

# DISPOSAL OF CONTRACTOR-OWNED PROPERTY ON TERMINATION

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## INTRODUCTION

The enormity of the task of disposing of the property resulting from termination of war contracts has been the subject of such voluminous discussion in the daily press that it will be given no further treatment here. It is significant that there is unanimity of opinion that this will become one of the major problems to be faced in the post-war period. At the present time the War Department is, because of the changing conditions of war, actively engaged in making final settlement agreements; in fact, one Technical Service of the Army Service Forces, the Ordnance Department, has already settled over 5,300 contract terminations with \$81,900,000 paid on the termination of \$2,390,000,000 of supply contracts. Naturally, a large volume of contractor-owned property has been involved in such an operation.

The purpose of this article is briefly to outline the basic policies and procedures under which disposition of the property involved in these settlements has been carried out and to cover the situation at the moment of writing. With a substantial amount of legislation pending which involves policies affecting the national economy, and with various new procedures in preparation affecting the fundamentals of present operation, no attempt will be made to go beyond the announced policy of the present. It is believed that an exposition of the present methods is the best approach at this particular point in the development of the property disposition program.

## GENERAL DISPOSITION PROBLEM AND POLICIES

The property disposition policy of the War Department may be briefly stated as follows:<sup>1</sup> "So far as permitted by the terminated contract, property acquired for the performance of the contract is to be disposed of with reasonable dispatch, as

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<sup>1</sup> PR 15-106(2), Disposition of Property. Note: "PR" is the abbreviation habitually used to refer to Procurement Regulations, the official regulations pertaining to the industrial procurement activities of the Army Service Forces and the Army Air Forces. CODE OF FED. REGS., Title 10, Ch. 8. PR 15 is the regulation relative to the termination of contracts. C. C. H. War Law Serv. ¶23,501 *et seq.*

advantageously as is reasonably possible, in a manner which makes such property available for other productive use at the earliest possible moment. . . . Property not disposed of is to be transferred to the Government." This expression of desired policy is further expanded in the Memorandum of the Under Secretary of War of June 30, 1943, which states in part,<sup>2</sup> "These inventories of materials, parts, supplies and work in process must be utilized promptly in war production in the most efficient manner possible. Much of this material is critically needed by other war manufacturers and producers and it is the duty of War Department procurement officers to see that the material is made available at the earliest possible moment for use in essential war work." At the time of this memorandum, the emphasis was on reusing in other war work the materials resulting from termination.

The report of Messrs. Baruch and Hancock on War and Post-war Adjustment Policies released by the Office of War Mobilization on February 15, 1944, while recognizing the importance of prompt and proper disposition of property, recommended the prompt clearance of property from contractors' plants not later than sixty days after the filing of inventory lists.<sup>3</sup> This policy was made effective for the War Department in a Memorandum for the Chiefs of the Technical Services issued on March 4, 1944, from Headquarters, Army Service Forces, which stated, "However, the settlement and payment of contractors' claims shall not be delayed by reason of failure to dispose of property." This policy was further implemented by a new section of PR 15, Section VI-A, issued on April 28, 1944.

These, then, are the *policies* to be followed. The question is how shall they be carried out? Although it is not necessarily the case in the usual termination of contracts between private parties, the Uniform Termination Article for use in lump sum supply contracts contains provisions<sup>4</sup> requiring approval by the contracting officer of all dispositions of contractor-owned property. In this way the contracting officer is enabled to carry out the desired policies.

The disposal activity should be distinguished from the settlement agreement itself. They have, of course, one common base—allocability.<sup>5</sup> It is only property properly allocable to the uncompleted portion of the contract for which compensation on the settlement agreement can be made. It is likewise only property allocable

<sup>2</sup> The complete text of the Memorandum is to be found in PR 15-350.2.

<sup>3</sup> The "Baruch-Hancock" report also stresses the general reasons for clearing of plants in its Appendix 2, 1st paragraph, "The speedy adjustment of terminated contracts depends to a large extent on the prompt removal and disposal of completed articles, component parts, work in process, raw materials and equipment in the possession of the contractor at the time of termination. So long as the war continues it is essential to clear the contractor's plant as soon as possible so that it may return to the production of other needed war materials and to make available for other war production any property which can be used for that purpose. After the war the speedy disposition of such property is essential in order to clear the contractor's plant for a return to civilian production."

