Critical Thinking
A Monthly Guest Column

Contractors Caught in the Cross Fire of Appropriations Law

By
David Z. Bodenheimer

The Anti-Deficiency Act (Act)[1] represents the weapon of choice with which Congress defends its power of the purse against raids by marauding executive agencies. To this end, the Act bristles with penalties — ranging from adverse personnel actions to criminal penalties — for any executive personnel that spend appropriated funds contrary to Congressional direction governing the amount, timing, or purpose of such expenditures.[2]

While Congress aimed this Act at the actions of executive agencies, the Act has a range and blast zone that can readily injure innocent bystanders, including government contractors. In particular, the Act creates special risks for contractors in three situations: (1) open-ended or contingent liabilities; (2) annual service contracts; and (3) "availability of funds" clauses.

Open-Ended Liabilities

Open-ended or contingent liabilities take many forms, such as risks associated with handling toxic wastes, producing hazardous products, or using high-value property. As a general rule, a contractor must be wary of any open-ended or contingent liabilities under a contract because the government agency will likely deny any such liability as being contrary to the Act.

Indemnification represents a classic open-ended liability that the government will not assume in the absence of express statutory authority.[3] In one of its rare decisions on government contract issues, the Supreme Court recently found that the Act generally bars the government from indemnifying contractors from third-party losses: "the Comptroller General has repeatedly ruled that Government procurement agencies may not enter into the type of open-ended indemnity for third-party liability that petitioner Thompson claims to have implicitly received under the Agent Orange contracts."[4] The Court reached this conclusion even though the Department of Defense had (1) forced the contractors to produce Agent Orange pursuant to the Defense Production Act, (2) specified the exact contents and labelling of the product, and (3) failed to provide appropriate warnings to the veterans exposed to Agent Orange.

The risk of property loss or damage represents yet another arena of conflict involving contingent liabilities and the Act. For example, the Comptroller General has found a lease with option to purchase to be improper where the agency assumed the risk of loss of leased computer equipment, but did not allocate appropriated funds to cover the potential loss.[5] Similarly, a court refused to find the government liable for repair or replacement of a utility company's equipment under a utility contract with the Bureau of Indian Affairs for a remote Eskimo village:[6]

> While the consequences of a utility shutdown would have been dire for the residents of Barrow, the court cannot derive from this circumstance a continuing, open-ended obligation for the BIA to fund maintenance and repair projects at the utility, other than those enumerated in the contract consistent with the estimates therein. The Government cannot enter into fluid and unlimited obligations, and to allow such a result would be contrary to law.

In such circumstances, the contractor must bear the risk of loss of its property — or the cost of insuring against such losses.

Annual Service Contracts

As a general rule, appropriated funds have a limited

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shelf-life, meaning that contracts may not be awarded before funds are appropriated or after the funds have expired. As one court noted, "[t]o make a contract obligating funds not yet appropriated is normally illegal, even criminal."[7]

For eons, service contractors suffered during the gap between the end of one fiscal year when funds expired and the start of the next fiscal year when funds had yet to be appropriated. During this period of limbo, contractors had the painful choice between stopping work and risking negative customer relations or continuing work and risking no payment for work performed before Congress appropriated funds. The regulations reinforced the strictures of the Act by generally prohibiting service contracts funded with annual appropriations from extending beyond the end of the fiscal year.[8]

> The buying practices of the government and private sector will never be the same so long as Congress continues to police expenditures with the Act.

The Federal Acquisition Streamlining Act lessened the sting of these limitations on annual service contracts by authorizing certain agencies to enter into annual service contracts that cross fiscal years, so long as the term of the contract does not exceed one year.[9] However, this new authority did not extend to the Department of Defense or the National Aeronautics and Space Administration (NASA).[10] As a result, many contractors will continue to feel the pinch between the cracks of the fiscal years.

Availability of Funds Provisions

For many government procurements, the path out of the anti-deficiency conundrum is to include a condition making the government's obligation subject to the availability of appropriated funds. Such provisions appear in a variety of places in the regulations and allow agencies to enter into certain types of contracts prior to appropriated funds being available.[11]

By including the "availability of funds" condition in a contract, the government agency addresses its obligations under the Act and the contractor assumes a risk that Congress will not appropriate funds to cover the effort. In a recent case, the Navy raised the Act as a defense, arguing that the agency could not be bound by its agreement to allocate a minimum percentage of its aircraft engine requirements to a second source (Pratt & Whitney) because such an agreement would run afoul of the Act.[12] In striking down this defense, the Board of Contract Appeals concluded:

> Because P & W's right to engine awards was expressly contingent on Congress first appropriating sufficient funds, and not in advance of them, we conclude that the procurement scheme contemplated by the Investment Incentive clause is not in violation of the Antideficiency Act.

Similarly, the Comptroller General has found that the "availability of funds" condition would satisfy the requirements of the Act with respect to the government's assumption of certain contingent liabilities to third parties under the "Insurance — Liability to Third Persons" clause.[13]

While the "availability of funds" condition may avoid violations of the Act, this condition often sows other mischief. For example, how does one prove that funds are available? What happens if the government adds an availability of funds provision to an option exercise?

