

COVERAGE AND EXEMPTIONS¹

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Section 403 of the Sixth Supplemental National Defense Appropriation Act, 1942, as amended,² contains several different methods for defining what Government contracts and subcontracts thereunder are subject to the statute. The delineation of the coverage of the statute is expressed in four ways: (1) definition (subcontract); (2) exclusion by definite tests (final payment prior to April 28, 1942, sales volume); (3) exemptions, both mandatory and discretionary; and (4) statutes of limitation

Subcontracts

Section 403, as originally enacted, made subject to renegotiation contracts with the War Department, Navy Department and Maritime Commission³ or "any subcontract thereunder." No further explanation or definition of the word subcontract was contained in the Act.

Webster's *New International Dictionary* (1940) contains the following definitions:

subcontract, n. "A contract under, or subordinate to, a previous contract."

subcontract, v. "To contract under, or for the performance of part or all of, another contract."

subcontractor, n. "One who contracts with a contractor to perform part or all of the latter's contract."

Bouvier defines "subcontract" as follows: "A contract by one who has contracted for the performance of labor or services with a third party for the whole

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¹ The opinions expressed herein are those of the writer and are in no way to be construed as an official pronouncement of the Navy Department.

² 56 STAT. 245, 41 U. S. C. A. note prec. §1 (Supp. 1942). Pub. L. No. 528, 77th Cong., 2d Sess. (April 28, 1942), was the original Act. It has been amended by: Pub. L. No. 753, 77th Cong., 2d Sess. (October 21, 1942); Pub. L. No. 108, 78th Cong., 1st Sess. (July 1, 1943); Pub. L. No. 149, 78th Cong., 1st Sess. (July 14, 1943). The Revenue Bill of 1943, which has passed the House of Representatives, proposes certain changes in renegotiation law. The changes proposed in the area of exemptions are particularly significant. Since it is not known what will be the eventual disposition of the Bill and its proposals, this article does not discuss them. For a full discussion of the significance of the pending proposals, the reader is referred to the concluding article in this symposium by Jules Abels, *infra*.

³ The Act was extended to the Treasury Department by Pub. L. No. 753, *supra* note 1, to Defense Plant Corporation, Metals Reserve Company, Defense Supplies Corporation and Rubber Reserve Company by Pub. L. No. 108, *supra* note 1 and to War Shipping Administration by Executive Order No. 9244, September 16, 1942.

or part performance of that labor or service."⁴ Subcontractor is defined as "One who has entered into a contract, express or implied, for the performance of an act with the person who has already contracted for its performance."

The most closely analogous statutory provision is to be found in the Vinson-Trammell Act,⁵ also designed to effectuate some control over profits, which provides that a Navy contractor under a contract for the construction of naval vessels or aircraft must agree to pay to the Treasury all profits as determined by the Treasury Department in excess of 10 per cent of the contract price of the vessels and in excess of 12 per cent of the contract price of aircraft, and "(e) to make no subcontract unless the subcontractor agrees to the foregoing conditions."

The Treasury Department has issued three sets of regulations under this statute and in Treasury Decision 4906, dated June 16, 1939,⁶ defines subcontract and subcontractor as used in the regulations as follows:

"(e) 'Subcontract' means an agreement entered into by one person with another person for the construction or manufacture of a complete naval vessel or aircraft or any portion thereof, the prime contract for such vessel or aircraft or portion thereof having been entered into between a contractor and the Secretary of the Navy or his duly authorized representative.

(f) 'Subcontractor' means any person other than a contractor entering into a contract."

Up to the time of the decision of the Board of Tax Appeals in the *Aluminum Company* case,⁷ there had been no decisions under the Vinson-Trammell Act as to the construction of the words "subcontract" and "subcontractor."

However, the Judge Advocate General of the Navy has written several opinions as to the application of the Vinson-Trammell Act and these opinions are helpful in determining what was the previously accepted meaning of the word "subcontract." In a letter dated September 24, 1936, to the Paraffine Companies, Inc., the Judge Advocate General said:

"Referring to your letter of August 29, 1936, stating that at times you furnish, as subcontractors, linoleums, paint and asphalt composition roofing for use in the construction of naval vessels, which material you consider as not coming within the purview of the Vinson-Trammell Act of March 27, 1934 (34 U. S. C. 496), this office is of the opinion that the above mentioned Act is applicable to all contracts and subcontracts for materials for complete naval vessels, aircraft or any portion thereof, provided the total contract or subcontract prices are in excess of \$10,000.00 and that such materials have not been specifically designated by the Secretary of the Navy as being exempt as scientific equipment under the authority contained in the amendatory Act of June 25, 1936 (Public No. 804)."