<sup>4</sup> PR 15-901(b)(6). This is true also of the Standard Termination Article formerly in use. Cf. PR 15-901 A(a)(2).

<sup>5</sup> By allocability is meant the determination of whether or not the cost of the property is, in fact, chargeable against the terminated portion of the contract. The principles used in this determination are found in PR 15-481, Statement of Principles for Determination of Costs upon Termination of Government Fixed Price Supply Contracts. See Part I of this symposium, in the Winter 1944 issue, pp. 512-4.

to the contract for which the Government has any obligation to dispose except when the contractor demands that property, which he claims to be allocable, be removed before the question of allocability has been settled; in that situation, the property is removed by the Government with a reservation that adjustment will be made later for any non-allocable property so removed.<sup>6</sup> It will be assumed, however, in the remainder of the discussion on general disposition, that the question of allocability has been resolved. Once allocability has been determined, the problem so far as the settlement agreement is concerned becomes one of accounting procedures to determine the cost of the property, the disposal credits of any authorized dispositions, the approved post-termination expenses connected with the disposition and any other financial aspects thereof. The problem of *property disposition*, however, is essentially one of exercising proper judgment, such as any business man has faced in finding himself with surplus property on hand; the issue is not what the property has cost but what can be done with it. For the solution of this problem, the War Department has depended to a large extent upon the assistance of its prime contractors.

Both the new Uniform and the old Standard Termination Articles obligate the prime contractor to assist in the disposition of property. From this has stemmed a vigorous program to utilize the full resources of the contractor's organization so as to dispose of the property rapidly and advantageously. Naturally, the contractor, if he is aggressive in his disposal assistance, benefits by more quickly clearing his plant and putting himself in funds. As a taxpayer, he also is interested in aiding the Government in obtaining the maximum return possible. Outstanding cases of assistance have been experienced, and more are anticipated with the development of techniques on the part of both contractor and Government personnel. Successful assistance, however, lies primarily in thorough cooperation between the contractor and the contracting officer, based on a common understanding of the problem faced and the parts to be played by both parties.

In summary, it appears that the problem of disposition is complicated by the tremendous size of the operation involved and the necessity for speed in action. It is further complicated by the fact that many contracting officers must exercise independent judgment on a tremendous volume of individual transactions which involve such diverse conditions that only general policies and procedures can be established. In addition it must be remembered that dispositions of surplus property are usually accompanied by substantial monetary losses since the costs of handling the property, and the inherent difficulties of finding the right buyer for widely varying items are involved. To solve these individual problems, procedures have been established and modified from time to time as discussed in the following paragraphs.

<sup>6</sup> PR 15-950 and PR 15-951, Article 7—Allocability.

## DISPOSITION PROCEDURE

One of the fundamental policies underlying the procedures for the disposition of property is that there shall be close cooperation and understanding between the contractor and the contracting officer. This applies not only to the disposition of property, but also to the other elements involved in the final settlement; but the teamwork required for adequate disposition is so important that special emphasis is warranted. Many contractors have set up separate departments for the handling of all termination matters, including the use of representatives to work with sub-contractors in establishing the groundwork for termination action when and if the necessity for it arises. Planning for terminations has caused some of these contractors to change their internal procedures with respect to controlling and recording inventories, allocation of charges and other factors pertaining to termination operations. Such changes have been effected to permit simpler and more direct action upon termination rather than the laborious disentangling of closely interwoven operations already experienced by contractors not properly organized.

