FAR – Cost Accounting Preambles and Regulations*

*Excerpts from FAR Appendices A & B

Appendix A – Cost Accounting Preambles and Regulations

Appendix B – Cost Accounting Preambles

FAR: Appendix A – Cost Accounting Preambles and Regulations

** This Appendix is provided for the convenience of users of the looseleaf FAR. The official codified Cost Accounting Standards appear at 48 CFR Chapter 99.*

Preambles to the Cost Accounting Standards, Related Rules and Regulations, and the FAR System

Part I
Preambles to the Cost Accounting Standards Published by the Cost Accounting Standards Board

Preambles to Cost Accounting Standard 401, Consistency in Estimating, Accumulating and Reporting

Preamble A
Original Publication of Part 401, 2-29-72

Preamble to the original publication of 4 CFR Part 401, 37 FR 4139, Feb. 29, 1972. Because that publication also added 4 CFR Parts 331, 351, 400, and 402, material relating to those parts has been omitted. It appears in the Supplements to those parts.

General Comments.

The purpose of the regulations promulgated today by the Cost Accounting Standards Board is to implement section 719 of the Defense Production Act of 1950, as amended, 50 U.S.C.App. 2168, which provides for development of Cost Accounting Standards to be used in connection with negotiated national defense contracts and for disclosure of cost accounting practices to be used in such contracts. The Board believes the materials being promulgated today constitute a significant initial step toward accomplishing one of its major objectives -- improved cost accounting and the proper determination of the cost of negotiated defense contracts. The regulations spell out contract coverage (Part 331), disclosure requirements (Part 351), a compilation of Definitions (Part 400), and two Cost Accounting Standards, one calling for consistency in estimating, accumulating, and reporting costs (Part 401), and the other calling for consistency in allocating costs incurred for the same purpose (Part 402).

Development of the material being promulgated today began many months ago with extensive research. It included examining publications on the subject, conferring with knowledgeable representatives of various Government agencies, Government contractors, industry associations, and professional accounting associations, and identifying and considering all available viewpoints. From this research, the initial versions of the material now being published were developed. As a part of the continuing research effort, these initial drafts were sent to 81 agencies, associations, and Government contractors which had expressed interest in assisting the Board in its work, and their comments were solicited. Some national defense contractors field-tested the material to see how it would apply to and affect their operations and advised the Board of their findings. In each step of the research process, the Board and its staff have urged and received active participation and assistance by Government, industry, and accounting organizations. Their cooperative efforts contributed in large measure to the exposure draft published in the December 30,1971, *Federal Register* for comment.

To better assure that all who might want to comment had an opportunity to do so, the Board supplemented the *Federal Register* notice by sending copies of the *Federal Register* materials directly to about 175 organizations and individuals who had expressed interest or had provided assistance in the development of the published material. Also a press release was distributed announcing the publication, which resulted in numerous articles in journals. The Board availed itself of all opportunities to publicize the proposals and solicit comments on them.

Written comments in response to the published material were requested by February 4, 1972. Comments were received from 105 sources, including Government agencies, professional associations, industry associations, public accounting firms, individual companies and others. The Board appreciates the obvious care and attention devoted by commentators, and as will be seen below, the Board has greatly benefited from the comments received.

Many of the comments received were addressed to all parts of the proposed Board rules as well as to the question of public availability of the Disclosure Statements. All of the comments received have been carefully considered by the Board taking into account the requirements of section 719. Understandably, many of the comments were addressed to issues which recur in two or more of the proposed parts while others dealt only with specific sections. Comments which dealt with 11 general issues are discussed separately below followed by a section-by-section analysis of other comments. Appropriate changes have been made in the material promulgated based on the Board’s disposition of the comments received.

Those comments and suggestions received which are of particular significance are discussed below.

Section 401.20 Purpose.

Commentators stated that the purpose of the standards would require each contractor to revise his formal system of accounts in order to maintain them on a basis used for estimating Government contracts. The Board did not intend that requirement. The standard does not contain any requirement that a contractor must revise his formal system of accounts. Cost accounting records are supplemental to, and generally subsidiary to a contractor's financial records. However, it is necessary that the cost accounting records be reconcilable to the contractor's general financial records.

Two commentators believed that the term "practices" in the phrase "Practices used in estimating costs in pricing proposals" could be confused as including estimating techniques relating to quantitative determination as well as the cost accounting practices used in estimating. The Board does not agree, because nothing in the standard precludes the use of any quantitative estimating tools.

Section 401.50 Techniques for Application.

Several commentators believed there may be an inconsistency between the requirements of the standard and the ability to make changes to established cost accounting practices. The Board intends that compliance with respect to proposals shall be determined as of the award date of the contract or as of the date of final agreement on price if the contractor has submitted cost or pricing data pursuant to Pub.L.87-653. Modifications of established cost accounting practices for accumulating and reporting costs are permitted by other regulations of the Cost Accounting Standards Board without causing a violation of this standard. The Board has modified the standard to express these intentions.

Section 401.60 Illustration.

An illustration has been added to this section to emphasize a requirement of the standard that any significant cost must be accumulated and reported in sufficient detail to permit its comparison the estimates made therefor.

Effective Date and Application.

For the convenience of readers, the following summarizes the effective dates set forth in 331.8, 351.4(e), and Parts 400, 401, and 402, which were transmitted to the Congress on February 24, 1972, pursuant to section 719(h)(3) of the Defense Production Act of 1950 as amended. After the expiration of a period of 60 calendar days of continuous session following the date of transmittal to the Congress, the regulations herein promulgated shall take effect as set forth in those regulations, unless there is passed by the two Houses a concurrent resolution stating in substance that the Congress does not favor the proposed standards, rules, or regulations.

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4. Any contractor having a contract awarded prior to July 1, 1972, which contains a clause which already incorporates requirements governing submission of Disclosure Statements and application of Cost Accounting Standards will be required to comply with the provisions of that clause. In this connection, such contractor and the respective contracting agencies whose contracts contain such a clause should review those contracts to determine whether negotiations should be instituted to make Parts 400 through 402 applicable to them.

Preamble B
Preamble to Amendments of 11-7-73

Preamble to revision of the definitions of "actual cost" and "Indirect cost pool" in 401.30(a)(2) and (4), published at 38 FR 30725, Nov. 7, 1973. Material referring to other parts of 4 CFR Chapter III has been omitted; it appears in the Supplements to those parts.

The purpose of this publication by the Cost Accounting Standards Board is to amend Parts 331, 351, 400, 401, 402, 403, and 404 of its rules and regulations. The amendments, which are minor clarifications to the regulations, were published in the *Federal Register* of September 5, 1973 (38 FR 23971). The amendments: * * * (c) modify certain definitions in Parts 400, 401, 402, 403, and 404 for the purposes of uniformity among the various parts. Only one comment in response to the September publication has been received by the Board. This expressed agreement with the proposed changes.

In view of the foregoing, the following amendments to the Boards regulations are being made effective November 7, 1973.

Preamble C
Amendment published 11-30-76

Preamble to the addition of Appendix -- Interpretation No. 1 added on Nov. 30, 1976, at 41 FR 52427.

Interpretation No. 1 to Part 401, Cost Accounting Standard, Consistency in Estimating, Accumulating and Reporting Costs, is being published today by the Cost Accounting Standards Board pursuant to Section 719 of the Defense Production Act of 1950, as amended. (Pub.L.91-379, 50 U.S.C.App. 2168.)

This Interpretation culminates extensive research over a period of several years on the subject of accounting for the costs of direct materials not incorporated in end items. This research indicated that, as a general rule, the cost of such materials is being allocated properly to cost objectives. Accordingly, the Board concluded that a Cost Accounting Standard on this subject was not warranted at this time. However, the research indicated that frequent questions were raised with respect to the requirements of Part 401 regarding consistency between estimating the costs of certain direct materials in pricing proposals and the accumulation and reporting of such costs. Thus, the Board concluded that it would be desirable to issue an Interpretation of Part 401 to address specifically the requirements regarding consistency between estimating and accounting for the costs of such direct materials.

Section 401.40 requires that a contractor's "practices used in estimating costs in pricing a proposal shall be consistent with his cost accounting practices used in accumulating and reporting costs." Many contractors estimate the cost of certain direct materials, such as materials that will be scrapped, as a percentage of basic direct material requirements or of some other base. A significant number of questions have been raised as to the cost accounting practices to be followed where the cost of such materials is estimated on the basis of percentage factors. The Interpretation being published clarifies the requirements of Part 401 in this regard.

A proposed Interpretation was published in the *Federal Register* of June 24, 1976, with an invitation to interested parties to submit written comments. The Board supplemented the invitation in the *Federal Register* by sending copies of the proposed Interpretation directly to over 1,000 organizations and individuals. The Board received 43 written comments, all of which have been carefully considered by the Board.

In addition to an evaluation of the written comments, conversations were held with thirteen of these commentators who indicated particular problems with the proposed Interpretation. The Board takes this opportunity to express its appreciation for the time and effort expended by those who met with the Board representatives or provided written comments.

Comments of particular significance with respect to the proposed Interpretation are discussed below.

1.**-- Need for an Interpretation**

Several commentators stated that as the Interpretation expands the scope and is not consistent with the intent of Part 401, which they say requires only a comparison of actual costs with estimated costs for direct material. They argued that the Defense Contract Audit Agency (DCAA) guidance to its field auditors in October 1973 satisfactorily explained the meaning of Part 401. In general, these commentators felt that an Interpretation to Cost CAS 401 was not needed.

The Board's research indicates that an Interpretation is needed. Numerous and widespread questions have been raised concerning whether application of a percentage factor to a base as a means of estimating the costs of certain additional direct material requirements is in compliance with Part 401 when the contractor accumulates direct material costs in an undifferentiated account. The Board notes that a similar question with respect to direct labor is specifically addressed in Part 401. Section 401.60(b)(5). In that Illustration, the accumulation of total engineering labor in one undifferentiated account is not in compliance with Part 401 where the contractor estimates engineering labor by cost function. Part 401 does not, however, specifically address the consistency requirement for direct materials, nor did the DCAA guidance specifically cover this matter. Accordingly, the Board concludes that this Interpretation is needed. In view of the fact that the Interpretation clarifies what is already required by Part 401, the Board does not agree that it expands the scope of the Standard.

2.**-- Materiality**

A number of commentators maintained that the cost of the materials estimated by means of a percentage factor was usually insignificant. These commentators were concerned that extensive records or analyses would have to be developed for insignificant amounts. The Board, of course, has always been concerned about the question of materiality and is on record as stating that the administration of its rules, regulations, and Cost Accounting Standards should be reasonable and not seek to deal with insignificant amounts of cost. To assure the application of the materiality criterion in this instance, specific language has been introduced which provides that the Interpretation applies only where "a significant part of costs" is estimated by means of a percentage factor. Furthermore, the Interpretation being published today recognizes that the accounting requirements of Part 401 depend on "the significance of each situation."

3.**-- Estimating Technique Versus Practice**

Several respondents were of the opinion that the proposed Interpretation was inappropriate because they felt that the use of percentage factors to estimate the cost of certain direct materials is an estimating "technique," rather than an estimating "practice." Thus, they contended, the Interpretation is improperly covering an area not subject to Part 401, i.e., "estimating techniques," and would limit the use of estimating factors as quantitative estimating tools. Some of these respondents noted that the Board recognized the difference between techniques and practices in the prefatory comments to Part 401, as published in the *Federal Register* of February 29, 1972. In that publication, the Board noted the concern of some commentators that the term "practices" in the phrase "practices used in estimating costs in pricing proposals" could be confused as including estimating techniques relating to quantitative determinations. In response to those comments, the Board stated that "nothing in the Standard precludes the use of any quantitative estimating tools."

The Board reaffirms this conclusion. However, the Board did not intend to deny all interest in practices so readily subject to abuse. There are cases in which contractor percentage estimates are not adequately supported either by data as to relevant past experience or in any other manner. In such cases, particularly, the Board feels that the use of a percentage factor as a means of estimating the costs of additional direct materials is an estimating practice which must be consistent with the practices used in accumulating and reporting costs.

4.**-- Retroactivity**

A few commentators were concerned about the possible retroactive application of this Interpretation. They noted that the requirement of Part 401, as interpreted, would apply as of the date a contractor was first required to use that Standard. The commentators were concerned that those contractors who have not accounted for material costs in accordance with the Interpretation could be held to have been in noncompliance with Part 401, and therefore subject to a downward price adjustment in accordance with paragraph a(5) of the Cost Account Standards clause (4 CFR 331.50). These commentators urged that the Interpretation be effective on a prospective basis only. Some of these commentators suggested that the substance of the Interpretation should be a new Standard, with the opportunity for an equitable adjustment under a(4)(A) of the Cost Accounting Standards clause.

As already noted, the Board has carefully considered whether the subject of the Interpretation should be encompassed in a new Standard. The Board has concluded that the accounting for direct material cost as explained by this Interpretation is required by Part 401 and therefore should have been accomplished as of the date that Standard first became applicable to a contractor. Nevertheless, the Board recognizes that there has been widespread uncertainty about the application of Part 401 in situations where certain material costs are estimated on the basis of percentage factors. In addition, the Board believes that the determination of the cost impact of a contractor's failure in the past to follow Part 401 as interpreted would be extremely difficult. Under the circumstances, the Board believes that the effort to seek contract price adjustments as a result of this Interpretation would, in most cases, be counterproductive. Accordingly, the Board believes that, in most cases, the process of attempting to determine price adjustments as a result of the retroactive application of Part 401 as interpreted would not be warranted.

5.**-- Cost Accounting Practices**

The proposed Interpretation stated that contractors who use a percentage factor to estimate certain direct material costs for a contract must "for that contract" maintain an adequate record or prepare an analysis of the actual cost. A number of commentators understood this sentence to require the recording or analysis on a contract-by-contract basis of the actual cost of materials represented by an estimated percentage factor. Many of these commentators noted that it would be difficult, if not impossible, to comply with this requirement. Other commentators questioned what was meant by an adequate record or an analysis.

As noted above the use of percentage factors for estimating direct material costs is an estimating practice which, pursuant to Part 401, must be consistent with the cost accounting practices used in accumulating and reporting costs. The Board notes however that Part 401 neither prescribes nor precludes any particular cost accounting practice. The Board recognizes that the consistency requirement of Part 401, as it pertains to direct material costs, could be met in a variety of ways. The Board is therefore of the view that it would be neither appropriate nor practical to prescribe by means of this Interpretation the amount of detail in accumulating and reporting costs which is deemed to be consistent with the use of percentage factors in estimating costs. The Board believes that the amount of detail which should be maintained with respect to direct material costs is a matter which is best left for decision by the appropriate Government procurement authorities on the basis of facts and circumstances of each situation. The Interpretation being published today has been revised accordingly and all references to the type of records to be maintained or analyses to be performed have been deleted.

6.**-- Application to Developmental and Research Type Contracts**

Many commentators urged that this Interpretation not apply to developmental and research type contracts. They said that since only material issued to these kinds of contracts is charged to such contracts, there would be no overstatement of material costs. They urged further that it would be impossible to maintain actual cost records by contract to record the additional material required and that it was extremely difficult to estimate additional material requirements because of the lack of past experience. Also, the commentators contended that material requirements on such contracts were not significant. Other commentators suggested that this Interpretation should not apply to cost type contracts.

It appears that these comments were generated mainly by the impression that the proposed Interpretation required records or analyses to be maintained by individual contract. As noted above, the Interpretation has been revised to make clear that no particular record or analysis is required by Part 401. The requirement for consistency in estimating, accumulating and reporting costs, however, applies to all contracts. The fact that a development contract or cost-type contract is involved does not remove this requirement. The Board feels that the changes made in the Interpretation should serve to minimize the problems described by these contractors.

7.**-- Application to Standard Cost Accounting Systems**

Several commentators suggested that this Interpretation not apply to standard cost systems. They argued that costs are not accumulated by contract or product and, therefore, compliance with the Interpretation would require a complicated and expensive recording system. They felt further that in setting standards, they use past experience plus engineering adjustments and could be charged by the Government with the need to comply with the records requirement of the Interpretation for each of their Standards.

Contractors using standard costs for material must comply with Part 407, the Use of Standard Costs for Direct Material and Direct Labor, which addresses the accounting for direct material and variances from standard costs of material. In the opinion of the Board, these contractors will be in compliance with Part 401 as interpreted.

8.**-- Application to Specific Factors**

Various commentators inquired about the application of this Interpretation to certain specific factors used in estimating contract price proposals, not necessarily related to the cost of additional direct materials. Among the factors mentioned were those to provide for inflation, contingencies resulting from indefinite or incomplete bills of material, losses in common inventory accounts, and miscellaneous small parts and hardware items. As noted in the Interpretation, its need was prompted by questions about the use of percentage factors to estimate the costs of "additional direct materials"; i.e., generally those direct materials not incorporated in end items. Factors such as those used to provide for inflation or allowances for incomplete bills of material do not represent costs of "additional direct materials," as that phrase is used in the Interpretation. In the opinion of the Board, this interpretation does not apply to the costs represented by such factors.

Factors used in a proposal to provide for inventory losses represent the costs of additional materials which are governed by this Interpretation. With respect to factors for small parts, the Board notes that in accordance with Part 401, 401.60, Illustrations, a practice of estimating an average cost for a minor standard hardware item is considered to be consistent with the practice of recording the actual costs of such items.

The amount of detail to be used in accumulating and recording such costs, however, is a matter to be decided in accordance with this Interpretation.

9.**-- Application of Interpretation to Direct Labor**

A number of commentators raised questions concerning the applicability of the Interpretation to direct labor. Several commentators said it should not apply to such labor but should be clearly limited to direct materials. One commentator felt that the Interpretation was equally applicable to direct labor and should so state.

As already noted in paragraph 1, above, Part 401 includes specific provisions on the consistency requirements regarding direct labor. Accordingly, the Board is of the opinion that no further specific coverage of direct labor is required in this Interpretation.

Preamble D
Preamble, to Document Published 6-8-78

The document published on June 8, 1978 at 43 FR 248 19, revised 401.10. This amendment was part or a publication which added 331.30(b)(3). Only the portion of the preamble which describes the revision to 401.10 is printed here. The remainder or the preamble appears as preamble K of the supplement to Part 331.

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In the *Federal Register* of February 16, 1977 (42 FR 9391), the Board proposed to amend section. 10, General Applicability, of standards 401 through 409 to conform these sections to the general applicability section as it appears in standard 410 et. seq. No comments were received on this proposed amendment. The Board considers this change to be appropriate and is amending standards 401 through 409 as set forth below.

Preambles to Cost Accounting Standard 402, Consistency in Allocating Costs Incurred for the Same Purpose

Preamble A

Preamble to Original Publication of Part 402, 2-29-72

Preamble to original publication of 4 CFR Part 402, 37 FR 4139. Feb. 29, 1972. That publication also included the addition of 4 CFR Parts 331, 351, 400, and 401, and so material relating to those parts has been omitted. It appears in the Supplements to those parts.

General Comments.

The purpose of the regulations promulgated today by the Cost Accounting Standards Board is to implement section 719 of the Defense Production Act of 1950, as amended, 50 U.S.C.App. 2168, which provides for development of Cost Accounting Standards to be used in connection with negotiated national defense contracts and for disclosure of cost accounting practices to be used in such contracts. The Board believes the materials being promulgated today constitute a significant initial step toward accomplishing one of its major objectives -- improved cost accounting and the proper determination of the cost of negotiated defense contracts. The regulations spell out contract coverage (Part 331), disclosure requirements (Part 351), a compilation of Definitions (Part 400), and two Cost Accounting Standards, one calling for consistency in estimating, accumulating, and reporting costs (Part 401), and the other calling for consistency in allocating costs incurred for the same purpose (Part 402).

Development of the material being promulgated today began many months ago with extensive research. It included examining publications on the subject, conferring with knowledgeable representatives of various Government agencies, Government contractors, industry associations, and professional accounting associations, and identifying and considering all available viewpoints. From this research, the initial versions of the material now being published were developed. As a part of the continuing research effort, these initial drafts were sent to 81 agencies, associations, and Government contractors which had expressed interest in assisting the Board in its work, and their comments were solicited. Some national defense contractors field-tested the material to see how it would apply to and affect their operations and advised the Board of their findings. In each step of the research process, the Board and its staff have urged and received active participation and assistance by Government, industry, and accounting organizations. Their cooperative efforts contributed in large measure to the exposure draft published in the December 30, 1971, *Federal Register* for comment.

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Written comments in response to the published material were requested by February 4, 1972. Comments were received from 105 sources, including Government agencies, professional associations, industry associations, public accounting firms, individual companies, and others. The Board appreciates the obvious care and attention devoted by commentators, and as will be seen below, the Board has greatly benefited from the comments received.

Many of the comments received were addressed to all parts of the proposed Board rules as well as to the question of public availability of the Disclosure Statements. All of the comments received have been carefully considered by the Board taking into account the requirements of section 719. Understandably, many of the comments were addressed to issues which recur in two or more of the proposed parts while others dealt only with specific sections. Comments which dealt with 11 general issues are discussed separately below followed by a section-by-section analysis of other comments. Appropriate changes have been made in the material promulgated based on the Board's disposition of the comments received.

Those comments and suggestions received which are of particular significance are discussed below.

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Part 402 Title.

One commentator pointed out that the definition of the word “allocate” covered all of the actions encompassed by the word “charge” and, therefore, the title of the standard should be changed to delete the words “charging and.” The Board agrees and has made the appropriate change here and elsewhere throughout the standard.

Section 402.40 Fundamental Requirement.

A number of commentators suggested a change to the standard to eliminate the requirement that direct and indirect costs be consistently allocated to all final cost objectives. Making the standard applicable only to individual contracts would permit a choice to be made solely on the basis of short-term economic benefit; the Board therefore has not adopted the suggestion.

Section 402.50 Techniques for Application.

Several commentators noted that the standard discusses the required treatment of incurred costs but does not cover estimated costs. The Board intends that both types of costs be covered by the standard and has therefore added a new paragraph to this section to make that intention clear.

A number of commentators suggested that the concept of materiality be included in the standard to allow the handling of minor direct cost items as indirect costs similar to the treatment accorded materiality in current ASPR regulations. The Board agrees, and has included a materiality statement in this section.

Several commentators did not understand the relationship of this standard to the Disclosure Statement. (This relationship is set out in paragraph (b) of this section). The Board intends to allow the contractor to disclose the cost accounting practices and criteria appropriate to his own situation while at the same time imposing the requirement that he adhere consistently to the choices once made. The Disclosure Statement is the vehicle by which the contractor describes the criteria and circumstances which define costs which are or are not incurred for the same purpose.

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Effective date and application. For the convenience of readers, the following summarizes the effective dates set forth in 331.8, 351.4(e), and Parts 400, 401, and 402, which were transmitted to the Congress on February 24, 1972, pursuant to section 719(h)(3) of the Defense Production Act of 1950 as amended. After the expiration of a period of 60 calendar days of continuous session following the date of transmittal to the Congress, the regulations herein promulgated shall take effect as set forth in those regulations, unless there is passed by the two Houses a concurrent resolution stating in substance that the Congress does not favor the proposed standards, rules, or regulations.

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4. Any contractor having a contract awarded prior to July 1, 1972, which contains a clause which already incorporates requirements governing submission of Disclosure Statements and application of Cost Accounting Standards will be required to comply with the provisions of that clause. In this connection, such contractor and the respective contracting agencies whose contracts contain such a clause should review those contracts to determine whether negotiations should be instituted to make Parts 400 through 402 applicable to them.

Preamble B
Amendments Published 11-7-73

Preamble to revision of the definitions of “cost objective” and “indirect cost pool”, 402.30(a) (2) and (6); 38 FR 30725, Nov. 7, 1973. Material relating to other parts of 4 CFR Chapter III, published in the same document, has been omitted, and appears in the Supplements to those parts.

The purpose of this publication by the Cost Accounting Standards Board is to amend Parts 331, 351, 400, 401, 402, 403, and 404 of its rules and regulations. The amendments, which are minor clarifications to the regulations were published in the *Federal Register* of September 5, 1973 (38 FR 23971). The amendments: * * * (c) modify certain definitions in Parts 400, 401, 402, 403, and 404 for the purposes of uniformity among the various parts. Only one comment in response to the September publication has been received by the Board. This expressed agreement with the proposed changes.

In view of the foregoing, the following amendments to the Board's regulations are being made effective November 7, 1973.

Preamble C
Amendment Published 6-18-76

Preamble to the addition of Appendix -- Interpretation No. 1 added on June 18, 1976 at 41 FR 24691.

Interpretation No. 1 to Part 402, Cost Accounting Standard, Consistency in Allocating Costs Incurred for the Same Purpose, is being published today by the Cost Accounting Standards Board pursuant to Section 719 of the Defense Production Act of 1950, as amended. (Pub.L.91-379, 50 U.S.C.App. 2168). The interpretation deals with the application of 402.40 of Part 402 to proposal costs. Section 402.40 provides that, "All costs incurred for the same purpose, in like circumstances, are either direct costs only or indirect costs only with respect to final cost objectives."

A number of questions had been raised by both the Government and contractors as to how Cost Accounting Standard 402 is to be applied to the accounting for proposal costs and, particularly, as to whether all costs incurred in preparing proposals are incurred for the same purpose, in like circumstances. A proposed interpretation was published in the *Federal Register* of February 4, 1976, with an invitation to interested parties to submit written comments if the proposed interpretation did not respond fully, or did not respond clearly enough, to what the Board understood to be the questions which had arisen. The Board also supplemented the invitation in the *Federal Register* by sending copies of the proposed interpretation to several hundred organizations and individuals. The Board received 32 written comments from companies, Government agencies, industry and professional associations, and others. All of these comments have been carefully considered by the Board. The issues of particular significance which were discussed by respondents in connection with the proposed interpretation are summarized below, together with explanations of the changes made in the interpretation being published today. The Board takes this opportunity to express its appreciation for the helpful suggestions and criticisms that were received.

(1) *Specific requirement provision.* Several commentators, while suggesting changes to the proposed interpretation published on February 4, 1976, commended the Board for recognizing the problem with respect to the application of 402.40 of Part 402 to the costs incurred in preparing proposals and believed that the interpretation would resolve a long-standing area of controversy. The most prevalent comments received dealt with costs incurred in preparing a follow-on proposal which is not specifically required by an existing contract. Many commentators suggested that the words "specific requirement" be deleted and that, in lieu thereof words such as "related to," "arising from," "identified with," or "directly associated with," be used. Other commentators, while agreeing that the "specific requirement" provision should be retained, suggested an expansion to also cover proposals "related to" existing contracts such as proposals for follow-on contracts. Still other commentators, however, believed that the "specific requirement" provision was appropriate and should be retained without addition or other change.

In the February 4, 1976, publication of the proposed interpretation, the distinguishing characteristic noted by the Board for determining if circumstances can be considered to be different with respect to costs incurred in preparing two proposals was whether one proposal was prepared pursuant to a specific requirement of an existing contract while the other was not. The Board continues in the belief that the "specific requirement" provision is the distinguishing characteristic and, accordingly, has retained this provision in the interpretation being published today.

Several commentators suggested that proposals prepared in order to comply with other contract provisions such as when the Government exercises an unpriced option or when an option is repriced, should considered to be specifically required under the Interpretation. The Board believes that the interpretation being published today accommodates this suggestion.

One commentator suggested that the Board's intent be clarified with respect to whether only proposals required by line items in a contract are considered to be specifically required by the contract. The Board intended that, while the "specific requirement" could be a line item in a contract, it need not be. Proposals specifically required by any other provisions of a contract, such as the requirement in the Changes clause of Standard Form 32, that any "claim by the contractor for adjustment under this clause must be asserted within 30 days from the date of receipt by the contractor of the notification of change," are considered to be specifically required under the interpretation.

(2) *Indirect allocation of all proposal costs.* A few commentators recommended clarification of the final paragraph in the proposed interpretation as published on February 4, 1976. One commentator stated that the paragraph could be interpreted as authorizing contractors to allocate all proposal costs indirectly while another commentator believed that the subject of indirect allocation of all proposal costs should be developed later as a separate issue. The paragraph has been revised (a) to give recognition to the fact that some contractors' accounting practices now provide that all proposal costs are pooled and allocated indirectly and (b) to make it clear that, in this respect, no change in a contractor's accounting practice or allocation method is required by this interpretation if the cost accounting practice is being followed consistently and if the allocation method provides an equitable distribution to all final cost objectives.

(3) *Determination of cost accounting practices by contracting officer.* A few commentators stated that the words, "specific requirement of an existing contract" would place contracting officers in the position of determining cost accounting practices because they could determine whether there would be a specific requirement in a contract.

Contracting officers now decide for almost every contract whether to include or exclude specific contractual requirements covering a wide variety of activities. The Board believes that inclusion or exclusion of a specific requirement in a contract may influence the cost accounting practice being followed but the decision to include or exclude the requirement is not the determinant of the cost accounting practice.

(4) *Prospective application.* Two commentators suggested that, under this interpretation, certain proposal costs which some contractors have allocated directly to contracts will have to be allocated indirectly. One of the commentators recommended that, consequently, the interpretation should be applied on a prospective basis only.

Cost Accounting Standard 402, which became effective July 1, 1972, states that, "All costs incurred for the same purpose, in like circumstances, are either direct costs only or indirect costs only with respect to final cost objectives." Interpretation No. 1 to Part 402 recognizes that the circumstances involved in preparing certain proposals are different from the circumstances involved in preparing other proposals. The interpretation explains when, under the Standard, certain proposal costs are consequently deemed to have been incurred in unlike circumstances and therefore may be accounted for differently.

Although the interpretation is being provided to explain in greater detail how Cost Accounting Standard 402 applies to costs incurred in preparing proposals, the Standard from its inception has applied to these costs in this way. As to any individual contractor, Standard 402 has applied to such costs from whatever date that Standard became applicable to that contractor. The commentator's recommendation therefore has not been accepted. In view of the widespread uncertainty over the application of Standard 402 to proposal costs, however, the Board believes that any failures to follow the Standard in this respect have been inadvertent. The Board also believes that any adjustments should be made with due consideration to the Board's statement on materiality.

(5) *Accounting for the cost of proposals for follow-on contracts.* Several commentators stated that the interpretation would create cost accounting problems with respect to accounting for the cost of proposals for follow-on contracts. The statement was made that a follow-on proposal is prepared by employees assigned full time to the on-going program and that it would be most difficult and impractical to attempt to separate their labor costs for preparing follow-on proposals from their other labor costs of the on-going program.

The Board recognizes the possibility that some contractors may have to refine somewhat their present practices for distributing incurred labor costs in order to separate the costs of preparing proposals for a follow-on contract from the costs of an existing contract. The Board does not agree, however, that whatever refinements may be necessary should be difficult or impractical to develop.