In a letter to the Secretary of the Navy dated May 18, 1938, the Judge Advocate General replied to a request as to whether contracts or subcontracts for material not forming a structural portion of the complete vessel fell within the classification

⁴ BOUVIER, LAW DICTIONARY, 8th ed. (1914).

⁵ 48 STAT. 505 (March 27, 1934), 34 U. S. C. 1940 ed. §§496, 497.

⁶ PRENTICE-HALL, GOVERNMENT CONTRACTS (1942) ¶22, 941.

⁷ *Aluminum Co. of America v. Commissioner Int. Rev.*, 47 B. T. A. 543 (1942).

of contracts or subcontracts for a "complete Naval vessel or aircraft" or any portion thereof, as provided in the Act. The Judge Advocate General cited the 1936 amendment⁸ to the Act which exempted therefrom certain scientific equipment, and then went on to say:

"In view of the foregoing, the Judge Advocate General is of the opinion that materials not forming a structural portion of the complete vessel are in general subject to the above mentioned acts, and that the administrative decision as to the exceptions to such rule must be made on the basis of a submission of the conditions affecting the procurement and use of specific items."

By an opinion dated December 16, 1938, to the Secretary of the Navy, the Judge Advocate General replied to a request "as to the application of the Vinson-Trammell Act to a contract for services only for the machining of Government owned castings and as to the distinction, if any, between a contract for services for the machining of castings, including the furnishing of jigs, dies and other materials used in the machining of the castings (a contract for services and materials), and a contract for the machining of the castings alone where no materials owned or produced by the machining contractor are delivered to the Government as a part of the service contract." In this opinion he stated:

"3. In the construction of the complete ship or of any portion thereof both labor and material are used; whether the labor and material are furnished by a single contractor or by several contractors, or whether one furnishes labor or services only and another the material, does not change the obligation of a contractor or subcontractor to pay into the Treasury excess profit where the contract or subcontract involves an amount in excess of \$10,000.

"4. In view of the foregoing, the Judge Advocate General is of the opinion that a contract or subcontract in excess of \$10,000 for furnishing labor and material, or labor or material only, if necessary, at any stage, to produce material or equipment ultimately forming a portion of the complete Naval vessel or aircraft, is to be generally considered as coming within the scope of the above mentioned Act."

In January, 1939, the Secretary of the Navy requested the views of the Treasury Department as to the application of the Vinson-Trammell Act to a subcontract for ingots of copper and zinc to be used in the manufacture of cartridge cases. Mr. Hanes, the Acting Secretary of the Treasury, replied in part as follows:

"In the specific instance stated, it is understood that the manufacturer (the prospective bidder in this case) is regularly engaged in using ingots of zinc and copper in the manufacture of articles not made under contracts coming within the Vinson-Trammell Act. It is not clear to this Department what the terms and conditions of the commitments referred to will be. It is assumed for purposes of this consideration that the ingot zinc and copper is ordinary commercial raw zinc and copper which is in fact purchased for general use in the operations of the manufacturer and not for use exclusively in the construction and/or manufacture of articles covered by its contract under the Vinson-Trammell Act; and that the seller of the zinc and copper is not by agreement made subject to any term of condition imposed upon the manufacturer under its con-

⁸ 49 STAT. 1926 (June 25, 1936).

tract with the Navy Department. The Treasury Department is of the opinion that under these circumstances such ingots of zinc and copper would not constitute portions of a complete naval vessel or aircraft within the scope of the Vinson-Trammell Act, as amended."

It is thus apparent that the term "subcontractor" in the Vinson-Trammell Act was held to include a person who furnished materials and supplies under agreement with the contractor, or a person who furnished equipment, tools or machinery (jigs, and similar equipment) which were specifically furnished for the purposes of the contract alone (*i.e.*, not for use in the general operation of the contractor's business).⁹ It would not appear that in the application of the Vinson-Trammell Act any attempt was made to go beyond the first tier of subcontractors; that is, there is nothing to indicate that it was applied to sub-subcontractors.

With these opinions as a precedent, the Price Adjustment Board of the Navy Department defined subcontracts as used in Section 403 of the Renegotiation Act, as originally enacted, to include the following agreements:

(a) Any purchase order from, or any agreement with, the contractor (i) to perform all or any part of the work to be done or to supply all or any part of the articles to be furnished, under his contract with the Government, (ii) to supply any services required directly for the production of any article or equipment covered by such contract or any portion thereof, (iii) to make or furnish any supplies, materials, articles or equipment destined to become a component part of any article or equipment covered by such contract, or (iv) to make or furnish any machinery, equipment, tools or supplies acquired by the contractor exclusively for the performance of such contract, but shall not include any agreement to supply machinery, equipment, tools or supplies or other materials or services for the general operation of the contractor's plant or business;

(b) Any purchase orders from, or any agreement with, a subcontractor who is obligated to furnish a portion of the completed articles called for under the agreement of the contractor with the Government, if such purchase order or agreement would be construed under paragraph (a) above as a subcontract if entered into with the contractor; and

(c) Any agreement of a subcontractor providing for the delivery to such subcontractor of a portion of the completed articles called for under his subcontract.

