

TO

W. A. E.

FROM

REMARKS:

This 3 page memo gives the substance of Patterson's 30 page statement. Believe it is worth the ten minutes it will take you to read it.

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CHAIRMAN'S OFFICE

BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM

10/13/43

Mr. Eccles:

The attached memo came up on yesterday just after you had left, so I am dropping it by the hotel in case you want to look it over before the meeting on Monday. There were no calls or mail of any great urgency.

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BOARD OF GOVERNORS  
OF THE  
FEDERAL RESERVE SYSTEM

# Office Correspondence

Date October 20, 1943.

To Chairman Eccles

Subject: \_\_\_\_\_

From Mr. Clayton

The following are the high lights of Judge Patterson's statement on contract termination before the House Military Affairs Committee on October 15, 1943.

The first five pages are background for what follows and develop the thesis that a solution of the problem of contract termination is necessary from two standpoints: (1) to maintain adequate current production of munitions; (2) to assist in maintaining economic and political stability at the end of the war. Thereafter he lays down three principles to be recognized in any legislation and administrative procedure relating to contract termination, as follows:

1. Termination adjustments must be effected by negotiated agreements.
2. The negotiations must be final and not subject to reopening by any independent agency, except for fraud.
3. The negotiations must be conducted by the procurement agencies.

As to the finality of adjustments, he makes this statement, which has reference to the Comptroller General's recent letter. "Consequently, any review of the many decisions taken, with authority to reopen those with which the reviewing agency disagreed, would really amount to a brand-new negotiation and would rob the original settlement of any real significance. It would just double the work."

The principal argument in behalf of the proposition that procurement agencies (rather than the Comptroller General's office) should make the settlements is that an increasing volume of contract terminations are occurring while the procurement program is still critical. He thus concludes, "It is apparent that during the war such settlements are an integral part of the procurement process and must be left with the procurement agencies."

To rebut the contention that the delegation and re-delegation of authority to settle would not protect the Government interest, Patterson devotes several pages to a description of the extensive machinery and experienced professional personnel already engaged in examining, auditing and settling termination contracts. The implication is that this machinery

is just as careful and as qualified to protect the Government interest as would be the technicians in the Comptroller General's office. Patterson concludes his argument with this statement. "But in doing this we have surrounded the delegations with careful safeguards, which ensure that the settlements will be handled by responsible officers assisted by capable technical personnel, and with all necessary information before them." The Comptroller General's function in these settlements would be a limited one, as set forth in this sentence. "The Comptroller General is therefore entitled to a copy of such agreements and to vouchers and documents showing compliance by the contractor with the settlement agreement to support any payments under it, but he has no right to disallow payments made pursuant thereto in the absence of fraud."

At this point Patterson called attention to the fact that the right of the procurement agencies to make negotiated settlements has apparently been questioned by the Comptroller General, which, he says, makes further legislation desirable. He adds, "Many contractors now fear that the Comptroller General may not recognize negotiated settlements and may suspend payments under them. This uncertainty among contractors is already having serious effects in the making of new contracts, and unless promptly corrected, threatens to create substantial obstacles to war production."

Patterson also includes a discussion of "Interim Financing for Termination". This follows the lines indicated in our recent discussions with the armed services in connection with the VT program. He proposes the following program: "First, authority to make advance or partial payments to contractors and subcontractors; second, authority to make guaranteed or direct loans to contractors and subcontractors; third, allowance of interest on termination claims in order to encourage the use of private financing and to equalize the position of contractors who use such private financing with that of contractors being financed by advance payments or guaranteed loans."

In connection with loans, Patterson makes a case for direct loans as follows: "To supplement guaranteed loans, however, especially for companies which may not have an adequate credit standing for normal banking purposes the War Department believes that it should have authority to make direct loans to contractors and subcontractors either through its own machinery or another government agency."

One proposal heretofore made by the Army is withdrawn. This is the authority to purchase the claims of subcontractors or suppliers when there is danger of the insolvency of an intervening subcontractor or prime contractor. Patterson says: "As a result of further study, however, we have concluded that the practical problems involved in such purchases of rights should be further explored before adoption of this method now."

In addition to his discussion of problems which would be met by the proposed legislation, Patterson draws the attention of the Committee to some other matters as to which the War Department later may suggest legislation or present its views with respect to such legislation.

1. Overall Settlements. This means settlements by one procurement agency of various contracts lumped together, even in some cases where the contracts may be with various procurement agencies.

2. Disposition of Property. Only one paragraph is devoted to this problem, which is the chief burden of the pamphlet of the Automotive Council for War Production which you brought to the attention of Judge Byrnes. Patterson recognizes the importance of the matter, however, since he states: "A sound solution for the many aspects of this question will require careful study by the Executive Department and by Congress. Such studies are of course already underway."

