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Modification to Contract Involving Cost Underrun

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The Internal Revenue Service may not use fiscal year 1993 cost underrun money to order an additional quantity of items under a contract. A modification of the contract to increase the quantity is chargeable only to funds current at the time of the modification.

DECISION

This responds to a request for an advance decision from the Regional Fiscal Management Officer, Southeast Region, Internal Revenue Service (IRS), concerning a proposal to use cost savings from a contract entered into with fiscal year 1993 funds to purchase an increased quantity of computer equipment under that contract. Cost savings resulted when the contractor, under the terms of the contract, reduced the price it charged IRS to reflect a price reduction it had received from its vendors. IRS has asked whether it may order an additional quantity of computer equipment using the savings from the price reduction (the cost underrun money). We conclude that these funds are not available for this purpose. A modification of a contract to increase the quantity constitutes a new obligation and is chargeable only to funds current at the time of the modification.

Under a longstanding rule of appropriations law, the "bona fide needs" rule, an agency may validly obligate an appropriation only to meet a legitimate and documented need existing during the period of the appropriation's availability. [1] B-226198, July 21, 1987; B-207433, Sept. 16, 1983. Funds from a fiscal year appropriation which are not obligated during that year are not generally available for new obligations in a subsequent year. See 31 U.S.C. Secs. 1341(a), 1553(a). However, contract modifications in a fiscal year subsequent to the year of the original contract that are found to be within the scope of the original contract are considered bona fide needs of, and thus chargeable to, the appropriation used to fund the original contract. 61 Camp. Gen. 609 (1982). IRS Regional Counsel argues that ordering an additional quantity is within the original scope of this contract, allowing use of the fiscal year 1993 savings, because the contract is an indefinite quantity contact. Memorandum to Chief, Centralized Procurement Branch, Atlanta Service Center, June 6, 1994. Such a contract, he asserts, contemplates changes in quantity, and he cited a 1947 Comptroller General decision, B-68707, Aug. 19, 1947, in support of his position. He notes, also, that the parties contemplated price reductions.

We disagree with the IRS position. We addressed this situation in a 1983 decision, B-207433, Sept. 16, 1983. The Army, in 1977 using funds that expired

at the end of fiscal year 1979, contracted with Magnavox for 509 thermal viewers. The Army had wanted to procure 557 viewers, but had enough money only for 509. In 1981, Magnavox discovered that its costs would be below the target cost in the contract, and proposed that the Army use the cost underrun to purchase the 48 additional viewers. We concluded that a modification of the contract to increase the quantity from 509 to 557 would be outside the scope of the original contract, and as a new obligation of the Army, chargeable to the appropriation current at the time the additional 48 viewers are ordered. The surplus funds resulting from the cost underrun were no longer available since the appropriation to which they should be credited expired at the end of fiscal year 1979.

Magnavox argued that the surplus funds should remain available to the Army because the Army had originally wanted to purchase 557 viewers, rather than just 509, and thus had a bona fide need for them attributable to the fiscal year 1977 appropriation. We disagreed:

"This is an inversion of the so-called 'bona fide needs rule.' . . . [N]othing in the bona fide needs rule suggests that expired appropriations may be used for an item for which a valid obligation was not incurred prior to expiration merely because there was a need for the item during that period. . . . Once the obligational period has expired, the procurement of an increased quantity must be charged to new money, and this is not affected by the fact that the need for that increased quantity may in effect be a 'continuing need' that arose during the prior period." B-207433, Sept. 16, 1983.

Although the IRS contract may be characterized as an indefinite quantity contract, no legally enforceable obligation arose until IRS ordered a specified quantity; that obligation is recorded against the supporting appropriation at the time the order is placed. See 47 Comp.Gen. 155, 158 (1967). While IRS may have had a bona fide need for the additional quantity of components during fiscal year 1993, it had not yet ordered the additional components. If IRS had placed an order in fiscal year 1993 for the additional quantity, it could have charged that obligation against available fiscal year 1993 funds including cost underrun funds had they been then available. Because each order constitutes a new obligation, any order now for additional quantities is chargeable to current year funds.

The fact that the contract contemplated price reductions does not change our view of the contract's scope. The contract provided that the contractor would pass on to IRS any price reductions received from its vendors in the form of a reduced contract price, not in the form of additional quantities. The 1947 decision cited by Regional Counsel in support of his position is not applicable here; it does not address an order under a contract for additional quantities. In that decision, the War Department contracted with Harvard Law School for seven terms of legal training for two officer trainees. After the completion of three terms, the War Department wanted to have two trainees other than those who began the course attend the remaining four terms. This modification did not change what was ordered under the contract, two semesters of legal education; it simply changed the persons attending Harvard. B-268707, Aug. 19, 1947.

We conclude that the IRS may not now use fiscal year 1993 cost underrun money to order an additional quantity of computer equipment. The availability of these funds has expired. Any contract modification to increase the quantity ordered constitutes a new obligation that IRS must charge to funds current at the time

of the modification.

1. Payments are chargeable to the year in which the obligation was incurred, even though funds may not actually be disbursed until a later year, as long as the need existed when the funds were obligated. See, e.g., 33 Camp. Gen. 57, 61 (1953).