Meanwhile, the Board of Tax Appeals decided the *Aluminum Company* case,¹⁰ and held that the term "subcontract" as used in the Vinson-Trammell Act did not include suppliers of raw materials or standard commercial articles even if incorporated in the completed article furnished under the prime contract with the Government. This decision caused a certain amount of confusion as it was contrary to the administrative interpretations already made under the Vinson-Trammell Act and to the interpretations given by both the War and Navy Departments to

⁹ The Maritime Commission in issuing its regulations under the Merchant Marine Act, 1936, June 29, 1936, as amended, 52 STAT. 958, 46 U. S. C. 1940 ed. §1155(b), likewise included within the definition of subcontract any agreement with a contractor "for the manufacture or furnishing of any materials or goods * * *" and did not distinguish materialmen from other types of subcontractors. See PRENTICE-HALL, GOVERNMENT CONTRACTS (1942) ¶22, 990.

¹⁰ *Supra* note 7. The decision of the Board of Tax Appeals has been appealed by the Commissioner to the Circuit Court of Appeals for the District of Columbia.

the term "subcontract" under the Act. As a result of this decision, contractors objected that the definition then used by both the War and Navy Departments extended the Act beyond its intended scope. It was agreed that Congress should be requested to define the term in order to eliminate any uncertainties.¹¹ At the hearings before the Subcommittee of the Committee on Finance, United States Senate, the War Department was initially of the opinion that in accordance with the decision in the *Aluminum Company* case, the definition of "subcontract" might properly exclude agreements for raw materials or standard commercial fabricated or semifabricated articles, and presented to the Subcommittee for consideration this definition:

"The term 'subcontract' means any purchase order or agreement to perform all or any part of the work or to make or furnish any article, required for the performance of another contract, except orders or agreements to furnish (i) raw materials, (ii) standard commercial fabricated or semifabricated articles ordinarily sold for civilian use, or (iii) articles for the general operation or maintenance of the contractor's plant. The term 'article' includes any material, part, assembly, machinery, equipment, or other personal property."¹²

Both the Maritime Commission and the Navy Department objected to this definition as being too restrictive, and the Navy Department submitted to the Subcommittee for consideration the following definition which was substantially similar to the definition it had adopted administratively:

"(5) The term 'subcontract' means (a) any purchase order or agreement (i) to perform all or any part of the work to be done or to supply all or any part of the articles to be furnished, under a contract with the Government, (ii) to supply any services required directly for the production of any article or equipment covered by such contract or any portion thereof, (iii) to make or furnish any supplies, materials, articles, or equipment specifically destined to become a component part of any article or equipment covered by such contract, or (iv) to make or furnish any material, part, assembly, machinery, equipment, or other personal property acquired by the contractor exclusively for the performance of such contract, but shall not include any agreement to supply services or any such articles for the general operation or maintenance of the contractor's plant or business in those cases where the Government is not obligated to reimburse the contractor for the cost of such articles; (b) any purchase order from, or any agreement with, a subcontractor who is obligated to furnish completed articles called for under the contract of the contractor with the Government if such purchase order or agreement would be construed under paragraph (a) above as a subcontract if entered into with the contractor; and (c) any agreement of a subcontractor providing for the delivery to such subcontractor of completed articles called for under his subcontract.

"For the purpose of subsections (d) and (e) of this section, the term 'contract' includes a subcontract and the term 'contractor' includes a subcontractor."

The distinction between the two definitions is to a certain extent explained in the letter from the Acting Secretary of the Navy to the Chairman of the Subcommittee as follows:¹³

¹¹ *Hearings before a Subcommittee of the Committee of Finance, Senate, on S403 of Pub. L. No. 528, 77th Cong., 2d Sess. (Sept. 29, 30, 1942) 22.* ¹² *Supra* note 11, at 51. ¹³ *Supra* note 11, at 58.