3. Dismissal Wages. Patterson suggests that Congress should consider to what extent dismissal wages or other assistance should be provided for war workers who are dismissed because of contract terminations.

4. Informal Contracts. This is evidently not very important.

5. Facilitating Suits. This has to do with setting up additional branch courts and other methods to provide more adequate legal machinery for handling suits against the Government for contract termination. Patterson states: "The War Department sees no reason to object to any such measures which Congress may consider appropriate. We do not believe however that the Courts can possibly handle any significant part of the settlement of contract terminations and we think that reliance must be placed upon efficient and administrative procedures in order to achieve prompt and expeditious settlements."

The draft of the proposed legislation is attached and is in substance the same as the draft furnished us some time back by Colonel Cleveland.

Attachment



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A BILL

(based largely upon HR 3022, S. 1268 and amended  
Committee Print of July 7, 1943)

To facilitate the termination financing of war production contracts and subcontracts, and for other purposes.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled,

SECTION 1. Advance and Partial Payments: (a) In connection with the termination in whole or in part of any prime contract which is connected with or related to the prosecution of the war, each department or agency which has been or may hereafter be authorized to place contracts pursuant to the authority granted by Section 201 of the First War Powers Act, 1941, is authorized to make or agree to make advance or partial payments to the prime contractor or to a subcontractor under such prime contract to the following extent:

- (1) Whenever the whole or any part of the amount payable to a subcontractor upon a subcontract has been finally determined by agreement between the prime contractor and subcontractor or otherwise, and has been approved by the department or agency as properly to be included in determining the amount payable by the Government to the prime contractor in connection with such termination, the amount so approved may be paid to the prime contractor

or directly to the subcontractor for the account of the prime contractor.

- (2) Where any amount payable to a subcontractor upon a subcontract has not been so determined and approved, the department or agency from time to time may estimate the approximate amount so payable and properly to be included in determining the amount payable by the Government to the prime contractor in connection with such termination and may pay not more than 90% of this estimated amount to the prime contractor or directly to the subcontractor for the account of the prime contractor.
- (3) The department or agency from time to time may estimate the approximate amount payable to the prime contractor in connection with such termination, after deducting the final or estimated amounts payable with respect to subcontracts, and may pay not more than 90% of this estimated amount to the prime contractor.
- (4) Whenever, at any time before final settlement, the department or agency finally determines, by agreement or otherwise, any amount or amounts to be payable to the prime contractor in connection with such termination, the department or agency may pay to the prime contractor such amount or amounts to the extent that such payment

will not duplicate any amounts paid under the foregoing paragraphs.

(b) (1) Except as provided in paragraph (2) below, all advance or partial payments made to or for the account of a prime contractor under subsection (a) shall be applied against the amount finally determined to be payable by the Government to the prime contractor in connection with such termination; but the authority conferred by this section shall not otherwise limit in any way the authority of the department or agency to make payments upon the final determination of any amount payable in connection with a termination of a prime contract. Where such advance or partial payments exceed the amount finally determined to be payable to the prime contractor, the excess advance or partial payment shall be treated as a loan to the prime contractor, except as provided in paragraph (2) below.

(2) Where the advance or partial payments made to a subcontractor by a department or agency under subsection (a)(2), or by the prime contractor at the direction or with the approval of the department or agency, exceed the amount finally determined to be payable to such subcontractor and includible in determining the amount payable by the Government to the prime contractor in connection with such termination, the excess shall be treated as a loan from the Government directly to such subcontractor. In such cases the prime contractor shall not be liable to the Government for such excess, and if he paid it to the subcontractor, shall receive credit from the Government for the amount of such excess.

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(3) Any such excess advance or partial payment shall be repayable on demand and shall bear interest at such rate, not to exceed 6% per annum, as the department or agency concerned may fix by general regulation or otherwise, for the period from the date the excess advance or partial payment is made to the date on which it is repaid. No officer of the Government in the absence of fraud on his part shall be liable for the making of any such excess payment.

(c) In its discretion, a department or agency may exercise the authority and discretion conferred by this section with respect to any two or more prime contracts or subcontracts as a group or unit, whenever the department deems such action appropriate.

SECTION 2. Loans and Guaranteed Loans: (a) The Department of War, the Department of the Navy and the Department of the Treasury, and the United States Maritime Commission are each authorized -

- (1) to enter into contracts with any Federal Reserve Bank, Reconstruction Finance Corporation, or any other public or private financing institution, guaranteeing such financing institution against loss of principal or interest on loans, discounts or advances, or on commitments in connection therewith, which may be made by such financing institution for the purpose of financing any contractor, subcontractor, supplier or other person who is or has been engaged in the performance of any contract

or operation deemed by such department or commission to be connected with or related to the prosecution of the war and who is deemed by such department or commission to have rights in connection with the termination in whole or in part of any one or more such contracts or operations.