(6) *Other comments.* One Commentator suggested that it be clearly stated in the interpretation that proposal costs allocated direct to contracts will have overhead and General and Administrative expenses (including indirect proposal costs) applied. The Board agrees that proposal costs allocated direct to a contract are no different than any other costs allocated direct to that contract but believes this is self-evident and that no change in the interpretation is required.

Another commentator suggested that the word “bid” be added to the interpretation in conjunction with the word “proposal.” The Board intends that the interpretation apply to a “proposal” as defined in 4 CFR, Part 400.

A few commentators requested clarification of the wording of the introductory comments and the proposed interpretation published on February 4, 1976. The introductory comments stated that, “Costs * * * are incurred in different circumstances * * *” whereas the proposed interpretation stated that, “The contracting parties can determine that the circumstances are different * * *.” Accordingly, the Board has deleted the words, “The contracting parties can determine that * * *” from the interpretation being published today.

Another commentator suggested that the phrase, “to all work of the contractor,” in the last sentence of the third paragraph of the interpretation be clarified because some companies have several indirect cost pools for proposal costs, one for each major product line within a division. The commentator believed that the phrase could be misinterpreted as limiting the number of such indirect cost pools to only one pool for each division. It is not the intent of the Board to change, through this interpretation, any of the established cost accounting practices now being followed by contractors with respect to the pooling and allocation of indirect proposal costs. Accordingly, if it is the contractor’s established cost accounting practice to pool and allocate indirect proposal costs by product groupings, he may continue to do so.

One commentator requested a statement in the interpretation with respect to solicited and unsolicited proposals, particularly as to “whether one or the other is properly included in the direct or indirect charge category.” The determination as to like or unlike circumstances does not depend on whether a proposal is solicited or unsolicited. The test is whether the proposal was specifically required by an existing contract.

Preamble D
Preamble to Document Published 6-8-78

The document published on June 8, 1978 at 43 FR 24819, revised 402.10. This amendment was part of a publication which added 331.30(b)(3). Only the portion of the preamble which describes the revision to 402.10 is printed here. The remainder of the preamble appears as preamble K of the supplement to Part 331.

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In the *Federal Register* of February 16, 1977 (42 FR 9391), the Board proposed to amend section. 10, General Applicability, of standards 401 through 409 to conform these sections to the general applicability section as it appears in standard 410 et seq. No comments were received on this proposed amendment. The Board considers this change to be appropriate and is amending standards 401 through 409 as set forth below.

Preambles to Cost Accounting Standard 403, Allocation of Home Office Expenses to Segments

Preamble A
Preamble to Original Publication, 12-14-72

Preamble to original publication of 4 CFR Part 403, at 38 FR 26680, Dec. 14, 1972.

The Standard on Allocation of Home Office Expenses to Segments is one of a series being promulgated by the Cost Accounting Standards Board pursuant to section 719 of the Defense Production Act of 1950, as amended, Pub.L.91-379, 50 U.S.C.App. 2168, which provides for the development of Cost Accounting Standards to be used in connection with negotiated national defense contracts.

Work on this Standard was initiated as the result of a variety of continuing problems between contractors and the Government concerning equitable allocations of home office expenses to segments involved in negotiated defense contracts. The problems include disagreements on:

> (i) The propriety in certain circumstances of using particular allocation bases, such as cost of sales or direct labor for allocating home office expenses to segments;
>
> (ii) whether and to what extent certain kinds of segments such as GOCO's, foreign subsidiaries and partially owned subsidiaries should be included in the allocation base; and
>
> (iii) the homogeneity of expense pools.

The allocation of home office expenses to segments is not now specifically governed or guided by an authoritative accounting statement. Home office expenses allocated to segments and then to contracts can constitute an important element of total contract cost. The lack of authoritative standards to guide contractors, procurement officers, auditors, and others, provides a great potential for disagreement and controversy over contract costs. Assurance of equity in cost determinations and contract settlement is singularly lacking.

This Standard prescribes criteria for allocation of the expenses of a home office to segments of an organization. The criteria are based primarily on the beneficial or causal relationship between such expenses and the receiving segments. The Standard governs how a contractor may allocate expenses of its corporate headquarters to various divisions, subsidiaries, plants, or other subsidiaries of the corporation. The Board believes that application of this Standard will result in sound cost accounting and will provide a great degree of uniformity in the determination of costs of negotiated defense contracts.

Research establishes that some home office expenses are incurred for specific segments and can be assigned directly to them. Other expenses, not incurred for a specific segment, have clear relationships to two or more segments, relationships which are measurable with reasonable objectivity. A third type of home office expense possesses no readily measurable relationship to segments.

The Cost Accounting Standards Board finds that a Cost Accounting Standard to govern the allocation of home office expenses is desirable to reduce wasteful and expensive controversy and to obtain equity for the contracting parties. The Standard published today requires that those home office expenses incurred for specific segments are to be allocated directly to those segments to the maximum extent practical. Those that can be allocated to segments on the basis of objective measurable relationships are to be accumulated and allocated by means of logical and homogeneous expense pools established for this purpose. The remaining or residual home office expenses are then to be allocated as discussed below.

The Board expects that this Standard will operate to reduce residual expenses to a relatively minor amount and by this means also reduce controversy and inequity. Where this is the case, the Board sees no reason to require one particular technique to allocate these expenses. Accordingly, where residual expenses are no greater than a specified percentage of operating revenues, the Standard allows the use of any appropriate allocation technique. However, if residual expenses exceed such specified percentages, the Board believes that its objective of reducing controversy and avoiding inequity would best be served by selecting a single allocation technique to be used. Its research in this connection has led the Board to conclude that for this purpose, a three-factor formula is superior to other allocation bases and techniques for the allocation of residual expenses.

Early research on this Standard included an extensive review of available literature on the subject, a review of decisions of contract appeals boards and courts, and a study of home office management philosophy and operations of 40 companies representing a wide variety of industries.

This research led to the publication of a proposed Cost Accounting Standard in the *Federal Register* of June 30, 1972, with an invitation for interested parties to submit written data views, and comments to the Board. To better assure that those who had already expressed interest or provided assistance had an opportunity to comment, the Board supplemented the *Federal Register* notice by sending copies of the *Federal Register* materials directly to 196 organizations and individuals, of which 86 companies were invited to furnish the Board with estimates of any additional or reduced costs which could arise from the implementation of the Standard.

Responses were received from 130 sources, including individual companies, Government agencies, professional associations, industry associations, public accounting firms, and others. All of these comments and data have been carefully considered by the Board. Those comments which are of particular significance are discussed below together with an explanation of resultant substantive changes to the Standard as published in the *Federal Register* of June 30, 1972.

As will be seen from the following discussion, the Board was greatly benefited by the many comments it received on the Standard as published in the *Federal Register* of June 30, 1972. The Board takes this opportunity to express its considerable debt to those who devoted time and skill to assisting the Board in this endeavor and to thank the many companies and individuals involved.

(1) *Materiality*. Many commentators urged that the Standard contain a general statement on materiality. The Board has previously stated that the administration of its rules, regulations, and Cost Accounting Standards should be reasonable and not seek to deal with insignificant amounts of cost. The Board does not believe that any further general statement is needed at this time. However, where specific changes could be made to clarify the intent of this Standard with respect to materiality, they have been made as further discussed below.

While most commentators agreed with the concept of maximum direct allocation of home office expenses, and accumulation of nondirectly allocated home office expenses into logical, homogeneous expense pools, a few of these commentators believed that the Standard did not adequately incorporate the concept of materiality for this purpose. The Board agrees that materiality is an important consideration in determining whether to specify that an expense is to be allocated directly or by means of a separate expense pool. Accordingly, 403.40 of the Standard has been revised to state that expenses are to be allocated to the maximum extent “practical” and that expenses not directly allocated are to be grouped into separate homogeneous expense pools “if significant in amount and in relation to total home office expenses.”

In addition, a number of commentators questioned the need for using what they considered to be a relatively complex formula to allocate residual expenses even when they are minor in amount. This requirement was contained in the Standard as published in the *Federal Register* of June 30, 1972. The Board believes the formula to be relatively simple, well understood, already used by many companies to satisfy State tax requirements, and based on financial data that is readily available. Nevertheless, the Board agrees that other allocation techniques may be acceptable if residual expenses are not material. Accordingly, 403.40(c) of the Standard being published today permits the use of any allocation base representative of total activity if residual expenses are less than a specified percentage of operating revenue.

The Board also considered a materiality test conducted periodically which would permit a contractor, otherwise covered, to choose not to follow the Standard if its application would result in little or no change in the total amount he allocates to his segments with Government business. The Board in this instance rejected this approach for the following reasons:

(a) Such an approach would put undue emphasis on the effect of this Standard on the allocation of costs to or away from Government contracts.

(b) The administrative problems and time spent by both the Government and the contractor in estimating the contract cost consequences of application of the Standard periodically and negotiating the pro forma application of the Standard for comparative test purposes would outweigh any benefits that might be derived from waiver of the entire Standard on the basis of materiality of result.

(c) There would be no assurance that a contractor's own procedures, which in the test year happened to provide nearly identical results to the results which would be provided through use of the Standard, would in other, subsequent years also produce the same nearly identical results. In effect, the results in the test year may have been an aberration.

(d) In light of the general acceptance by the majority of commentators of the concept of direct charging and grouping of homogeneous expense pools, the provisions for materiality considerations previously described are deemed sufficient.

(e) The Board has applied the concept of materiality to the extent it believes practical in this Standard. The Board, however, as noted in its prefatory comments on the first two published Standards (37 FR 4141), will give consideration to stating a concept of materiality applicable to all Standards if subsequent events indicate the desirability and feasibility of doing so.

The Board has eliminated a requirement, originally contained in the June 30, 1972, proposal, for interdepartmental allocations of home office expenses. This proposal would have required part of the cost of certain home office functions to be allocated to other home office functions before being reallocated to segments. The Board accepts the views of a number of commentators that this procedure would be complex and unwarranted in the light of a relatively insignificant effect on the allocation of home office expenses.

The proposed Standard, as published in the *Federal Register* of June 30, 1972, required that all segments be included in an allocation base unless it could be demonstrated that any segment did not receive benefit from, or contribute to the cause of, an expense to be allocated. A number of commentators observed that it would be virtually impossible to demonstrate that a segment received no benefit. Others commented that a segment should not be included in an allocation base if it received only negligible benefit. The June 30, 1972 proposal has been revised to accommodate these comments and to emphasize again the application of the concept of materiality.

(2) *Hierarchy of allocation methods.* A number of commentators were concerned that a provision in the *Federal Register* of June 30, 1972, that costs be "* * * allocated on the basis of expenses caused by the segments, benefits received by the segments, or benefits available to the segments," did not provide adequate guidance for the selection of appropriate allocation bases. The Board believes that with the exception of centralized service functions, the allocation criteria contained in the fundamental requirement are sufficiently specific so as not to require additional guidance. The Board is persuaded, however, that it is desirable to establish more definitive criteria for the selection of an appropriate allocation base for centralized service functions. For this purpose, the Board has added in 403.50(b) a hierarchy of allocation methods. The hierarchy is based on achieving the most realistic representation of the beneficial or casual relationship that is practical in the circumstances.

(3) *Allocation of residual expenses.* With few exceptions, commentators objected to the establishment of a single formula to allocate costs of managing the company as a whole, i.e., residual costs. Many noted that the formula, in conjunction with a broadly inclusive definition of a "segment," would produce inequitable allocations to certain segments. Most often concern was expressed that the allocations would have to be made to segments which receive little benefit from the home office, such as independent subsidiary corporations, subsidiaries in which the organization has only a minority ownership, foreign segments, and Government-owned contractor operator (GOCO) plants. Others were concerned that the formula was unduly complex to administer and that the results of its use would not be worth the effort, particularly where home office expenses are relatively minor in amount.

The most commonly suggested alternative to the formula was that the Standard should provide "criteria" for allocation, rather than a specific method or procedure. Some suggested, for example, that the Standard require only that the allocation base be representative of the activity of the segments. Most often the recommended criteria were phrased in such general terms as equity, fairness, and reasonableness. Some suggested total cost input, cost of sales, revenue, payroll, number of employees, or value-added, as a single allocation base.

The Board recognizes that where residual expenses are minor in amount in relation to a contractor's total business volume, the use of other techniques is unlikely to affect materially the amount allocated to a given segment, and is even less likely to affect materially the allocations to individual contracts. The Board has therefore provided in 403.40(c) that, where residual expenses are no greater than specified percentage of the organizations, operating revenue, they may be allocated by means of any appropriate allocation technique. To develop the percentages specified in the Standard the Board considered both actual statistics of various companies and the results of a staff study to determine the effect of the Standard on the home office allocations of a number of companies. The choice of an alternative technique for allocation of residual expenses is expected to be available to many contractors whose home offices perform relatively few functions, or which adequately employ direct allocation or allocations by means of other homogeneous expense pools.

The Board has concluded that where residual expenses are material in amount, a single allocation technique should be specified. Accordingly, 403.40(c) of the Standard requires the use of the three factor formula if residual expenses are in excess of the specified percentage of total company revenues. If residual expenses are material in amount, the Board believes that selection of a single allocation technique is necessary to reduce costly controversy in an area where disputes have been commonplace. Furthermore, the Board is of the view that the greater the amount of residual expenses, the greater the likelihood that the use of a single factor base for all contractors could result in inequitable allocations. The use of the three factors in the formula minimizes any distortion that may result from any one of the factors.

The three-factor formula is selected because it takes into account the major subjects of management concern, i.e., volume or activity, employees, and invested capital. Some companies consider that the time, effort, and attention of top management attributable to various segments are approximately proportionate to the volume or activity of those segments. Revenue is considered by some companies to be a generally reliable and convenient measure of volume or activity. Other companies believe that top management efforts are primarily devoted to the employees of an organization and therefore, advocate the use of payroll for allocating the cost of these efforts. Still others believe that a major top management concern is the management and deployment of the capital invested in the organization; for the purpose of this formula, the net book value of tangible capital assets and inventories is considered by the Board to be a reasonable representation of invested capital.

(4) *The formula factors.* In addition to permitting an alternative to the three-factor formula for allocating residual expenses, the Board has made certain modifications to the formula itself.

A number of commentators opposed the inclusion of intraorganizational sales, in the revenue factor. Several of these commentators were concerned that this procedure would "pyramid" the allocation of home office expenses to those products which progress through several segments of an organization before they are finally sold to outside customers. Others noted that a segment established primarily to sell products produced by other segments would receive a disproportionately large share of home office expenses under the formula. However, a segment which sells much or all of its output to other segments would receive a disproportionately small allocation of home office expenses if such sales were excluded from the revenue factor. The Board, therefore, has concluded that the operating revenue of a segment shall include sales to other segments, but such operating revenue shall be reduced by purchases from other segments. This procedure will assure an appropriate allocation to each segment, regardless of whether it sells to other segments or to outside customers while at the same time avoiding "pyramiding" of home office expenses.

As originally published in the *Federal Register* of June 30, 1972, the Standard required the inclusion of rental property in the property factor of the formula. Such property was to be valued at eight times the annual rental rates. Many commentators opposed the inflexible valuation of such property. Others believed the inclusion of rental property at all was entirely inappropriate. Questions were also raised whether, and to what extent, minor, short-term leases would have to be included. In view of these comments, the Board has concluded that tangible capital assets to be included in the formula should be those capitalized in accordance with a contractor's established practices.

The Board, however, did not adopt the recommendation of many commentators that the value of Government-furnished property be included in computing the property factor of each segment. These commentators were of the view that Government property requires as much, or more, management attention as owned property. The Board believes that such administration is mostly accomplished at the segment level, and therefore, residual expenses of the home office are not significantly related. Rather, property is included in the formula as a measure of top management's attention to invested capital.

(5) *Allocation of residual expenses to special segments.* As originally published in the *Federal Register* of June 30, 1972, the Standard would have required, as a general rule, the allocation of a proportionate share of residual expenses to all segments pursuant to the three factor formula. For this purpose, "segments" included domestic and foreign subsidiaries owned more than 50 percent as well as those subsidiaries owned between 20 percent and 50 percent if the home office exercised significant guidance and control.

Numerous comments were received in regard to these provisions. Commentators observed variously that the percentage of ownership is not in proportion to the benefits received from the home office, that the amount of guidance and control is not in proportion to the percentage of ownership, or that the benefits received are not in proportion to the amount of guidance and control. Some commentators noted that the absence of significant guidance and control is difficult to demonstrate. A number of commentators were particularly concerned about the resultant allocations to subsidiaries owned less than 50 percent, foreign subsidiaries, unconsolidated subsidiaries, and sales subsidiaries. Many commentators observed that subsidiaries often perform their own home office functions, that the necessary information to make the required allocation would not always be available, that subsidiaries could not always be billed for home office costs, or that such allocations would cause tax and legal problems. Various commentators recommended alternatively that allocations to subsidiaries be based on management judgment, on the degree of guidance and control, or on the basis of benefit, rather than on any ownership criteria. Others recommended variously that no allocation be made to subsidiaries owned less than 100 percent, to subsidiaries owned less than 50 percent, or to subsidiaries which are unconsolidated. Still others suggested partial allocations in various forms. One industry association recommended that allocations to subsidiaries be based on advance agreement with the Government.

Upon analysis of the comments received on this subject, the Board is persuaded that a requirement to allocate a pro rata share of residual expenses by means of the formula or other allocation base to all segments, without exception, could result in inequitable allocation in certain situations. In the opinion of the Board, this problem is not necessarily limited to subsidiary corporations, but can extend to other segments. Accordingly, the Board has provided in 403 40(c)(3) of the Standard that, where the Contracting Officer and the contractor agree that a particular segment receives significantly more or less benefit from residual expenses than would be reflected by the allocation of such expenses pursuant to the formula or other representative base, they may agree to establishing a special allocation of residual expenses to such segment. Any such special allocation must reasonably reflect the benefits received by the segment. Guidance to implement this provision is contained in a new paragraph (d) under 403.50 of the Standard.

(6) *GOCO's.* Some commentators urged that GOCO facilities be excluded from the definition of segment to receive allocations of home office expenses, arguing that the GOCO facilities receive little or no benefits from home office activities. Several commentators were concerned that this Standard would result in contractors being required to make greater allocations to GOCO's than would be reimbursed to them under the terms of some GOCO contracts. The Board believes that contractual problems associated with the allocation of costs to a GOCO contract pursuant to this Standard, where such costs represent significantly more or less benefit than the GOCO contract actually receives, can be dealt with by agreement, as discussed in the preceding section. The Board

intends to consider in the near future the pervasive question of the treatment required by relevant Federal agencies of the costs allocated in accordance with any Standard.

(7) *State and local income and franchise taxes.* The Board believes that the nature of this expense is essentially the same for all companies and that there is little justification for the observed multiplicity of allocation methods being used to allocate to segments their share of corporate State and local income taxes and franchise taxes. By means of an illustration in the *Federal Register* publication of June 30, 1972, the Board proposed the allocation of State and local income taxes on the basis of the profit and loss of each segment and specifically requested comments on this particular illustration. Numerous comments were received. While some commentators agreed with the proposed illustration, most did not. Of those that did not, most advocated an allocation method which would allocate such taxes on the basis of the same factors used to compute a segment's share of total corporate taxable income, that generally being the percentage of payroll, sales, and property of the segment to the corporate total of each of these factors. Several commentators noted that they use different allocation bases, such as income or sales, but that these result in approximately the same allocation as one based on the same factors used to compute the tax.

> After evaluating the comments, the Board continues to be of the view that the nature of this expense is essentially the same for all companies. Further, allocation of this expense on the same basis used to compute a segment's share of total corporate taxable income is, in the Board's judgment, more in accord with the concept of allocating home office expenses on the basis of the beneficial or causal relationships between such expenses and receiving segments. The Board has therefore revised the illustration for the allocation of State and local taxes to permit "any base or method which results in an allocation that equals or approximates a segment's proportionate share of the tax imposed by the jurisdiction in which the segment does business, as measured by the same factors used to determine taxable income for that jurisdiction." As a practical matter, this means that the tax for any State must be allocated only to those segments that contribute to the factors used to measure taxable income for that State. If there are several segments that do business within a State, each segment's share of that State's tax is to be measured by the proportionate contribution made by such segment to the total of the factors for that State.

(8) *Cost-Benefits.* Many commentators addressed themselves to the last sentence of section 719(g) of the Act which provides that. "In promulgating such standards, the Board shall take into account the probable costs of implementation compared to the probable benefits."

> The Board has not neglected its obligation and continues to measure the costs and benefits involved in implementing both proposed and promulgated standards. Its experience to date leads to the conclusion that the kind and amount of empirical data called for by some commentators is neither available nor possible of accumulation. In the final analysis, the Board must determine whether the information that has been assembled and evaluated is sufficient to enable it to make reasonable judgments.

> In making this determination with respect to the present Standard, the Board gave careful consideration to the evidence bearing on the likely initial and continuing implementation costs involved, both for contractors and for affected agencies of the Government. At the same time, consideration was given to the benefits which will be achieved through simplified negotiation, administration, audit, and settlement procedures; one of the major gains of standards, to contractors and the Government alike, is the reduction in the number of costly controversies. After evaluating the Standard being promulgated today, the Board finds that the probable benefits of this Standard clearly outweigh the probable cost of implementation.

(9) *Exemptions.* A number of educational institutions requested that they be exempted from the provisions of this Standard. There appears to be no disagreement that many educational institutions have "home offices" similar in many respects to those of commercial organizations. However, the educational institutions contend that, unlike commercial organizations, they develop overhead rates for institution-wide functional activities, such as education or research, in lieu of overhead rates for organizational segments. According to these educational institutions, it would serve no purpose, therefore, to require allocation of an institution's "home office" expenses to organizational segments. In addition, a number of these commentators noted that there are problems in defining

the segments of an educational institution; e.g., whether a segment is a campus, a school, a department or some other organization.

The Board is persuaded that in the light of the present practices of educational institutions in carrying out Government contracts, little purpose would be served at this time by requiring educational institutions to adhere to a standard which prescribed criteria for allocating home office expenses to organizational segments. The Board recognizes that Office of Management and Budget Circular No. A-21, which contains the cost principles applicable to grants and contracts with educational institutions, does not presently require development of indirect cost rates for individual segments of an educational institution. Therefore, for the time being, these organizations which are subject to Office of Management and Budget Circular No. A-21 are exempted from the provisions of this Standard.

In addition, the Board is exempting State and local governments subject to Office of Management and Budget Circular No. A-87 from the provisions of this Standard pending further study of the applicability of this Standard to such organizations.

(10) *Effective date.* As originally published in the *Federal Register* June 30, 1972, the Standard would have had to be followed by a contractor for his first fiscal year following the receipt of a contract to which the Standard is applicable. A number of commentators observed that if a contractor received a contract shortly after the effective date of the Standard and his fiscal year began shortly thereafter, little time would be available to implement the Standard. Most of these commentators requested that at least 6 months be allowed to make the necessary preparations to implement the Standard. To accommodate these requests, the Standard, now being published, requires that it must be followed for a contractor’s fiscal year beginning after September 30, 1973.

(11) *Other comments.* In addition to those changes already discussed, the Board has made a number of other changes as a result of the comment received. While these are considered to be of a minor or editorial nature, the Board calls particular attention to the following additional comments.

Various commentators stated that this Standard would require contractors to accumulate and allocate home office expenses on a different basis than that used for internal management purposes. As a consequence these commentators were concerned that the Standard would necessitate two separate sets of records. Others urged that the Standard specifically permit the use of memorandum records. The Board notes that even in the absence of this Standard, many contractors now use memorandum records to make home office allocations for purposes of Government contracts because they do not make formal allocations of home office expenses to segments, or do so on a different basis. The Board sees no need to disturb the practice of using memorandum records for home office allocations, nor does it view this as being significant burden on contractors who find the need to do so. However, the Board does not consider it necessary or appropriate to refer specifically to the use of memorandum records by means of this Standard.

Certain commentators recommended that the Standard be specific as to the use of estimated or budgeted amount either for pricing purposes or for purposes of actual allocations. The use of estimates or budgets for pricing purposes or for purposes of provisional rates for cost accumulation is customary, and is not considered by the Board to require specific authority by the terms of this Standard.

There is also being published today (37 PR 26678) an amendment to Part 400. Definitions, to incorporate in that part the words and phrases defined 403-30 of the Standard.

Preamble B
Amendments, 11-7-73

Preamble to revisions of the definitions of “home office” and “tangible capital asset,” 403.30(a)(2) and (5), and editorial amendments to 403.50(c)(2) and 403.70, 38 FR 30725, Nov. 7, 1973. The document amended 4 CFR Parts 331, 351, 401, 402, and 404 as well as Part 403; material relating to those parts is omitted. It appears in the supplements to those parts.

The purpose of this publication by the Cost Accounting Standards Board is to amend Parts 331, 351, 400, 401, 402, 403, and 404 of its rules and regulations. The amendments, which are minor clarifications to the regulations, were published in the *Federal Register* of September 5, 1973 (38 FR 23971). The amendments: * * * * (c) modify certain definitions in Parts 400, 401, 402, 403, and 404 for the purposes of uniformity among the various Parts. Only one comment in response to the September publication has been received by the Board. This expressed agreement with the proposed changes.

In view of the foregoing, the following amendments to the Board's regulations are being made effective November 7, 1973.

Preamble C
Amendments, 8-4-75

This publication, 40 FR 32747, August 4, 1975, revised 403.70(a) and made several amendments to Part 351. Only those portions of the preamble which describe the revision of 403.70(a) are printed here, although the complete preamble appears as preamble F of the supplement to Part 351. A correction to the language which amended 403.70 was printed at 40 FR 33819, August 12, 1975.

The purpose of this publication by the Cost Accounting Standards Board is to modify Part 351, Basic Requirements, of its rules and regulations and Part 403, Allocation of Home Office Expenses to Segments. A proposed modification to Part 351 was published in the *Federal Register* of April 3, 1975 (40 FR 14942). Twenty-seven sets of comments were received in response to that publication. After considering those comments, the most significant of which are discussed below, the Board is today publishing an amendment to its rules relative to the requirement for the submission of Disclosure Statements by defense contractors and subcontractors.

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6. *Applicability of CAS 403.* A number of commentators noted that the April 3 proposal deleted paragraph 351.41 of the Board's regulations. This paragraph restated the requirement that only companies that met the Disclosure Statement filing requirement for Federal fiscal year 1971 were required to comply with CAS 403, Allocation of Home Office Expenses to Segments. These commentators asked that the Board's position be clarified as to whether or not any current revision to the Disclosure Statement requirement also changed the coverage of CAS 403. It was not the Board's intention to broaden the coverage of CAS 403 at this time. The possibility of extending the coverage of that Standard is the subject of a separate study currently underway. To make the Board's intention wholly clear, 403.70 of CAS 403 is being revised to state explicitly rather than by cross reference the continuing coverage of that Standard. This revision has no substantive significance whatever, but instead merely sets out specifically what was and continues to be the exemption from that Standard, which was before today accomplished by reference to 351.40 of the Board's Basic Requirements. Contractors and subcontractors which together with their subsidiaries did not receive net awards of negotiated national defense prime contracts during Federal fiscal year 1971 totaling more than $30 million continue to be exempt from Standard 403.

Preamble D
Amendment Published 9-12-77

This document amended 403.70(a) and designated the existing text or 403.80 as (a) and added (b). The amendment was published at 42 FR 45625, Sept. 12, 1977 as a part of the publication which added Part 332 and amendments to Parts 331 and 351 of this title. The complete preamble appears on the supplement to Part 332.

<u>Comments on Part 403</u>

With respect to the amendment of Part 403, the November 30, 1976 proposal was to revise that Standard to make it applicable to any contract which was subject to Cost Accounting Standards generally. The amendment being promulgated today retains this concept. However, as recommended by a number of commentators, the Board deferred the promulgation of this amendment pending the amendments to Parts 331 and 351 and the addition of Part 332 discussed above.

The decision to extend the application of Part 403 to additional contractors was made on the basis of extensive research. This research included both those contractors who were already required to use Part 403 and those who were expected to use it as a result of this amendment. With respect to the current users, the Board is satisfied that this Standard has resulted in more equitable allocations, with little administrative effort in most cases. With respect to potential additional users, the research indicated that many of these would have to make few, if any, changes to comply with Part 403 and that the remainder could comply with little difficulty. The Board notes in addition, an independent study by the Conference Board which found that defense contractors who are using Part 403 for contract costing purposes are using the same allocation procedures for internal reporting purposes. According to the Conference Board, it was typical of these companies to allocate home office expenses on a blanket basis prior to the promulgation of Part 403. (Information Bulletin No. 17, February 1977.)

A number of commentators suggested various limitations for the application of Part 403. Some of these suggestions were expressed in general terms. Some of the commentators recommended, for example, that the requirement to use Part 403 should not be extended to “small contractors.” Alternatively or additionally it was recommended that Part 403 should not be required for a large contractor with little work subject to Cost Accounting Standards. More specifically, recommendations were received to exempt those contractors with less than 10 percent of their revenue from Government work. Others recommended that contractors who have less than $10 million in contracts subject to Cost Accounting Standards should be exempt. The Board believes that the recommendations of this nature have been accommodated to the extent desirable and practical by the amendments to Parts 331 and 351 and the addition of Part 332 being promulgated today. Accordingly, any further exemption from Part 403, specifically, is considered to be necessary.

In publishing the proposed amendment to Part 403 in the *Federal Register* of November 30, 1976, the Board stated that there is evidence that almost all contractors who were required to make significant changes in their allocation practices as a result of Part 403 did so without undue trouble or expense. Several commentators questioned the Board’s conclusion in this regard. The Board’s conclusion was based in part on Staff research in involving 147 home offices who now use Part 403 to allocate home office expenses. This research sought to determine, among other things, the administrative problems and expense involved in making allocations pursuant to Part 403. Government auditors reported that of the 147 home office only 4 had problems in developing the necessary data and that there was evidence of significant administrative costs at one of these four offices. In addition, evidence of significant administrative costs in making the allocations was found by the Government auditors at four other of the 147 home offices.

Some of the respondents who questioned the Board’s conclusions regarding administrative problems and expense referred to an industry report on the economic impact of Cost Accounting Standards as support for this position. These respondents variously referred the Board to those sections of the report which summarized

> (i) contractor’s appraisal of benefits from Part 403;
>
> (ii) the number of contractors who were required to make changes as a result of Part 403;
>
> (iii) the number of noncompliance notices issued in connection with Part 403; and
>
> (iv) the increase and decrease in costs allocated to Government work as a result of CAS 403. Nothing in these sections, however, specifically addresses the question of administrative problems or expense involved in complying with Part 403.

Two associations reported that, contrary to the Board’s findings, their member companies had experienced trouble and expense in complying with Part 403. These associations declined to identify the companies involved, the nature of the problems, or the amount of the expenses. Under these circumstances, there is no basis to alter the conclusion that contractors have been able to make changes required as a result of Part 403 without undue trouble or expense.