“(a)(5) This is a new paragraph defining the term ‘subcontract’ and differs from the definition submitted by the War Department. The definition of the War Department excluded orders or agreements to furnish (1) raw materials, (2) standard commercial fabricated or semifabricated articles ordinarily sold for civilian use, and (3) articles for the general operation or maintenance of the contractor’s plant. It is the opinion of the Navy Department that it was the intention of Congress that excessive profits should be removed from all war contracts, irrespective of whether such contracts were of the character referred to in (1) and (2) above. For this reason, the Navy Department has proposed a definition of subcontract which includes virtually all contracts made with prime contractors of the Government. It is our opinion that this definition is in accord with the suggestion of the Chairman of the Maritime Commission as contained in his letter of September 22, 1942, to Senator George.”¹⁴

Apart from the distinction referred to in the letter from the Acting Secretary of the Navy, a further distinction in the scope of the coverage should be noted. With the exception of contracts covered by clauses (b) and (c) of the Navy Department definition and contracts “to make or furnish any supplies, materials, articles or equipment specifically destined to become a component part of any article or equipment” covered by a prime contract, the Navy Department definition is applicable only to subcontracts in the first tier, *i.e.*, subcontracts entered into directly by the prime contractor with the Government. The War Department definition, while more restricted with respect to subcontracts entered into directly with the prime contractor, in that even in the first tier it excluded “orders or agreements to furnish (i) raw materials and (ii) standard commercial fabricated or semifabricated articles ordinarily sold for civilian use,” extended beyond the first tier to sub-subcontractors other than in the excepted area.

At this point, the Subcommittee requested the representatives of the various Departments to endeavor to agree upon a definition of the term “subcontract” that could be submitted for consideration. The Departments drafted and submitted the following definition which, without change, was enacted into the statute:

“(5) The term ‘subcontract’ means any purchase order or agreement to perform all or any part of the work, or to make or furnish any article, required for the performance of another contract or subcontract. The term ‘article’ includes any material, part, assembly, machinery, equipment, or other personal property.

“For the purposes of subsections (d) and (e) of this section, the term ‘contract’ includes a subcontract and the term ‘Contractor’ includes a subcontractor.”¹⁵

Examination of this definition makes it obvious that both the War and the Navy Departments had receded somewhat from their positions; the definition is of sufficient scope to include raw materials or any other type of materials and to go beyond the first tier of subcontractors. This is supported by the fact that in order to exempt raw materials, it was found necessary to incorporate Subsection (i) (1) (ii) in the Act.¹⁶

¹⁴ *Ibid.*

¹⁵ Section 801, Pub. L. No. 753, 77th Cong., 2d Sess., approved Oct. 21, 1942.

¹⁶ *Supra* note 11, at 147.

The legislative history thus clearly indicates the intention of Congress to give the term "subcontract" a broad meaning and not the restrictive one given in the *Aluminum Company* case or suggested by the War Department. There are, however, two qualifications to the coverage of subcontracts by this amendment in that (1) the subcontract must be for work or an article "required for the performance of any other contract or subcontract" and (2) article is defined to include "any material, part, assembly, machinery, equipment or other personal property." Under the first qualification of requirement for performance, contracts for such articles as fuel, light, power, and general office equipment could be included. While general factory supplies may be "required for the performance" in the strictest sense, they contribute only indirectly to the actual manufacturing process, and contracts therefor should not be included in the definition of subcontract. No one indicated to the Subcommittee any desire to include such contracts¹⁷ and the Departments have so interpreted the Act to exclude them.¹⁸ The second qualification excludes from the purview of the statute subcontracts for real property. The remoteness of a subcontract for real property from the article eventually purchased by the Government probably affords a sound basis for this exclusion. The test as to whether a subcontract involves "real property" should be whether it is for the purchase or sale of real property as such. The mere fact that the subject matter of the contract may subsequently be affixed to real property would not appear to be sufficient to exempt it from the provisions of the statute. Thus, a contract for the sale of bricks which are to be incorporated in a furnace required for the performance of the contract with the Government should be subject to the provisions of the statute. The Departments have adopted an interpretation which excludes a contract with a contractor or subcontractor for the construction of an open hearth furnace but includes such contract for the installation of machinery or equipment to be used in the processing of an end product or of an article incorporated in an end product, even though after construction or installation both become real property.¹⁹ The line of demarcation is perhaps justified in view of the inclusion of the words "machinery" and "equipment" in the definition of the term "article" in the statute.

Brokers' and Representatives' Fees

The agitation against contingent fee brokers resulted in a further extension of the term "subcontractor" by Public Law 149, 78th Congress approved July 14,

¹⁷ *Hearings before the Committee on Naval Affairs pursuant to H. Res. 30, 78th Cong., 1st Sess.* (1943) Vol. 2, 1282 (hearings on investigation of renegotiation of war contracts).

