The Tax Court and Profit Renegotiation

Arthur Edward Burns

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ARTHUR EDWARD BURNS
The George Washington University

RENEGOTIATING the profits of government contractors is a special and unusual form of profit control. It bears no resemblance to such forms of profit control as public utility rate regulation or profits taxation. The renegotiation process seeks out what is determined to be "excessive profits" made on doing business with the Federal Government, particularly defense and space business, and recaptures these profits. The process is both complex and controversial.

Complexity arises for a number of reasons. Firms doing business with government show great diversity in financial structure, accounting methods, ways of doing business, degrees of risk, efficiency, and reliance on government financing. Products and services range widely, from familiar commercial-type products to wholly new weapons and space systems, to research, management, and developmental work. Contractual arrangements take many forms and contractor-government relationships vary importantly. Other elements enter the picture. Statutory guidelines for excessive profit determination are indeed general; court decisions shift directions, and profit analysis leaves much to be desired. All this breeds endless controversy in the renegotiation process as seen in the four Tax Court cases reviewed later in this paper: Boeing, North American Aviation, Offner Products and LTV.

LEGISLATIVE BACKGROUND AND PROVISIONS

Profit renegotiation as Federal policy extends back more than a quarter of a century. In 1942 Congress authorized the Secretaries of War and Navy and the Chairman of the Maritime Commission to renegotiate war contracts and to recapture profits found by them to be excessive; this authorization was included in legislation appropriating funds for the conduct of the war.[1] Given the emergency of the time, war procurement had to be speeded up with quickly mobilized industry whose costs were highly uncertain. Careful contract negotiation would have been a time-consuming process. Consequently, renegotiation was adopted to speed the contracting process, with

[1] Act of April 28, 1942, ch. 247, sec. 403, 56 Stat. 245.