One commentator stated that it would not be desirable to make more contractors subject to Part 403 because he believes it to be defective, particularly with respect to its application to the allocation of state and local taxes. With respect to the application of the Standard to the allocation of state and local taxes specifically, the Board notes that it reached its conclusion on the basis of considerable research and extensive deliberation. Moreover, it has reexamined its conclusion, even after the promulgation of Part 403. Notwithstanding the views of the commentator, the Board continues of the view that the provision in question is proper. Accordingly, the Board does not agree that this Standard should not be extended to additional contractors because of the tax allocation provision.

Effective Date

The effective date of the regulations being published today is March 10, 1978. Pub.L.91-379 provides that regulations shall take effect not earlier than the expiration of the first period of sixty calendar days of continuous session of the Congress following the given date on which a copy of the regulations is transmitted to the Congress. The calendars of the Congress indicate that the required sixty days will not pass until some time in February 1978. Accordingly, March 10, 1978, has been selected to assure sufficient time for the regulation to lie before the Congress.

Preamble E
Preamble to Document Published 6-8-78

The document published on June 8, 1978 at 43 FR 24819, revised 403.10 and 403.70(b). This amendment was part of a publication which added 331.30(b)(3). Only the portion of the preamble which describes the revision to 403.10 and 403.70(b) are printed here. The remainder of the preamble appears as preamble K of the supplement of Part 331.

. . . .

In the *Federal Register* of February 16, 1977 (42 FR 9391), the Board proposed to amend section. 10, General Applicability, of standards 401 through 409 to conform these sections to the general applicability section as it appears in standard 410 et seq. No comments were received on this proposed amendment. The Board considers this change to be appropriate and for amending standards 401 through 409 as set forth below.

Preambles to Cost Accounting Standard 404, Capitalization of Tangible Assets

Preamble A
Preamble to Original Publication of Part 404, 12-27-73

Preamble, Published at 38 FR 5318, Feb. 27, 1973, to the original Publication of this part.

The Standard on Capitalization of Tangible Assets published today is one of a series being promulgated by the Cost Accounting Standards Board pursuant to section 719 of the Defense Production Act of 1950, as amended (Pub.L.91-379, 50 U.S.C.App. 2168), which provides for the development of Cost Accounting Standards to be used in connection with negotiated national defense contracts.

Work preliminary to the development of this Standard was initiated as the result of recognition that the general subject of fixed asset accounting has been the source of continuing problems between contractors and the Government concerning equitable determinations of the costs attributable to performance of specific contracts. The problems include

(1) determination of the acquisition costs to be capitalized as opposed to those which are charged against revenues of the current period,

(2) determination of appropriate depreciation charges for a given fiscal period,

(3) determination of the appropriate allocation of depreciation charges among contractor activities, and

(4) determination of appropriate techniques for treating dispositions of fixed assets. The Standard establishes the beginning point for fixed asset accounting as described in (1) above. It does not cover the other related topics.

Early research on this Standard included an extensive review of available literature on the subject and a review of decisions of contract appeals board and courts. A preliminary analysis of the entire topic of fixed asset accounting was made and a number of issues were identified; comments on this analysis were obtained in response an extensive mailing. After careful evaluation of the comments, the Board developed and circulated a questionnaire on tangible fixed asset accounting practices. The replies to the questionnaire were considered in the preparation of a preliminary draft of the Standard on Capitalization of Tangible Assets, which was, in turn, widely distributed for informal comment by interested parties.

The Standard now being promulgated is derived from the proposal which was published in the *Federal Register* for October 5, 1972, with an invitation for interested parties to submit data views, and arguments to the Board. The Board supplemented that *Federal Register* publication by sending copies of the *Federal Register* material directly to organizations and individuals who were expected to be interested. Responses were received from 107 sources, including individual companies, Government agencies, professional associations, industry associations, public accounting firms, universities, and others. All of the comments have been carefully considered by the Board.

Most of those who commented expressed general concurrence with the provisions of the proposal. Many of the contractors who commented indicated that their practices in most respects already complied with the Standard; most suggested that the proposal should be modified only in a few respects. The Board takes this opportunity to express its appreciation for the helpful suggestions and criticisms which have been furnished. Many companies and individuals have devoted significant talent and effort to the improvement of this Standard.

The comments below summarize the major issues discussed in connection with the October 5 proposal and explain the major changes which have been made.

(1) *Adequacy of existing situation.* Some commentators contended that the Board should not promulgate any rules in this area because the applicable principles have been well established and accepted. The Board, however, finds that the existing regulations have failed to establish reasonable uniformity of capitalization practices among comparable organizations.

(2) *Specificity.* Some interested parties criticized the proposed Standard on the basis that it was “too procedural.” Those who comment in this vein tend to assert that this Cost Accounting Standard should deal only with criteria and policies. Others criticized the October 5 proposal as being too general and failing to provide sufficient guidance about treatment of specific types of costs (such as sales tax) or certain types of transactions (such as deferred maintenance).

The Standard provides practical implementation for the basic concept of direct identification of costs with final cost objectives to the maximum practical extent. The acquisition costs of tangible assets should be identified and capitalized wherever the service lives and amounts involved are so significant that contract costs would be distorted if the acquisition costs were not capitalized. The main feature of this Standard is the requirement that contractors consistently apply reasonable capitalization policies in accordance with criteria stated in the Standard.

A policy for capitalization is a policy for distinguishing between assets and expenses. Immediate charge-off is justifiable as a practical expedient in those situations where the improved allocation of cost among cost objectives and accounting periods which would be attainable by capitalization is worth the administrative costs which would be required. Assets with either short service lives or minor acquisition costs are conveniently accounted for as charges against current revenues.

When a transaction is identified as the acquisition of a tangible capital asset, the full cost of acquiring the asset should be capitalized. The Board might have applied this concept by requiring the inclusion of specific elements of cost in the determination of acquisition cost. As one example, it would be appropriate in concept to capitalize sales and use taxes as a part of the acquisition cost because such taxes are clearly caused by the acquisition. However, as many commentators have stated, as requirement to capitalize such taxes and similar costs would require significant changes in contractor's accounting systems, and the benefit from such increased uniformity may not exceed the expected cost to contractors if required to change from their present practices. The Standard, therefore, does not specifically require the capitalization of sales or use taxes or other collateral costs of acquiring tangible capital assets. The subject remains under active consideration by the Board and if further study should indicate that the benefits from increased uniformity in this area would outweigh probable administrative costs, the Board will take affirmative action on this subject.

This Standard does not provide procedural detail for determining the accounting treatment for some specific kinds of transactions related to existing assets. The major problems encountered in practice are those of clarification; once specific work is defined, for example, as "preventive maintenance," "routine repair," "major overhaul," "extensive renovation," "addition," "betterment," or some other such classification in accordance with contractor policy, the appropriate accounting treatment can readily be agreed upon.

The Standard leaves latitude to the contractor in establishing his capitalization policy, but it provides some reasonable limits. A major purpose of Cost Accounting Standards is increased uniformity and consistency; this goal implies some reduction in the flexibility which was formerly available.

(3) *Capitalization as an independent issue.* As indicated above, the research which has led to this Standard began as a broad inquiry into a number of closely related issues. Capitalization is only one of those issues. Interested parties have suggested that the Board should not issue a Standard on any single part of the subject of fixed asset accounting until it is prepared to deal comprehensively with all related issues. The major objection is that changes in this Standard may be found to be appropriate when the details of a Standard on depreciation are agreed upon.

After careful consideration of all issues presented, the Board is confident that the Standard being promulgated will be compatible with future Standards. Nonetheless the Board acknowledges that because of future Standards, or for other reasons, modification in this, or indeed in any Standard which it promulgates, may be necessary. Should such modifications be needed, they will be made. This Standard, by helping identify those acquisitions which should be capitalized, will be useful immediately in connection with identifying items whose cost should not be allocated to current contracts.

(4) *Definition of tangible capital asset.* The term "Tangible Capital Asset" has already been defined by the Board in connection with the Cost Accounting Standard on Allocation of Home Office Expenses to Segments. The definition provides that such assets "are to be held for continued use or possession * * * for the services they yield." Some interested parties have suggested that this definition could apply to inventories which are held for sale. The Board considers that the phrase "for the services they yield" is sufficient to show that the term does not apply to inventories. No change is deemed necessary in the published definition.

(5) *Nature of limits.* The Standard requires that each contractor establish and adhere to a reasonable capitalization policy. The Board feels that, in most cases, the contractor is best able to determine what policy will be most suitable for his situation, and that all interested parties will be benefited by consistent application of appropriate criteria for distinguishing between capital items and those which should be charged off at time of acquisition. In consideration of the possible distortion and inequity which might result from application of an unreasonable policy (significant amounts of long-term fixed asset costs charged to expense at acquisition), the Board considered the desirability of a specific definition of the limits of reasonableness. The proposal published in October, as well as earlier drafts distributed informally, included the requirements that the policy deal with both the expected service life and the acquisition cost. An acceptable policy would not allow an asset to be charged off immediately against revenue if its service life was expected to be in excess of 2 years and its acquisition cost was in excess of $500.

The Board received many comments on the provision of these specific limitations. Critics have used the term "arbitrary." The Board has considered carefully all the pertinent points and has continued the limits which were earlier proposed. Disclosure statements and other research data obtained by the Board indicate that very few contractors will be required change their present policies and those few required changes will impact only a few acquisitions. A review of disclosure statements filed with the Board indicates that only 3 percent of the reporting companies had dollar capitalization criteria in excess of $500. In addition, the fact that specific limits, appropriate today, may need to be revised in the future is not a reason to avoid establishing them today. Limitations can be revised promptly if developments warrant a change.

There have been no established limits on capitalization policies.

Accordingly, wide diversity exists among contractors. The Board does not seek to establish a single uniform accounting system for all contractors, but it believes that limits for total cost and useful life should be placed under some uniform constraints. Indeed, the Board feels that procurement authorities are entitled to assurance that contractor capitalization policies will result in the capitalization of those acquired assets which are within specific limits of reasonableness.

(6) *Comparing benefits and cost.* The Congress provided, in section 719(g) of the Act which established the Board, that in promulgating Cost Accounting Standards “the Board shall take into account the probable, costs of implementation compared to the probable benefits.” Those commenting on the Board’s work show considerable interest in this aspect; the comments on the October proposal included a number of remarks on this comparison.

The Board considers the benefits and the costs which can be related to each specific proposal and also to the total program of developing Cost Accounting Standards. This Standard has, for most contractors, almost no cost. It requires the adoption of a policy; most contractors already have policies which comply with the criteria. Some contractors, however, will have to establish or modify capitalization policies; for these contractors there may be costs. Benefits will be available immediately; contract administration will be improved. Once a capitalization policy is established in accordance with the standard, individual acquisitions can be handled in accordance with the established policy, with a reduction in controversy. This Standard establishes the beginning point for the determination of the costs associated with use of capitalized tangible assets. One of the major benefits of this Standard is, therefore, the provision of a more uniform basis on which the Government and contractors may deal with depreciation expense.

During the development process which led to this Standard, the Board asked for, and received, a number of comments from contractors about the likely costs attributable to the implementation of a proposal such as this one. Most replies indicated little or no cost. Some indicated compliance with this Standard will cause divergence from practices now accepted for other purposes. The Board has found no requirement imposed by other authoritative bodies for continuance of practices inconsistent with this Standard. Divergence, therefore, will occur only if an affected contractor elects, for other purposes, practices inconsistent with the criteria set forth in this Standard.

The Board concludes that this Standard will provide benefits which outweigh the costs of implementation.

(7) *Accounting for assets acquired by lease.* Many commentators suggested to the Board various methods of accounting for assets acquired by lease. This problem is not a new one. Tangible assets can be acquired by various kinds of business transactions and relationships. The accounting principles related to capitalization are most readily applied in connection with purchases. Some lease agreements provide to the user of an asset many of the attributes of ownership. The accounting profession has long been cognizant of difficulties related to determining when assets acquired by lease should be treated as purchases.

The Board agrees that assets actually purchased should (if otherwise appropriate for capitalization) be capitalized even when the purchase transaction is in the form of a lease agreement. This same determination must be made for other accounting purposes. The accounting profession is now guided, in this regard, primarily by opinions of the Accounting Principles Board; it is our understanding that the Financial Accounting Standards Board will soon undertake to provide a new statement for the profession on this issue. This Board will carefully consider all authoritative statements of accounting principles to the extent that it can do so while maintaining progress toward its own primary goal of increased uniformity and consistency in cost accounting for contracts.

Those lease acquisitions which are treated as purchases will be subject to this standard; those which are treated as leases will for the time being be subject to the existing procurement regulations which deal with rental costs. The Board is, therefore, willing that the contractor determine, for each acquisition, whether it is a

purchase and hence subject to his capitalization policy (which must comply with the criteria established in this in Standard) or a rental transaction and hence subject to established regulations on rental costs. In either case, determination of the reasonableness of the lease costs remains the responsibility of the procurement agencies and is not dealt with here by the Cost Accounting Standards Board.

(8) *Investment Credit.* The October proposal included a specific provision that the Investment Credit pursuant to the Revenue Act of 1971, Pub.L.92-178, need not be deducted from the purchase price of tangible capital assets in establishing the acquisition cost of the assets. Several interested parties criticized the language used in this provision. Public policy on the point is clear; the Board, by including a specific provision, did not intend to change the situation. The Investment Credit need not be deducted, and there is no need for a specific provision on this point. The Board has, therefore, removed the provision.

(9) *Indirect cost for constructed assets.* The October 5 proposal contained a provision that the acquisition costs of assets constructed or fabricated by a contractor should include the indirect costs allocable to final cost objectives. The Board specifically drew in attention to this treatment of such an assets and requested that anyone advocating an alternative treatment should set it forth in detail with reasons for favoring it. Numerous commentators opposed the Board's proposed treatment of constructed assets, stating variously that the allocation of general and administrative expenses to such assets was contrary to generally accepted accounting principles (since such expenses are period costs), was not required by existing Government regulations, and no one accounts for such assets in this manner. A few suggestions for alternative treatment were made. Most of them dealt with allocating to constructed assets only variable indirect costs that could be directly identified with the assets constructed.

For financial reporting purposes some indirect costs are identified as period costs and are not considered to be inventoriable. Consistent application of the full costing concept generally applicable to Government contract costing is not compatible with that period cost concept; for such contract costing, all costs -- including those otherwise considered as period costs -- must be associated with final cost objectives. The October 5 proposal identified constructed assets as projects which should be treated as final cost objectives and share in indirect cost allocations. This treatment is consistent with the casting practice which would be followed if the Government contracted for the construction of fabrication of the assets in question.

The Board continues to be of the view that application of the full costing techniques applicable to Government contract costing requires that full consideration be given to the applicability of fixed overhead including general and administrative expense to constructed assets. Some fixed overhead at the operations level and certain general and administrative expenses are often allocable to constructed assets based on their beneficial relationship to the construction effort. Costs generally not so allocable could include selling expenses, bid and proposal expenses, and the like.

Therefore, tangible capital assets constructed which are identical with or similar to the contractor's normal product should receive an appropriate share of all indirect cost including general and administrative expenses. In addition, other constructed tangible capital assets requiring significant indirect support also should be burdened with their allocable share of indirect costs, where such indirect costs are material. The revised 404.50(b) reflects this position.

(10) *Grouping of assets.* The proposed standard as published October 5 was construed by a number of readers to imply that capital assets should be accounted for on a unit basis and not in groups. The Board did not intend any such implication. The Board's interest is in costing principles and the requirements to capitalize does not extend to the specific type of records to be maintained.

(11) *Rearrangement costs.* Many of the controversies related to capitalization are encountered in connection with

costs incurred subsequent to the acquisition of an asset. Routine repair costs are unquestionably to be charged off against current revenues, while costs of major betterments are clearly to be capitalized. Costs which are not at either extreme are more difficult to account for. The October 5 proposal included a restatement of the principle that "costs incurred subsequent to the acquisition of a tangible capital asset for activities which extend the life or increase the usefulness of the asset (e.g., betterments) and which meet the contractor's established criteria for capitalization shall be capitalized." This aspect of the proposal was generally favored by commentators. The proposal continued with the requirement that expenditures for rearrangement and reconversion of tangible capital assets, if they extend the life or increase the usefulness of those assets, and which meet the capitalization criteria, should be capitalized. This requirement has been criticized; many contractors assert that rearrangement costs, as they use the term, should never be capitalized.

> The Board agrees that rearrangements of the sort normally expected to maintain the usefulness of assets should not be capitalized. The Board expects that rearrangements of the sort which extend the life or increase the usefulness otherwise anticipated from tangible capital assets, will be classified as betterments and capitalized in accordance with the requirements of the standard. Accordingly, the term "rearrangement" has been deleted from the standard.

(12) *Special purpose equipment.* The Board has received a number of suggestions that the Standard should provide explicit coverage for special purpose assets. Consideration was given to this issue in the research which led to the October 5 proposal. "Special tooling" and "special test equipment" are defined in Government procurement regulations; expenditures of such assets are properly charged against the contracts for which their acquisition is authorized. The suggestions for modification of the October 5 proposal on this point mostly deal with acquisitions which do not qualify as "special tooling" or "special test equipment."

> Contractors do acquire assets which are expected to have technological or engineering capabilities for long periods but for which the contractor does not foresee any significant utility after the completion of a particular contract. Such assets are not "special purpose" assets. Rather they are assets for which the contractor expects relatively short economic service life (as compared with the physical potential). Most suggestions for a change in the standard at this point seemed to be based on the belief that these assets should not be capitalized. The standard being promulgated today is applicable to all acquisitions; each contractor's policy is required to include appropriate criteria (e.g., estimated service life and economic usefulness) for identification of capitalizable assets, including those which are unusual.

(13) *Donated assets.* Some commentators opposed that part of the standard which requires the capitalization of assets donated by the Government. These commentators pointed out that such treatment may eventually result in depreciation charges to Government contracts and that Government regulations today make such depreciation charges unallowable. The allowability of depreciation costs of assets as donated by the Government will not be influenced by the requirement that such assets be capitalized.

(14) *Original complements of low cost equipment.* A number of interested parties were concerned with the concept of original complement. Those who commented asserted that there was an inconsistency in capitalizing items of little value, that it would be difficult to identify or control individual items, and that alternative accounting methods were used to achieve the same results of normalization of cost between periods.

> The Board's primary purpose in requiring the capitalization of original complements is to assure allocation of incurred cost to applicable current and future accounting periods. The Board sees no inconsistency in this purpose.
>
> The total original complement should be treated as a tangible capital asset. Therefore, the Board expects that a contractor will identify and control the original complement as an entity rather than account separately for each individual item which comprises the total complement.
>
> The Board recognizes that several methods are used to distribute the cost of original complements to future accounting periods:

(1) Treating the complement as a tangible capital asset subject to depreciation,

(2) treating the cost as a deferral charge, or

(3) treating the original complement as an inventoriable asset. A standard on depreciation is expected to prescribe acceptable methods for charging the cost of original complements to accounting periods; the standard being promulgated today requires that the complement be capitalized.

(15) *Asset accountability unit.* A number of interested parties indicated problems with both the concept and definition of a retirement unit as published in the October proposal. The term retirement unit has been changed to "Asset Accountability Unit" which the Board believes to be more descriptive of the concept actually applied in identifying components of major assets. These units, to the maximum extent practical, should be identified and separately capitalized upon acquisition and, whether or not they have been previously separately capitalized, they should be removed from the asset accounts when disposed of. Replacement units should also be capitalized.

(16) *Application of the standard.* Several universities commented that the proposed Standard should not apply to them because universities generally do not use depreciation techniques. Under existing procurement regulations, universities are entitled to use allowance for fixed assets in lieu of a depreciation charge. The Board believes that the Standard on Capitalization is applicable to universities and others in determining capitalized cost for computation of use allowances or similar purposes and for identifying those items which are not appropriate for current charges. Therefore, no exemptions are provided for by this Standard.

There is also being published today (38 FR 5318) and amendment to Part 400, Definitions, to incorporate in that part the words and phrases defined in 404.30 of the Standard.

Preamble B
Amendments, 11-7-73

This publication, 38 FR 30725. Nov. 7, 1973, amended 404.30(a)(4) by revising the definition of "tangible capital assets".

The purpose of this publication by the Cost Accounting Standards Board is to amend Parts 331, 351, 400, 401, 402, 403, and 404 of its rules and regulations. The amendments, which are minor clarifications to the regulation, were published in the *Federal Register* of September 5, 1973 (38 FR 23971). The amendments:

(a) Renumber Parts 331 and 351 to facilitate insertion of future modifications those parts;

(b) clarify one section the contract clause at 331.5; and

(c) (modify certain definitions in Parts 400, 401, 402, 403, and 404 for the Purposes of uniformity among the various Parts. Only one comment in response to the September publication has been received by the Board. This expressed agreement with the proposed changes.

In view of the foregoing, the following amendments to the Board's regulations are being made effective November 7, 1973.

Preamble C
Preamble to Document Published 6-8-78

The document published on June 8, 1978 at 43 FR 24819, revised 404.10. This amendment was part of a publication which added 331.30(b)(3). Only the portion of the preamble which describes the revision to 404.10 is printed here. The remainder of the preamble appears as preamble K of the supplemental to Part 331.

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In the *Federal Register* of February 16, 1977 (42 FR 9391), the Board proposed to amend section. 10, General Applicability, of standards 401 through 409 to conform these sections to the general applicability section as it appears in standard 410 et seq. No comments were received on this proposed amendment. The Board considers this change to be appropriate and is amending standards 401 through 409 as set forth below.

Preamble D
Amendments Published 3-3-80

This publication, 45 FR 13721, Mar. 3, 1980, revised 404.40(b)(1) and 404.80(b) and amended 404.60(a)(1) introductory text, (a)(1)(i) and (ii).

Summary

Part 404 includes a requirement that defense contractors have written policies for capitalization of tangible assets. Each such policy must include a minimum acquisition cost criterion, which has not been allowed to exceed $500. The Standard is being amended to raise the limit to $1,000. The purpose of the change is to permit contractors to adopt practices appropriate in today's economy.

Effective Date

December 20, 1980.

Supplementary Information

(1) *Background.* The amendment being promulgated today was, in one sense, anticipated at the time the Board promulgated Cost Accounting Standard 404. In its publication of February 27, 1973 the Board commented ".that specific limits, appropriate today, may need to be revised in the future. Limitations can be revised promptly if developments warrant a change." This amendment is a specific recognition that a change is warranted.

The amendment now being promulgated is derived directly from the proposal which was published in the *Federal Register* for January 2, 1980 (45 FR 48) with an invitation for interested parties to submit comments. The Board sent copies of the proposal directly to organizations who were expected to be interested. The Board received 25 letters of comment on the January 2 proposal. The Board appreciates the participation by interested parties in its continuing effort to maintain the effectiveness of its Standards and regulations.

The remarks which follow summarize the major issues discussed in the comments on the January 2 proposal.

(2) *The specific change from $500 to $1,000.* CAS 404, as promulgated in 1973, contained a requirement for a written capitalization policy. The policy was required to include a minimum acquisition cost criterion, and that criterion was not allowed to exceed $500. The $500 limitation, selected as a ceiling to prevent unreasonable policies, encompassed the practices of 97% of the companies whose Disclosure Statements were filed with the Board.

The Board, recognizing that circumstances have changed significantly since the promulgation of Standard 404, authorized an inquiry into capitalization practices. With the cooperation of the National Association of Accountants, the Board mailed a questionnaire to about 200 NAA members who were able to describe the practices of large, medium, and small manufacturing firms which had not been influenced by the limitation of Standard 404. The Financial Executives Institute also mailed a similar questionnaire to about 900 of its members and asked them to furnish information directly to the Board. The responses received by the Board indicated that capitalization practices have indeed changed since the promulgation of Standard 404. Freely adopted policies now tend to include higher monetary criteria than were common in 1973.

The Board is persuaded that the change is related to changing economic circumstances, and that a change in the acquisition cost criterion is warranted. The January 2 proposal was to change from $500 to $1,000. Those who commented on the proposal were generally in favor of the specific change which had been proposed. The amendment being promulgated is unchanged from the January 2 proposal in this regard.

(3) *Use of index techniques for future changes.* The Board received several suggestions dealing with the idea that, in considering similar revisions in future years, the Board should use index techniques. The Board considered this general idea before making the January 2 proposal. The Board had reviewed the performance of several official measures which might have been used if an index technique were to be adopted. The increases from 1972 to 1979 were from about 60%, to about 80%, suggesting that if $500 was the right limit at the time Standard 404 was developed, a limit of about $800 or $900 might be appropriate at the end of 1979. The questionnaire responses included a significant number of business units using $1,000. The Board will continue to consider to the appropriateness of the $1,000 limitation now being imposed. The impact of inflation, as recorded in several official indexes, will be among the factors considered. The Board is, however, not prepared to provide for any automatic amendment of the dollar limitation in Standard 404.

(4) *Other clarifying language.* It was he suggested that, while the Standard is being amended anyway, the Board could reduce possible misunderstandings by modifying the language in two places.

The fundamental requirement of the Standard calls for a written capitalization policy which designates ". economic and physical characteristics for capitalization of tangible assets." The suggestion was made that this provision be modified by adding a clarifying phrase so that it would read ". economic and physical characteristics which must be met before an item is required to be capitalized." This suggestion was made in order to emphasize that the service life and unit cost are not the only characteristics to be considered in making a capitalization decision. The basic belief behind the suggestion is valid. The Board agrees that other criteria, such as ability to maintain physical identifiability, may be appropriately included in a policy, and items which are not capitalizable because of failure meet one of the criteria specified in the policy should not be capitalized even if the estimated service life and monetary cost are in excess of those stated in the policy. The Board believes that the existing language 404.40(b) is clear in this regard, and no change is considered necessary.

The Standard now provides, at 404.40(b)(4), that ". higher minimum dollar limitations." may be designated for betterments and for original complements. Some accountants believe that the distinction between an expenditure for "repair" and one for "betterment or improvement" can best be made by considering the relationship between the expenditure and the original cost or the replacement value of the item being rebuilt or modernized. They believe it is reasonable to propose a capitalization policy which includes a percentage criterion which will, in turn, result in a different dollar criterion in each situation. One commentator suggested that the Board should eliminate the word "dollar," so that the amended Standard would allow the designation ". higher minimum limitations." The Board has no objection to policies which are stated in percentage terms over the range typical application. The Board, however, feels that it is quite reasonable to provide a monetary limit above which any betterment will be capitalized even if its cost is a low percentage of some other asset's cost. The Board is therefore not making the suggested change, but it does take this opportunity to recognize that a capitalization policy for betterments can quite reasonably include a sliding scale or percentage technique provided that it also includes a specific monetary limit.

(5) *Effective date.* The January 2 proposal would have applied to asset acquired in contractors' cost accounting periods which begin on or after January 10, 1981. Several commentators urged an earlier effective date. The Board always tries to allow adequate time for contract administrators to prepare for changes. This amendment does not require any action; rather it provides the possibility for action. The Board has changed the effective date to December 20, 1980. This change will make the amendment effective much sooner for many contractors while still allowing sufficient time for administrative implementation of the amendment.

(6) *Comparing Costs and Benefits.* The Board's January 2 publication included an explicit request for advice with

respect to probable costs of implementation as compared with probable benefits. Only a few commentators dealt at all with this issue, and none of them in quantitative terms. All those who discussed this issue indicated that they expected benefits from the amendment, and that the benefits would outweigh any costs of implementation. No commentator objected to the proposal. The Board is persuaded that the probable benefits will exceed the probable costs of implementation.

Title 4 CFR 404, Capitalization of Tangible Assets is amended as follows:

Preambles to Cost Accounting Standard 405, Accounting for Unallowable Costs

Preamble A
Preamble to Original Publication, 9-6-73

Preamble to the original publication of Part 405. Sept. 6, 1973, at 38 FR 24195.

The Standard on Accounting for Unallowable Costs is one of a series being promulgated by the Cost Accounting Standards Board pursuant to section 719 of the Defense Production Act of 1950, as amended, Pub.L.91-379, 50 U.S.C.App. 2168, which provides for the development of Cost Accounting Standards to be used in connection with negotiated national defense contracts.

Work preliminary to the development of this Standard was started as a result of recognition of the continuing problem concerning the accounting treatment of unallowable contract costs. There has been a lack of uniformity or comparability in the cost accounting treatment accorded unallowable costs after specific determination of their unallowability. There have also been reported problems concerning the content of indirect-cost allocation bases where unallowable costs are involved. Further, there have been instances reported of inclusion of unallowable costs in the base for progress payment billings.

There is no present requirement in agency regulations for contractor identification of unallowable costs. As a result, reports prepared by Government auditors contain frequent references to costs which are known to be unallowable but disclosed only through an audit. The Board has concluded that the identification of costs determined to be unallowable should be the subject of a Cost Accounting Standard.

This Standard requires the identification of specific costs at the time such costs first become defined or authoritatively designated a unallowable. The Standard also establishes guidelines for the cost accounting treatment to be accorded such identified costs. The Board believes that application of this Standard will provide a greater degree of uniformity in the determination of costs of negotiated defense contracts.

Early research on this Standard included a review of available literature on the subject, a review of the decisions of contract appeals board and courts, and meetings with contractors and other organizations and individuals concerning their operations and philosophy relative to the treatment of unallowable costs.

This research led to the publication of a proposed Cost Accounting Standard in the *Federal Register* of March 30, 1973, with an invitation for interested parties to submit written data, views, and comments to the Board. To assure that those who had already expressed interest in the proposed Standard had an opportunity to comment, the Board supplemented the *Federal Register* notice by sending copies of the published material directly to several hundred organizations and individuals.

Responses were received from 67 sources, consisting of individual companies, Government agencies, professional associations, industry association, public accounting firms and others. All of these comments have been carefully considered by the Board. Those comments which are of particular significance are discussed below, together with an explanation of the changes made to the proposed Standard published in the *Federal Register* of March 30, 1973.

Government commentators generally regarded a requirement for identification unallowable costs as being reasonable and desirable as long as it recognized that there is room for agency judgment relative to the allowability of individual cost elements. The reaction from industry sources was generally in opposition to a Standard on this subject. The reaction from other commentators was mixed. The Board notes that in the comments by industry representatives are a significant number of admissions that at least some unallowable costs can be identified clearly in advance and, in fact, are so identified by many contractors.

The Board has greatly benefited from the many comments it received on the Standard as published in the *Federal Register* of March 30, 1973. The Board takes this opportunity to express its appreciation for the suggestions it has received, and for the time devoted to assisting the Board in this endeavor by the many companies and individuals involved.

1.**-- General -- Need for a Standard.**

Those who took specific exception to the need for or propriety of a Standard raised a number of issues. Following is a summary and discussion of each of the major issues raised:

(a) Existing procurement regulations and procedures are adequate to resolve what is essentially an administrative issue, and are more appropriately relied upon for accomplishing the stated purposes of the Standard.