¹⁸ THE JOINT STATEMENT BY THE WAR, NAVY AND TREASURY DEPARTMENTS AND THE MARITIME COMMISSION OF PURPOSES, PRINCIPLES, POLICIES AND INTERPRETATIONS (March 31, 1943) at page 10 interprets subcontract "to include contracts with contractors and subcontractors (a) for the sale or processing of an end product or an article incorporated therein, (b) for the sale of machinery or equipment, used in the processing of an end product, or an article incorporated in an end product, (c) for the sale of component parts of or subassemblies for such machinery or equipment, and (d) for the performance of personal services required for the contracts and subcontracts included in (a), (b), and (c)."

¹⁹ Supplemental Interpretation (July 10, 1943) to the JOINT STATEMENT, *supra* note 18.

1943. The problem of unconscionable fees in the procuring of Government contracts has existed in every war in which this country has been engaged. The camp followers of war procurement arrive long before the commencement of hostilities. The policy against the payment of unconscionable fees, particularly during time of war, to agents specializing in the procurement of Government contracts was first enunciated during the Civil War by the Supreme Court of the United States.²⁰ The Supreme Court has consistently held that contracts calling for payment of compensation to an agent for the use of improper influence upon Government officials to obtain Government contracts are contrary to public policy and therefore unenforceable.²¹ A contract, contemplating no improper influence, to pay a commission or other fee to an ordinary salesman or agent for securing a Government contract was probably enforceable.²²

By Order of June 10, 1927, the President required the insertion of the following warranty in all subsequent Government contracts:

"The contractor warrants that he has not employed any persons to solicit or secure this contract upon any agreement for a commission, percentage, brokerage, or contingent fee. Breach of this warranty shall give the Government the right to annul the contract, or, in its discretion, to deduct from the contract price or consideration the amount of such commission, percentage, brokerage, or contingent fees. This warranty shall not apply to commissions payable by contractors upon contracts or sales secured or made through bona fide established commercial or selling agencies maintained by the contractor for the purpose of securing business."

This order has remained in effect since this date.²³ It is apparent that the exception contained in the third sentence of the warranty is extremely broad. It has never been construed by the courts.²⁴ Government procurement officers have been reluctant to adopt a strict construction of the exceptions, because to do so would penalize companies employing agents who had performed useful and valuable services, and in any event the enforcement of the warranty would strike solely at the principal, rather than the agent, and would afford the principal no protection against court action by the agent to recover the amount of compensation agreed upon.²⁵

The tremendous increase in Government procurement caused by the present war again brought this problem to public notice. During the summer of 1942, the House Naval Affairs Committee conducted a series of hearings to investigate excessive contingent fees and commissions chargeable to the cost of the war effort.

²⁰ *Tool Company v. Norris*, 69 U. S. (2 Wall.) 45 (1864).

²¹ *Oscanyan v. Arms Co.*, 103 U. S. 261 (1880); *Crocker v. United States*, 240 U. S. 74 (1916); *Steele v. Drummond*, 275 U. S. 203 (1927).

²² See *Oscanyan v. Arms Co.*, 103 U. S. 261, 275-276 (1880); *Hazelton v. Sheckells*, 202 U. S. 71 (1906) *semble*; *Valdes v. Larrinaga*, 233 U. S. 705 (1914) *semble*; *Steele v. Drummond*, 275 U. S. 199 (1927) *semble*. The *Tool Company* case, *supra* note 20, could probably be distinguished.

²³ For a complete history of the development of the "warranty clause" see *Hearings before the Committee on Naval Affairs on H. Res. 30*, 78th Cong., 1st Sess. (1943), Vol. I, 380-385.

²⁴ *United States v. Buckley*, 49 F. Supp. 993 (Dist. Col. 1943).

²⁵ *Bradford v. Durkee Marine Products Corp.*, 40 N. Y. S. (2d) 448 (Sup. Ct. 1943).

These hearings disclosed that certain individuals and firms being paid on a commission basis were receiving enormous sums in connection with the procurement of Government contracts, in some cases from \$500,000 to \$1,000,000 per year. At the close of the hearings, the Committee reported out H. R. 7304, a bill which in effect made invalid and unenforceable any agreement to pay a commission or contingent fee to any third party for securing a Government contract. The bill imposed criminal penalties upon both agent and principal for entering into such a contract. It was passed by the House on July 20, 1942, and sent to the Senate where it never was voted out of the Committee on Naval Affairs. There were several defects in the bill; it appeared overly stringent in that it disallowed any compensation whatsoever to commission agents who, in many cases, performed a useful and valuable function in bringing together small manufacturing concerns and Government procurement needs; it did not reach excessive amounts paid to manufacturers' representatives on a salary or other fixed basis; and finally, it did not reach compensation paid to representatives of subcontractors.

In March and April, 1943, the House Naval Affairs Committee conducted further hearings in connection with the problem and at the conclusion of the hearings, the Committee reported out H. R. 1900, which passed both the House and the Senate unanimously and was approved by the President on July 14, 1943, as Public Law 149, 78th Congress.

