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DECISION



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

FILE: B-125045 **DATE:** October 13, 1977
MATTER OF: Department of Water Resources of the State
of California

DIGEST:

1. Cost principles in FPR § 1-15 are applicable to grants and contracts with State and local governments under FPR § 1-15.701-1. Therefore, supplemental agreement entered into by Department of Interior and State of California after effective date of regulation is subject thereto whether properly characterized as grant or contract.
2. No authority found to support conclusion that cost principles override specific inconsistent agreement between the parties. Therefore, payment may be made pursuant to agreement even though inconsistent with cost principles. However, Department should take action to bring agreement in line with cost principles.

By letter dated July 7, 1977, the Department of the Interior (Interior) requested a decision concerning the allowability of legislative costs incurred by the State of California in the performance of contract 14-06-200-9755.

The contract for the design and construction of water resource facilities for the joint use of the State and the United States was executed on December 30, 1961. Article 15 of the contract, in pertinent part, provided:

"The cost of construction of the joint-use facilities * * * shall include:

* * * * *

"(7) Indirect costs distributed in the customary manner of the agency which incurred the related direct cost."

On January 12, 1972, the parties to the contract executed a supplemental agreement which established operating criteria for the joint-use facilities. Article 35(c) of the supplemental agreement provided as follows:

"The costs of caring for, operating, maintaining, and replacing the joint-use and Federal-only facilities * * * shall include:

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"(11) Indirect costs relating to the above items distributed in the customary manner of the party which incurred such costs. For the State these will be determined in accordance with the manual entitled 'Application and Use of Indirect Costs in the Department of Water Resources,' as it may be amended or superseded, and for the United States these will be determined in accordance with the manual of 'Reclamation Instructions,' and the Region 2 supplement, as they or either of them may be amended or superseded."

Under the contract and the supplemental agreement, the State has allocated legislative expenses as indirect costs.

In the interim between the execution of the contract and the supplemental agreement, Bureau of the Budget Circular A-87 (now Federal Management Circular 74-4) was issued (May 9, 1968) and the Federal Procurement Regulations (FPR) were amended to implement the Circular (January 11, 1970). The Circular and the implementation contain principles for determining costs under grants and contracts with State and local governments. FPR § 1-15.713-8 specifically provides that legislative expenses are unallowable.

In view of the cost principles, Interior raises two questions:

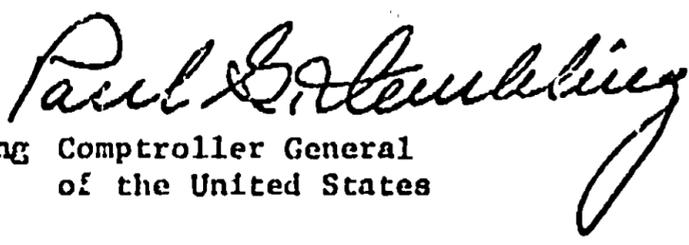
"1. Was the then Bureau of the Budget Circular A-87, dated May 9, 1968 (Subpart 1-15.7 of Title 41 of the Code of Federal Regulations), intended to apply to long-term cost sharing agreements executed by Federal agencies prior to the effective date of that Circular?

"2. Was Circular A-87 intended to apply to all contracts with State Governments or only to Federally assisted programs?

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The purpose of the questions is to ascertain whether the State is precluded from allocating the legislative costs as part of its indirect costs.

To reach a conclusion, it is not necessary to answer the questions as presented. With respect to the initial agreement executed before Circular A-87 and the provisions of FPR § 1-15 were effective, we see no reason why the contract should not be carried out in accordance with its terms. The supplemental agreement, however, was executed after the effective date of the Circular and the regulatory provision. We conclude that the agreement is either a grant or a contract and therefore is covered under FPR § 1-15.702.1. While, as noted, legislative expenses are not allowable under FPR § 1-15.700, we have been able to find no authority to support the proposition that the cost principle overrides a specific inconsistent agreement of the parties. Cf. G. I. Christian v. United States, 100 Ct. Cl. 1. (1963), cert. denied, 375 U.S. 954 (1963). Therefore, payment may be made in accordance with the agreement even though that is inconsistent with the cost principles of FPR § 1-15. However, we concur with a suggestion of the Office of Management and Budget that action be taken to bring the agreement in line with the cost principles.


Acting Comptroller General
of the United States