> The Board does not agree with this argument. Although the regulations of procurement agencies deal extensive with the definition of those items of cost which are not to be accepted as allowable under Government contracts, they do not require contractor identification of unallowable costs and provide only minimal guidance as to the cost accounting treatment to be accorded such costs.
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> The Board notes that the idea of “unallowable costs” is a concept not generally applied in commercial cost, accounting, and that it apparently has no direct relevance to the process allocating costs incurred to final cost objectives. The Board’s function is to promulgate Cost Accounting Standards to “be used by all relevant Federal agencies and by defense contractors and subcontractors in estimating, accumulating, and reporting costs in connection with the pricing, administration and settlement of all negotiated prime contract and subcontract national defense procurements with the United States in excess of $100,000. The identification and measurement of unallowable costs are directly relevant to this function. In the performance of its assigned responsibility, therefore, the Board finds that a Standard establishing a concept of unallowable costs and providing for the identification, measurement, and reporting of such costs will be useful and desirable.
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> The Board believes that recognition of the cost accounting concept that all costs incurred in carrying on the activities of an enterprise are allocable to the cost objectives of the enterprise is essential to the maintenance of sound and consistent contract cost accounting. This is particularly significant in providing for consistent policies governing allocations of indirect costs, as discussed in greater detail in connection with the issue of indirect cost allocation bases. It is also important in connection with the profit determinations of the Renegotiation Board, where it is necessary to determine the total costs properly allocable to renegotiable contracts. Cost Accounting Standards should result determination of costs which are all cable to contracts and other cost objectives. The use of Cost Accounting Standards, however, has no direct bearing on allowability determinations.

(b) The published proposal constitutes an inflexible procedural requirement rather than a cost accounting standard; it deals with minutiae and will necessitate considerable additional accounting effort and record keeping.

> The Board does not believe that a requirement for contractor identification of costs known to be unallowable, or which have clearly been designated as unallowable, represents an undue burden. It is reinforced in this belief by the fact, as stated in several of the comments received and as further shown by the Board’s research, that many contractors already provide this identification, and often with a greater detail of recorded cost segregation than is required by the Standard. Revised wording has been provided to make clear the Board’s intent to require only such detail and depth of cost allocation and record keeping as is necessary to provide appropriate cost visibility. Provisions for accounting recognition of unallowable costs are considered appropriate for a Standard.

The Board does not agree that this standard deals with minutiae. A significant amount of the time of both Government and contractor personnel is spent in identifying contract costs and in negotiating their allowability. The cumulative impact of unallowable costs can significantly affect contract cost reimbursement and pricing. For example, in fiscal year 1973, the Department of Defense disallowed costs exceeding $200 million. The Board believes that a Standard which will foster earlier and more precise identification of unallowable costs, and thereby narrow the areas of cost search, disagreement and negotiation of differences, will be beneficial.

(c) A standard requiring specific identification of unallowable costs will only lead to added controversy and impair the freedom of contracting parties to negotiate equitable treatment of costs.

This issue is closely related to the first issue discussed above, but is addressed to the problems and interpretative differences involved in the classification of costs as allowable or unallowable.

The Board acknowledges that there may seldom be full agreement between the parties to a contract as to all of the specific items of costs which are unallowable under pertinent laws, regulations and contractual provisions, and that negotiation must, therefore, be resorted to as a practical means of resolving differences. The Standard does not contemplate interference with such negotiations. However, by requiring consistent cost accounting recognition and appropriate accounting treatment of costs agreed to be unallowable, or which are authoritatively designated as unallowable, the Standard should encourage more definitive negotiated agreements. More specificity in agreements should help to limit the areas of future negotiation or dispute to those where there is a rational basis for disagreement.

2.**-- Directly Associated Costs.**

The published version of the proposed Standard defined a directly associated cost as, "Any cost which is generated solely as a result of the incurrence of another cost and which would not have been incurred had the other cost not been incurred." It then provided, in effect, that directly associated costs of identified unallowable costs should be included with the unallowable costs with which they are associated, and be accorded similar cost accounting treatment. These provision of the Standard which were intended solely to cover costs which were incremental with respect to identified unallowable costs, drew comment from disparate sources. Those who disagreed with any attribution of nonallowability to costs which were not unallowable by nature but merely by association were opposed to the directly associated cost concept. Also, some of those favoring such attribution, while not opposed to the concept, interpreted the Standard as encroaching upon, or narrowing the application of, existing regulatory provisions governing cost disallowances, and expressed disagreement with the proposed coverage on this basis. After careful consideration of the comments on this issue, the Board has concluded that coverage in the Standard of directly associated costs is appropriate and necessary.

The Board notes that various regulatory provisions use such nondefinitive terms as "corollary administrative costs," "related collection costs," "related legal costs," "incidental costs relating thereto," "other related costs," etc., in describing unallowable costs. In such cases, the Board considers that the identification and measurement of costs covered by these broadly worded provisions is a function of cost accounting, and therefore appropriate for coverage in this Cost Accounting Standard as directly associated costs.

In light of the above considerations, the Board has retained coverage of directly associated costs. The Board, however, recognizes that treatment of a cost as an unallowable directly associated cost in certain circumstances could result in double counting with respect to a class or category of costs included in an indirect-cost pool that will be allocated over a base containing the designated unallowable costs with which the cost in question is associated. In such circumstances, the Standard requires that the cost shall not be classified as a directly associated cost, but rather shall be retained in the indirect-cost pool and allocated through the regular allocation process.

3.**-- Expressly Unallowable Costs.**

The requirement in the proposed Standard for contractor identification of "cost which are patently unallowable" gave rise to expressions of concern on the part of number of respondents. These ranged from allegations of general impracticability of compliance to apprehensions that the lack of a clear definition would lead to overzealous implementation by auditors and contracting officers and to increased controversy.

Various alternative suggestions were made by commentators. One such suggestion was that identification be required only when there is mutual agreement on unallowable costs by the parties to a contract. This, however would be likely to minimize one of the benefits of the Standard; namely, the reduction of the time and effort spent in audit and negotiation covering cost whose nonallowability is obvious. Also, items requiring agreement are covered by other provisions of the Standard.

A second suggestion made by respondents was that this requirement be made applicable only to costs which the contractor considers or determines to be “patently” unallowable. This suggestion, however, is subject to obvious criticism that any requirement that would provide the party subject thereto with absolute freedom of choice as to what constitutes compliance would be of dubious effectiveness. The Standard, of course, clearly provides for the contractor to be the party having the primary responsibility of making the initial determination as to what costs incurred by him are obviously unallowable.

A third suggestion offered by respondents was that the Standard provide a definition, or examples, covering the costs which are considered to be “patently” unallowable. The Board felt that this suggestion had merit. Because of apparent confusion as to the usage of the term “patently,” the Board has substituted the word “expressly” in the Standard, and has included a definition of “expressly unallowable cost.” Most of the items cost that are of the type required to be accounted for as expressly unallowable are specified in agency procurement regulations (e.g., ASPR 15-205). It would not be practical to list the items of cost that may be made expressly unallowable under the special provisions of contracts. The Board, its definition of an “expressly unallowable cost,” has used the word “expressly” in the broad dictionary sense -- that which is in direct or unmistakable terms.

With regard to the stated concern about overzealous implementation auditors and contracting officers, the Board has previously stated that the administration of its rules, regulation, and Cost Accounting Standards should be reasonable. The Board anticipates that this rule of reason will be applied in the implementation of this Standard. Thus, where a good faith effort has been made by a contractor, in the development and implementation of his cost accounting rules, procedure and practices, to provide for identification of expressly unallowable costs, it is intended that inadvertent failure to properly classify a particular item of cost will not be regarded as noncompliance.

The Board has retained the requirement for contractor identification of costs which are unequivocally made unallowable by the express provisions of an applicable law, regulation or contract. The Standard, however, has been revised to make clearer the accounting distinction between costs which are either expressly unallowable or mutually agreed to be unallowable and costs which are designated as unallowable by the unilateral exercise of a contracting officer’s authority under contract disputes procedures. Solely for the purposes of this distinction, the provision in the revised Standard setting forth the identification requirement for expressly unallowable and mutually-agreed unallowable costs also specifies that these are costs which shall be excluded from Government-contract billings, claims, or proposals.

4.**-- Indirect-Cost Allocation Bases.**

By far the largest number of comments were addressed to the requirement in paragraph (c) of 405.40 of the proposed Standard, that unallowable costs shall be subject to the same cost accounting requirements as allowable costs in determining the content of cost-oriented bases for allocation of indirect costs. This is an issue which appears to have produced an almost complete polarization of the viewpoints of Government representatives and of the parties with whom they contract.

Current agency regulations (e.g. ASPR 15-203(c)) provide, in essence, that indirect-cost allocation bases should not be fragmented for purposes of removing individual elements therefrom. They therefore provide that unallowable costs in an allocation base shall “bear” their pro rata share of the indirect costs in the pool being distributed. The wording of these regulatory provisions has commonly been interpreted as meaning that the indirect costs shall assume the allowability status of the costs in the allocation base. Comments on this regulatory requirement, therefore, have centered on the issue of making otherwise allowable costs unallowable, rather than on the broader accounting principles that should govern cost allocation.

As previously indicated, the Board believes that the issues concerning cost allocation and those relating to cost allowance are distinct and separate. Allowability should not be a factor in the selection or in the determination of the content of an allocation base used to distribute a pool of indirect costs. The appropriateness of a particular allocation base should be determined primarily in terms of its distributive characteristics. Any selective fragmentation of that base which eliminates given base elements for only some of the relevant cost objectives would produce a distortion in the resulting allocations. The Board, therefore, is retaining the requirement that unallowable costs be subject to the same cost accounting principles as e those governing allowable costs.

When an item, activity, or function has been deemed unallowable by other relevant authority, the Board in this Standard has approached the determination of the costs related to the unallowable item, activity, or function in three stages: (a) Its direct cost, (b) its directly associated cost, and (c) the indirect costs allocable by means of a base containing such costs. This has been done because, while there is usually no question that the relevant authority intended that the direct cost (a) be disallowed, there may be questions as to whether costs (b) and (c) otherwise allowable, were intended to be disallowed. The latter two costs are therefore, required to be separately, identified and measured so that their allowability can be resolved through the procurement process.

In concluding that indirect-cost allocation bases should not be fragmented solely for purposes of removing unallowable base elements, the Board is not implying that the elimination of all or part of a base element for other of purposes is always inappropriate and inconsistent with sound cost accounting.

5.**-- Contracting Officer Decision.**

Many respondents questioned the requirement, in 405.40(a) of the proposed Standard, for identifying as unallowable those costs "designated as, unallowable as a result * * * of * * * a final decision of the contracting officer issued pursuant to contract disputes procedures." Concern was expressed that this gave too much standing to the unilateral administrative decision of the contracting officer, and did not recognize contractors' right of appeal to the boards of contract appeals and the courts.

The Board recognizes that legitimate disagreements over allowability often are not finally resolved by contracting officers' decisions. The Board notes, however, that the Standard distinguishes between costs which are "expressly unallowable" and costs which are "designated as unallowable." To further the distinction, and to remove a possible source of misinterpretation, the words "final decision" have been changed to "written decision," to conform to wording in agency regulations governing dispute procedures. The Board believes that, although the written decisions of contracting officers pursuant to formal disputes clause procedures are subject to appeal and possible reversal, they nevertheless constitute authoritative designations, and represent the culmination of a process of audit and negotiation. Furthermore, they are binding on the parties to a contract until and unless changed on appeal. The Board, therefore, considers that any definitive designations of unallowable cost which are provided in the contracting officers' written decisions warrant identification, and it has retained this requirement.

A further objection was raised by some commentators to the requirement, in paragraph (a) of 405.50 of the published proposal, for future recognition of costs identified as unallowable, or of other costs incurred for the same purpose in like circumstance. The observation was made that future circumstances might warrant different conclusions as to allowability.

The Board recognizes that identical costs may be unallowable under one set of circumstances, but nevertheless be determined to be allowable under different conditions, or as a result changed criteria. The Board, however, believes that specific designations of the allowability status of particular classes or categories of cost should be given consideration in the evaluation of any like costs which are governed by the same allowability criteria and which are incurred for the same purpose in like circumstances. The provisions in the Standard which reflect this viewpoint have been clarified.

The Board notes that the identification of costs covered by an adverse contracting officer decision will not prevent a contractor from continuing to claim such costs, where disagreement as to allowability continues. It serves merely to identify the costs special consideration, thereby helping to assure adequate reevaluations, and to promote resolution of the issues involved in the disagreement. Reversal of the contracting officer's decision by a final appeals board or court ruling would, of course, relieve the contractor of any identification requirement under the Standard covering the costs involved in the ruling.

6.**-- Accountability for Unallowable Costs.**

A number of comments were received concerning what some writers interpreted as an unnecessary and improper requirement for detailed accountability covering costs which are absorbed by the contractor and therefore should not be of any legitimate concern to the customer. The Board does not intend requiring cost identification or cost allocation which is not relevant to the determination or Government contract cost. The Standard requires identification of unallowable costs only to the extent needed audit verification of the costs which are included in, or which provide backup support for, proposals, billings or claims. Appropriate revisions have been made in the Standard.

7.**-- Colleges and Universities.**

A number of comments were received from university officials expressing concern that, because colleges and universities contracting with the Government are subject to a different set of contract cost reimbursement principles than commercial organizations, and operate in a different accounting environment, the proposed Standard might present implementation problems if applied to these institutions. These comments have been carefully considered, and supplementary discussions have been held with some of the officials concerned.

On the basis of its analysis of the practices described by commentators as having been deemed acceptable in the past, and of the underlying principles and contractual requirements, the Board believes that the Standard, as revised, can be applied to colleges and universities without any disruption of practices which are acceptable under applicable laws and regulations.

Particular concern was expressed over what was reported to be a common situation, where certain costs, such as faculty salaries, are excluded from contract costs even though such costs may directly pertain to work performance which is an intrinsic part of the contract project. The Board notes that specific identification with, or allocation to, individual contracts and other final cost objectives is not required for costs which will not be included in, nor constitute pertinent backup support for, any proposal, billing, or claim. The Standard requires only that sufficient identification be provided to enable verification of the allocability status of unallowable costs and the accounting treatment actually accorded such costs. The Board, therefore, does not believe that any special provision is required covering the situation described.

8.**-- Materiality.**

A number of comments were received suggesting that the question of materiality be given more consideration in the Standard. The recognition of the materiality problem in paragraph (f) of 405.50 of the proposed standard was endorsed, but concern was expressed that limiting application to circumstances where there was a "low incidence of negotiated Government contracts relative to other types of work" would render the provision ineffective.

Several instances of potential problem areas were mentioned. One of these concerned the situation where corporate headquarters' expenses are allocated to segments which are involved in a relatively insignificant volume of Government contract work. Another cited the case of a standard cost accounting system covering the manufacture of standard products which may incidentally be used as material or components contract work. A third referred to the problem of determining "true" cost of an individual product in a joint-product, joint-cost production situation. Further problem area is that involving determination of the share of indirect expense to be assigned as costs of a proscribed organizational or functional activity.

The Board recognizes that accounting for unallowable costs (which are themselves often determined only through negotiation) is an area where the question of materiality should be given special consideration. In providing this consideration, many factors should be taken into account. These include not only the materiality of the total unallowable costs, but also the materiality of the refinements in determinations of unallowable costs which might be achieved through requiring detailed application of the Standard, as contrasted with negotiating the agreements authorized under the proposed paragraph (f) of 405.50. The Board, accordingly, has revised the Standard to include an amended paragraph (c) which, "based upon considerations of materiality," permits agreements that will satisfy the purpose of the Standard. The Board believes that, in applying the materiality provision of the revised paragraph (c), consideration should be given to the criteria listed in the section titled *"Materiality"* in the Board's March 1973 "Statement of Operating Policies, Procedures and Objectives."

9.**-- Improperly Allocated Costs.**

One commentator raised a question concerning the accounting treatment to be accorded costs which are disallowed because they are erroneously allocated to the contract under which they are claimed. The Board does not believe that the Standard needs to deal with accounting errors of this type. It is obvious that the accounting treatment to be accorded any item of cost should be determined by that cost's correct positioning in the cost accounting structure.

10.**-- Cost/Benefit.**

Only limited comments were received on the subject of the implementation cost of the Standard, and several of these indicated only minimal impact. Of those claiming significant additional implementation expense, none provided any data as justification for the claim. The Board has concluded from its research that the Standard, as revised, constitutes a reasonable requirement, and that the costs of implementation will be minimal. The potential benefits to the audit and negotiation processes accruing from the increase in visibility and in uniformity of cost accounting treatment will be substantial and will greatly outweigh any added costs.

11.**-- Effective Date and Application.**

With respect to the date that this standard becomes effective, it is anticipated that its provisions will be applicable to all solicitations issued on or after January 1, 1974, which are likely to lead to contracts covered by Standards, rules, and regulations of the Cost Accounting Standards Board.

There is also being published today an amendment to Part 400.

Definitions, to incorporate in that part the words and phrases defined in 405.30 of the Standard.

Preamble B
Preamble to Document Published 6-8-78

The document published on June 8, 1978 at 43 FR 24819, revised 405.10. This amendment was part of a publication which added 331.30(b)(3). Only the portion of the preamble which describes the revision to 405.10 is printed here. The remainder of the preamble appears as preamble K of the supplement to Part 331.

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In the *Federal Register* of February 16, 1977 (42 FR 9391), the Board proposed to amend section. 10, General Applicability, of standards 401 through 409 to conform these section to the general applicability section as it appears in standard 410 et seq. No comments were received on this proposed amendment. The Board considers this change to be appropriate and is amending standards 401 through 409 as set forth below.

Preambles to Cost Accounting Standard 406, Cost Accounting Period

Preamble A
Preamble to Original Publication, 11-7-73

The material below is the preamble to the original publication of Part 406, on Nov. 7, 1973, at 38 FR 30732.

The Standard on Cost Accounting Period published today is one of series being promulgated by the Cost Accounting Standards Board pursuant to section 719 of the Defense Production Act of 1950, as amended (Pub. 91-379, 50 U.S.C.App. 2168), which provides for the development of Cost Accounting Standards to be used in; connection with negotiated national defense contracts.

Work preliminary to the development of this Standard was initiated as the result of recognition that the selection of time periods to be used for contract cost accumulation and allocation has been the source of continuing problems between contractors and the Government. The problems include:

> (1) The lack of a firm requirement specifying the cost accounting period to be used,
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> (2) the absence of specificity as to when a cost accounting period other than a contractor's fiscal year should be used, and
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> (3) the lack consistency in selecting the cost accounting period in which specific types of expenses and adjustments are recognized.

Early research on this Standard included an extensive review of available literature on the subject and a review of decisions of contract appeals boards and courts. A preliminary draft of the Standard on Cost Accounting Period was widely distributed for informal comment by interested parties.

The Standard now being promulgated is derived from the proposal which was published in the *Federal Register* for August 7, 1973, with an invitation for interested parties to submit data views, and arguments to the Board. The Board supplemented that *Federal Register* publication by sending copies of the *Federal Register* directly to organizations and individuals who were expected to be interested. Responses were received from 50 sources, including individual companies, Government agencies, professional associations, and industry associations. All of the comments have been carefully considered by the Board.

Most of those who replied to the Board's solicitation indicated satisfaction with the proposal as published. Several contractors indicated that their practices already complied with the Standard. Several commentators voiced objection to parts of the Standard.

The Board takes this opportunity to express its appreciation for the helpful suggestions and constructive criticisms which have been furnished, both informally in response to the circulation of a Staff draft of a Standard and formally in response to the initial *Federal Register* publication.

The comments below summarize the major issues raised in connection with the August 7 proposal and explain the decisions which have been made.

> (1) *Monthly allocations.* A few commentators felt that the Standard should permit monthly allocations of indirect costs on the basis of the data accumulated for each month. This alternative was considered by the Board; however, the idea of monthly cost accounting periods is not appropriate for contract cost accounting. A number of fairly stringent requirements for accruals, deferrals, and other adjustments would have to be incorporated in the provisions of any Standard if there were to be assurance that monthly accruals, deferrals, and other adjustments were appropriate. The administrative costs would outweigh any benefits. To allow monthly closings for some contract situations and to require full-year allocations for others would not be in the interest of comparability and uniformity. The Board, therefore, has not adopted the suggestion.
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> (2) *Identity of cost accounting periods for indirect cost pools and allocation bases.* A few commentators stated that it may not be necessary to require in every instance the identical allocation base period as the cost accumulation period. They stated that they presently use various clerical expedients to accomplish this, such as measuring the base for a period other than, but representative of the activity of, the period used for accumulating

costs in an indirect cost pool. As a matter of principle, the Board does not agree that mismatched periods are proper. The Board, however, recognizes the value of appropriate expedients where cost allocations are not expected to be materially affected. It acknowledges that there may be occasions when it is necessary to use combinations of actual and estimated data to comply with this Standard.

The Board has given recognition to issues of materiality in its Statement of Operating Policies, Procedures, and Objectives in the *Federal Register* of March 6, 1973, and believes that materiality should be considered in the administration of its Standards. In order to alleviate practical problems which might be experienced in implementing this concept of materiality, the Board has changed 406.40(c) and has added 406.50(e).

(3) *Use of a cost accounting period for estimating.* Several commentators stated that 406.50(c) was ambiguous. Some pointed out that this provision might be interpreted as always requiring the use of a full fiscal year, not withstanding the permissible use of short period under the conditions provided in 406.50(a). There was no provision in 406.50(a) which precluded its application, when appropriate, in the circumstances described in 406.50(c). Nevertheless, the Board has modified 406.50(c) to assure that there is no misinterpretation of its intent.

One commentator recommended that detailed guidelines be established for estimating cost data when estimates were necessary under the provisions of 406.50(c). The Board believes that this is a matter of contract administration and negotiation. If the parties do not agree on proposed overhead rates for early settlement or closing of contracts, they are not required by this Standard to agree to an expedited settlement.

Two commentators recommended that variances resulting from a difference between the estimated overhead rates used for expediting the closing contracts and the rates finally negotiated or determined for a cost accounting period should be accounted for by making appropriate elimination's from affected indirect cost pools and allocation bases. As a matter of principle, the Board believes that actual cost should be allocated in accordance with the contractor's disclosed or established practices to all cost objectives of the cost accounting period, including closed or settled contracts. In a settlement the price is fixed, but costs are not. By agreeing to a settlement price the parties take the risk that actual costs allocated to that contract might be higher or lower than expected. However, the Board finds no need to specify how variances are to be accounted for in this Standard. Normally, the expected variances will be estimated to be minor in amount, or the parties will not agree on the settlement price. Also, the manner of accounting for the actual variance should be agreed upon by the contractor and the Administrative Contracting Officer. If the amount is negligible, it may be agreed that it should be absorbed by other cost objectives of the period. In any event, the Board believes that this is a matter of contract administration and negotiation.

(4) *Terminations.* A few commentators recommended that guidance be provided in 406.50(c) for the treatment of unabsorbed overhead and continuing overhead charges allocable to contract terminations. The Board has noted the possible need for Cost Accounting Standards on termination costs and delay claims, situations in which the problems of unabsorbed overhead and continuing overcharges frequently arise, and has initiated research projects on those subjects. At this time, the Board sees need to disturb the expectations of the parties to a contract with respect the absorption of overhead assigned cost accounting periods (normally fiscal years) by cost objectives of those same periods, whether or not those cost objectives exist throughout an accounting period.

(5) *Applicability of the standard both direct and indirect costs.* One commentator recommended that the Standard be applied only to indirect costs. The Standard does apply both direct costs and indirect costs those terms are defined in 4 CFR Part 400. However, this Standard also includes provisions with specific applicability only to indirect cost pools. The Standard does not require that direct costs be allocated in the same manner as indirect costs. For example, it does not require that direct costs be annualized or averaged for purposes cost allocation. Direct costs, however are often used in establishing allocation bases for a period; therefore, they must be assigned and accounted for as costs of the particular cost accounting of periods to which they are application. Consistency in making adjustments both direct and indirect costs for purposes of determining the total costs allocable to the cost objectives of a cost accounting period is an important objective of this Standard.

(6) *Permitting the use of periods less than a Year.* A few interested parties recommended that the Standard permit

the use of a period shorter than a fiscal year when, for example significant contract was begun or concluded during a fiscal year. No one advanced any criteria for determining when to use a short period or how to apply it, even after specific requests for such suggestions. The only rationale advanced for using less than an annual period in such circumstance was the assertion that a short period might be employed to arrive at “more equitable allocations,” or to avoid inequitable burdens on other cost objectives. In view of the vagueness of the criterion of “equity,” the possible effect of changing the risks assumed by the respective parties at the time of contracting, the possible impact on matters of cost allowability and contract administration and negotiation responsibilities, and the continuance of disputes and disagreements over the equity of a short period in particular circumstances, the Board has concluded that the Standard should not authorize the use of a short period except for allocating the costs of an indirect function which exists for only a part of a cost accounting period and for establishing a transitional period when a change of fiscal year occurs.

> As published this Standard precludes either party to the contract from insisting upon a short period in order to maximize or minimize cost recoupment. It precludes, for example, the calculation of overhead rates after-the-fact for alternative application on the basis of either the fiscal year or the period of performance, and the consequent polarization of the positions of the parties as to which period is appropriate or “equitable” when there is a substantial difference between these rates. The Board believes that this Standard will significantly enhance fairness and objectivity in this regard.

(7) *Equitable adjustments.* One professional accounting organization requested that a specific provision be added whereby an equitable adjustment would be made where the contract cost was affected by a change in the contractor’s fiscal year and the change in the fiscal year was adopted for financial accounting and income tax purposes as well as for contract cost accounting. The principal argument advanced for this position is that “there seems to be no valid reason why a contractor should necessarily suffer and the Government should necessarily benefit in such a circumstance.” In the illustration in 406.60(c), the Board noted that under this Standard, a change in the fiscal year data is a change in accounting practices, and that an adjustment of the contract price might therefore be required in accordance with the adjustment provisions of the contract clause set out at 4 CFR 331.50. Those provisions do contemplate that no change in disclosed or established cost accounting practices, other than changes under paragraph (a)(4)(A) of the clause, may result in an agreement whereby costs paid by the United States are increased. The Board recognizes that a contractor may change his fiscal year ending date for substantial business reasons, and has illustrated this possibility in the Standard. A change in fiscal year may not have any cost impact. Where it does, the Board believes that it would be improper for the Government to agree to pay increased costs caused by a voluntary change in accounting practices, no matter how valid and unrelated to cost recovery the motives of the contractor for making the change in this fiscal year ending date may have been. A new paragraph (f) in 406.50 makes it clear that a change in the contractor’s cost accounting period is a change in accounting practices for which an adjustment in contract prices may be required in accordance with paragraph (a)(4)(B) of the contract clause set out at 4 CFR 331.50.

(8) *Choice of transitional period.* A public accounting firm suggested that it might help to avoid disagreements if the Standard made it clear as to the permissible choices in selecting the transitional period other than a year whenever a change of fiscal year occurred. This suggestion has been adopted in the new paragraph (f) of 406.50.

(9) *Applicability to Renegotiation Board.* One commentator noted that the Renegotiation Board, a “relevant Federal agency” under Pub.L.91-379, defines the term “fiscal year” to mean the taxable year of the contractor or subcontractor under Chapter I of the Internal Revenue Code, and that it has been the Renegotiation Board’s practice to renegotiate a contractor on the same basis as the contractor reports for Federal income tax purposes. Hence, it was recommended that, especially because of 406.40(a)(2) and 406.50(d) of the Standard, the Renegotiation Board be exempted from the application of the Standard.

> The Board’s research confirms the possibility that a few contractors may use cost accounting periods which are different from their tax years. In most cases, however, there will be no conflict. Where there are differences, any use of a cost accounting period or fiscal year which is not identical with the period used for Federal income tax reports will involve reconciliation’s by the taxpayer. Contractors who presently use “model years” for their cost accounting periods now file reports with the Renegotiation Board on a taxable

year basis. The Board finds no need to disturb this practice, and has provided a new 406.40(a)(4) to acknowledge it as an exception. The Board believes that the Standard is, however, otherwise applicable, and that there is no need for an exemption.

(10) *Comparing benefits and costs.* The Board concludes that this Standard as published herein has, for most contractors and for the Government, almost no cost impact. The only contrary expressions received in response to our requests have been answered by the changes described above. One major Defense agency expressed concern that the Standard might result in higher cost allocations to its contract insofar as it did not permit the use of short periods. While this may be true the Standard might also yield lower cost allocations to Government contracts as a result of the requirement to use a full fiscal year. No estimate of the amount of any shifts in cost allocations was provided. Because of the different circumstances of each application of the requirement, both increases and decreases in cost allocations can be expected.

The Board concludes that significant benefits, far outweighing any costs of implementation, will be realized from the promulgation of this Standard. Such benefits include reduction of disagreements and disputes; increase consistency, fairness, and objectivity and improvement of estimates for proposals.

(11) *Effective date.* It is anticipated that the effective date in 406.80(a) may be July 1, 1974.

There is also being published in this document an amendment to Part 400, Definitions, to incorporate in that part the term “fiscal year” defined in 406.30 of the Standard.

Preamble B
Preamble to Document Published 6-8-78

The document published on June 8, 1978 at 43 FR 24819, revised 406.10. This amendment was part of a publication which added 331.30(b)(3). Only the portion of the preamble which describes the revision to 406.10 is printed here. The remainder of the preamble appears as preamble K of the supplement to Part 331.

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In the *Federal Register* of February 15, 1977 (42 FR 9391), the Board proposed to amend section. 10, General Applicability, of standards 401 through 409 to conform these section to the general applicability section it appears in standard 410 et seq. No comments were received on this proposed amendment. The Board considers this change to be appropriate and is amending standards 401 through 409 as set forth below.

Preambles to Cost Accounting Standard 407, Use of Standard Costs for Direct Material and Direct Labor

Preamble A
Preamble to Original Publication, 4-1-74

Following is the preamble to the original publication of Part 407, on April 1, 1974, at 39 FR 11869.

The Cost Accounting Standard on the Use of Standard Costs for Direct Material and Direct Labor published today is one of a Series being promulgated by the Cost Accounting Standards Board pursuant to Section 719 of the Defense Production Act of 1950, as amended, Pub L. 91-379, 50 U.S.C App. 2168, which provides for the development of Cost Accounting Standards to be used in connection with negotiated national defense contracts.

Work preliminary to the development of this Cost Accounting Standard was initiated as the result of the recognition that practices concerning the use of Standard costs for contract costing purposes have not been well defined in Government procurement regulations. The Board has undertaken research on this subject with a view that Cost Accounting Standards promulgated on this subject will provide better guidance in the use of Standard costs.

Because the subject of Standard costs is extremely complex, the Board has elected to address this subject in phases. The Cost Accounting Standard being promulgated covers the use of Standard Costs for direct material and direct labor; the use of Standard costs for Service centers and the use of Standard costs for overhead represent two other phases of this subject that are currently under research.