In general, Public Law 149 is designed to keep payments to manufacturers' representatives within reasonable bounds, rather than to forbid the payment of compensation to any class of persons for procuring Government contracts or subcontracts. It accomplishes this purpose by expanding the definition of "subcontract" in the act to embrace within the scope of renegotiation the contracts or arrangements between manufacturers' representatives and their principals. The first section of Public Law 149 effects this expansion as follows:

“. . . the first sentence of section 403 (a)(5) of the Sixth Supplemental National Defense Appropriation Act, 1942, as amended, is amended to read as follows: "The term "subcontract" means (i) any purchase order or agreement to perform all or any part of the work, or to make or furnish any article, required for the performance of any other contract or subcontract or (ii) any contract or arrangement (other than a contract or arrangement between two contracting parties, one of which parties is found by the Secretary to be a bona fide executive officer, partner, or full-time employee of the other contracting party), (A) any amount payable under which is contingent upon the procurement of a contract contracts with a Department or of a subcontract or subcontracts thereunder, or determined with reference to the amount of such a contract or subcontract or such contracts or subcontracts, or (B) under which 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 thereunder: Provided, that nothing in this sentence shall be construed (1) to affect in any way the validity or construction of provisions in any contract with a Department or any subcontracts thereunder, heretofore at any time or hereafter made, prohibiting the payment of contingent fees or commissions; or (2) to restrict in any way the authority of

the Secretary to determine the nature or amount of selling expenses under subcontracts as defined in (ii) herein, as a proper element of the contract price or as reimbursable item of cost, under a contract with a Department or a subcontract thereunder.’”

Subdivision (i) above is a repetition of the previously existing definition of “subcontract”; the remainder of Section 403(a)(5) above is new. In order to include within the scope of renegotiation all types of arrangements between representatives and principals. Subdivision (ii) has a dual approach. Subdivision (ii)(A) defines the representatives’ contracts embraced by this statute by describing the nature of the compensation to be paid thereunder. In general, it subjects to renegotiation any contract calling for compensation contingent upon the procurement of a prime Government contract or subcontract thereunder or the amount of compensation under which is determined with reference to the amount of such prime contract or subcontract. This portion of the definition regards the nature of the services which the representative has contracted to perform for his principal. Contracts for engineering services and even legal services are therefore subject to renegotiation if the compensation called for thereunder is in any way contingent upon the procurement of a prime contract or subcontract. Subdivision (ii)(B), on the other hand, approaches the problem from the standpoint of the description of the services rendered without regard to the manner of compensation. Any contract calling for compensation in return for solicitation of a prime Government contract or subcontract is made subject to renegotiation. Thus excessive salaries or fixed fees paid for soliciting prime contracts or subcontracts may be renegotiated.

Proviso (1) in the above section is self-explanatory. Proviso (2) reserves in the respective Government departments their pre-existing authority and discretion to refuse to enter into any contract which includes excessive compensation to a sales representative as part of the contract price, regardless of the fact that such compensation may later be refunded to the Government in whole or in part in the renegotiation of the representative’s profits.

Sections (2) and (3) of Public Law 149 amend the act so as to except from renegotiation those representatives whose aggregate compensation from all their principals does not exceed \$25,000 per year, as contrasted with the \$100,000 exception applicable to the sales of contractors and subcontractors as originally defined in the basic act.

Section (5) of Public Law 149 declares the effective date of its provisions to be April 28, 1942 (the effective date of the basic Act).

Exemptions

There are various exclusions and exemptions from renegotiation provided for in the Act: (1) Subsection (c)(6)(i) excludes contracts and subcontracts on which final payment “was made prior to April 28, 1942”; (2) Subsection (c)(6)(iii) excludes contractors and subcontractors whose sales otherwise subject to the Act for

the fiscal year under consideration do not exceed \$100,000,²⁶ except solicitors of Government business defined in Subsection (a)(5)(ii), for whom the limit is \$25,000 of sales in the fiscal year; (3) Subsection (i)(1) provides that the Act shall not apply to—

“(i) any contract by a Department with any other department, bureau, agency, or governmental corporation of the United States or with any Territory, possession, or State or any agency thereof or with any foreign government or any agency thereof or

“(ii) 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; and the Secretaries are authorized by joint regulation, to define, interpret, and apply this exemption”; and

(4) Subsection (1)(2) grants discretionary power in each Secretary to exempt (a) contracts or subcontracts which are to be performed outside the territorial limits of the United States or Alaska, (b) contracts or subcontracts where profits can initially be determined with reasonable certainty and (c) portions of contracts or subcontracts or performance thereof for specified periods if the provisions of the contract are otherwise adequate to prevent excessive profits.²⁷