As soon as possible after the Notice of Termination has been issued, it is required<sup>7</sup> that the contracting officer hold a preliminary conference with the contractor to make arrangements for the settlement. At this conference, the contractor should explore all factors connected with the disposition of property. He should obtain from the contracting officer specific instructions and authorization for his disposition activities which will result in post-termination expenses. Arrangements should be made, in the larger terminations, for the assistance of representatives of the contracting officer, familiar with termination inventory methods and requirements and with the technical aspects of the item being terminated, who can aid the contractor in setting up proper procedures for taking and recording the inventory. These arrangements are intended to facilitate the presentation of inventory lists which will be acceptable, and to prepare the contractor for disposition activity at the earliest possible moment, even before the submission of the inventory lists. In those important and complex cases justifying such action, and where time permits, it is suggested<sup>8</sup> that a conference be held between the contracting officer and the contractor prior to the issuance of the Notice of Termination. This permits the formulation of plans for termination operations of the contractor where such have not yet been established. Emphasis must be placed on getting the two parties together for the purpose of jointly making plans. Lack of understanding or willingness to cooperate can be very troublesome in introducing difficulties where none need exist.

## INVENTORY LISTS

The proper taking of an inventory of property resulting from the termination of a contract and the correct recording of the information on an inventory list is basic to sound disposition. Efforts on the part of the contractor or the contracting officer to dispose of the property quickly become ineffectual if prospective purchasers

<sup>7</sup> PR 15-322 (5)(c).

<sup>8</sup> PR 15-312(b).

cannot interpret the lists and readily recognize what is being offered for sale. Inaccurate recording also discourages disposal efforts because it frequently necessitates the retraction or correction of sales already effected since property represented on the inventory list cannot be delivered. Accurate and complete descriptions are essential to disposal as well as to proper verification of the charges claimed as a result of the property.

New Standard Inventory<sup>9</sup> forms have been issued to the contracting officers by Headquarters, Army Service Forces, and are in the process of being incorporated in the termination settlements now under way. The advantages to the contracting officer of forms are obvious since their use emphasizes the type of information desired and encourages complete data by the provision of headings and columns. The advantage of standardization to the contractor is equally apparent since it requires his interpretation of only one set of forms and instructions, with a subsequent reduction in the training and organization required for his personnel. Instances have occurred in which contractors have received as many different sets of inventory forms from their various contracting officers and prime contractors as they have had terminated prime and subcontracts. The resulting confusion within the contractors' organizations under these conditions is apparent, and the use of Standard Inventory forms will substantially improve this situation. Care and intelligence must nevertheless be used in their preparation and completion, with particular attention given to the matter of description. The test to be applied to an inventory list is for the writer of the list to examine it from the standpoint of a reader. General instructions are repeated several times in the new standard forms that sufficient information be given to enable a purchaser to make an intelligent selection from the list. In interpreting this instruction, it is important that the writer divorce himself from his familiarity with the property in question and think in terms of an outsider. He should adopt the attitude of a sales department which is preparing a catalog or brochure.

The contractor should establish a method for taking and recording the inventory which is suitable to the scope of the termination involved. On simple jobs, a small group can perform satisfactorily with relative informality. On larger jobs, more complex organization and procedure will be required.<sup>10</sup> In any case, certain basic functions are performed: First, the property should be segregated, if reasonably possible, and similar items grouped to eliminate confusion and duplication in recording. Second, the items must be counted by the usual means used in taking inventories and the general condition of the property noted. Third, the items must be analyzed for recording. This step requires that adequate business and engineering ability be assigned so that the necessary decisions can be made.

In the classification of the items for recording, the first breakdown must be made in accordance with the different types of property to be listed on the three standard

<sup>9</sup> Three Inventory Schedules of April 18, 1944, W.D., A.G.O. Forms 247, 248, and 246; PR 15-402.

<sup>10</sup> The War Department's Termination Accounting Manual, Chapter 2, Physical Inventory, indicates the various instructions and provisions which should be covered.

inventory forms; (1) materials, (2) work in process, (3) and production equipment. A second breakdown must be made to classify the items on each standard inventory form into the commodity groups appearing in the accompanying General Instructions. After these classifications, the proper recording on the inventory forms, together with the very important question of proper description, remains. In addition, the contractor is asked for his recommendations as to which items should be scrapped and what disposition might best be made of the remainder of the items. The Government also desires that the items be priced, even though the Total Cost method of presenting the claim is used.<sup>11</sup> Although such pricing is not necessary to actual disposition of the property, it is highly desirable since most administrative procedures for approving sales are related to the cost of the property sold.

