering agency will know the costs of their operations. Also, the requirement that prices of the performing agency be based on full costs affords the ordering agency a financial measurement for determining whether to deal with one or another Government agency, procure the services elsewhere, or forego the undertaking entirely. * * * Moreover, as noted in the submission, this would make the Federal reimbursement procedures under the Economy Act consistent with the practices and policies applicable to provision of goods and services to non-government recipients

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under the user charge statute, 31 U.S.C. § 483a, which specifically requires the provider agency to take into account both direct and indirect costs in prescribing fees and charges." Id. at 277-78.

Our 1977 decision also elaborated upon the concept of actual cost as follows:

"We have held that 'actual cost' as used in the statute includes overhead and other indirect expenses. In 32 Comp. Gen. 479, at 480 (1953), we said:

'This language [of section 686(a)] was discussed in 22 Comp. Gen. 74 and it was there held that the statute required reimbursement to be made "on the basis of the actual cost of performing the service 'as may be agreed upon' by the agencies concerned." Such cost was construed in the said decision to include overhead or indirect costs--"items which commonly are recognized as elements of cost, notwithstanding, such items may not have resulted in direct expenditures * * *." Also, it was stated therein that "the question as to the 'proper adjustments' to be made as reimbursement for services rendered under the terms of the applicable statute is one primarily for administrative consideration to be determined by agreement between the agencies concerned."

'The statute as thus construed clearly establishes the principle that payment for the services shall be upon a cost basis and such principle is binding upon both the procuring and requisitioned agency in fixing the charges to be billed and paid. * * *'" Id. at 276.

Applying the foregoing considerations to the problems raised, we believe that the Academy is entitled to recovery of IR&D costs in connection with its Government work to the full extent compatible with the Federal procurement policies to which it agreed to be bound. Section 3 of the Academy's Charter Act does not, in our view, preempt the Federal procurement requirements so as to permit open-ended recovery of IR&D by the Academy. As noted previously, our decisions concerning section 3 recognize that some contractual limits may be placed on the Academy's cost recovery. Moreover, it seems to us that the procurement regulations are sufficiently flexible by their terms to accommodate the Academy's situation and to comply with the actual expense reimbursement provision of the Charter Act.

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It appears that the Academy's basic problem centers upon use of the ASPR formula for determination of allowable IR&D costs. However, as explained above, ASPR § 15-205.35(d)(2) specifically authorizes the negotiation of advance agreements for IR&D in lieu of the formula stated therein "where the contractor can demonstrate that the formula would produce a clearly inequitable cost recovery."

Apparently the original decision by the contracting officer to apply the formula in lieu of a negotiated overhead rate for fiscal year 1975 has now been overturned. We have been advised by the Acting Director, Defense Research and Engineering, that ONR and NAS have entered into negotiations for final overhead rates for fiscal year 1975 and will use the same approach in finalizing overhead rates for fiscal year 1976. Further, the Acting Director states:

"* * * the DoD will attempt to negotiate an advance agreement for IR&D and B&P expenses beginning with FY 1977. Such an agreement should preclude similar problems in the future."

In summary, we cannot agree that the procurement regulations do not apply but we believe that the difficulties presented can be resolved by application of the negotiation alternative provided by the ASPR.


Deputy Comptroller General
of the United States