The exclusion first above referred to raises the legal question as to whether a series of transactions constitute one contract or several contracts. The question is most frequently encountered in cases involving increases in quantities, orders under option agreements, work performed under repair contracts which specify in general the conditions for performing work under job orders, and the furnishing of material under requirement contracts. The test is the severability of the transactions not the divisibility of the contract; did the parties give a single assent to a whole transaction or did they assent separately to several separate transactions? The divisibility of performance does not of necessity connote separate contracts. In the strictest sense, a divisible contract is always one contract, and not several contracts.²⁸ Under this test, a valid contract covering work performed and material furnished at various times, even though the contract does not contain all of the details of performance, would constitute a single contract—divisible, it is true, as to performance, but *not* separable; and all profits under such contract would therefore be subject to renegotiation if final payment thereupon was made subsequent to April 27, 1942. The fact that one or both of the parties could under certain conditions refuse to perform or that the consideration is not definitely stated should not alter this rule.²⁹

²⁶ H. R. 2324, 78th Congress, introduced by Representative Doughton on March 29, 1943, and the Revenue Act of 1943, which has passed the House of Representatives, propose to increase this figure to \$500,000.

²⁷ S. 1366, 78th Congress, introduced by Senator Hatch on September 21, 1943, if enacted, would provide that profits shall not be deemed excessive if they amount before the deduction of Federal income and excess-profits taxes to 8 per centum or less of sales prices for the fiscal year under consideration and sales for such period are not more than three times the average total sales during the base period from 1936 to 1939 inclusive.

²⁸ 3 WILLISTON, CONTRACTS (Rev. ed. 1936) §861.

²⁹ 3 WILLISTON, CONTRACTS (Rev. ed. 1936) §862.

The exemptions afforded in Subsections (c)(6)(iii) and (i)(1)(i) are self-explanatory. The exemption in (i)(1)(ii) is the so-called raw material exemption, which was added to the Act by Section 801 of the Revenue Act of 1942. The legislative record is somewhat meager as to precisely what was intended to be covered by the language employed. It does, however, appear that none of the Departments wished the power to renegotiate contracts or subcontracts for raw materials and that certain members of the Senate Finance Subcommittee felt that the various Price Adjustment Boards could not adequately consider in renegotiation the problems involved in vanishing assets, the production of which was a drain on the capital account of the producer.³⁰ The broader definition of the term "subcontractor," recommended to the Subcommittee, made necessary a specific exemption to provide a cut off for subcontracts for raw materials at some point this side of the mines.³¹ A reasonable conception of raw materials is that they constitute the product of a mine, oil or gas well or other mineral or natural deposit, which has been extracted from the earth and then turned over for manufacturing use. While depletion was a phase of the problem to be covered,³² the language employed clearly indicates that it was not the sole factor. In addition, there are certain "materials" such as copper for which incentive prices had been established to encourage their extraction from the earth.³³ To make contracts or subcontracts for such products subject to renegotiation would tend to nullify the incentive. To the draftsmen of this subsection, the language of Subsection (i)(1)(ii) met the problem in general although its application to specific situations may be in many instances difficult. The test of exemption of a raw material is the point at which the extracting industry customarily disperses the product in substantial quantities in the channels of industry other than that of extraction. Under this test, the industry of origin may generally perform certain processing, refining or treatment of the product so that different analogous products may be exempted at different stages of the processing, refining or treating. For example, aluminum ingots or pigs, and copper ingots, rather than bauxite or copper concentrates, are the customary form in which the trade acquires this raw material from the extracting industry, whereas crude oil is the form in which the oil refining industry normally acquires that raw material for industrial use. The language of the subsection requires that the product, to retain its exemption, must not have been "processed, refined, or treated beyond the first form or state suitable for industrial use." No implication should be drawn from this language that some processing, refining, or treatment is required in order to progress beyond the point of exemption. Clearly the oil refining industry is an industry, so that the utilization of crude oil by that industry is an industrial use of the product of an oil well, notwithstanding the fact that there has

³⁰ *Supra* note 11, at 128.

³¹ *Supra* note 11, at 147.

³² *Supra* note 11, at 128.