From this description, it should be apparent that the presentation of inventory lists presents a number of problems with which the contractor may desire assistance. This is one of the reasons that conferences between the contracting officer and the uninitiated contractor have been strongly recommended. With proper instruction and understanding, the inventory problems tend to disappear, but without a sound foundation on which to build, they can be extremely difficult to solve.

#### SALVAGE AND SCRAP<sup>12</sup>

The Surplus War Property Administrator (hereafter referred to as SWPA) has stated: "The many groups who have analyzed the problem of contract termination have uniformly agreed that much of the property involved is of such special nature, or has been processed in such a way, as to admit of no possibility of use in its existing form. There is an additional amount which might be used if time permitted an extended search for an appropriate use, or if use restrictions could be relaxed. The necessity for prompt clearance of plants severely limits the amount of effort and time that can be expended on such a search. It is essential to make an early determination that property either offers reasonable possibility of sale, or should be scrapped."<sup>13</sup> For assistance in making this determination, the War Department has requested the contractor's opinion as indicated under the inventory procedure above. Great stress is laid on the fact that contracting officers must be vigorous in quickly exhausting possibilities of use and then, with full realization of the gravity of their decision, proceed to authorize disposition of the property concerned as scrap.<sup>14</sup>

Even though much, if not all, of the special materials, tooling, manufacturing

<sup>11</sup> PR 15-351.1.

<sup>12</sup> Throughout this section, the general emphasis is on the making of a determination that the property in question has no reasonable possibility of use but must be disposed of at a great monetary sacrifice. It is assumed that when such a determination is made, the natural result will be to salvage all possible desired items for maximum realization before the remainder is disposed of as scrap. Therefore, for the sake of brevity, the reference herein to scrap or scrapping will also be considered as including salvaging operations.

<sup>13</sup> 9 FED. REG. 4559, 4560 (April 29, 1944).

<sup>14</sup> OPI (Ordnance Procurement Instructions) 15,307.4.

gages and equipment and the parts and components in process may have no other reasonable use except as scrap, all possibilities of other use are considered. The requirements for such property for the manufacture of spare parts, the production capacity required for possible future war needs, the possibility of use in a continuing program for the same or a similar item, the possibility of conversion or application to other military or civilian use must all be satisfactorily weighed before the decision is made to scrap the property.

Because of its special nature, much of the property indicated above can be satisfactorily evaluated as having no other use by those experienced in manufacturing and military requirements. For this reason, it is recommended that representatives of the contractor and the contracting officer jointly study the problem of what property can be classed as scrap before a widespread attempt is made to find possible purchasers by circularization or other means. This is done in the interest of eliminating, from the item offered for sale, those items which obviously would have only a slight possibility of use. The wisdom of the decision not to circularize certain types of property has been demonstrated by the negative results of circularizations of similar property for substantial periods of time in the past. The decision that special property and work in process can have no other reasonable use is thus based on thorough consideration. Any property which appears to be salable or to have a reasonable use is subjected to selling procedures discussed hereafter,<sup>15</sup> and the property to be scrapped is disposed of as such by the contractor at the direction of the contracting officer.

If it is not practicable for the representatives of the contractor and the contracting officer to get together before taking the inventory to work out the general bases on which the contractor will segregate the items recommended for scrapping, the contractor performs this function alone to the best of his ability. Immediately after the submission of the inventory lists, in that case, the contracting officer's representatives will review the contractor's recommendations. Those items on which they concur will be authorized for disposition by the contractor as scrap, and those for which the contracting officer's representatives deem there is a reasonable possibility for use will be subjected to further disposal action. The contracting officer's representatives will also analyze the remaining items on the inventory lists to discover any additional items which might be scrapped. Again, after diligent efforts have been made to sell the remaining items as usable property, a further review is made to see whether or not any of the residual property should be salvaged or scrapped rather than to go to the expense of packing, shipping and storing.