Early research on this Cost Accounting Standard included a study of available literature on the subject and of relevant decisions of boards of contract appeals and courts. Following this study, several issues were identified. A review of Disclosure Statements on file suggested that standard costs are in use by a large number of defense contractors. In an effort to learn the reasons underlying the use or non-use of standard costs for contract costing purposes, and to gain a better understanding of the standard-cost practices by companies in different industries, the Board developed and circulated a questionnaire on the use of standard costs. Selected respondents of this questionnaire were then visited for further discussion. Information derived from replies to the questionnaire and from visits suggested the complexity of the subject and the desirability of addressing it in phases. Accordingly, in the preparation of a preliminary draft, the subject was limited to the use of standard costs for direct material and direct labor. This preliminary draft was widely distributed for comment. Incorporating many comments thus received, a revised proposal was drafted and published in the *Federal Register* of November 21, 1973, with an invitation for interested parties to submit written views and comments to the Board. The Board also supplemented the invitation in the *Federal Register* by sending copies of that issue directly to Several hundred organizations and individuals who had expressed an interest in the proposal or who had provided the Board with comments on the earlier proposal.

These direct and public invitations for comments resulted in the Board's receiving 47 sets of written comments from individual companies, Government agencies, professional associations, industry associations, public accounting firms, universities, and others. Some of these commentators also supplemented their written comments with discussions at individual or group meetings. All of these comments and views have been carefully considered by the Board. Those issues that are of significance are discussed below, together with an explanation of the changes made in the Cost Accounting Standard being promulgated from the proposal published in the *Federal Register* of November 21, 1973.

The Board wishes to take this opportunity to express its appreciation for the helpful suggestions and constructive criticisms it has received, and for the time devoted to assisting the Board in this endeavor by the many organizations and individuals involved.

1. *Management Uses of Standard Costs.* Several commentators emphasized the value of information generated from the use of standard costs for management-control purposes and urged the Board to retain these control features. The Board agrees with this view and has consequently modified the proposed standard to better assure that its use will be fully compatible with the use of standard costs for management-control purposes.

2. *Exclusion of overhead and service centers in the Cost Accounting Standard.* A few commentators expressed the view that the Cost Accounting Standard being promulgated should be broadened to include the treatment of overhead and service centers. The Board believes that the Cost Accounting standard being promulgated may be used effectively without such broadening. Further, because the use of standard costs for overhead and for service centers involves different issues, the Board believes that this Cost Accounting Standard should be promulgated as is.

3. *Coverage of this standard.* Many commentators suggested that the proposed standard did not clearly state that the use of standard costs for Government contract costing purposes is at the option of a contractor; they recommended various changes in wording to make this point clear. The Board has accommodated this suggestion by appropriate modifications in 407.40.

4. *Use of the term production unit.* Many commentators expressed a need for a better understanding of the meaning and significance of the term production unit. As defined in 407.30(a)(7), a production unit is a grouping of activities which either uses homogeneous inputs of direct material and direct labor or yields homogeneous outputs. Where a grouping of activities meets either one of these two criteria, it is the proper level at which to accumulate standard costs of direct material and direct labor and to accumulate variances related thereto. Since variances are allocated on the bases of costs and statistics of each production unit, homogeneity of standard costs of direct material an direct labor would assure that data thus accumulated would be appropriate as bases for allocating variances to cost objectives. The concept of

homogeneity embodied in the term production unit, then, would permit contractors a degree of flexibility in setting and revising standards based on individual needs and circumstances and still provide for the proper cost assignment of variances.

> To further clarify the intended meaning and purpose of a production unit, the Board has added an illustration as 407.60(b).

5. *Homogeneous grouping of material.* A few commentators suggested that the concept embodied in the term homogeneous grouping of material be enunciated. The Board agrees; accordingly, the Board has added a statement under 407.50(b)(2) and an illustration as 407.60(d).

6. *Cost accounting period.* Quite a few commentators felt that relating the establishment of standards to cost accounting period, which is the subject of a Cost Accounting Standard (4 CFR Part 406), is both undesirable and unnecessary, in view of the differences in industry practices and management needs for establishing and using standards; they urged the Board to reconsider. Upon reconsideration the Board finds this argument persuasive. The Board has revised 407.50(a)(1), which provides that a contractor shall state the period during which Standards are to remain effective.

7. *Interim revision of standards.* Many commentators stated that, to maintain comparable information to management-evaluation purposes, revising standards during a cost accounting period is undesirable and counterproductive; they suggested the deletion of this provision. The Board finds this suggestion persuasive; accordingly, the Board has deleted this provision from the Cost Accounting Standard being promulgated.

8. *Procedural details.* Several commentators felt that the proposed Cost Accounting Standard contained too much procedural detail. The Board does not share this feeling. This Cost Accounting Standard, in addressing itself to the entire process of standard cost accounting for direct material and direct labor and to alternatives in each step of the process, necessitates attention to a great many issues. The Board feels that the provisions of this Cost Accounting Standard only reflect the complexity of the subject matter and the diversity of practices being addressed.

9. *Recording allocation of variances in books of account.* A few commentators misconstrued the proposed Cost Accounting Standard and thought that certain provisions required the recording of variance allocations in formal accounting records; they urged the Board to permit the use of adjustments based on memorandum worksheets for covered contracts. To avoid this misconstruction, the Board has made appropriate revisions in the Cost Accounting Standard being promulgated by using the term books of account to mean formal accounting records, and by adding 407.50(e) to specifically permit the use of memorandum worksheet adjustments.

10. *Adjustment of material-price variance recognized at the time of purchase.* Several commentators objected to a provision whereby material-price variances, recognized at the time purchases of material are entered into books of account, are allocated between items introduced into production units and items remaining in ending purchased-items inventory. They argued that this provision does not conform to their practices, particularly where the allocation of unfavorable variances would increase inventory carrying values, and that the provision infringes upon financial accounting.

> In all its research, the Board gives extensive consideration to existing contractor practices. In this instance, however, the practices advocated by those contractors are likely to create inequities and are without adequate conceptual support. As to the second argument, the Board believes that this provision, which concerns the proper allocation of material-price variances between reporting periods for cost accounting purposes, is compatible with objectives of financial accounting. In view of these considerations, the Board has retained this provision in 407.50(b)(3).

11. *Annual allocation of variances.* Quite a few commentators felt that a provision that permitted the allocation of variances not more frequently than once each cost accounting period does not reflect industry practices and management needs. The Board finds this argument persuasive. Accordingly, a provision that permits the allocation of variances more frequently than annually has been added under 407.50(d)(1).

12. *Five percent materiality criterion.* Many commentators to the proposed Cost Accounting Standard objected to the

inclusion of a 5 percent materiality criterion as a basis for determining whether variances are allocated to cost objectives or are included in indirect cost pools for subsequent allocation. Several of the commentators felt that the materiality criterion was arbitrary; others felt that it would delay the process of allocation where it is undertaken monthly; and still others felt that it could result in inconsistencies.

The Board's early research showed that a majority of respondents had variances below 5 percent, and quite a few experienced variances below 2 percent. Later, an overwhelming majority of those commenting on a preliminary draft of this Cost Accounting Standard, which contained a 2 percent materiality criterion, suggested that a materiality criterion set at 5 percent would be reasonable.

The intent of the materiality provision was to permit contractors to use a simpler method of allocation of variances where the amount was below the 5 percent level. Nevertheless, the Board is persuaded by the comments received, and has deleted this provision from the Cost Accounting Standard being promulgated. In its stead, the Board, in 407.50(b)(4) and (d)(2), provides that, where variances are immaterial, such variances may be included in appropriate indirect cost pools for subsequent allocation.

13. *Cost/benefit.* As to benefits, this standard provides needed criteria which the Board believes will improve cost measurement and will result in more equitable assignment of contract costs. As to costs, the Board anticipates little or no cost of implementation by those contractors who are currently using standard costs: the Standard permits contractors to choose from many recognized standard cost practices. Consequently, the Board believes that the benefits to be derived by this standard clearly outweigh any costs of implementation.

The Board expects that the effective date of this Cost Accounting Standard will be October 1, 1974. There is also being published today an amendment to Part 400, Definitions, to incorporate in that part terms defined in 407.30(a) of this Cost Accounting Standard.

Preamble B
Preamble to Document Published 6-8-78

The document published on June 8, 1978 at 43 FR 24819. revised 407.10. This amendment was part of a publication which added 331.30(b)(3). Only the portion of the preamble which describes the revision to 407.10 is printed here. The remainder of the preamble appears as preamble K of the supplement to Part 331.

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In the *Federal Register* of February 16, 1977 (42 FR 9391), the Board proposed to amend section 10, General Applicability, of standards 401 through 409 to conform these sections to the general applicability section as it appears in standard 410 et seq. No comments were received on this proposed amendment. The Board considers this change to be appropriate and is amending standards 401 through 409 as set forth below.

Preambles to Cost Accounting Standard 408, Accounting for Costs of Compensated Personal Absence

Preamble A
Preamble to Original Publication, 9-19-74

The following is the preamble to the original publication of Part 408, on Sept. 19, 1974, at 39 FR 33681.

The Cost Accounting Standard on Accounting for Costs of Compensated Personal Absence is one of a series being promulgated by the Cost Accounting Standards Board pursuant section 719 of the Defense Production Act of 1950, as amended, Pub.L.91 379, 50 U.S.C.App. 2168, which provides for the development of Cost Accounting Standards to be used in connection with negotiated national defense contracts. This Standard deals primarily with the amount and time recognition of costs of compensated personal absence.

Work preliminary to the development of this Cost Accounting Standard was initiated as a part of the study of the larger subject of accounting for labor costs. The costs of compensated personal absence are an important element of labor costs, but under existing procurement regulations there is no assurance that the costs of compensated personal absence are assigned to the cost accounting period in which the related labor is performed and in which the related wage or salary cost are recognized. Because the volume and mix of contracts of a particular Contractor may vary significantly from period to period, the assignment costs to the proper cost accounting periods is important.

Early research on this Cost Accounting Standard included a study of available literature and relevant decision of boards of contract appeals a Courts. Initial meetings were held with major procurement agencies and with a number of Contractors, and certain issues were tentatively identified. The relationship of Government procurement regulations to Federal Income Tax laws which govern the accounting for costs of compensated personal a sense was explored. It was noted that the exact nature of the employer's ability to employees under a specific plan was an important consideration in determining the income tax treatment which might be permitted. A review of Disclosure Statements file indicated a disparity in existing accounting practices.

A questionnaire and a statement issues were then sent to 117 companies, 40 Government agencies, and 53 others, including industry and professional associations, to obtain detail information, particularly in regard to benefit plans and the reasons for selecting a specific accounting method. Data on benefit plans and accounting practices were received from 68 companies and comments on the issues were received from 37 respondents. Analysis of the data and Comments indicated that the issue could be classified broadly into two group -- those relating to the amount and timing of recognition of costs of compensated personal absence and those relating to methods of allocation of these costs to cost objectives. Some problems were noted in connection with the charging of costs of compensated personal absence directly to final cost objectives at the time of payment; these have been addressed in the Standard. Detailed criteria for the allocation of costs of compensated personal absence are not included in this Standard. Additional study of other labor-related costs is being undertaken and when it has been completed such criteria may be provided.

Based on analysis of the responses to the questionnaire and issues paper and on further discussions, a preliminary draft Standard was developed and widely distributed for comment. Comments and suggestions were received from 87 respondents; these comments were considered in developing a revised Standard which was published in the *Federal Register* off March 4, 1974, with an invitation to interested parties to submit written views and comments to the Board. The Board also supplemented the invitation in the *Federal Register* by sending copies of that issue to several hundred organizations and individuals who had provided the Board with Comments or the earlier proposal or who had otherwise expressed interest in the proposal.

Following the *Federal Register* publication, the Board received 86 sets of written comments from companies, Government agencies, professional associations, industry associations, public accounting firms, universities, and others. All comments have been carefully considered by the Board and those addressing areas of significance are discussed below, together with explanations of the Changes made in the Cost Accounting Standard being promulgated from the proposal published in the *Federal Register* Of March 4, 1974.

The Board wishes to take this opportunity to express its appreciation for the helpful suggestions and constructive criticisms it has received, and for the time devoted to assisting the Board in this endeavor by the many, organizations and individuals involved.

(1) *Need for a standard.* The most significant problems and issues relate to the amount and timing of recognition of costs of compensated personal absence appear to stem from the reliance of existing procurement regulations on the Internal Revenue Code and income tax regulations to govern accounting for these costs. Three disadvantages arise from this reliance. First, current regulations and prior rulings permit, but do not require, the use of accrual accounting for vacation pay, and they do not specify the amount to be accrued if accrual is elected; of three contractors with identical vacation plans, one may elect to recognize vacation costs pro-rata as the related work is performed, the second in the year the related work is completed, and the third only at the time vacation is taken. Consequently, current regulations do not require uniformity in the measurement of such costs among years. Second, the Internal Revenue Code and Treasury Department rulings have imposed different criteria at different times; of two contractors with identical plans, one historically may have been permitted to recognize costs of

compensated personal absence on the accrual basis, while the other, who applied at a later date, is denied the same privilege because of a subsequent ruling. Finally, a change in the Internal Revenue Code or income tax regulations may not be appropriate for contract cost accounting.

> Many commentators said that they were not aware of problems relating to accounting for costs of compensated personal absence and they questioned the need for a Standard on the subject. Discussions with a number of these commentators disclosed, however, that they were unaware of the lack of uniformity created by the reliance of Government procurement regulations on income tax regulations. The Board believes that the promulgation of a Standard dealing with accounting for costs of compensated personal absence is desirable to improve, and provide uniformity in, the measurement of these costs for a cost accounting period and thereby to increase the probability that the measured costs are allocated to the proper cost objectives.

(2) *Scope of the standard.* Several commentators questioned the exclusion of such costs as severance pay or group insurance from the Standard and they concluded that these costs were thereby unallowable as contract costs. This conclusion is not correct. A Standard does not define which costs are or are not allowable. Moreover, these costs were excluded from this Standard because our research disclosed that the associated accounting problems are sufficiently dissimilar from those of compensated personal absence to warrant separate consideration.

(3) *Basis for recognition of cost.* The Standard that was published for public comment relied on the degree of certainty of the employer's obligation as the principal criterion for accrual or nonaccrual of costs of Compensated personal absence. Some commentators suggested that costs not be recognized prior to payment unless the obligation to provide the benefits were irrevocable in all circumstances. Using this test, most company benefit plans which we have seen in the course of our research would not qualify for accrual accounting. Others suggested that the Standard set no restrictions whatsoever on the use accrual accounting for these costs.

> After considering all of the comments and after additional staff research and discussions with contractors, Government agencies, and others, the Board has concluded that the distinction which it previously stated between a "certain" and a "reasonably certain" obligation for purposes of determining liability, was unnecessary. The Standard has been simplified to state directly that the proper measure of the liability and the criterion for cost recognition is the amount which would be payable if the employer were to terminate the employment for any reason not involving disciplinary action. Under generally accepted accounting principles, liabilities are usually recorded when obligations to transfer assets or provide services in the future are incurred. If the employee would be paid a give amount in the event of lay-off, then that employee must have completed the service necessary to have earned that amount of entitlement to benefits.
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> Some Commentators suggested that only so much of the employer's liability as would be payable on voluntary termination be considered to "earned." The Board does not accept this position. Even in cases where voluntary termination causes a forfeiture, the employer cannot unilaterally avoid the liability. The employer's liability should not be disregarded merely because an employee may later act to relieve the employer of actually making the payment.
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> Even if the obligation is viewed as one of a contingent nature, generally accepted accounting principles provide that where the outcome is reasonably foreseeable and the contingency may be expected to result in a Cost, it should be reflected in the account based on its research, the Board believes that only a small percentage of those employees of any contractor who are entitled to benefits forfeit those benefits. Therefore, the Board believes that the obligation should properly be recognized (with appropriate adjustment for anticipated forfeitures), and to fail to do so is to misstate the costs of Compensated personal absence which are properly assignable to that cost accounting period.

(4) *Utilization of benefits criterion.* A number of commentators objected to the provision in the proposed Standard that if the employer's obligation were not "certain," then accrual accounting could be used only if at least 80 percent of the entitlement which was potentially earned in any year would ultimately be used by the employees. The intent of this provision was to assure that accrual accounting was not permitted in situations where the

utilization rate was so low that it was questionable whether accruals based on estimated utilization provided any better cost accounting information than did actual cash disbursements. The Board has reviewed the utilization data of a number of contractors and finds that by adhering to the amount which is payable on involuntary termination of employment as the measure of the accrual, a utilization criterion is unnecessary. It has therefore been deleted.

(5) *Adjustments for unrecognized liabilities.* The Standard requires the recognition of costs when the entitlement to compensated personal absence is earned. Initial application of the Standard or a change of compensated personal absence plan may necessitate an adjustment to recognize the cost of entitlement already earned but not yet recognized for cost accounting purposes. The proposed Standard made no explicit provision for the disposition of such adjustments. A number of commentators cited the failure to provide explicitly for the disposition of adjustments as a deficiency in the proposed Standard. For example, it was hypothesized that a contractor who was recording vacation costs at the time of payment might not recognize any vacation cost in the year an employee was hired; on the completion of the contract, the employee might be terminated and paid for both the vacation to be taken in the year of termination and the vacation earned in that year. If the Standard were applicable to the contractor, he might be able to allocate only those costs accrued in that year. As a result, he might not recover Costs paid in that year for vacations earned before accrual was instituted. The Board recognizes the validity of this hypothesis in some instances. However, if the contractor is viewed as a going concern and Government contracting as a continuing process, then that hypothetical “last year of contracting” may be infinitely far in the future, the lay-offs may never take place, and the contractor will continue to receive “one year’s worth of Costs” in each year.

All commentators who questioned the method of adjustment, and certain other contractors who did not raise the question but who the Board believed might be significantly affected by the Standard, were asked to provide detailed information concerning involved, the number of the estimated amount of the adjustment. In addition, each contractor was asked to provide background information concerning its history as a Government contractor and, to the extent available, data on past employment, labor costs, and extent of contracts. The Board also contracted several contractors who already record costs of compensated personal absence on the accrual basis to determine the circumstances under which this accounting treatment had been adopted, whether adoption resulted in adjustment and, if so, how it had been handled.

The Board reviewed the information submitted in response to its requests. The Board has considered

(1) refraining from explicitly providing for handling the adjustment,

(2) providing a procedure by which the adjustment could all be assigned to the year of change, and

(3) providing a procedure for amortizing the adjustment over a fixed period of years. The Board finds disadvantages to each of these alternatives. If no procedure for adjustment is provided, appropriate procedures for cost recovery may not be devised by contracting parties. If the procedure resulted in assignment of the entire adjustment to the year of change, then some contractors may recover more than the appropriate cost of that year and all of the contracts in the year of change will be overcharged. The same deficiencies, albeit to a lesser extent, exist if the procedure provides for the adjustment to be amortized over a fixed period.

The Standard has been revised to provide an explicit procedure for disposing of the adjustment for unrecognized liability. Under it, the adjustment is initially placed in a suspense account. In the cost accounting period of change and in any subsequent period, if the employer’s liability for compensated personal absence under the related plan at the end of a period is less than the amount in the suspense account at the beginning of that period, the suspense account is reduced by the amount of the difference. That difference is assigned to that cost accounting period as an additional cost of compensated personal absence.

If the employer’s liability remains above that at the time of change, then costs of compensated personal absence are measured on the accrual basis. If the employer’s liability falls below that amount because of additional cash payments to employees, then the costs are measured on the cash basis. This latter condition will arise whenever employment levels fall below that existing at the time of change. Whenever such conditions occur, the costs of those periods are measured on a cash basis until the entire suspense has been written off. The contractor is not precluded from allocating costs which might otherwise have been allocable, absent the Standard but he cannot allocate more than he otherwise would have allocated, so that premature cost allocations cannot occur.

(6) *Complexity.* Many of the Commentators suggested that the proposed Standard was too complex, too detailed, or too procedural. As previously mentioned, the Criteria for accrual have been changed to eliminate the distinction between a “certain” and a “reasonably certain” obligation and to eliminate the utilization test. These changes permitted a significant reduction in the length and complexity of the Standard. In addition, the Board has made a number of simplifying changes in the wording of the Standard based on suggestions from commentators.

(7) *Adjustments for interim rates.* A number of commentators objected to the requirement in the proposed Standard that where costs of compensated personal absence are allocated using an interim rate, any difference between the interim rate and actual cost must be adjusted in the same period. They objected on the grounds that the necessary computations to determine the actual cost in accordance with the provisions of the Standard could not be completed by the end of the cost accounting period. Although the Board is not persuaded by this argument, the provision involved has been deleted for the following reasons. The accrual required by this Standard is identical to that required for any other year-end accrual, and the adjustment process is not essentially different from that which is required to adjust any interim allocation for a cost difference.

The requirement is well established that if overhead costs are allocated to Government contracts on an interim basis, there must be an adjustment when the actual costs are known. The Board therefore has concluded that is unnecessary to restate it in the Standard, although the requirement of course, remains in effect.

(8) *Requirement to maintain records.* Some contractors were concerned about the nature and extent of records which might be necessary to support the determinations and computation required by the proposed Standard. In particular, the need to maintain records of benefit utilization was questioned. The benefit utilization criterion has been deleted from the Standard; consequently, the maintenance special records for this purpose is unnecessary. Others were concerned that the proposed Standard would require changes in their formal accounting records. Upon further consideration the Board believes maintaining appropriate records is implicit in cost accounting and that the inclusion of additional record-keeping requirements in the Standard is unnecessary. In determining what records are necessary to achieve verifiability for purposes of this Standard, consideration should be given to the relative ease or difficulty of making and verifying assumptions and estimates, to the materiality the amounts involved, and to the use of techniques such as statistical sampling for determining the amount of the employer’s liability.

(9) *Exemptions.* Representatives of educational institutions pointed out two problems with the proposed Standard. First, it required that where costs of compensated personal absence are allocated using an interim rate, any difference between the interim rate and actual cost must be adjusted in the same period. These commentators pointed out that Pub.L.87-638 authorized use of negotiated predetermined overhead rates by these institutions and that this permission is presently set forth in Federal Management Circular 73-8: Cost Principles for Educational Institutions. Second, they pointed out that many educational institutions do not record costs on an accrual basis; but use fund accounting on a cash basis; and that for state and local governmental institutions, such accounting may be required by law. While the Standard does not require any change in the formal accounting records, in many instances it would be very difficult for these institutions to comply with the Standard.

In view of the foregoing, the Board does not believe it desirable to require educational institutions or state and local governmental agencies to account for costs of compensated personal absence on the accrual basis. Accordingly, the Board has exempted such institutions and state and local governmental agencies from the provisions of this Standard.

(10) *Costs and benefits.* The anticipated benefits of this Standard are improved cost measurement and increased uniformity in accounting for costs of compensated personal absence, leading to increased assurance that the measured costs are assigned to the proper cost objectives.

Several commentators objected that the Standard would not increase uniformity because the accounting for particular benefit plan would depend on the provisions of that plan, and not all benefit plans are alike. The Board is aware of the diversity of benefit plans. However, under present procurement regulations different contractors with essentially similar plans could be accounting differently for them and may be prevented from using similar accounting even if they wish to do so. To the extent that uniformity is thus actually inhibited, the Standard will correct the situation. Other past problems relating to the measurement of these costs in the event of layoffs, or employee transfers would also be alleviated.

Many commentators said that they were already accounting for costs of compensated personal absence in the manner required by the Standard. Some commentators said that implementation costs would depend on the extent of detail which would be required to comply. The Board has attempted to minimize such detail: First, by its previous statements that compliance with Standards may be accomplished through the use of memorandum records; second, by eliminating the utilization of benefits test and, thereby, the necessity of maintaining the supporting utilization records; and, finally, by emphasizing the acceptability of estimates based on statistical sampling or historical data. As a consequence, the costs of implementation should be negligible.

In summary, the Board believes that the benefits to be derived from this Standard clearly outweigh any costs of implementation. The Board expects that this Standard will become effective on April 1, 1975.

Preamble B
Preamble to Document Published 6-8-78

The document published on June 8, 1978 at 43 FR 24819, revised 408.10 and 408.70. This amendment was part of a publication which added 331.30 (b)(3). Only the portion of the preamble which describes the revision to 408.10, 408.70 are printed here. The remainder of the preamble appears as Preamble K of the supplement to Part 331.

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In the *Federal Register* of February 16, 1977 (42 FR 9391), the Board proposed to amend section. 10, General Applicability, of standards 401 through 409 to conform these sections to the general applicability section as it appears in standard 410 et seq. No comments were received on this proposed amendment. The Board considers this change to be appropriate and is amending standards 401 through 409 as set forth below.

Preambles to Cost Accounting Standard 409, Depreciation of Tangible Capital Assets

Preamble A
Preamble to Original Publication, 1-29-75

The following is the preamble to the original publication of Part 409, 40 FR; 4259, Jan. 29, 1975.

The Standards on Depreciation of Tangible Capital Assets being published today is one of a series being promulgated by the Cost Accounting Standards Board (CASB) pursuant to sec. 719 of the Defense Production Act of 1950, as amended (Pub.L.91-379, 50 U.S.C.App. 2168), which provides for the development of Cost Accounting Standards to be used in connection with negotiated national defense contracts.

On February 27, 1973, the Board promulgated a Standard on Capitalization of Tangible Assets. At that time the Board described its work to date in the area of fixed asset accounting including studies of practices used for both capitalization and depreciation. The responses to an issues paper and a questionnaire which were used in the development of the capitalization Standard were also useful in the development of the Standard being promulgated today. A preliminary draft of the Cost Accounting Standard on Depreciation of Tangible Capital Assets was widely distributed in March 1973 for informal comment by interested parties. The Board's further consideration of the issues related to depreciation has been significantly enhanced by the responses received from well over 100 respondents to that informal proposal.

The Board's research into fixed asset accounting practices included a survey of 107 profit centers selected to be representative of the diversity of firms to which Cost Accounting Standards apply. Reports on their fixed asset accounting practices and statistical information for a five-year period were received and analyzed. The Board was assisted in its deliberation by information available from the 1960 Treasury Department Survey which provided the data base for the "Asset Guideline Lives" used in Revenue Procedure 62-21 and data developed in an accounting research study performed for the American Institute of Certified Public Accountants.

A proposed Cost Accounting Standard dealing with depreciation was published by the Board on June 11, 1974 (39 FR 20505). After reviewing the responses to that publication, the Board revised its proposal. The revised version was published in the *Federal Register* for October 3, 1974 (39 FR 35678). The Board supplemented both *Federal Register* publications by sending copies of the *Federal Register* material directly to organization and individuals who were expected to be interested. The Board receive almost 200 responses to the June 11 and the October 3 proposals. Comments were received from individual companies, Government agencies, professional associations, industry associations, public accounting firms, universities, and individuals. All of these comments have been carefully considered by the Board. In addition, the Board invited representatives of Government agencies, professional accounting and industry association; and defense contractors to attend Board meetings and discuss their views on the significant issues concerning depreciation practices in Government contract costing. The Board takes this opportunity to express its appreciation for the helpful suggestions and criticisms which have been furnished. The comments furnished by organization and individuals have resulted in many changes in the Standard.

The comments below summarize major issues discussed by respondents in connection with both preliminary publications. They explain the major changes which have been made since the June 11 proposal.

(1) *Economic Impact of the Standard.* Many of the comments on June 11 and October 3 proposals were concerned with the economic impact of the Standard. They cited such concerns as delays in cash flow, impact of inflation, incentives for modernization, and administrative cost of additional recordkeeping requirements.

The Board's consideration of each of these primary concerns is dealt with in detail in other sections of these prefatory comments. The Board has recognized the potential overall impact of the Standard as expressed in the comments received and has endeavored to establish the needed guidance on depreciation accounting with as little disruption as possible to contractors and current contractual relationships.

The Standard provides for a phasing in of requirements over a period of time so that the principal impact of the Standard will be a number of years in the future. The Standard applies only to assets acquired by a contractor after the beginning of its next fiscal year after receipt of a CAS-covered contract. If the Standard were to become effective six months after submission to Congress, application of any provisions of the Standard to any newly acquired assets would be delayed more than six months from date of promulgation and for most contractors at least 12 months.

The Standard provides for a two year period to develop records on past experience to support estimates of service lives. The same period could be used to develop any necessary changes in accounting for fixed asset lives. The two-year period begins after required compliance with the Standard, and, therefore, most contractors would have at least three years in which to apply the recordkeeping provisions for newly acquired fixed assets.

For those contractors who use the two-year period to develop new estimated service lives, the effect of the use of those new estimates would begin on assets acquired in the fourth year after submission of this Standard to Congress. In the fourth year and the next several years thereafter the impact of changes in cash flow because of changes in service life estimates would be minimal, since the difference in cash flow each year is the difference between depreciation amounts under the old and new estimates of service life for the newly acquired assets. The total impact on cash flow of changes in estimates of service life would not occur until the full cycle of asset replacement is completed. In addition, the impact of the rules on accounting for gain or loss would only begin to take place where new assets acquired after compliance with the Standard would be sold or otherwise disposed of and such impact will be many years in the future.

It is the Board's opinion that the immediate economic and administrative impact of the Standard is minimal and will, over time, provide for a more appropriate recognition of cost accounting considerations distinct and apart from profit level determinations for defense contract cost and pricing actions.

(2) *Need for a Standard.* The accounting profession has established general principles to govern depreciation accounting. These broad principles require that depreciation practices be systematic and rational. Accountants consistently urge that the estimates of service lives used for depreciation should be realistic. These broad goals are almost universally agreed upon.

Some Commentators suggested that the Board should not promulgate any Standard dealing with depreciation because the applicable principles have been well established as a part of generally accepted accounting principles. These same commentators also argue that procurement regulations have allowed contractors to rely on depreciation practices found to be acceptable for other purposes; they believe that contract costing should continue to rely entirely upon the depreciation practices used for Federal income tax and for financial reporting purposes pursuant to the current procurement regulations. The Board believes, however, that depreciation charges based entirely on income tax and financial reporting practices do not necessarily assure reasonable representation of the costs of the services provided on Government contracts.

Various mathematical formulas have been suggested to represent the typical patterns of consumption of services over the lives of assets. Certain of these methods of depreciation have been incorporated into the Internal Revenue Code as acceptable for Federal income tax purposes. These same methods have, in general, been accepted as systematic and rational and therefore within the scope of generally accepted accounting principles. The Board finds that there has been a range of choice as to depreciation methods available for contract costing, without adequate criteria for the choices made.

The Treasury Department and Internal Revenue Service have established guidelines for determination of estimated periods of useful service. These guideline periods are said to be based on observed industry experience, but lives shorter than the averages experienced were established so that most companies would experience longer actual asset utilization periods than the permitted tax lives. Tax accounting lives for an industry are, therefore, not good representations of expected actual asset utilization periods for many individual contractors within that industry.

