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The Comptroller General
of the United States

Washington, D.C. 20548

# Decision

Matter of: Tacoma Boatbuilding Company

File: B-200692.2

Date: September 1, 1987

## DIGEST

Fiscal year 1982 Shipbuilding and Conversion (Navy) appropriation, available for obligation through fiscal year 1986, may not be used beyond original period of availability to fund replacement contract for two vessels deleted from original contract by a modification initiated by the Navy in order to prevent possible rejection of the contract under section 365 of the Bankruptcy Code by a contractor who had filed in bankruptcy for reorganization. Originally obligated funds remain available for replacement contract to complete unfinished work only when failure of performance is beyond the agency's control. Modification here was an essentially voluntary act on the part of the Navy. Cost of replacement contract is therefore chargeable to appropriations current at the time the replacement contract was made.

## DECISION

The Deputy Commander for Contracts, Naval Sea Systems Command (NAVSEA), requested our opinion on whether fiscal year 1982 "Shipbuilding and Conversion, Navy" (SCN) funds are available for reprocurement following a contract modification made after the contractor filed for reorganization under chapter 11 of the Bankruptcy Act. For the reasons stated below, we conclude that NAVSEA may not use the expired 1982 SCN funds for the reprocurement.

BACKGROUND

In September 1980, the Navy entered into a contract with the Tacoma Boatbuilding Company (Tacoma) for 12 Ocean Surveillance Ships (T-AGOS). After partially performing the contract, Tacoma began to have cash flow problems. Because of its cash flow problems on the T-AGOS contract and others, Tacoma filed for reorganization under chapter 11 of the Bankruptcy Act in September 1985. At that time, it had delivered six of the 12 ships contracted for.

In order to minimize disruption of the T-AGOS shipbuilding program, the Navy initiated a modification of its contract with Tacoma.1/ The Bankruptcy Act provides that, subject to the court's approval, the debtor (or his trustee) may assume or reject any executory contract of the debtor (with exceptions not pertinent here). 11 U.S.C. §§ 365(a) and (d)(2). Since it seemed likely that Tacoma would reject the balance of its T-AGOS contract completely under this provision because of its severe cash flow problems, the Navy initiated a contract modification, signed March 27, 1986, permitting Tacoma to liquidate its performance bond and use the proceeds to ease its cash flow problems. The modification also reduced the number of ships to be provided under the contract from 12 to 10.

Because the Navy still needed the 12 ships originally contracted for, it decided to competitively reprocure the two ships that had been deleted from the Tacoma contract. However, it was not possible to enter into the reprocurement contract prior to the end of fiscal year 1986.

The T-AGOS contract was an incrementally funded multiple-year contract. The funds originally obligated for the two vessels in question were fiscal year 1982 SCN appropriations with a 5-year period of availability, expiring for obligational purposes on September 30, 1986. If these funds cannot be used for the reprocurement, the Navy would have to return them to the Treasury, and charge the reprocurement to current appropriations.

It has long been held that where a contract is terminated because of the contractor's default, funds obligated under the contract remain available beyond their normal expiration date to complete the unfinished work. E.g., 9 Comp. Dec. 10 (1902). The Navy asks whether this general rule may be extended to permit the use of the fiscal year 1982 SCN appropriation for reprocurement under the circumstances present here--where there is no actual termination for default but where the contract is modified to prevent its rejection under the Bankruptcy Act.

DISCUSSION

When an agency terminates a contract because of a contractor's default, it may enter into a replacement contract with another contractor to complete the unfinished work and may, within limits, charge the cost to the appropriation which

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1/ The procedural history of the contract is more complicated. We recite only those facts necessary to decide the question before us.

was originally obligated even though that appropriation has expired for purposes of new obligations. See generally, e.g., 60 Comp. Gen. 591 (1981). The cited decision points out that to not allow use of prior year funds would require deobligation of those funds and obligation of current year funds available when the replacement contract is entered.

However, this concept is not available to the Navy in this case. An essential element of the replacement contract rule, as reflected in decisions such as 60 Comp. Gen. 591, is that the failure by the original contractor to complete performance must be beyond the agency's control. Thus, the originally obligated funds remain available for the replacement contract in the case of a termination for default, but not in the case of a termination for convenience. 60 Comp. Gen. at 595.

In this case, there was no default by Tacoma, nor was there a rejection of the contract under section 365 of the Bankruptcy Code. Indeed, whether Tacoma would have sought to invoke section 365 and whether this action would have been approved by the court at the time the Navy and Tacoma agreed to the modification is speculative. What we have here is, at best, an "anticipatory modification" of the contract based upon Navy's assessment of what might otherwise have happened.

Whether the modification was an appropriate means of protecting the government's interests, or whether it was wise from a program or financial perspective, are questions beyond our present concern. The fact remains that the modification was an essentially voluntary act on the part of the Navy, and as such is beyond the scope of the replacement contract rule. Therefore, the replacement contract for the two ships deleted from the Tacoma contract is properly chargeable to SCN appropriations current at the time the replacement contract is made.

Finally, we note that the submission refers to the deleted ships as a "continuing obligation." While they may well

have been a continuing need, they were not, for the reasons stated above, a continuing obligation.2/

for Milton J. Socolar
Comptroller General
of the United States

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2/ For discussions of this distinction in different contexts, see B-226198, July 21, 1987, and B-207433, September 16, 1983.