While the decision whether property was to be approved for disposition as salvage or scrap was formerly left to the discretion of the individual contracting officer,<sup>16</sup> review is now required<sup>17</sup> by boards consisting of three or more members, of such cases involving property of \$50,000 cost value or more. Thus, the authority

<sup>15</sup> Pp. 653 ff., *infra*.

<sup>16</sup> PR 15-360.

<sup>17</sup> PR 7-408. This Procurement Regulation 7 now covers the disposition of all property including termination inventories.

and responsibility for making such determinations in the larger cases has been divided among several individuals instead of being placed on a single person. In the Ordnance Department, contracting officers have had local review boards available for the consideration of salvage and scrap determinations for some time with their use optional with the contracting officers.<sup>18</sup> The tendency has been to refer cases for board action at lower monetary levels than the one prescribed above.

Once the determination has been made that the property should be disposed of as scrap, the problem of pricing policies arises. Formerly, the entire matter was within the discretion of the contracting officer. The May 25, 1944 revision of Procurement Regulations now directs that sales of scrap be related to "the going price of the type of scrap in question" as determined, "by reference to published trade indicators or inquiry among Government agencies, dealers or other informed sources, taking into account transportation costs and sundry other charges."<sup>19</sup> If the sale is at the going price it may be made without competitive bidding. Otherwise, competitive bids are to be obtained and the sale awarded to the highest bidder unless all bids are rejected as unsatisfactory. All sales of scrap are subject to a warranty given by the buyer that he will use or sell the property only as scrap. Further, on April 28, 1944, the Surplus War Property Administrator issued a statement of policy which stated: "By subsequent regulations the Surplus War Property Administration will provide for . . . a mechanism for stopping of sales in any area where prices drop to unsatisfactory levels."<sup>20</sup> In this way, the sales of salvage or scrap property will be controlled through the authority of the contracting officer to direct dispositions made by the contractor.

#### SELLING PROCEDURE

The procedure for making sales of usable property is built around the fact that the contractor makes the sales of the contractor-owned property under the direction of or with the approval of the contracting officer.<sup>21</sup> All sales are made in an "as is" condition, and the contractor is not required to make sales on credit nor does the Government assume any resulting credit losses if such arise from the contractor's extension of credit. Unless some type of blanket prior approval to make sales has been issued to the contractor,<sup>22</sup> individual sales must be approved by the contracting officer before they are consummated. Such approval assures the contractor that any loss suffered by him (the difference between cost and realization), will be paid by the Government in the termination settlement. The contractor may retain property with the approval of the contracting officer. Under the standard instructions issued with the Notice of Termination,<sup>23</sup> the contractor is normally

<sup>18</sup> OPI 15-308.

<sup>19</sup> PR 7-410.2. This Procurement Regulation 7 now covers the disposition of all property including termination inventories.

<sup>20</sup> Statement by SWPA, April 28, 1944, Part IV B (2)(c); 9 FED. REG. 4559, 4560 (April 29, 1944).

<sup>21</sup> This is clearly set forth as follows in an excerpt from the Uniform Termination Article, "(b) . . . the contractor shall . . . ; (7) use his best efforts to sell . . . at the price or prices directed or authorized by the contracting officer, any property . . . provided, however, that the contractor (i) shall not be required to extend credit to any purchaser and (ii) may retain any such property at a price or prices approved by the contracting officer."

<sup>22</sup> P. 655, *infra*.

<sup>23</sup> PR 15-936, 7a.



permitted to retain any property for which he will not present a claim to the Government. If, however, he wishes to retain the property below cost, he must include the property on his inventory lists along with his offers for retention. The contracting officer must then determine whether or not such offers are satisfactory and promptly issue approval on the acceptable offers for retention. In the contracting officer's consideration of the contractor's offers, the latter are placed in the same position as any other bids with an allowance for any expenses such as packing and shipping normally present in the case of sales to other bidders.