The Board's research has indicated that the asset lives and depreciation methods selected by defense Contractors under existing regulations may result in an unduly accelerated allocation of depreciation to the final cost objectives of earlier cost accounting periods in the life of a tangible capital asset. Contractor representatives have expressed the view that the choices are typically appropriate in view of the uncertainties of Government contracting. These uncertainties, however, have not precluded utilization assets well beyond the short estimated service lives based on the IRS guideline periods. Other commentator were concerned that any Standard which would restrict cash flow would adversely impact profits. The Board has determined that a Cost Accounting Standard is needed to provide more assurance that depreciation cost identified with performance of negotiated defense contracts are appropriately measured. Consideration of risk and capital investment in the determination of the adequacy of profits is a policy question for the procuring agencies and not a cost accounting problem.

(3) *Method of Depreciation.* Many of the comments received on depreciation method center on whether accelerated methods or straight-line methods are more appropriate for contract costing purposes. The Board, however, believes that no particular method is necessarily appropriate for all contract cost accounting situations. The Board is establishing criteria by which the method or methods appropriate in the specific situation can be

determined.

Both the June 11 proposal and the October 3 revision provided that the method selected "shall reflect the expected consumption of services in each accounting period." This basic goal generally recognized as appropriate. Commentators have raised question relating to the practical aspects of compliance with the basic goal. What kind of evidence should be available to support a selection of a depreciation method? In the absence of authoritative criteria for selection, contractors have had no need to support their choices, nor have they accumulated much experience in collecting evidence relevant to the consumption of services. Thus a requirement for support of accelerated methods is seen by some as a prohibition of the use such methods. However, the proposed made no distinction between an accelerated method or the straight, method of depreciation in determining the quantity and quality of supporting evidence. The Board's proposals included descriptions of the technique which should be used to determine appropriate methods for depreciation. The Board recognized the difficulty which might be experienced by contractors attempting to demonstrate the appropriateness of their choices. The Board's proposals included, therefore, the provision that the method of depreciation used for financial accounting purposes should generally be acceptable for contract costing.

Representatives of the accounting profession pointed out that there is strong economic motivation to choose rapid depreciation write-off techniques where cost is the basis for pricing and reimbursement, as in the defense contracting environment. They say that this same motivation may not apply to external financial accounting for the same companies. Accordingly, they expect that any Cost Accounting Standard which required that, in order to use a technique for contract costing, a company must use the same technique for financial accounting, might create an incentive to modify financial accounting practices solely for the purpose of obtaining an advantage in contract pricing. Because of these considerations the Board would prefer not to base its criteria primarily on practices used for external financial reporting. Most commentators have asserted that the depreciation methods now in use for external reporting purposes are appropriate methods for contract costing, too. The Board believes that this is generally true, and it further recognizes that a requirement to change to a particular depreciation method might result in significant cost to many contractors. In the belief that the methods selected as appropriate for financial accounting are usually intended to approximate the actual consumption of services, the Board has provided for continuance of those methods where this is a reasonable assumption. Therefore, in the October 3 proposal the word "reasonably" was used to modify the requirement that the method of depreciation reflect the expected consumption of services; this provision is continued in the Standard being promulgated today. In those few cases where existing methods used for financial accounting purposes are obviously poor representatives of the expected pattern of consumption, and in any case when the contractor proposes to change methods, the choice should be made on the basis of a reasonable expectation of the future pattern of consumption of services in accordance with the criteria provided in this Standard.

It has been asserted that some-assets purchased for Government contract purposes are used on an intermittent basis with periods of use and periods of nonuse following one another in a pattern that fits neither the classical accelerated nor straight-line models and that does not conform with the active-standby dichotomy. "The pattern of consumption of services" for such an asset is difficult to determine either prospectively or historically and is not necessarily dependent solely on use.

In circumstances such as the foregoing, it is not the intent of the Board to introduce uncertainty into contract negotiation and settlement by encouraging challenge of contractors' depreciation methods. If the method selected is also used for external financial reporting Q'Bd(sic) is acceptable for income tax purposes, the Board's expectation is that it will be accepted.

(4) *Service Lives.* Depreciation is to be charged during the period of estimated usefulness of a tangible capital asset. Some commentators have expressed concern lest the Board not give appropriate recognition to the importance of possible obsolescence in estimating the period of usefulness. The Board recognizes that for many contractors the likelihood of obsolescence is an important factor in estimating the period of usefulness, and has so provided in the Standard.

The June 11 proposal provided that estimated service lives used for financial accounting, where such lives reasonably represented expected usefulness, were to be used for contract costing. However, several commentators expressed concern that the requirement to use financial accounting lives would continue to influence the motivation of some financial reporting entities to select for financial accounting purposes those practices which would be most advantageous for other purposes. The Board's research showed that defense contractors often used minimum lives permitted for tax purposes for financial accounting rather than lives based on actual experience. Therefore, the October 3 revised proposal placed the primary reliance for estimation of service lives on records at of the age of assets at disposal or withdrawal from active use. The proposal is further provided that the historical data would be a baseline for estimates of useful life which could be adjusted or based on expected changes in physical or economic lives.

Contractors commenting on the October 3 proposal pointed out that they have not been required to have records which would show the retention periods of assets. Therefore, while most contractors have the basic information from which they could determine typical asset retention periods, few contractors have made analyses or summaries of the information available. Furthermore, they stated that contractors did not have records reflecting the withdrawal of assets from active use. The contractors expressed the opinion that to develop such records would be costly. The Standard has been modified to provide that the development of records of asset withdrawal from active use be at the option of the contractor; however, it should be pointed out that such records could be additional support to reduce historical asset lives.

The Standard also provides a two-year period for the development of analyses of historical asset lives. The Board believes the two-year period should provide adequate working time to develop such analyses. The Standard does not prescribe the nature of the analyses which should be performed, nor does it prescribe the number of prior years to be analyze or the extent of support necessary; it recognizes that the adequacy of records depends upon individual need and circumstances. The Board believe that most contractors have adequate records on asset retention. Estimates of experienced lives can be developed from these existing records on the basis of samples. Statistical sampling from existing records or judgmental samples with analyses to support a large portion of the dollar amounts involved may allow reasonable estimates in many cases with a relatively small sample. The Board expects that contractors will develop sufficient data support the lives used and that procurement agencies will enforce this requirement in a reasonable manner.

Several commentators criticized October 3 proposal on the basis that it would engender disagreements about the impact of the physical and economic factors recognized as appropriate to consider in relating actual past experience to expected future usefulness. The Board, in effect, places a burden of proof on the contractor who proposes that expected changes in physical and economic factors should be used to justify any specific reduction in estimate from that supported by his records.

The Board recognizes that many contractors would still be concerned not only about the concept of developing service life estimates from records of actual use but also about the risk of disagreements related to the appropriate adjustments to be made in relating actual past experience to expected future usefulness. The Board believes that procurement agencies generally recognize the significance of the physical and economic factors listed in the Standard. The Board encourages the procurement agencies to provide written guidance for use by field personnel, with the goal of making an effective transition from amortization periods derived from tax regulations those based on reasonable estimates actual useful service. The staff of the Board will participate, if requested, the development of appropriate guidance to field personnel.

(5) *Reliance on Internal Revenue Service.* Many commentators throughout the Board's research process in the development of this Standard, have suggested that the Board should rely on the experience accumulated by the Internal Revenue Service. Under this general approach the Board would be expected to concede that there is so much uncertainty about depreciation that auditors should not ask for support of estimates from individual contractors, but should accept for contract purposes the operation of a broad band of averages which have been developed for other purposes but which do deal with the same depreciation practices. The Board has recognized that contract costing often deals with the same expenditures and the same problems of allocation to time periods as are of interest in income tax accounting. Tax regulations, however, are intended to achieve a variety of social

goals quite foreign to the purposes of contract costing. In this regard, the “Asset Guideline Periods,” first established in 1962, were based on write-off periods substantially shorter than actual average experienced lives and these periods were subject to further reduction under the “Asset Depreciation Range System” in 1971.

> In addition, tax assessment and collection are continuous so that, except for differences in tax rates, shifts of income or expense from one year to another generally do not have a significant effect on total tax paid over a period of time. However, similar shifts of cost from one year to another could have a decided impact on the costs chargeable to the Government on contracts with it.
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> The Board has considered very seriously the issues which are related to its decision not to rely solely or necessarily on IRS regulations with respect to depreciation. Early versions of this Standard placed some reliance on IRS regulations. However, spokesmen for contractors criticized the specific techniques used, including the difficulty of using lives shorter than those permitted by IRS, while representatives of the accounting profession tended to encourage less reliance on IRS in any way. The Standard now being promulgated continues to make limited use of IRS regulations for estimating service lives where more pertinent information is not available.

(6) *Beginning and Ending Periods.* Several commentators expressed concern that the proposed Standard (both the June 11 and October 3 versions, which were alike in this regard) would not permit accounting conventions to be used for the beginning and ending periods of asset use. The Standard permits the application of conventions (such as the half-year convention) where reasonable in the circumstances and consistently followed. The Board sees no need for change in this respect.

(7) *Asset Groups.* Some commentators felt that the June 11 proposal implied a desire by the Board for depreciation accounting on an asset-by-asset basis. The Board does not intend to force any changes in decisions reasonably made with respect to accounting in terms of groups or of individual assets. Since depreciation is largely based on the application of estimates, when groups are used the estimates are intended to represent the average or typical experience for all individual assets in the group. The October 3 proposal was modified to make clear the Board’s acceptance of grouping practices in accounting for assets and in determining applicable depreciation lives and methods. The Standard permits accounting for assets either individually or in any reasonable grouping, provided that the accounting treatment is consistently applied.

(8) *Use Rates.* In its June 11 proposal, the Board pointed out that the proposed Standard is expected to be applied by contractors in situations where depreciation cost is a factor in determining equitable charging rates to be used as a basis for contract costing. For example, the development of rate schedules for construction plant and equipment and ownership costs for comparison to lease or rental costs would be accomplished in conformance with the requirements of the proposed Standard. The proposed Standard also would have been required to be used by educational institutions in a determining amounts to be compensated for use of buildings, capital improvements and equipment.

> University commentators stated that few colleges and universities recognize depreciation in their accounting records. Replacement of capital assets is often handled by special appropriations or by bequests and other contributions. Federal Management Circular 73-8 has provided for use allowances as recognition for the employment of capital assets on contract work.
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> A number of commentators have pointed out that many educational institutions prefer the current use allowance system even though they recognize that conventional depreciation accounting would result in higher recognized costs. The most important reason stated is that the administrative cost and effort involved in establishing depreciation accounts would be significant.
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> These comments have been persuasive. Universities who choose not to incur the additional administrative expense should have an acceptable alternative basis for reimbursement for the use of tangible capital assets. The Standard has been modified to provide that it does not apply where FMC 73-8 use allowances are a part of contract costs. However, the Standard does apply whenever depreciation accounting is used by an educational institution for a covered contract.

(9) *Residual Value.* Several commentators expressed concern that the proposed Standard defined “residual value” even though the only available numeric value during the service life of an asset is that for “estimated residual value.” The wording in the definition has been modified to clarify the Board’s recognition of this point.

The proposal included permission to disregard minor residual values (those-under ten percent of capitalized cost) in determining a schedule of depreciation charges -- until the net book value approaches the residual value. Some commentators suggested that residual values be ignored completely. Others suggested that they be permitted to depreciate beyond actual residual values because of practicality considerations.

The Board has several times expressed its belief that the administration of Cost Accounting Standards should be reasonable and not seek to deal with insignificant amounts of cost. (See, for example, the March 1973 “Statement of Operating Policies, Procedures and Objectives.”) Except for depreciable real property, there would usually be little improvement in the accuracy of cost measurements if estimates of minor residual values were explicitly considered in establishing amounts to be depreciated. However, the Board continues to believe that the magnitude of the expected residual value should be considered for each asset or for each group. If the estimate is greater than ten percent of capitalized cost or if it is applicable depreciable real property it should be deducted from the capitalized amount determining the depreciable cost. The Standard has been modified to clarify the applicability of the ten per cent materiality rule to personal property only.

The June 11 proposal prohibited the charging of any depreciation amount which would reduce book value below residual value. Where fixed asset accounting is by groups, this provision was not intended to require separate identification of the book values and residual values of individual assets. For individual assets, where actual residual values are not material, the Board does not intend that such material amounts be identified. The criterion of materiality applies to all Board promulgation’s, and therefor the Board does not believe it necessary to restate it in every circumstance.

(10) *Gain or Loss.* Both the June 11 and October 3 proposals required that gain or loss on disposition of tangible capital assets be assigned to the cost accounting period in which disposition occurs. A number of commentator suggested that gain or loss on disposition, as an adjustment of depreciation previously recognized, should be assigned to the cost accounting period; and cost objectives to which the depreciation had been charged. This suggestion is conceptually sound but impractical to apply. The records necessary to identify prior depreciation charge would be difficult to maintain. In addition, where losses occur on disposition, application of the cost to prior periods and cost objectives would often be precluded because applicable contracts may have been closed or funding for the additional cost may not be available. Accordingly, the Board believes it would be fair to both contractors and the Government to adjust for gain or loss in the current cost accounting period.

Commentators suggested that if adjustment is to be made in the current cost accounting period, it should be made to some general indirect cost pool so that adjustments could be absorbed by all work of the period. The Board believes, however, that -- to the extent practical -- adjustments should be made to the same cost accounts to which the depreciation cost of the asset had been or would have been allocated in that cost accounting period. To the extent that depreciation cost is assigned to individual departments or cost centers, so should the adjustments to depreciation resulting from the disposition of assets.

Commentators expressed the opinion that gains on disposition of assets in today’s economy are often the result of inflation and not adjustments of depreciation expense. The Board recognizes that assets held for long periods, especially real property, may be disposed of for amounts in excess of net book value. The gain may have been caused by any of several factors, including the rising general price level. In some situations it may be arguable that the gains should not be considered as corrections to previous depreciation charges. The Board and others in the accounting profession are examining new techniques to deal with accounting for inflation. However, accounting for cost on an historical basis is now generally accepted and until the new techniques are developed and accepted, the Board does not see a practical way to differentiate those gains deemed by some to be based on inflation from those resulting from excessive depreciation charges.

Because the Standard applies only to assets acquired after the date when the Standard must first be followed by a contractor, the impact of the Standard on recognition of gains or losses in some years in the future. At that time it is expected that guidance will be available on the appropriate treatment for price-level changes reflected in gains or losses from disposition of fixed assets.

Current procurement regulations of Government agencies are not consistent in their provisions for gains and losses. A number of commentators were apparently unaware of this diversity; they encouraged the Board to leave the present situation alone. The existing procurement regulations have been carefully considered and the Board believes that contract cost determinations will be improved by more uniform treatment of such gains and losses.

Several commentators were concerned that the treatment of gain or loss from involuntary conversion, while in agreement with the Federal income tax treatment, differed from the generally accepted financial accounting practice. The Standard has been changed to permit the contractor to use either basis in accounting for involuntary conversions.

(11) *Original Complements.* The Standard on Capitalization of Tangible Assets defined and required the capitalization of original complements of low-cost equipment. There has been some controversy over the appropriate write-off technique for such capitalized amounts. Informal staff proposals require amortization over the life of the complement, or of the asset for is which it has been required, were challenged by contractors as being unreasonable. The Board recognized the intensity of this feeling and the June 11 proposal included a provision developed specifically to assign such costs among cost accounting periods.

Some commentators pointed out that the June 11 proposal for amortization of original complements would have required a practice which is not at all common and would be difficult to implement.

The provisions of the proposal were, modified for the October 3 version to require simply that an original complement be treated as a tangible capital asset, and that the basic requirements of the Standard be applied to it. Thus, the costs of each original complement would be amortized over its period of expected usefulness, and in accordance with its pattern of expected usage, either separately or as a part of an appropriate group. Comment received on the October 3 version have a suggested some misunderstanding of the principle involved. Some additional language has been added to the illustration on depreciation for original complements in 409.60(c) to further clarify the principle that an original complement is a single asset and not group of individual items.

(12) *Retroactive Impact of Changes.* The Board called attention, in the June 11 publication, to the conflict between some aspects of Opinion No. 20 of the Accounting Principles Board and the treatment proposed, in 409.50(i), for changes made in depreciation accounting during the service life of an asset. The position proposed by the Board, that of making changes applicable prospectively only, was approved by most of those who commented on the point. A very few commentators asked that the Board agree with the financial accounting principle and insist upon retroactive impact, even though this would require reopening settled contracts. The Board was not convinced that any improvement in costing accuracy resulting from reopening settled contract would merit the obvious administrative inconvenience involved. The Standard is, therefore, not changed in this regard.

(13) *Service Center Costs.* The June 11 proposal provided that when depreciable assets are part of an organizational unit whose costs are charged to users on the basis of service, the depreciation cost of such assets should be included as part of the costs of the organizational unit. A number of commentators expressed concern that the Standard might be thought to require the assignment of building depreciation separately to each organizational unit which occupied a building, even though the applicable building depreciation might be only a very minor part of the total organizational unit cost. If an organizational unit occupies a entire building, and the depreciation cost of that building is significant and can practicably be identified, that building depreciation cost should be included as a cost of the organizational unit for assignment to cost objectives on the basis of service. If, however, the total depreciation cost of a building, which is allocable to a number of cost objectives, is accounted

for as indirect cost and its allocation on that basis would not materially distort the measurement of costs to a benefiting cost objective, little point would be served by insisting that each organizational unit receive a specific charge for building depreciation.

Several commentators were concerned that the paragraph on service centers might restrict the base or bases used for charging service center costs to other cost objectives. Nothing in that paragraph is intended to limit or prescribe the base or bases used for charging service center costs.

(14) *Cost of Capital.* Many commentators have pointed out that the requirements to be imposed by the Standard may result, on assets acquired after the effective date, in less depreciation charged in earlier years of asset life. The resultant slowdown in recovery of funds could, they pointed out, have an adverse impact on the profitability of defense contracts. Many of the comments seek to justify rapid write-off as a partial offset to the costs of capital actually involved but not directly recognized in contract pricing.

The purpose of this Standard is to provide a better measurement and a location of depreciation cost. Accounting practices used for these functions should be justified on the basis their effectiveness for such measurement and allocation. They should not be justified on the basis of problems identified with other aspects (e.g. profitability) of defense contracts.

The Board has no authority to extend itself into the area of profitability of defense contracts. This is a matter for the procuring agencies. In this regard, current procurement regulations provide guidance with respect to negotiating proposed profits; this guidance includes some implicit recognition of the cost of capital. The Board believes that accounting for the costs of capital and determining equitable measures of profit are issues separate from depreciation accounting and these issues cannot be resolved effectively by adoption of any particular depreciation practices.

(15) *Modernization and Public Policy.* Many commentators have pointed out, throughout the process of developing this Standard, that no Cost Accounting Standard should be adopted if it would interfere with public policy to encourage investment in facilities which might provide a more modern, more effective industrial mobilization base. The Board favors appropriate improvements in the physical facilities used in performance of negotiated defense contracts; its purpose however does not include such public policy decisions as the introduction or continuation of incentives to encourage investment in certain classes of assets. This Standard is being promulgated for the purpose of improving the measurement and allocation of depreciation on acquired assets. The Board does not believe that this purpose is inconsistent with or a deterrent to effective plant modernization.

(16) *Inflation Accounting.* Some commentators were concerned with the effect of inflation in depreciation accounting. They suggested that this Cost Accounting Standard should provide for the use of replacement cost or current value rather than historical cost as the basis for determining depreciable amounts. Present Government procurement regulations as well as financial and tax accounting are based on historical costs. Current inflationary trends, however, suggest that more attention should be given to the impact of inflation on established accounting concepts.

The Financial Accounting Standards Board (FASB) is considering this subject. The FASB issued an Exposure Draft on “Financial Reporting in Units of General Purchasing Power” on December 31, 1974. The CASB is also studying the subject.

The cost impact of this Standard for most contractors is some years in the future. The Standard is required to be followed by contractors at the start of their next fiscal year after receipt of a covered contract requiring compliance with this Standard. The Standard provides for a two-year period after required compliance to accumulate necessary supporting records. The requirement of the Standard for determining lives applies only to new assets acquired after the necessary records are available. Therefore, for most contractors implementation of the requirements of life determination will apply only to new assets acquired in accounting periods beginning January 1, 1978, or later.

The Board sees this Standard as establishing proper techniques for the measurement and allocation of depreciation expense. The Board believes, therefore, that this Standard can properly be promulgated at this time. The subject of inflation accounting concerns not only depreciation cost but all costs, and will be dealt with as part of the studies now in progress by a both the CASB and the FASB.

(17) *Costs and Benefits.* Comments received on the June 11 and October 3 proposals indicated that there would be substantial administrative cost entailed in complying with this Standard. Part of the increased cost is attributed to required changes in accounting practices; a greater part is alleged to be related to increased controversy over the acceptability of current and proposed depreciation methods and lives.

A number of the administrative problems described in the comments have been reduced or eliminated by changes to the Standard. The requirement for recordkeeping, however, has not been eliminated. As discussed above, the Board recognizes that for some companies additional cost will be incurred to implement this aspect of the Standard. Also as discussed above, there may be some one-time analytical effort during the next two years to develop starting estimates of actual retention periods. The Board believes that these administrative costs, when reasonably managed in light of the purpose to be served, are warranted by the likelihood of better measurement of depreciation cost than has previously been available.

The Standard does not prescribe uniform accounting treatment. It enunciates principles and criteria for the implementation of these principles, which will achieve a practical degree of increased uniformity and consistency in fixed asset depreciation accounting techniques. In some cases, as for the determination of estimated service life, the Standard requires the establishment of records to achieve a better measurement of cost based on the manner in which contractors manage their fixed assets.

The benefits to be expected are better accounting for depreciation cost and enhanced ability to meet the responsibilities of the Government and of defense contractors to properly account for the expenditure of public funds. The Board recognizes that some additional costs will be incurred in obtaining compliance with this Standard. The benefits to be obtained are substantial, and the Standard contributes to fulfilling the Board's obligation to seek improved accounting for defense contracts.

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There is also being published today (40 FR 4259) an amendment to Part 400, Definitions, to incorporate in that part terms defined in 409.30(a) of this Cost Accounting Standard.

Preamble B
Preamble to Document Published 6-8-78

The document published on June 8, 1978 at 43 FR 24819, revised 409.10. This amendment was part of a publication which added 331.30 (b)(3). Only the portion of the preamble which describes the revision to 409.10 is printed here. The remainder of the preamble appears as preamble K of the supplement to Part 331.

In the *Federal Register* of February 16, 1977 (42 FR 9391), the Board proposed to amend section. 10, General Applicability, of standards 401 through 409 to conform these sections to the general applicability section as it appears in standard 410 et seq. No comments were received on this proposed amendment. The Board considers this change to be appropriate and is amending standards 401 through 409 as set forth below.

Preambles to Cost Accounting Standard 410, Allocation of Business Unit General and Administrative Expenses to Final Cost Objectives

Preamble A
Preamble to Original Publication, 4-16-76

The following is the preamble to the original publication of Part 410, 41 FR 16141, Apr. 16, 1976, as corrected at 41 FR 22241, June 2, 1976.

The Standard on Allocation of Business Unit General and Administrative (G&A) Expenses to Final Cost Objectives being published today is one of a series being promulgated by the Cost Accounting Standards Board (CASB) pursuant to section 719 of the Defense Production Act of 1950, as amended (Pub.L.91-379, 50 U.S.C.App. 2168) which provides for the development of Cost Accounting Standards to be used in connection with negotiated national defense contracts. Preliminary work on the development of this Standard was based in part on the "Report on The Feasibility of Applying Uniform Cost-Accounting Standards to Negotiated Defense Contracts," which cited the allocation of G&A expenses as one of the most frequently encountered problems in the area of allocation of indirect cost.

Another basis for the early work in this area was the absence of a requirement in procurement agency regulations dealing specifically with the allocation of business unit G&A expenses. Up to now, practices related to the allocation of G&A expenses have been covered by general provisions dealing with allocability and indirect costs. These provisions do not include criteria for the selection of allocation practice in given circumstances. The Board undertook research with the view that a Cost Accounting Standard on this subject should increase the likelihood of achieving objectivity in the allocation of G&A expenses to final cost objectives and comparability of cost data among contractors in similar circumstances.

Early research included an extensive review of available literature including decisions of contract appeals boards and courts. A preliminary analysis of accounting for the allocation of G&A expenses was made and significant issues were identified. A research questionnaire based on these issues was distributed on July 28, 1972; it was designed to solicit a sample of existing practices used for the allocation of G&A expenses and the reasons supporting existing practices. Responses were obtained from 65 sources.

After evaluation of the responses to the questionnaire, the Board developed a preliminary research draft of the Standard which was widely distributed, on December 13, 1973, to obtain informal comment and to ascertain the cost impact of adoption of the Standard as proposed. The Board's further consideration of the issues related to the allocation of G&A expenses has been enhanced by almost 100 responses to this preliminary proposal.

A proposed Standard was published in the *Federal Register* of September 24, 1974, (39 FR 34300). After reviewing the responses to that publication, the Board revised its proposal. As part of its research in preparing the revised proposal, the Board surveyed, as described below, a number of companies who use a cost of sales base to allocate G&A expenses. The revised proposal was published in the *Federal Register* of September 9, 1975, (40 FR 41801). As part of the comments with the September 9, 1975 publication, the Board stated that it was particularly interested in receiving comments on the alternative methods for the proposed requirement for the transition from a cost of sales base for allocation of the G&A expense pool to use of a cost input base. Respondents were specifically asked to comment on the administrative cost and effort entailed by each of the alternatives and to indicate their preference between the alternatives. The Board supplemented both *Federal Register* publications by sending copies of the *Federal Register* material directly to organizations and individuals who had expressed an interest in the work of the Board.

The Board received a total of 136 responses to both *Federal Register* publications; 65 to the September 24, 1974 proposal and 71 to the September 9, 1975 proposal. Responses were received from individual companies, Government agencies, professional associations, industry associations, public accounting firms, universities and others. The Board takes this opportunity to express its appreciation for the helpful suggestions and criticism which have been furnished. The comments furnished by organizations and individuals have resulted in a number of changes in the Standard.

The comments below summarize the issues discussed by respondents in connection with both proposed Standards. They incorporate the still relevant portions of the comments which accompanied the September 24, 1974 publication. The comments also explain the major changes which have been made to the prior proposals.

1.**-- Selection of an Allocation Base for the G&A Expense Pool**

Allocation Relationship. Commentators expressed the view that the choice of an allocation relationship between the

G&A expense pool and final cost objectives is arbitrary; particularly, the selection of any single allocation base is arbitrary. Commentators also took the position that the G&A expense pool cannot be allocated on a demonstrable beneficial or causal relationship, that G&A is not specifically relatable to all costs, nor does it bear any relationship to cost objectives or any particular final cost objectives. Other commentators stated that the selection of the cost input base must be based on the assumption that G&A is caused by cost input. The commentators with reference to the Martin-Marietta case, ASBCA 14159, March 16, 1971, noted that the decision in that case rejected this position.

While some commentators on the September 9, 1975 publication supported the choice of cost input, others agreed with the views expressed above. The Board has concluded that the expenses in the G&A expense pool are the expenses of the general management and administration of a business unit as a whole: that the allocation base chosen should be one which measures the total activity of the business unit during a cost accounting period and not just some part of total activity and that a cost input base accomplishes this objective.

Cost of Sales Survey. Shortly after the initial *Federal Register* publication, the Board surveyed segments of a number of companies who use a cost of sales base to allocate G&A expenses. The survey was designed compare the results of using a cost of sales base with the results of using a cost input base to allocate these expenses. Responses were received from 91 segments. The results of the survey established that in the case of individual segments the use of a cost of sales base as compared with a cost input base can result in a significant difference in the G&A rate and in the allocations of G&A expenses to final cost objectives. For example, one of the segments in the survey had a G&A rate based on cost of sales of 8.0 percent. When that segment used a total cost input rate, its G&A rate for the same period was 10.4 percent or a 30 percent difference. A change to a total cost input rate would have resulted in substantially different allocations of G&A expense to that segment’s final, cost objectives.

Some commentators were critical of the Board’s using a single year as the basis for the survey. These commentators noted that there could be isolated instances where the use of a cost sales base would not produce equitable results. However, they noted that over time a cost of sales base will give equitable costing results.

For a cost of sales base to provide an equitable allocation consistent with that of an allocation to the total activity of a business unit during a cost accounting period, a contractor’s mix of work between Government and commercial, types of contracts and the level of G&A expenses would have to remain constant over many periods. In this regard, the cost of sales survey demonstrated that in any given period, one period being selected, the use of a cost of sales base can result in significant differences in the allocation of G&A expenses to final cost objective as compared with the results obtained using a cost input base.

Cost of Sales Base. A number of commentators suggested that the use cost of sales as a measurement of the allocation base for the G&A expense pool should be permitted. Commentators asserted that this base has long been used for the allocation of the G&A expense pool and is consistent with generally accepted accounting principles and the concept of period costs. The Board’s position is that the measurement of a cost of sales base is representative, in part, of the productive activities of prior periods and subject to fluctuations which can distort the allocation of G&A expense to activities of the current period. Although the measurement of cost of sales is based on a recorded date of sale, that is not necessarily an index of the activities of a period.

Under current regulations as interpreted by the Armed Services Board Contract Appeals, the use of a cost sales base will not result in an equitable allocation of G&A expenses where there are significant changes in the mix of business or significant changes in the beginning and ending inventory balances. The Board has considered the existence of these past disputes and cases involving the use of a cost of sales allocation base. In given circumstances, due to the definition and accounting for sales under various types of contracts, the cost of similar types of productive activities may be treated differently in terms of the measurement of a cost of sales allocation base. The use of a cost of sales base can result in unwarranted shifting of costs between different types of final cost objectives. Therefore, the Board has concluded that the use of a cost of sales base is inappropriate for establishing the proper cost of final cost objectives within a cost accounting period.

Cost Input Base. Commentators took the position that the use of a cost input base would violate generally accepted accounting principles used for financial accounting purposes because G&A expenses are most commonly viewed as a period cost and not allocated to production nor inventoried. The use of a cost input base would result in inventorying G&A expenses for contract costing purposes. Further, commentators asserted that there is no beneficial or causal relationship between the G&A expense pool and cost input, cost objectives or specific final cost objectives.

The logical extension of this argument is that these expenses should not be allocable to Government contracts. If no beneficial or causal relationship can be established then there should be no recovery, because for a cost to be attached to cost objectives some beneficial or causal relationship should exist.