(2) to make, enter into contracts to make, or to participate with any department or agency of the United States, any Federal Reserve Bank, the Reconstruction Finance Corporation or other public or private financing institution in making, loans, discounts or advances, or commitments in connection therewith, for the purpose of financing any such contractor, subcontractor, supplier or other person; Any such loan, discount, advance, guarantee or commitment in connection therewith shall be secured, if the department or agency concerned deems it reasonably practicable, by either assignment of or covenants to assign appropriate rights of such contractor, subcontractor, supplier or other person in connection with the termination of such contract or operation.

(b) Subject to such regulations as the Board of Governors of the Federal Reserve System may prescribe after consultation with the departments and agencies concerned, any Federal Reserve Bank is authorized to act, on behalf of any such department or agency, as fiscal agent of the United States in carrying out the purposes of this Section.

SECTION 3. Allowance of Interest: (a) In connection with the termination, otherwise than for the default of the prime contractor, of any prime contract connected with or related to the prosecution of the war, interest shall be allowed and paid at the rate of  $2\frac{1}{2}$  per cent per annum, computed as follows:

(1) On amounts paid or payable by the prime contractor to subcontractors, up to the amount approved by the department or agency as properly to be included in determining the amount payable to the prime contractor, interest shall be computed from the date of payment by the prime contractor.

(2) On the remainder of the amount finally determined to be payable to the prime contractor interest shall be computed the effective date of the notice of termination.

(3) Any advance or partial payments made pursuant to Section 1 of this Act shall be applied, as of the date made (or tendered), to reduce the amounts on which interest is otherwise payable under paragraphs (1) and (2) above.

(4) If the prime contractor unreasonably delays the final determination of the amount payable to him, interest shall not be payable for the period of such delay.

(5) If the prime contractor has received a Government guaranteed loan or interest bearing advance payments, and interest on such loan or advance payments has been waived, in whole or in part, during the period following the effective date of the notice of termination, by virtue of the terms of the loan or advance payment

agreement, such waived interest shall be deducted from the interest otherwise allowable under this subsection (a).

(b) In determining the amount payable to or for the account of the prime contractor in connection with the termination of a prime contract, a department or agency may recognize interest paid or payable to subcontractors on amounts due them to such extent as it deems proper.

SECTION 4. Use of Appropriated Funds: For any of the purposes described in this Act which it is authorized to carry out, any department or agency may utilize any funds now available to it or hereafter made available to it for the purposes of the contracts terminated or being terminated in connection with which action is authorized to be taken pursuant to this Act. For the purposes of Section 2, each department and agency authorized to act under that section may utilize any funds now available to it or hereafter made available to it for purposes of procuring war materials, supplies, and equipment, or expediting the production thereof. The Secretary of the Treasury upon request of the head of any department or agency concerned may make any such transfers of appropriated funds as may be necessary to carry out the provisions of this Act.

SECTION 5. Miscellaneous Provisions: (a) The head of each department or agency is authorized to prescribe for his department or agency such regulations as he deems necessary to carry out the provisions of this Act. Such regulations may require such statements,

certificates and affidavits for the purposes of Sections 1 and 2 of this Act as the Department or Agency concerned deems necessary to protect the interests of the United States; and any such statement, certificate or affidavit shall be subject to the provisions of Section 35A of the Criminal Code (Title 18, U.S.C. 80). A department or agency may subject any advance or partial payment or any loan, discount, advance or commitment made under this Act to such terms and conditions as it deems appropriate to protect the interests of the United States or to effectuate the purposes of this Act.

(b) The head of any department or agency may delegate any authority or discretion conferred by this Act upon him or upon his department or agency to such officers or civilian employees within his agency or within any other department or agency of the United States as he may prescribe and may authorize any such officer or civilian employee to make successive delegations or such authority and discretion, with power of redelegation.

(c) Each department or agency shall have authority to make any contract necessary or appropriate to carry out the provisions of this Act and any such contract need contain only such provisions as are appropriate to the type of contract involved. Any agreement of a type referred to in this Act may be made at any time, whether before or after the giving of a notice of termination of a prime contract which is connected with or related to the prosecution of the war.

(d) Nothing in this Act shall be construed to limit or modify any authority granted by the President to the Chairman of the War Production Board or to any other department or agency with respect to procurement by the several federal departments and agencies and to war production.

(e) As used in this Act, the term "subcontract" means any contract, agreement or purchase order directly or indirectly connected with or related to the performance of any prime contract or any other subcontract; and the term "subcontractor" means the holder of one or more subcontracts.