Other than the contractor's offers for retention, the first consideration in the procedure of selling is to obtain acceptable bids from prospective purchasers. To accomplish this, the contractor will contact his suppliers for possible return for credit with necessary reduction for handling charges. In the standard instructions issued with the Notice of Termination,<sup>24</sup> he is authorized in advance to make such returns which are subject only to reasonable packing and shipping charges. If the suppliers will not accept return on such a basis, he is to obtain their best offer, which will be subject to the sales policies outlined below. The contractor is further requested to furnish lists of raw materials, purchased parts and supplies, to the Regional Office of the WPB in which the property is located. This action is for the purpose of obtaining the assistance of the War Production Board in finding possible users through publication in the "Redistributor," a weekly bulletin of its regional offices. The contractor is finally requested to contact the local industrial market for possible users, applying his knowledge of the potential purchasers so that only the most likely ones will be contacted. This effort is all in the interest of obtaining acceptable bids.

During this time, the contracting officer also searches for purchasers.<sup>25</sup> In the Ordnance Department,<sup>26</sup> each contracting officer has been advised to utilize, for this purpose, the services of the local Redistribution and Salvage Officer of his Ordnance establishment. These R & S officers have organizations which have gained wide experience in handling Government-owned property. Since the problem of finding purchasers for contractor-owned property is similar, this experience is very valuable. Therefore, the general rule in Ordnance is that the R & S officers perform most of the functions of the Contracting Officers in disposing of property.

The usual procedure followed by an Ordnance R & S officer is to break down the inventory lists submitted on the various terminations in process in accordance with the markets which he is contacting. These portions of the lists are directed to his representatives who specialize on the particular markets in question; thus, in Ordnance activity, he will have a steel man, a cutting tool man, a production equipment man, and other specialists depending on the type and variety of the property he is handling. These specialists compile periodic lists, of all the property in their charge, which they arrange to furnish to the most likely purchasers. Bids are normally requested to be sent directly to the individual contractor concerned, with a copy of the bid sent to the specialist. The contractor selects the best bid and

<sup>24</sup> PR 15-936, 7b.

<sup>25</sup> PR 15-361.

<sup>26</sup> OPI 15,311.

makes his recommendation for approval of a sale. After completing all possible dispositions, the specialist submits the residue which has not been disposed of to the R & S officer with any possible recommendations for scrapping or for taking title by the Government.

All of the sales made under the above system must comply with the standards set forth in the May 25, 1944, revision of Procurement Regulations, Part 7, which incorporates the policies of the Statement of April 28, 1944, by SWPA.<sup>27</sup> While, formerly, contracting officers operated entirely within their own discretion in this field, this recent statement sets limits which must be observed, and this applies to all sales including retentions by the contractor. The entire field of property is divided into two classes: (1) crude and raw materials and (2) all other property (except for capital equipment, which is to be covered by subsequent regulations). Crude and raw materials must be sold, with the approval of the contracting officer, at the current market price or reported to the disposal agency concerned<sup>28</sup> for disposition. For all other property, the general policy is that sales will be made with the approval of the contracting officer at the best price obtainable but may be made as low as "75% of (a) cost or (b) the price which that buyer would have to pay if he bought an equivalent quantity from a normal source of supply, whichever is lower."<sup>29</sup> If the property cannot be sold within a reasonable time under those conditions, sales may be made, "to a buyer who will consume the property in the United States for manufacturing or maintenance purposes, and who will agree that if he does not so consume it, he will not resell it at a profit."<sup>30</sup> Thus, the property may be sold at less than 75% of the cost or buyer's replacement price after a reasonable time if the purchaser is a direct user. All property not disposed of under these conditions will be scrutinized further to see if the reaction to its circularization furnishes sufficient additional evidence for authorizing its disposition as scrap. Upon demand of the contractor to remove the property to clear his plant, title will be taken by the Government.<sup>31</sup>

In all of this selling action, delay is inherent in the requirement that individual approval must be obtained by the contractor from the contracting officer before a sale can be consummated. As a result, the policy of authorizing contracting officers to grant blanket prior approval to contractors to make sales of various classes of property within definite limits was established.<sup>32</sup> This principle, judiciously applied, has been very successful in one particularly large termination of the Ordnance Department. As a result, the Ordnance Department has strongly recommended to its contracting officers the extension of this policy.<sup>33</sup> With blanket prior approval to contractors to make sales, the flexibility of the contractor in his selling activity is greatly enhanced since he is in a position to accept immediately a desirable offer and to make prompt shipment to the buyer.