There are a number of firms which inventory G&A expenses on Government contracts for financial disclosure purposes. Moreover, the IRS and the SEC have recognized that in some instances G&A expenses are being applied to the inventory of Government contracts, and the G&A expense pool allocation remains in the inventory of these contracts at the end of the accounting period. While the Standard does not require that G&A expense be inventoried for financial reporting purposes, the inventorying of G&A expenses on Government contracts has been an acceptable accounting procedure for financial reporting as well as for filing with the SEC. Under current IRS regulations, G&A expenses may be allocated to inventory.

The Standard being promulgated today is based on the concept of full-costing of final cost objectives. For Government contracting purposes, both direct and indirect costs, including G&A expenses, are allocable. Thus, for contract costing purposes, the concept of period expense is inapplicable. The Board has concluded that there is a beneficial or causal relationship between G&A expenses and all of the final cost objectives of a cost accounting period. Therefore, these costs are allocable to such final cost objectives.

Commentators also asserted that the Standard was unduly rigid because it permitted only one base for the allocation of the G&A expense pool. The Standard is not limited to the use of one allocation base; rather, the scope of the base, the measurement of total activity, is limited to cost input as this is the measure of the total activity of the business unit. The Standard provides that the measure of cost input best representing the total activity of the business unit during cost accounting period is to be the one chosen as the base. The Standard includes criteria for determining the cost input base which will best measure total activity. The criteria are provided so that the allocation base for the G&A expense pool can be selected giving consideration to the differing circumstances of individual business units.

Commentators expressed a variety of views concerning the criteria for the selection of a cost input allocation base. Some commentators noted that the criteria included the necessary guidance and means for selecting the base. Others expressed concern that the criteria for selection of a particular cost input base were not clear and could lead to disputes. Some commentators expressed the view that the inclusion of value-added and single-element allocation bases was redundant. Also, a contractor should be required to demonstrate that the use of a total cost input base would not result in an appropriate allocation before the use of one of the other bases was permitted. Other commentators stated that explicit inclusion of direct labor hours and direct dollars serves to clarify the Standard. Commentators suggested that the selection criteria should be modified to remove any bias favoring a total cost input base.

The Board has recognized the merit of the numerous comments and suggestions received during the research process. The Standard has been modified to clarify the criteria for the selection of an allocation base in a particular circumstance.

Under the Standard, only a cost input base may be used. Three cost input bases have been provided and criteria have been established for selection of the appropriate base. The individual circumstances of a given business unit must be analyzed, and the cost input base that best represents the total activity of that business unit would be the base selected. The Board’s research indicates that generally total cost input, because it is a broad measure of all of the work done and includes all of the costs allocable to the contracts of the period, will be a measure that is representative of the total activity of the cost accounting period.

In this context the term “total activity” refers to the production of goods and services during a cost accounting period. This scope of activity is selected in light of the fact that the purpose of this Standard is to provide guidelines for the allocation of expense to all of the work of a given cost accounting period.

Commentators questioned whether other indirect costs not part of cost of goods sold, such as unallowables and nonoperating expenses, should be part of the measurement of cost input. These commentators took the position that such costs should not be part of cost input. Commentators pointed out that there could be an inconsistency in the cost input bases used by various contractors depending on whether costs such as selling costs or IR&D and B&P costs were included in the G&A pool or excluded from the G&A pool and included as part of the cost input base. Commentators also questioned whether costs such as service center costs and intersegment transfers should be included in the cost input base for the allocation of the G&A expense pool.

The cost input base has been selected as the measure of the total activity of the work performed during the cost accounting period. Therefore, it is appropriate that the costs of all activities, functions, materials, services, etc., allocable to final cost objectives during a cost accounting period be included in the total cost input base for that period. This relationship is based on the scope of the G&A expenses which represent the cost of the general management and administration of the business unit as a whole. For example, where a total cost input base has been selected, all significant costs other than the costs included in the G&A expense pool should be included in the base. The Board is aware that there can be a difference in the allocation bases used depending upon the treatment of selling costs and IR&D and B&P costs. This result occurs from the Board's accommodation of existing practices for accounting for selling costs and IR&D and B&P costs within the structure of this Standard. The Board has specifically required the inclusion of these costs in the cost input base in 410.50(f). The illustrations concerning the accounting for these indirect costs as part of a cost input base have been revised to clarify the required treatment.

Commentators suggested that minor variations from the specific bases presented should be allowed. The Board points out that the Standard requires that the allocation base selected should include all significant elements of cost input necessary to represent the total activity. If in a given circumstance, the exclusion of a particular item does not invalidate the chosen base's representation of total activity this is acceptable under the Standard. The Board notes that these are the kinds of decisions which involve consideration of the individual circumstances of a business unit; accordingly the Standard provides the opportunity for the exercise of judgment in these situations.

Commentators noted the Standard lacks an explicit consistency requirement for the use of the cost input base selected. It was pointed out that allocation bases once selected are then used for considerable periods of time, usually as long as the underlying economic circumstances do not change. In this situation the selected base would remain representative of the total activity of the business unit. The Board does not intend to change this practice. In fact, the Board notes that in concert with Cost Accounting Standard 401, the selection of the allocation base for the G&A expense pool should provide the basis for allocation of that pool until such time as the basic economic circumstances change. The Standard has been modified to require that the base selected should be one that measures activity of a typical cost accounting period.

Commentators were uncertain as to the relationship of cost input to the purchase of raw materials inventory and to Cost Accounting Standard (CAS) 404 -- Capitalization of Tangible Assets. To help clarify the relationship of this Standard to the purchase of raw material inventories and to CAS 404, an illustration has been added. Cost input is basically a measure of the costs and expenses allocated to production of goods and services during a cost accounting period. The illustration has been revised to make clear that items purchased for raw material inventory which have not been committed or used in production during a cost accounting period would not be part of the cost input base for that cost accounting period. As to the acquisition costs of assets constructed or fabricated by a contractor, CAS 404 and the Standard must be read together. The requirements of CAS 404 provide that those G&A expenses which are identifiable with the constructed asset and are material in amount shall be allocated to the cost of the asset. CAS 404 also provides that the cost of constructed assets that are identical with or similar to the contractor's regular product shall include a full share of indirect costs -- thus, the costs of these assets will be included in the cost input base.

2.**-- A Transition Provision**

Some commentators suggested that to avoid disputes and inequities the Board should provide a specific method of transition for any contractor that is required to change from a cost of sales or sales base to a cost input base. In the September 9, 1975 publication, the Board proposed alternative transition. Methods X and Y as a means of avoiding potential disputes and minimizing the administrative cost of implementing the change from a cost of sales or sales base to a cost input base. Either of the proposed methods would have eliminated the major portion of potential equitable adjustments arising from compliance with the Standard.

Numerous comments regarding the equity administrative complexity, and costs of both X and Y were received. Some commentators asserted that Y was more equitable in that both CAS-covered and non-CAS-covered work would be treated alike, on the basis on which the work was negotiated. Others felt X was more equitable in that there would be less impact on non-CAS-covered work. Some commentators expressed the view that neither X nor Y was equitable in that both methods effectively repriced existing contracts by impacting, "squeezing down" the cost input rate on new contracts, and both methods would result in a deferral of recovery of G&A expenses.

While some commentators found one method less administratively complex than the other method, other commentators saw little difference in the administrative cost and effort required by either method. Most commentators expressed the view that either X or y would require some additional administrative effort and the generation of data not currently produced.

A number of alternative transition methods were suggested including:

(1) An option to use either X or Y,

(2) An option to use X or Y or switch over immediately,

(3) Neither X nor Y, but use equitable price adjustment,

(4) The use of a combination method involving the actual cost of sales and cost input rates for a period and some type of suspense account to prevent an over-recovery of G&A expenses.

In addition, commentators proposed a number of variations of these basic alternatives. The Board is persuaded, after reviewing all of the comments received on transition methods, that a variation of one of those methods favored by many industry associations and several defense contractors offers substantial promise for avoiding potential disputes and for minimizing the impact of shifting from a cost of sales or sales base to a cost input base. This transition method is set forth in 410.50(e) and Appendix A of the Standard. Business units required by the Standard to change from their present allocation base to a cost input base are not required to use this transition method; rather, a business unit has the option of choosing this transition method or proceeding with an immediate change over to a cost input base and seeking adjustment under the equitable adjustment provision of the contract clause.

Use of the optional transition method will, in the Board's opinion avoid the need to use the equitable adjustment provision of the contract clause to reprice prime contracts an subcontracts of business units using this technique. The Board believes that this procedure is appropriate for this Cost Accounting Standard.

It is the Board's view, however, that for most Standards the impact of changes in cost accounting practice required by new Cost Accounting Standards will be accommodated by price adjustments for covered prime contracts and subcontracts through the equitable adjustment provisions of the contract clause.

For any business unit which chooses not to use the transition method set forth at 410.50(e) and Appendix A, the contractual provision requiring appropriate equitable adjustment of the prices of affected prime contracts and subcontracts will, of course, be implemented with consequent adjustment of the price of such contracts and subcontracts. The optional transition method provided in 410.50(e) and Appendix A permits a business unit whose disclosed or established cost accounting practice was to use a cost of sales or sales base -- and which is performing work on final cost objectives which came into existence prior to the date the business unit must first allocate its cost in compliance with the requirements of this Standard -- to allocate the G&A expense pool to these cost objectives using a cost of sales or sales base. These final cost objectives often include:

(1) Government contracts which contain the CAS clause;

(2) Government contracts which do not contain the CAS clause;

(3) Contracts other than Government contracts, or customer orders awarded, prior to the date the business unit

must first allocate its cost in compliance with the requirements of this Standard; and

(4) Production not specifically identified with contracts or customer orders under production or work orders existing prior to the date on which a business unit must first allocate its cost in compliance with this Standard and which are limited in time or quantity.

Production under standing or unlimited work orders, continuous flow processes and the like, not identified with contracts or customer orders, are to be treated as final cost objectives awarded after the date on which a business unit must first allocate cost in compliance with the requirements of this Standard.

The business unit will allocate its G&A expense pool to those final cost objectives which arise on or after the date on which a business unit must first allocate costs in compliance with the requirements of this Standard using a cost input base calculated in compliance with 410.50(d).

A business unit will use the transition method until all pre-existing final cost objectives using the cost of sales or sales base are completed. At that time the business unit will be using and will continue to use a cost input base selected in accordance with the requirements of 410.50(d) to allocate the G&A expense pool to all CAS-covered contracts.

In order to prevent possible windfalls and to provide equity to both parties to applied to the inventory suspense account must be established. The amount of the inventory suspense account shall be the beginning inventory of contracts subject to the CAS clause of the cost accounting period in which a business unit must first allocate costs in accordance with the requirements of this Standard. The G&A expense allocation rate to be applied to the inventory suspense account is the cost of sales rate for that first accounting cost period.

The suspense account will be amortized in any cost accounting period subsequent to the last cost accounting period in which final cost objectives negotiated by using a cost of sales or sales base are still being performed and in which the amount of the ending inventory of contracts subject to the CAS clause for that cost accounting period is less than the amount of the inventory suspense account. The G&A expense pool of that cost accounting period shall be reduced by the difference between the inventory suspense account and the ending inventory of contracts subject to the CAS clause of that cost accounting period times the cost of sales rate applicable to the inventory suspense account.

The Standard must be followed after the start of a contractor’s next fiscal year after January 1, 1977. This long lead time provides both the Government and contractors an opportunity to prepare appropriate administrative procedures for using this transition method.

3.**-- Definition of G&A Expense**

G&A Expense. Some commentators expressed the view that the definition was consistent with their current practice; others were concerned that the definition of G&A expense was narrower than those definitions currently in use, and the result might be excessive fragmentation of existing G&A expense pools to remove insignificant items.

Board research indicates that while accountants are in agreement about the general character of G&A expenses, practice has resulted in the cost of a variety of functions and expenses being included in the G&A expense pool. As a result, from the early stages of this project onward, the Board has seen a need to provide a definition of G&A expense in order to bring some uniformity to this area of accounting. Commentators expressed concern about problems involving the classification of those persons and functions of top level management that are concerned with both the overall planning and administration of a business unit and the direction of a particular function. Some commentators suggested that top level management people could keep time records, and split their costs between the G&A expense pool and the administration of the function which they are directing. While this may be appropriate in some circumstances, the Board believes the determination of the content of the G&A expense pool and the identification and classification of expenses in a particular circumstance must be based on judgment giving consideration to the characteristics of the individual business units. Similarly, the distinction between those expenses which are other indirect costs, including manufacturing overhead and those which are G&A expenses must be based on the individual circumstances using the guidelines provided in the Standard and the definition.

The definition has been revised to provide guidance for making those decisions. The definition now requires that for an expense to be classified as G&A expense, it must be incurred for the management and administration of the business unit as a whole. Further, the definition specifically excludes from G&A expense those management expenses whose beneficial or causal relationship to cost objectives can be more directly measured by a base other than a cost input base representing the total activity of a business unit during a cost accounting period.

Commentators indicated concern and expressed some confusion regarding the interaction of the definition of G&A expense and the requirements of 410.40(d). Commentators were uncertain as to if and when expenses which do not meet the definition of G&A expenses contained in the Standard should be removed from the G&A expense pool. The Board has revised 410.40(d) to clearly express the Board's intent that those expenses which do not meet the definition of a G&A expense and whose beneficial or causal relationship to business unit cost objectives is best measured by base other than a cost input base representing the total activity of a business unit during a cost accounting period should be removed from the G&A expense pool.

Materiality. With respect to the questions about materiality, the Board has several times expressed its belief that the administration of Cost Accounting Standards should be reasonable and not seek to deal with insignificant amounts of cost. See, for example, the March 1973 "Statement of Operating Policies, Procedures and Objectives." The Board has considered the comments concerning the potential problems that could arise without a clearer statement of materiality related to the composition of the G&A expense pool. The Board believes in this instance a significance test will be particularly useful and the Standard has been appropriately modified (410.50(c)).

Accounting for Specific Items of Expense in the G&A Expense Pool. Commentators also expressed concern about the treatment of specific items of expense that are sometimes found in the G&A expense pool. In particular, commentators expressed concern over the treatment of selling and marketing costs, independent research and development (IR&D) costs and bidding and proposal (B&P) costs. Commentators questioned whether under the Standard these costs were G&A expenses to be included in the G&A expense pool.

The Board recognizes that at the present time selling costs (marketing or selling costs) may constitute a significant amount of cost and are accounted for in a variety of ways. Some account for selling costs in a separate cost pool while others include selling costs as part of the G&A expense pool.

Contractors who have included selling costs in a cost pool separate and apart from the G&A expense pool may continue that practice or may change and include selling costs in their G&A expense pool. Further contractors who will have to change the allocation base used for the G&A expense pool and who have in the past included selling costs as part of the G&A expense pool may account for selling costs by establishing a separate cost pool for the selling costs and using the allocation base they previously used for their G&A expense pool. Where selling costs are accounted for in a cost pool separate and apart from the G&A expense pool and are allocated using a different allocation base, they shall become part of the cost input base used to allocate the G&A expense pool. Also, the Board notes that the current ASPR provision related to the accounting for IR&D and B&P cost requires that generally the allocation of these costs shall be on the same basis as the contractor's allocation of his G&A expense pool, although these expenses are not termed G&A expenses. Under the provisions of this Standard, business units which have included IR&D and B&P costs in their G&A expense pool may continue to do so. Those business units which choose to use the optional transition method in 410.50(e) and in which the IR&D and B&P costs remain in the G&A expense pool will account for these costs as follows:

(a) During the transition period, those business units which were using a cost of sales or sales base will continue to use that base to allocate the G&A expense pool to final cost objectives which were in existence as of the date the business unit must first allocate its costs in accordance with the requirements of this Cost Accounting Standard.

(b) During the transition period and subsequent to that time, the G&A expense pool would be allocated to new contracts subject to the CAS clause using a cost input base as required by 410.50(d).

As a result of the current ASPR provision, a business unit which is required under this proposed Standard to change the allocation base used for its G&A expense pool could, because of the ASPR requirements, also be required to change the allocation base for IR&D and B&P. For those contractors who include IR&D and B&P in their G&A expense pool, this change in the business unit's method of accounting for IR&D and B&P costs, however, would be subject to the transition provision of the proposed Standard, and would only affect allocation of these costs to contracts awarded on or after the date on which a business unit must first allocate its costs in accordance with the requirements of this Standard.

Commentators expressed the view that since IR&D, B&P costs, and selling cost could become part of the allocation base for the G&A expense pool it might lead to the concept that these costs are final cost objectives themselves and should receive an individual allocation of G&A expense. As was stated in the Prefatory Comments to the September 9, 1975 publication, the Board is currently working on projects involving IR&D, B&P and selling costs. The Board at this time does not require changing the accounting for these costs. However, where these expenses are treated separately and apart from the G&A expense pool they shall become part of the allocation base used to allocate the G&A expense pool to final cost objectives and are not to be treated as individual cost objectives in and of themselves.

The illustrations concerning the accounting for costs which are removed from the G&A expense pool and the accounting for IR&D and B&P costs and selling costs have been clarified in response to comments received.

Expenses Transferred from the G&A Expense Pool. Commentators expressed the view that those items which will be taken out of the G&A expense pool and transferred to the benefiting segment for which they were incurred, are not really G&A expenses of the segment but are G&A type expenses. These expenses come out of the pool and are transferred in what may be described as a purification of the G&A expense pool before it is allocated. The Board agrees with this position, but does not believe an amendment of the Standard is necessary.

4.**-- Use of Memorandum Records**

Some commentators urged that the Standard specifically permit the use of memorandum records for the allocation of G&A expenses to final cost objectives. The Board notes that even in the absence of this Standard, many contractors now use memorandum records to perform the allocation of G&A expenses for purposes of Government contracts, because in their formal records they do not make an allocation of G&A expenses to contracts or they do so on a different basis. The Board sees no need to disturb the practice of using memorandum records for the allocation of G&A expenses to final cost objectives.

5.**-- Allocation of Home Office Expenses to Final Cost Objectives**

Commentators expressed concern about the handling of home office expenses which are received by a segment as residual expenses under CAS 403 or as a lump sum which is not designated as a particular type of expense. The Standard now provides explicitly that individual handling of various types of home office expenses would be required only where a separate allocation of expenses is received from a home office, and where the amount of the allocated expense is significant.

Other commentators suggested that in given circumstances a different allocation base than the allocation base used for the allocation of home office expense to the segment may be appropriate for the allocation of home office expense to final cost objectives of the segment. The Standard does not require that the same base be used for the allocation of home office expenses to final cost objectives of the segment as was used for the allocation of home office expenses to the segment. The Standard requires establishment of a beneficial or causal relationship between the cost objectives and the expense wherever separate and significant allocations of home office expenses are received by a segment. It may be appropriate to use a different allocation base for the allocation of home office expenses received by a segment than the allocation base used to allocate home office expenses to the segment.

A number of commentators state that allocations of home office expenses, either in total or part, are the type of expenses which should be accounted for as period expenses and should not be inventoried nor should these allocations be part of a cost input base for the allocation of the G&A expense pool as they are not part of the activity being managed. The Standard provides that certain allocations of home office expenses are always to be included in the G&A expense pool. Allocations of certain other types of home office expenses, where they are separately received and significant in amount, may or may not be included in the segment's G&A expense pool. The Standard provides that these costs shall be allocated to cost objectives of the segment based on the beneficial or causal relationship between the cost objectives and the expense. As such, where a beneficial or causal relationship between these expenses and cost objectives the segment can be established, these expenses shall be included in cost objectives other than the segment's G&A expense pool. Where a beneficial or causal relationship for the expenses is not identifiable with other cost objectives of the segment then the expense would be included in the G&A expense pool.

The total cost of a final cost objective is made up of a variety of cost and expenses incurred in different manners and at different times. The functions and services represented the allocation of home office expense is recognized, for contracting purposes, as part of the total cost of final cost objectives. As such, these costs are not unlike the other costs incurred in the effort to produce the final cost objectives. These costs shall become part of the appropriate cost input base selected to allocate the G&A expense pool. The illustrations have been revised to clarify that a segment must receive the home office expenses as a separate allocation if the requirements of 410.50(g)(2) are to be applicable.

6.**-- Allocation of G&A Expenses to Special Contracts**

Commentators suggested that the special allocation provision be stated in terms of class of contracts or types of situations. If the G&A expense pool meets the requirements of the Standard, the existence of a need for special allocation to a class of contracts or type of situation would indicate that the allocation base being used is not representative of the total activity of the business unit during a typical cost accounting period. The Standard is designed to provide consistent accounting treatment for all contracts, except for a particular contract or other final cost objective, which is an exception to a business unit's normal operation.

The cost input allocation base for G&A expense is a broad measure which is normally representative of the total activity of a business unit during a cost accounting period. Thus, for a given final cost objective to qualify for special treatment, the difference in its beneficial or causal relationship to G&A expense as compared with the relationship of other final cost objectives to G&A expenses should be one which is apparent and capable of being supported. The provision of the Standard calls for the exercise of judgment; nonetheless, the Board believes a materiality criterion based on a measure of significantly different benefits is proper for use in evaluating and establishing a separate and exceptional allocation to a given final cost objective.

7.**-- Miscellaneous**

Some commentators stated that the Standard should provide for the allocation of G&A expenses to intermediate cost objectives, such as service centers and other overhead pools. Their position was based on the concept that in various types of full-cost responsibility accounting systems, all costs are allocated to cost objectives for more accurate costing and control purposes. A few commentators stated that for certain management expenses within the G&A expense pool they are able to determine a discrete beneficial or causal relationship between these expenses and the cost objectives of the business unit. Therefore, these expenses are allocated on a separate allocation base to the cost objectives of the business unit.

Where a beneficial or causal relationship between certain management expenses and business unit cost objectives can be determined using an allocation base other than the base used for the G&A expense pool, then by definition, these management expenses are not G&A expenses and should be excluded from the G&A pool. Where a beneficial or causal relationship other than one based on a broad measure of total activity can be determined, generally the resulting allocation represents improved contract costing. However, for those expenses which are in the G&A expense pool, the Board's research indicates that the beneficial or causal relationship between these expenses and business unit activities of a cost accounting period is such that if they are allocated to intermediate cost objectives the allocation to final cost objectives could be significantly distorted.

Some commentators took the position that G&A expenses should not be allocated to stock or product inventory items. Other commentators suggested that the cost input of stock or product inventory items should be included in the G&A allocation base only in the cost accounting period when these items are used. The Board has taken the position that work on stock or product inventory 1 items represents part of the productive activity of the business unit for a cost accounting period, and therefore, these items should receive an allocation of G&A expenses.

The Board has recognized the administrative difficulties that can arise as a result of inventorying G&A expenses on these items for contract costing purposes and at the same time complying with requirements of generally accepted accounting principles for financial reporting. The Board has concluded that a practical solution to this circumstance is provided by the accounting treatments set forth in the Standard. A contractor can include G&A expense with the inventory cost of these items for contract costing purposes and provide his own procedure for complying with generally accepted accounting principles. Alternatively, contractors who do not include G&A expenses in the inventory cost of these items in order to conform with generally accepted accounting principles, are permitted to apply G&A expenses using the G&A rate of the period in which the items are issued.

In either situation, the cost of stock or product inventory items is to be included in the computation of the allocation base in the year produced. The Board believes this procedure will provide the appropriate determination of the G&A rate for each year, and the difference in the G&A rate applicable to final cost objectives by using the G&A rate of the year in which the items are issued rather than manufactured will not be significant.

The illustration dealing with the timing of inclusion of stock or product inventory cost input in the allocation base has been revised to make clear that stock or product inventory items cost input is to be included in the year in which the cost input is incurred.

Commentators suggested that a transition provision be provided for other types of changes, e.g., changing from a value-added cost input base to a total cost input base, or removing an item of expense from the G&A expense pool, required for compliance with the Standard. The Board recognizes that a variety of changes may occur as individual business units take action necessary to comply with the Standard. The Board believes that the equitable adjustment provision of the CAS contract clause provides the best means of handling the variety of changes which may take place.

Commentators suggested that some type of exemption threshold for this Standard should be adopted. It was suggested that the threshold could be based on either total sales to the Government by a business unit or corporate entity or Government business stated as a percentage of total business. The Board is currently studying the question of whether an exemption from its regulation could be appropriately based on the proportion of total business which a contractor does with the Government. Pending the results of that study, the Board does not believe that a percentage-of-sales exemption in individual Standards is appropriate.

Cost-Benefit. Section 719(g) 50 U.S.C.App. 2168(g), as amended provides “In promulgating such standards and major rules and regulations for the implementation of such standards, the Board shall take into account, and shall report to the Congress in the transmittal required by Section 719(h)(3) hereof, the probable costs of implementation, including inflationary effects, if any, compared to the probable benefits, including advantages and improvements in the pricing, administration and settlement of contracts.”

In a draft of the proposed Standard that was distributed for comment, the Board specifically requested commentators to provide data on the administrative costs of compliance with that proposal. In the second publication of the proposed Standard, the Board made the same request for data to indicate the administrative costs of compliance with Alternative X or Alternative Y. Of the 165 comments received only two comments on the draft proposal and one comment on the second publication provided quantitative data. Many comments received indicated that there would be some administrative costs incurred in complying with this Standard. As indicated above, a number of the potential administrative problems described in the comments have been reduced or eliminated by changes to the Standard being promulgated today. Moreover, the practices of many contractors already conform with all or some of the provisions of this Standard.

Commentators indicated that part of the increased administrative cost is attributed to the transition to a cost input allocation base for those business units currently using a cost of sales allocation base. Another part of the increased administrative cost for these same business units is attributed to the accounting for the G&A expense allocated to ending inventory. The Board recognizes that these administrative costs will arise in some cases.

Among the benefits which the Board believes will be derived from use of this Standard No. 410 are a more equitable treatment of all costs incurred during a period, in terms of the G&A expense pool allocation to final cost objectives; improved measurement of the cost of final cost objectives; a reduction in disputes through the establishment of criteria for evaluation and selection of the allocation base for the G&A expense pool; increase in the likelihood of achieving objectivity in the allocation of G&A expenses to final cost objectives; and an increase in comparability of cost data, among contractors in similar circumstances.

The Board concludes that the costs anticipated for administrative compliance with this Standard when reasonably managed in light of the purposes to be served are outweighed by the probable benefits expected to be derived from its use.

As required by section 719(g) 50 U.S.C.App. 2168(g), as amended, the Board has evaluated the potential inflationary effect of this Standard. The Board has concluded that any inflationary effect of this Standard will be insignificant.

Effective Date. The availability of the transition method to contractors who choose to use it requires especial care in complying with the effective date and application provisions of the Standard. The following comments are offered to illustrate those provisions. The comments assume that the contractor has a January 1 fiscal year; contractors with different fiscal years would of course apply the requirements of the Standard using different dates appropriate to their own fiscal year. For those contractors using a cost of sales base, having a fiscal year beginning on January 1, and electing to use the transition method provided in Appendix A, all contracts entered into prior to January 1, 1978, would be accounted for using the contractor's cost of sales base in accordance with the cost accounting practice previously disclosed or established. Contracts entered on or after January 1, 1978, should be accounted for using a cost input base in accordance with the requirement of 410.50(d). The transition period would begin January 1, 1978, and continue until all contracts entered into prior to January 1, 1978 are completed. This situation is illustrated in Appendix A, Illustration 1.

Under certain circumstances, a contractor who has been using a cost of sales base must be presumed, during the time between the effective date of this Standard and the date when it becomes applicable to him, to have elected to use the transition method provided in 410.50(e). These circumstances arise when

> (1) the contractor proposes to receive an award of a contract priced by use of a cost of sales base for the entire contract and
>
> (2) the period of performance specified or anticipated for the contract extends beyond the date when the Standard becomes applicable to the contractor. Contracting agencies should take appropriate action to advise the contractor that consistent with the concepts of Part 401, Cost Accounting Standard -- Consistency in Estimating, Accumulating and Reporting Costs, his decision to price the proposal entirely by use of a cost of sales base is deemed an election to operate under the transition method prescribed in 410.50(e) when this Standard becomes applicable to him.

Those contractors using a cost of sales base, having a January 1 fiscal year, and electing to proceed with a complete change-over to a cost input base on January 1, 1978, would have to be careful to comply with Standard 401 in making proposals for those contracts which will span part or all of the period October 1, 1976, through December 31, 1977, and cost accounting periods beginning January 1, 1978, and thereafter. The proposal should indicate that the cost of sales base will be followed until the date when the requirements of this Standard must be followed; at that later time, the practice required by this Standard, a cost input base, should be proposed to be used as the contractor's practice for the remaining life of the contract.

To illustrate, assume a contractor having a January 1 fiscal year currently allocates G&A expense using a cost of sales base. When the contractor makes a proposal for a contract which will be entered into after October 1, 1976, and prior to January 1, 1978, his proposal must recognize that his G&A expense pool will be allocated by using a cost of sales base from the date of the contract through December 31, 1977, and by using a cost input base thereafter.

The Board expects that this Standard will become effective on October 1, 1976.

There is also being published today an amendment to Part 400, Definitions, to incorporate in that part terms defined in

410.30(a) of this Cost Accounting Standard.

Preamble B
Preamble to Document Published 6-8-78

The document published on June 8, 1978 at 43 FR 24819, revised 410.70. This amendment was part of a publication which added 331.30(b)(3). Only the portion of the preamble which describes the revision to 410.70 is printed here. The remainder of the preamble appears as preamble K of the supplement to Part 331.

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In the *Federal Register* of February 16, 1977 (42 FR 9391), the Board proposed to amend section. 10, General Applicability, of standards 401 through 409 to conform these sections to the general applicability section as it appears in standard 410 et seq. No comments were received on this proposed amendment. The Board considers this change to be appropriate and is amending standards 401 through 409 as set forth below.

Preambles to Cost Accounting Standard 411, Accounting for Acquisition Costs of Material

Preamble A
Preamble to Original Publication, 5-5-75

The following is the preamble to the original publication of Part 411, 40 FR 19425, May 5, 1975.

The Standard on Accounting for Acquisition Costs of Material being published today is one of a series being promulgated by the Cost Accounting Standards Board (CASB) pursuant to section 719 of the Defense Production Act of 1950, as amended (Pub.L.91-379, 50 U.S.C.App. 2168) which provides for the development of Cost Accounting Standards to be used in connection with negotiated national defense contracts.

Preliminary work on the development of this Standard resulted from the absence of a requirement in agency regulations that the same costing method be used for similar categories of material within the same business unit and that the method be consistently applied. The Board undertook research with a view that a Cost Accounting Standard on this subject might improve cost assignment and cost measurement in accounting for acquisition costs of material.

Early research included an extensive review of available literature and a review of decisions of boards of contract appeals and courts.

A preliminary analysis of material accounting concepts was made and a number of issues were identified; comments on this analysis were obtained from interested persons. After evaluation of all of the issues, the Board developed and circulated preliminary research drafts of Standards which were widely distributed for informal comment and to ascertain the cost impact of adoption of the Standard as proposed.