Proof of availability of funds often requires a look at an agency's appropriations act. In particular, the availability of funding is determined, not by the agency's internal allocation process, but by the overall amount of funds appropriated by Congress.[14] When Congress appropriates a lump-sum amount without placing specific restrictions on what may be done with those funds, the contractor is entitled to look to the entire amount of the lump-sum appropriation to determine whether funds are available.[15] Another type of proof arises when an agency claims not to have sufficient funds, but proceeds to award a contract for the same or similar items to a competitor. Not surprisingly, such an award has been considered "incontrovertible evidence" of the availability of funds.[16]

Prior to exercising an option, agencies sometimes find that they do not yet have the funds in hand. To remedy this problem, an agency has occasionally attempted to wedge an availability of funds condition into the option at the time of exercise. Such attempts have been

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regularly rebuffed as invalidating the option exercise because the acceptance of the option must be unconditional and in exact accord with the terms of the option.[17] To avoid this pitfall, the government must, at least, include the availability of funds condition in the initial contract.

Conclusion

During the last few years, Congress and the Executive Branch have taken major steps to commercialize the government procurement process, attempting to make it work more like the private sector. However, the buying practices of the government and private sector will never be the same so long as Congress continues to police the Executive Branch's expenditures with the Anti-Deficiency Act. In the meantime, contractors should consider protecting their interests by carefully defining the allocation of risk for open-ended liabilities (and if necessary, insuring against such risks), determining how the government will handle funding for service contracts crossing fiscal years, and assessing the effects and risks associated with "availability of funds" provisions.

Endnotes:

[1] 31 U.S.C. § 1341(a)(1)(A) (amount of appropriations); 31 U.S.C. § 1301(a) (purpose of appropriations); 31 U.S.C. § 1502(a) (timing of appropriations); 31 U.S.C. § 1342 (augmentation of appropriations).

[2] 31 U.S.C. § 1349 (adverse personnel actions) and § 1350 (criminal penalties).

[3] California-Pacific Utilities Co. v. U.S., 194 Ct. Cl. 703, 715 (1971).

[4] Hercules Inc. v. U.S., 116 S. Ct. 981, 987 (1996).

[5] Federal Data Corp., B-194709, 81-2 CPD ¶ 28.

[6] Barrow Utilities & Elec. Co-op, Inc. v. U.S., 20 Cl. Ct. 113, 119 (1990).

[7] Applied Devices Corp. v. U.S., 219 Ct. Cl. 109, 113 (1979).

[8] See, e.g., Federal Acquisition Regulation ("FAR") § 37.106(a).

[9] 41 U.S.C. 253l, as amended by Federal Acquisition Streamlining Act, Pub. L. 103-355, § 1073; FAR § 37.106(b).

[10] The Department of Defense does have limited authority to cross fiscal years for certain types of service contracts, such as depot maintenance, operation and maintenance of equipment, and leases of property. 10 U.S.C. § 2410a(a). See also Department of Defense Federal Acquisition Regulation Supplement ("DFARS") § 237.106(2).

Upcoming Events

June 18 **Brown Bag Seminar**, presented by the Washington DC chapter of NCMA. The seminar will be held at noon. Topic: **FAA Acquisition System**. Crystal Square 5, 1755 Jerrerson Davis Highway, Crystal City, VA. Information: (703) 575-3191.

June 19-20 **Government Contract Audits** seminar, presented by the George Washington University Government Contracts Program. Marina del Rey, CA. Registration/Information: (202) 223-2770.

July 14 **ADPA/NSIA Procurement Planning Committee, Finance Subcommittee Meeting.** Boston Backbay Hilton, Boston, MA. Open to members only. Next meeting: September 24, 1997. Information: (202) 775-1440.

Sept. 24 **ADPA/NSIA Procurement Planning Committee, Finance Subcommittee Meeting.** Fort MacGruder Inn, Williamsburg, VA. Open to members only. Information: (202) 775-1440.

Fax your Upcoming Event information to (202) 833-1959, Attn: Valerie Spiess. The publication of any events will be at the sole discretion of the editor and as space permits.

[11] See, e.g., FAR §§ 52.232-18 Availability of Funds, 52.232-19 Availability of Funds for the Next Fiscal Year, and 52.228-7 Insurance — Liability to Third Persons.

[12] United Technologies Corp., Pratt & Whitney Group, ASBCA Nos. 46880, 46881, 97-1 BCA ¶ 28,828 at 143,797.

[13] Assumption by Government of Contractor Liability to Third Persons — Reconsideration, B-201072, 83-1 CPD ¶ 501.

[14] See Blackhawk Heating & Plumbing Co. v. U.S., 224 Ct. Cl. 111, 135 (1980); The Boeing Co., ASBCA No. 37579, 90-3 BCA ¶ 23,202 at 116,439.

[15] See ANGUS Chemical Co., B-227033, B-227034, 87-2 CPD ¶ 127 at 3; 55 Comp. Gen. 812, 820 (1976).

[16] VARO, Inc., ASBCA No. 13739, 70-1 BCA ¶ 8099 at 37,628.

[17] See Lear Siegler Inc., ASBCA 30224, 86-3 BCA ¶ 19,155 at 96,795; J.E.T.S., Inc., ASBCA No. 26135, 82-2 BCA ¶ 15,986 at 79,274-75. But see Contel Page Services, Inc., ASBCA No. 32100, 87-1 BCA 19,540 at 98,736 (valid option exercise where availability of funds condition appeared in initial contract).