<sup>27</sup> 9 FED. REG. 4559-61. In discussions of these standards and policies, limitations of space make possible discussion only of the major items bearing on the general problem.

<sup>28</sup> PR 7-206.3(1).

<sup>29</sup> PR 7-206.3(2).

<sup>30</sup> PR 7-206.3(3).

<sup>31</sup> Pp. 656 ff., *infra*.

<sup>32</sup> PR 15-359.

<sup>33</sup> OPI 15,309.

## CLEARING OF PLANT

As indicated above, under the policy of requiring the contractor to sell the usable property, it is apparent that such operations would tend to delay settlement and to keep the plants of contractors filled with property resulting from terminations unless a time limit for the completion of these operations were established. In the Report of Messrs. Baruch and Hancock of February 15, 1944, the following statement was made, "On the clearance of Government property from private plants, we recommend: A deadline of not later than 60 days after the filing of inventory lists, with manufacturers having the right to remove and store the property earlier at their own risk." This created the now familiar "60-day" limit which has been the subject of substantial study and consideration in order to create the regulations necessary for its implementation.

The new Uniform Termination Article places the financial risk upon the Government for loss or damage to property resulting from termination if the property remains in the hands of the contractor more than 60 days after the delivery of the pertaining inventory lists. This provision has provided a strong incentive for Government personnel to prepare administrative regulations for the removal of the property before this time limit has expired. Headquarters, Army Service Forces, issued a memorandum on March 4, 1944, to the Chiefs of the Technical Services to the effect that every effort would be expended in attempting to remove the property within 60 days and that contractors would be given the right to store the property elsewhere, at their own expense, prior to such time. This memorandum further stated that storage would be arranged and that, in the face of a lack of available warehouse space, efforts should be made to store the property with the contractor where possible.

Specific regulations further expanding this policy and providing the necessary procedures were issued on April 28, 1944, in the form of a new section of PR 15; *i.e.*, Section VI-A. This regulation is based on the principle that the property will be removed from the plant of, or stored with, the contractor, on his demand for removal after the expiration of 60 days from the submission of inventory lists.<sup>34</sup> It recognizes that inventory lists inherently contain various minor discrepancies in quantity between the property listed and the property actually present.<sup>35</sup> It further recognizes that complete and accurate verification of the quantities of all items delivered would place an impossible burden on the manpower available to the Government for such operations.<sup>35</sup> It provides a suggested form of a separate storage contract to be used for reimbursing the contractor for storage services.<sup>36</sup> The remaining point covered is the necessary adjustment of Government property accounting practices to carry out the policies above.<sup>37</sup>

From the standpoint of the contractor, the importance of this section is that it instructs contracting officers to remove or store the property promptly upon demand. Therefore, a prime contractor or a subcontractor (through his prime contractor)

<sup>34</sup> PR 15-853.

<sup>36</sup> PR 15-951.

<sup>35</sup> PR 15-860.1.

<sup>37</sup> PR 15-860.3, 860.4, 860.5.

can issue his demand to the contacting officer for removal and expect reasonable action in this regard. In taking delivery for shipment, the contracting officer is permitted to apply the principles of spot checking as he desires and is instructed to accept deliveries of the quantities and weights stated in the inventory lists within reasonable plus or minus tolerances in accordance with good commercial practice.<sup>38</sup> The acknowledgment of receipt given on delivery is final as to the property called for by such lists.<sup>38</sup> However, if the demand for removal is made before the question of allocability has been determined, the acknowledgment of receipt will contain a statement that acceptance of delivery of the property does not waive the Government's right to challenge allocability later.<sup>39</sup>

The subsequent steps of this procedure affect only internal Government procedures. The accountable property officer is permitted to establish "jacket accountability" in which he uses the inventory list, submitted with the demand for removal, as the prime record of the property received and without making entries of all of the items on individual record cards.<sup>40</sup> The treatment of any discrepancies on shipment to another Government establishment is also covered.<sup>41</sup> The general theory is that no liability for such discrepancies is to be carried back to the contractor, since the acknowledgment of receipt granted him is final and does not permit future reopening of the question of quantities delivered, except for fraud or such gross error as amounts to fraud.