³³ The writer participated in the drafting of this subsection for the consideration of the Committee, and in analyzing the problems for which a solution was sought, does, to a certain extent, go beyond the legislative record.

been no refining up to that point. This is the rationale of the joint regulation promulgated as of February 1, 1943 by the Secretaries.³⁴

Subsection (i)(2)³⁵ confers discretion on the Secretary to exempt under circumstances where it was felt that renegotiation would not further the general purposes of the Act. To require a native of Iran constructing in Iran a railroad or other works necessary for the prosecution of the war to renegotiate his contracts is an unnecessary extension of the extraterritorial powers of the United States, and to enforce such action might interfere with the prosecution of the war. Accordingly, such contracts may be exempted under Subsection (i)(2)(i). A similar situation might not arise in the construction of a naval base in the Caribbean, and therefore the power granted to the Secretary is discretionary. The class of contracts enumerated in (i)(2)(ii) is not definitive or all-inclusive, but merely indicative of the general class or type which may be exempted.³⁶ The sole test is whether in the opinion of the Secretary profits can be determined with reasonable certainty when the contract price is established. Acting under this subsection the Secretaries of War and the Navy have exempted contracts and subcontracts for the purchase or lease of any interest in real property, for certain food products, with public utilities when made at public rates or charges, fixed, approved or subject to regulation by a public regulatory body, and for commodities, the minimum price for the sale of which has been fixed by a public regulatory body.³⁷ The last provision of Subsection (i)(2)(ii) was added in order to extend the discretion of the Secretary in making firm prices for limited periods and to permit the exemption of so-called "target price" contracts.³⁸

There are four provisions of the Act that provide periods of limitations for the commencement of renegotiation proceedings:

³⁴ JOINT STATEMENT, *supra* note 18, at 12, 13. H. R. 3015, 78th Congress, has been introduced by Representative Price on June 21, 1943, and, if enacted into legislation would permit the Secretaries to exempt raw materials by joint regulation, at any stage of processing, refining or treating.

³⁵ Subsection (i)(2) provides:

"(2) The Secretary of a Department is authorized, in his discretion, to exempt from some or all of the provisions of this section—

(i) Any contract or subcontract to be performed outside of the territorial limits of the continental United States or in Alaska;

(ii) any contracts or subcontracts under which, in the opinion of the Secretary, the profits can be determined with reasonable certainty when the contract price is established, such as certain classes of agreements for personal services, 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, of leases and license agreements, and of agreements where the period of performance under such contract or subcontract will not be in excess of thirty days; and

(iii) a portion of any contract or subcontract or performance thereunder during a specified period or periods, if in the opinion of the Secretary, the provisions of the contract are otherwise adequate to prevent excessive profits.

The Secretary may so exempt contracts and subcontracts both individually and by general classes or types."

³⁶ See *Springer v. Philippine Islands*, 277 U. S. 189, 206 (1928) for statement of pertinent exception to the *expressio unius exclusio alterius* rule.

³⁷ The Bituminous Coal Act of 1937, 50 STAT. 77, 15 U. S. C. 1940 ed., §833, gives the Commission power to prescribe minimum and maximum prices.

³⁸ *Supra* note 11, at 56, 58.

(1), Subsection (c)(6) specifies that no renegotiation shall be commenced more than one year after the close of the fiscal year of the contractor or subcontractor within which completion or termination of the contract or subcontract, as determined by the Secretary, occurs. It should be noted that this provision refers to completion or termination of the contract rather than the time of payment provided for in Subsection (c)(6)(i). For the purposes of this subsection the completion of a contract occurs at the time of final delivery or acceptance under the contract, rather than at the time of final payment; the fact that a contractor may still have certain obligations under guarantees of performance or the fact that there may be unliquidated items outstanding does not extend the time of completion beyond the date of final delivery or acceptance.³⁹ The date of termination would be that date on which all work under the contract has been terminated. Renegotiation commences on the date set for the initial conference unless otherwise agreed.

(2), Subsection (b) authorizes the parties to agree upon the period or periods when or within which renegotiations may be had. This agreement may lengthen or shorten the periods of limitations otherwise provided for in the Act.

(3), Subsection (c)(5) provides that, if a contractor or subcontractor files a statement of costs of production for prior fiscal periods in form prescribed by the Secretaries, no renegotiation shall be required for the fiscal period covered by the statement unless the Secretary shall within one year after the date of filing give written notice of a time and place for an initial conference to be held within sixty days thereafter.

(4), Subsection (h) provides that the Act shall remain in force during the continuance of the present war and for three years after the termination of the war, but no court proceedings brought under the Act shall abate by reason of the termination of the Act. The termination of the war would be the date of the signing of the final treaty of peace and not the cessation of hostilities. If three years after that date renegotiations have not been completed, all further authority to proceed under the Act, except for court proceedings instituted would be gone. In view of the requirement in the Act for the insertion of a renegotiation clause in contracts and subcontracts subject to the Act, the question is raised as to the power to renegotiate after this date under the renegotiation clause rather than under the Act. Congress in requiring the inclusion of the clause clearly intended to give some potency to the clause apart from the Act. A fairer result might be to terminate renegotiations for all contracts at the same time irrespective of the inclusion of the renegotiation clause.

³⁹ *Supra* note 18, at 16.