The lack of available warehousing space is the basis for a policy of requesting contractors and subcontractors to store the property in their plants if at all possible.<sup>42</sup> To permit this storage, a separate storage contract is presented in suggested form.<sup>43</sup> Under this contract, a joint selective check of the quantities of items stored is required to be made by representatives of the contractor and the contracting officer. Under these arrangements, title to the property passes from the contractor to the Government upon execution of the separate storage contract which is terminable by either party on 30-day notice. Provision is made for the payment of charges for storage services at a negotiated rate. Additions may be made to the property stored and deliveries taken from time to time by the Government with provision for payment to cover the packing and shipping charges. In making the deliveries, the contractor will be held to plus or minus tolerances of quantities and weights within reasonable limits in accordance with good commercial practice. The contractor's liability for the property stored with him shall be for loss or injury to the property caused by his failure to exercise such care in regard to it as a reasonably careful owner of similar goods would exercise. There is no restriction on covering this risk by taking out insurance. The Government assumes the tax liability under this storage contract for increases in tax payable by the contractor by reason of his storing the property.

By this series of provisions, the storage contract effectively changes the status of

<sup>38</sup> PR 15-860.2.

<sup>40</sup> PR 15-858 (1) and (2).

<sup>42</sup> PR 15-854.

<sup>39</sup> Cf. *supra*, p. 648, text to footnote 6.

<sup>41</sup> PR 15-861.7.

<sup>43</sup> PR 15-951.

the property from the situation in which its disposition is holding up settlement to the one in which settlement of the termination can be made, and the question of storage and reimbursement therefor can be handled separately. Under both the storage agreement and the delivery for shipment as above, payment of the termination settlement can be made promptly upon the handling of the residual property under either of these two methods. The situation in which the property is neither shipped from the plant by the Government nor stored under a storage contract is not covered by this Section VI-A of PR 15, and is to be treated by subsequent regulations.

In the above paragraphs, the disposition of contractor-owned property by the contractor has been carried through the various channels now established, although this treatment has not exhausted the numerous variations and detailed situations existent. The most difficult decisions, which could only be indicated, are found in the daily transactions wherein contracting officers and review boards must decide whether or not property shall be salvaged or scrapped, and whether or not the offers for purchase are acceptable. Nevertheless, the system is working and a large volume of contractor-owned property is being disposed of, regularly.

#### SUBCONTRACTORS

The position of the subcontractor in the disposition procedure is prescribed by Procurement Regulations in paragraph 15-365 as follows:

"Disposition of property by subcontractor.—The sale or disposition of property related to the terminated contract which is in the hands of subcontractors or suppliers will be dealt with in accordance with any applicable provisions of the subcontract or purchase order in question and with substantially the same procedures, prescribed . . . , for the disposition of property in the hands of prime contractors. Except as provided in paragraph 15-359,<sup>44</sup> all disposals or retentions of property by subcontractors involving a loss which will become a part of termination charges to be borne by the Government should be submitted to the prime contractor for necessary approval or should be made consistently with a program approved by the prime contractor acting pursuant to authority granted by the contracting officer."

#### CONCLUSION

It is quite apparent from the foregoing that the procedure of property disposition is involved. In order to operate successfully, thorough understanding of the problems and procedures by all concerned is vital and the suggestion that the contractor work closely with their contracting officers cannot be overemphasized. It is also apparent that the progressive changes in the policies and procedures have been quite rapid, and it appears, at this time, that more changes are imminent. By studying the problems of terminating contracts and of property disposition carefully and by planning for the future, contractors should be in a position to keep in step with the changes which are sure to come.

<sup>44</sup>This reference is to Blanket Prior Approval to Make Sales, *supra*, p. 655.