Suggestions and comments were received from 70 respondents; these comments were considered in developing a revised Standard which was published in the *Federal Register* of November 26, 1974, with an invitation for interested parties to submit written views and comments to the Board. The Board supplemented that *Federal Register* publication by sending copies of the *Federal Register* material directly to organizations and individuals who had provided the Board with comments on the earlier proposal or had otherwise expressed an interest in the proposal.

Responses were received from 86 sources including individual companies, Government agencies, professional associations, industry association, public accounting firms, universities, and others. All of these comments have been considered by the Board and those addressing areas of particular significance are discussed below, together with explanations of the changes made in the Cost Accounting Standard being promulgated from the proposal published in the *Federal Register* on November 26, 1974.

The Board takes this opportunity to express its appreciation for the helpful suggestions and criticisms which have been received, and for the time devoted to assisting the Board in this endeavor by the many companies and individuals involved.

1. *Need for a standard.* Many comments were received questioning the need for a Standard in this area. Suggestions were received that because Disclosure Statements at present deal with this subject matter, the Board should accept them in place of a Standard. Other commentators contended that Standard 402, Consistency in Allocating Costs Incurred for the Same Purpose (4 CFR Part 402), dealt with any problems encompassed by this Standard. Some commentators argued that current practices concerning material costs used on Government contracts are well defined, of long duration, and are continually monitored by the Government. Others contended that inventory costing methods are covered by generally accepted accounting principles (GAAP) and, for this reason the Board should not issue a Standard on this subject.

With respect to the makeup of the draft Standard itself, some commentators said it was too broad, while others said it was too detailed and procedural. Some commentators stated that any Standard in this area should deal with direct materials only and should not contain any reference to indirect materials.

The Board has considered the arguments raised above as well as other facets of this particular subject matter. After studying this matter further, the Board has concluded that a Standard dealing specifically with accounting for the acquisition costs of material is needed to complement the Disclosure Statement and Cost Accounting Standard Contract Clause requirements, and to provide consistency in the application of material costing methods. Further, the Board believes that issuance of a Standard may be entirely appropriate even if the Standard does no more than establish as a Cost Accounting Standard the currently prevailing procurement regulations dealing with the allocation of costs to cost objectives. Accordingly, the Board is promulgating today a Standard, appropriately revised in light of the comments received, dealing with Accounting for Acquisition Costs of Material.

2. *Inventory costing methods.* The draft Standard published in the *Federal Register* on November 26, 1974, provided for the use of three inventory costing methods and asked commentators to identify any other methods they believed should be acceptable, for contract costing purposes, along with a justification and criteria for the use of such methods. Many commentators expressed the view that the last-in, first-out (LIFO) inventory costing method, under which the recent costs of material are allocated to cost objectives and the older costs are allocated to material remaining in inventory, should be permitted. Some commentators noted that LIFO should be allowed because it is acceptable to the Internal Revenue Service and the Securities and Exchange Commission, and because it is a recognized method for valuing inventory under generally accepted accounting principles and it is acceptable for other purposes. Other commentators expressed the view that the LIFO method results in a better matching of current costs with current revenues thereby reducing the “inventory profits” that develop during inflationary periods.

The purpose of this Standard is to provide for better allocation and measurement of material costs as they relate to specific contracts. The accounting practices used to achieve this purpose should be justified on the basis of their effectiveness for such allocation and measurement. They should not be justified solely on the basis that they are practices acceptable for tax and financial reporting purposes. Further, generally accepted accounting principles do not specify the details of cost allocations to particular contracts but are concerned with reporting the financial results of operations of the company as a whole.

The Board realizes LIFO is considered by some as a partial answer to accounting for the impact of inflation. The Board has noted however, that most of the companies that recommended that the LIFO method be permitted for contract costing purposes charge almost all of their material to contracts at the time the material is acquired or produced. The direct allocation of the costs of materials to contracts tends to counter the effects of inflation since the current cost of the material is charged against the contract. Moreover, few of these companies use LIFO for material that is issued to contracts from inventory.

The Board believes that accounting for the impact of inflation should be the subject of a separate Standard. The Cost Accounting Standards Board is currently conducting research into this subject. The Board did not include LIFO as a permitted inventory costing method in the draft Standard because contractors which currently follow

LIFO for Government contracts use it in a manner which does not permit systematic and rational identification of the cost of material issues to specific cost objectives. The Board believes such identification is essential in cost accounting for Government contracts. Accordingly, while the Board has included the LIFO inventory costing method as a permitted method in the Standard being promulgated today, it has also included a requirement that the costing method used be applied in a manner which results in systematic and rational costing of issues of material to specific cost objectives.

The costing of such issues to cost objectives must be reasonably current; it would not appear rational to hold in abeyance for months, pending a LIFO determination, the cost of materials issued to a Government contract.

3. *Direct charging of material.* The proposed Standard included a provision whereby the cost of a category of material could be allocated directly to a cost objective provided the cost objective is specifically identified on the purchase order at the time of purchase or on the work order at the time of production of material and provided there is no established material inventory account for that category of material. Some commentators felt that contractors should be permitted to allocate the cost of material directly to a contract without the identification requirement. A greater number of contractors supported the identification requirement provided by the Board. These commentators felt that if identification with the end use was feasible, direct allocation should be permitted.

Most commentators objected to the prohibition of direct allocation if a material inventory account existed. They complained that this requirement forced the contractors to stock material at their own expense. They said this requirement would discourage purchase of material in economical lots. Commentators also pointed out that this requirement would make off-site shipments uneconomical, and would adversely affect contractors' compliance with requirements in other Standards concerning their price proposals.

The Cost Accounting Standards Board favors the direct identification of costs where possible. The Board stated in its "Statement of Operating Policies, Procedures and Objectives" (March 1973):

As an ideal, each item of cost should be assigned to the cost objective which was intended to benefit from the resource represented by the cost or, alternatively, which caused the incurrence of the cost. To approach this goal, the Board believes in the desirability of direct identification of costs with final cost objectives to the extent practical. The Board recognizes the need for care in application of the concept of direct identification of costs with final cost objectives * * *

In furtherance of this objective, the Board has concluded that the specific identification of the end use of a category of material at the time of purchase or production should remain a requirement for the direct allocation of the cost of material. The Board is persuaded, however, that the existence of a material inventory account should not prohibit the direct allocation of the cost of material, and the Standard being promulgated has been revised to delete that prohibition. If contractors have previously established material inventory records for categories of material, however, the Standard does not require any change in this practice.

4. *Cost of material.* The draft Standard provided that material costs should be the acquisition cost of material adjusted to the extent practical by extra charges paid or discounts and credits received. Many commentators objected to this provision since they said that it is not in accordance with the practices currently followed by most companies. They argued that they charge many of the types of adjustment items referred to above to an indirect cost account and distribute those costs to all material on a base that they say is now acceptable to the Government. They also allege that there would be considerable work involved in identifying these kinds of additional charges with the individual purchases of material and to then spread the charges against the categories of material being purchased.

The Board intended this requirement to define broadly the net acquisition cost of material. This provision has been retained in the Standard being promulgated. A section has been added to the Standard stating that where it is not practical for a contractor to handle charges and credits as set out above, the contractor may provide for the consistent inclusion of such charges or credits in an appropriate indirect cost pool.

5. *Definitions.* Many comments were received on several of the definitions included in the draft Standard. Most commentators raised questions about the definitions of "Category of Material" and "Material Inventory Account."

Some commentators concluded that "Category of Material" would include items such as lubricants, paper, ink, towels, and items of that type. The Board intended that material such as this could be handled as provided under 411.40(c) of the promulgated Standard which permits the cost of material to be allocated, under certain conditions, to an indirect cost pool for distribution to cost objectives.

Other commentators felt that the requirement that a category of material be comprised of identical or interchangeable units would be unduly restrictive. Their contention was that the different, individual items of material would have to be considered as separate categories of material. The Board intended its definition to be read in this way. It was not meant that all sheet steel, for example, should be considered as a single category of material. Most contractors would maintain separate inventory records of different sizes and thicknesses of sheet steel. Each of these would be a category of material.

Many of the comments concerning the definition of "Material Inventory Account" indicated that commentators assumed the Board was talking only about general ledger or subsidiary ledger accounts. Such is not the case. The Board was referring to any record used for accumulating the cost and quantity of material for subsequent issue to one or more cost objectives. The records the Board had in mind could include card files, computer data, bin tags, or other forms of detailed information used in the company's system of accounting for receipt in and issue of material recorded as an asset.

Many commentators objected to the inclusion of the word "quantity" and the word "cost" in the definition of material inventory account. Some said they maintained records of either cost or quantity only. It was not the Board's intention that each record must show both cost and quantity. The word "quantity" has been deleted from the definition. The records referred to are those used to accumulate the cost of materials for allocation to specific cost objectives.

The Board has concluded that the definition of "Category of Material" as presented in the draft Standard published on November 26, 1974, should be retained. The reference to "Material Inventory Account" has been deleted and the term "Material Inventory Record" substituted. Several words in this definition have been changed to make it more clear that the Board is referring to any records maintained in support of general ledger or subsidiary ledger financial accounts.

6. *Need for written policies.* Many commentators said that a requirement for written policies should be deleted from this Standard. They contended that such a requirement was not in accordance with their understanding of what Cost Accounting Standards should cover. They felt the Board was becoming too deeply involved in procedural details with such a requirement.

Contractors who have submitted Disclosure Statements felt that such submission should exempt them from a requirement for written policies. They contended that in responding to the Disclosure Statement, they were, in effect, setting forth their written policies and practices. During the Board's development of the Disclosure Statement, many contractors suggested that a Disclosure Statement such as the Board had designed was not justified because they said they had accounting manuals and similar written documents which set forth their accounting practices. They contended further that these manuals and similar written documents were available to Government auditors and provided sufficient information concerning the contractor's accounting practices. Although these manuals could not be used to fulfill the disclosure requirement, the Board recognizes that these are the kinds of documents that should contain written policies that are needed to permit effective implementation of this Standard. The Board also notes that many companies which are subject to Cost Accounting Standards are not required to file Disclosure Statements.

Some commentators questioned whether there would be a need for written policies for each category of material. Certainly the Board does not intend that this be the case. It is expected that contractors will have written policies establishing criteria which would apply to all of their material transactions.

Other commentators concluded that the written policies were listed as a requirement by the Board solely for the Government's use in determining compliance with the Standard. The Board feels that written policies and practices are beneficial as evidenced by the many companies which have them.

7. *Applicability of standard to indirect material.* The draft Standard provided a means by which a category of material used solely in performing indirect functions or which is not a significant element of production costs could be handled through an indirect cost pool rather than accumulated in a material inventory record. There was a further requirement that when quantities of such material were not consumed in a cost accounting period and were estimated to be significant in total costs, the cost of such material was to be established as an asset at the end of the period.

Many commentators stated that the Standard should not deal with indirect materials, while a few questioned the use of an indirect cost pool for allocating the cost of such material. Other commentators stated that many contractors generally do not maintain inventory records of such material and that the provision set forth in the first sentence of the preceding paragraph was necessary, otherwise the Standard might present major problems for contractors. Most of those commenting on this point recommended the retention of this provision.

Many commentators disagreed with the requirement to establish remaining material of this type as an asset at the end of the period. Some commentators felt that this requirement contradicted the first part of the provision. They argued that if the material was not a significant element of production cost and thereby was permitted to be allocated to an indirect cost pool, it did not seem logical to require that any amounts of such material should be established as an asset at the end of the period. They stated that if this situation occurred, then presumably the material should not have been charged to cost objectives through an indirect cost pool.

These commentators apparently misinterpreted the Board’s intention. The draft Standard referred to the value of unconsumed material to be set up as an asset, not the amount charged to an indirect cost pool during the cost accounting period. The provision deals with significant amounts of unconsumed material of this type remaining at the end of the period.

Another commentator stated that the expensing of indirect supplies has long been a generally accepted practice and, if consistently applied, would not result in inequities in contract costing as long as unconsumed amounts do not fluctuate significantly from year to year. Other commentators were concerned that the use of the word “significant” would generate endless disputes with Government auditors since such a determination is subjective and no definition of that word was included in the Standard.

After considering all the comments the Board has received on this point, it has decided to retain the provision allowing the use of an indirect cost pool for allocation of the cost of material of the type described in this provision of the Standard. The Board is also persuaded that when quantities of such indirect material are not consumed in a cost accounting period and the excess of the ending inventory over the beginning inventory is estimated to be significant in relation to the total cost included in the indirect cost pool, the cost of such unconsumed material is to be established as an asset at the end of the period. The setting up of this material as an asset is to be accomplished by reducing the indirect cost pool by a corresponding amount.

On numerous occasions the Board has stated that it agrees that the administration of its rules, regulations, and Standards should be reasonable and not seek to deal with insignificant amounts of cost. Because of this, the Board does not believe it essential to define the term “significant” as used in this provision of the Standard. Generally accepted accounting principles, as stated in the American Institute of Certified Public Accountant’s Accounting Research Bulletin No. 43, recognize that the term “inventory” includes goods to be consumed directly or indirectly in operations, such as supplies.

The aforementioned requirement has therefore been retained in the Standard being promulgated.

8. *Transfers of material.* The draft Standard contained a requirement that a transfer of the cost of material from one cost objective to another was to be made at the same cost that was allocated to the initial cost objective or at the current market value. Many commentators objected to this provision on the grounds that it would be extremely difficult to identify the cost that was allocated to the initial cost objective. They contended that this requirement would also generate disagreements with Government auditors as to whether or not initial cost information was, in fact, available. Also, some commentators felt that determination of current market value would be a difficult and time consuming

chore.

While not agreeing or disagreeing with the commentators' statements, the Board has concluded that the transfer of material is of sufficient significance to warrant consideration as a subject for a separate Standard. The Board has initiated a research project to consider what factors affect the cost of transfers between cost objectives and between organizations. For this reason, the provision concerning cost of transfers of material between cost objectives has been deleted from this Standard.

9. *Periodic vs. perpetual inventory accounting.* The published draft Standard contained a provision permitting either periodic or perpetual inventory accounting procedures. This was coupled with a requirement that the period for periodic inventory accounting should not be longer than one quarter of a year. It was further stated that these provisions were not intended to establish a requirement regarding the taking of physical inventories.

Many commentators stated that this provision appeared to contain contradictory statements since the periodic inventory accounting method normally requires a physical inventory when the inventory value is established. They further said that as they understand that provision, they would be required to take physical inventories quarterly, which they felt was unnecessarily frequent.

The Board was referring to the period involved for the establishment of costs of material issues, not to the taking of physical inventories. It is the Board's intention that costing of material issues should be on a current basis. To achieve this goal, the Board has inserted a requirement in the Standard that the inventory costing method used is to be applied in a manner which results in systematic and rational costing of issues of material to specific cost objectives.

10. *Costs and benefits.* Few comments were received on the subject of implementation costs of the Standard. This Standard has, for most contractors, almost no cost. It does require written policies; most contractors already have such policies. A few contractors, however, may have to establish or modify inventory policies; for these contractors there may be minimal costs.

The Board believes that this Standard will result in improved understanding of the requirements involved in accounting for acquisition costs of material during the negotiation and audit of contracts and these potential benefits will outweigh any costs of implementation.

11. *Other comments.* The published draft Standard contained a provision excepting small quantities of material used for purposes such as prototype and developmental work from the definition of an established material inventory account. While only a few commentators offered comments on this provision, in view of the revisions being made to the Standard as set out above, this provision has been deleted from the Standard.

A number of commentators raised questions concerning the potential conflict between requirements of this Standard and those set out in Standard 407, Use of Standard Costs for Direct Material and Direct Labor (4 CFR Part 407). The Board recognizes the nature of the potential conflict described by the commentators, but feel that an inventory costing method using standard costs in accordance with the requirements of Standard 407 would meet the inventory costing requirements of this Standard.

Section 411.10, General Applicability, has been shortened and simplified from the material under this section appearing in earlier promulgated Cost Accounting Standards. The earlier material was a restatement of the statutory requirements of Pub.L.91-379. The Board believed it was helpful to repeat this material to assist users of the Standards. However, the Board has from time to time provided for certain exemptions from the requirements to follow Cost Accounting Standards, and these exemptions were not recognized in the "applicability" sections of earlier Standards. The Board believes that the shortened material in 411.10, referring users to the Board's detailed regulations, will provide users with helpful information on general applicability.

There is also being published today an amendment to Part 400, Definitions, to incorporate in that part terms defined in 411.30(a) of this Cost Accounting Standard.

Preambles to Cost Accounting Standard 412, Composition and Measurement of Pension Cost

Preamble A
Original Publication, 9-24-75

The following is the preamble to the original publication of Part 412, 40 FR 43873, Sept. 24, 1975.

The Cost Accounting Standard on Composition and Measurement of Pension Cost is one of a series being promulgated by the Cost Accounting Standards Board pursuant to section 715 of the Defense Production Act of 1950, as amended, Pub.L.91-379, 50 U.S.C.App. 2168, which provides for the development of Cost Accounting Standards to be used in connection with negotiated national defense contracts. This Standard establishes the components of pension cost, the bases for measuring such cost, and the criteria for assigning pension costs to cost accounting periods.

As part of the Board's early research relating to the subject of pension costs, it developed an Issues Paper in August 1973, and a preliminary draft Standard in September 1974. Both the Issues Paper and preliminary Standard were sent to a large cross-section of companies, Government agencies, industry and professional associations, actuaries, and other interested individuals. The Board received responses to these research papers which were useful in identifying the key issues involved in pension cost accounting and in developing a proposed Standard which was published in the *Federal Register* of May 5, 1975, with an invitation to interested parties to submit written views and comments to the Board. The Board also supplemented the invitation in the *Federal Register* by sending copies of the proposed Standard to several hundred organizations and individuals who had provided the Board with comments on the preliminary proposal or who had otherwise expressed interest in the subject of the Standard.

The Board received 80 sets of written comments from companies, Government agencies, professional associations, industry associations, public accounting firms, universities, actuaries and others in response to the *Federal Register* proposal. All of these comments have been carefully considered by the Board. The Board's views on each of the major issues discussed by commentators are outlined below, together with explanations of the changes made in the Cost Accounting Standard being promulgated.

The Board wishes to take this opportunity to express its appreciation for the helpful suggestions and constructive criticisms it has received, and for the time devoted to assisting the Board in this endeavor by the many organizations and individuals involved.

(1)**Relationship to the Employee Retirement Income Security Act of 1974 and to Generally Accepted Accounting Principles**

The Board received a variety of comments relative to the relationship between the proposed Standard, the Employee Retirement Income Security Act of 1974 (ERISA), and generally accepted accounting principles set forth in "Accounting for the Cost of Pension Plans," Opinion No. 8 by the Accounting Principles Board (APB-8). Some stated that, with the enactment of ERISA, Congress has expressed its will relative to pensions and a Cost Accounting Standard on pension costs which is different than ERISA is unnecessary. Others stated that APB-8 is a viable and proven document which provides sufficient guidance for both financial accounting and cost accounting purposes. Others stated that the combination of ERISA and APB-8 provides all the guidance needed for cost accounting purposes. Still others stated that a Standard should be deferred until the Federal regulations required by ERISA have been promulgated, and/or the Financial Accounting Standards Board (FASB) completes its reevaluation of APB-8.

The purpose of the Board in promulgating this Standard is to establish the accounting bases for measuring the proper amount of pension cost to be assigned to cost accounting periods for subsequent allocation to negotiated Government contracts.

ERISA establishes, among other things, minimum funding standards for pension plans and provisions affecting deductibility of pension costs for tax purposes. Although there is some commonality between the funding provisions of

ERISA and the provisions of the Standard, ERISA does not provide for the measurement of pension costs for assignment among cost accounting periods or for the subsequent allocation of such costs to contracts. Accordingly, the Standard contains requirements, not contained in ERISA, to accomplish these purposes. Nevertheless, on the basis of its research, the Board is confident that the Standard being promulgated is compatible with the requirements of ERISA, i.e., compliance with the provisions of the Standard does not violate the provisions of ERISA, although certain provisions of the Standard are more restrictive than is permitted by ERISA.

APB-8 provides criteria for accounting for the cost of pension plans for financial accounting purposes. The Board believes that certain of these criteria are not appropriate for Government contract costing purposes. For example, a fundamental concept of APB-8 is that the annual pension cost to be charged to expense for financial accounting purposes is not necessarily determined by the funding of a pension-plan. The Board believes that a requirement of law for annual minimum funding of pension costs on an irrevocable basis, is strong evidence that an obligation for at least such period.

The Board is aware of the FASB’s projects to establish financial accounting and reporting Standards for employee benefit plans and to reevaluate APB-8, as well as the need for the cognizant Government agencies to develop regulations relative to ERISA. It is our understanding that the FASB reevaluation of APB-8 is not likely to result in a Standard that would be applicable before the end of calendar year 1976. The Board believes however, that the issuance of a Cost Accounting Standard is needed promptly for contract costing purposes.

For example, there does not now exist any authoritative guidance which sets forth the components of pension cost that are properly includable and excludable for contract costing purposes. In addition, there are no existing criteria to resolve how the components of pension cost, once determined, shall be measured and assigned to cost accounting periods. The need for such measurement and assignment criteria for contracts is particularly critical because of the long-range projections used in computing pension cost and because the many techniques available for measuring and assigning such cost have significant impact thereon. The significant amounts involved in annual pension cost calculations, the changes in the mix of contractors’ Government and commercial business, and the settlement of individual contracts long before actual pension costs can be determined create a special need to provide criteria relative to the assignment of pension costs among cost accounting periods and the allocation of such costs to the cost objectives of the periods.

In developing the accompanying Cost Accounting Standard, the Board has attempted to stay within the general constraints of APB-8 and the funding provisions of ERISA. The Board recognizes that in the FASB’s reconsideration of APB-8, the FASB could make significant changes in the manner in which pension costs are to be treated for financial accounting purposes and that the FASB’s project on financial accounting and reporting for employee benefit plans may influence the conclusions reached in the reevaluation of APB-8. However, any such changes would be directed to external financial reporting and would not necessarily impact contract costing. The Board is also aware that Federal regulations which may be issued could conflict with a provision of this Standard. The Board maintains constant liaison with the FASB with regard to the two Boards’ respective responsibilities for developing Standards. It also maintains liaison with the legislative and regulatory bodies responsible for developing and administering ERISA. The Board will review whatever pronouncements these bodies may issue and will make whatever revisions to the Standard it deems appropriate for contract costing purposes.

(2)**Need for Two Standards Relative to Pension Cost**

Several commentators suggested that this Standard should deal not only with the composition and measurement of pension cost, but also with actuarial gains and losses [1] and the allocation of pension costs. The Board believes that the development of a separate Standard covering the latter two areas is advisable. First, the development of a single Standard would result in an extremely large and complex Standard that could create many problems in implementation and administration. For example, the Issues Paper developed by the Board set forth a total of 50 distinct accounting issues requiring resolution; the Standard being promulgated covers only 24 of these issues. In addition, the Board believes that the subjects covered by the two Standards are separable; a Standard can be issued relative to the composition and measurement of pension cost without creating a concurrent need for a Standard relative to the adjustment and allocation of such costs. Moreover, in computing actuarial gains and losses, it is necessary to determine how fund assets should be valued. APB-8 does not cover this aspect of pension cost accounting. In its project on accounting for pension funds, the FASB is endeavoring to specify the manner in which assets should be valued. The Board intends, as part of its continuing liaison with the FASB on this matter, to exchange research so that any possible differences in concept or approach could be minimized or eliminated entirely.

> *Note 1: "The effect on pension cost resulting from differences between actuarial assumptions and actual experience."*

(3)**Treatment of Actuarial Gains and Losses**

The *Federal Register* proposal noted that an adjustment for actuarial gains or losses is a component of pension cost. Several commentators expressed concern over the Board's intent. Some commentators interpreted the proposed Standard as requiring that actuarial gains and losses be spread over a number of years. Other commentators believed that the proposed Standard required the immediate recognition of actuarial gains and losses.

The Board emphasizes that the Standard does not delineate how actuarial gains and losses shall be accounted for at this time. The Standard being promulgated neither requires nor prohibits immediate recognition of gains and losses or the spreading of such gains and losses to future years. Therefore, actuarial gains and losses should be accounted for in accordance with pertinent laws and regulations, and should be consistently applied, Section 412.50(a)(5) has been amended to clarify this concept.

(4)**Actuarial Cost Methods (See Note 2)**

> *Note 2: "A technique which uses actuarial assumptions to measure the present value of future pension benefits and pension fund administrative expenses, and which assigns the cost of such benefits and expenses to cost accounting periods."*

Many commentators expressed their concern over the section of the *Federal Register* proposal which limited acceptable actuarial cost methods to the accrued benefit cost method [3] or to a projected benefit cost method [4] which separately identifies unfunded actuarial liabilities [5] and actuarial gains and to losses. This section, in effect, ruled out be the use of an aggregate [6] cost method for measuring pension costs for negotiated Government contracts. Most of these commentators noted that ERISA and APB-8 permit these methods to be used.

> *Note 3: "An actuarial cost method under which units of benefit are assigned to each cost accounting period and are valued as they accrue -- that is, based on the services performed by each employee in the period involved. The measure of normal cost under this method for each cost accounting period is the present value of the units of benefit deemed to be credited to the employees for service in that period. The measure of the actuarial liability at a plan's inception date is the present value of the units of benefit credited to employees for service prior to that date. (This method is also known as the Unit Credit cost method.)"*

> *Note 4: "Any of the several actuarial cost methods which distribute the estimated total cost of all of the employees' prospective benefits over a period of years, usually their working careers."*

> *Note 5: "Pension cost attributable, under the actuarial cost method in use, to years prior to the date of a particular actuarial valuation. As of the date, the actuarial liability represents the excess of the present value of the future benefits and administrative expenses over the present value of future contributions for the normal cost for all plan participants and beneficiaries. The excess of the actuarial liability over the value of the assets of a pension plan is the Unfunded Actuarial Liability."*

> *Note 6: "As used herein, an aggregate cost method is any actuarial cost method which spreads the entire cost of future pension benefits over the average future service lives of the current work force and which does not develop actuarial gains or losses.*

The Board's primary reason for prohibiting the use of an aggregate cost method in the proposed Standard was because such a method does not disclose actuarial gains and losses. Any method that does not disclose actuarial gains and losses impairs the ability to determine whether actuarial assumptions [7] are reasonable. Actuarial assumptions are significant underlying factors for determining the amount of pension costs to be assigned among cost accounting periods. It is only when such assumptions are visible that a determination can be made that they are reasonable. The most appropriate means for determining reasonableness is to compare assumed events with actual events.

> *Note 7: "A prediction of future conditions affecting pension cost; for example, mortality rate, employee turnover, compensation levels, pension fund earnings, changes in values of pension fund assets."*

Also, because most aggregate cost methods do not develop unfunded actuarial liabilities, the Government cannot ascertain the funding status a plan, i.e., whether it is excessively funded at any point in time. Consequently, the Government could be making larger reimbursements than is required to defray its fair share of pension costs incurred by contractors. Many of the comments received acknowledge that most aggregate cost methods do not disclose overfunded situations.

Nevertheless, the Board is impressed by certain of the views of commentators who advocate the use of an aggregate methods. The Board recognizes that aggregate methods are widely used and that they generally spread pension costs evenly and within the periods established in the Standard for amortizing unfunded actuarial liabilities. The Board also notes that commentators stated that a required change in actuarial cost methods may result in substantial actuarial fees and, in some cases, could result in contractors violating current labor commitments.

The Board's solution to this problem was provided generally in several of the comments received. First, several commentators who recognized that aggregate cost method does not disclose the funding status of a plan, suggested that contractors using such cost method develop an alternative computation to determine such status. They pointed out that such a computation is required under the full funding limitation of ERISA and is often required by the IRS when it believes a plan may be overfunded.

Other commentators suggested that contractors who use an aggregate cost method provide supplemental information identifying actuarial gains and losses that have occurred and the extent to which such gains and losses have been amortized through subsequent pension contributions or offset by gains and losses in subsequent accounting periods. These commentators informed us that the incremental costs of providing such additional information would be relatively minor.

Accordingly, the Board has added a section, (412.50(b)(2)) which permits a contractor to use any projected benefit cost method if the contractor

> (1) makes an alternative computation (under a projected benefit cost method which separately discloses unfunded actuarial liabilities and actuarial gains and losses) to disclose the funding status of the plan and reduce pension cost as indicated by such computation,
>
> (2) provides supplemental information relative to actuarial gains and losses and gains or losses resulting from changed actuarial assumptions, and
>
> (3) uses that method in developing costs for financial accounting purposes.

The third requirement was added because the Board has tried unsuccessfully to ascertain criteria for determining the circumstances under which an aggregate cost method is a preferable method for assigning costs to cost accounting periods for Government contracting purposes.

Finally, to assure that the aggregate cost method used spreads pension costs within the time frames set forth in this Standard for other projected benefit cost methods, 412.50(b)(2) requires that such aggregate cost methods spread the cost of future pension benefits over the average remaining working lives of the work force.

(5)**Actuarial Assumptions**

A large number of commentators were concerned with the manner in which the *Federal Register* proposal dealt with actuarial assumptions. They were particularly concerned with that provision of the proposed Standard which stated that when an actuarial assumption differs significantly from historical experience, the contractor shall provide evidence supporting its conclusion that such experience is no longer appropriate. Most commentators who objected to this provision in the Standard interpreted it as requiring separate gain and loss analyses for each assumption each time an actuarial valuation is performed. They cited the large cost of performing such analyses and noted that ERISA merely requires that actuarial assumptions be reasonable "in the aggregate."

Although the Board believes that the basis and rationale for each assumption should be made visible by contractors, it believes that the test of reasonableness of such assumptions should be applied to the end result. It is not the intent of the Board to require a separate gain or loss analysis for each assumption each time an actuarial valuation is made. Rather, the intent is that contractors not use an undocumented composite factor to a represent all assumptions used in measuring pension costs, as this practice would inhibit any evaluation of the reasonableness of individual assumptions as applied to future periods. Such evaluations may be necessary when assumptions, taken in the aggregate, are found to be unreasonable, as discussed below.

Once individual actuarial assumptions have been set forth by contractors, the Board believes that the validity of these assumptions can be evaluated by the overall results obtained. Therefore, the Standard provides that the validity of the assumptions used may be evaluated in the aggregate. However, if an actuarial valuation discloses that the assumptions were not reasonable in the aggregate, the Standard requires that the contractor shall identify the major causes for the resultant actuarial gains and losses and set forth the bases and rationale used for either retaining or revising each such assumption.

In order to recognize the long-term nature of pension plans, the Standard provides in 412.50(b)(5) that actuarial assumptions should reflect long-term trends, rather than short-term fluctuations. Also, the Standard does not specify how often determinations of actuarial gains and losses should be made. ERISA provisions require that such determinations be made not less frequently than once every three years except that more frequent determinations may be prescribed by regulation in particular cases, i.e., for plans which have sustained substantial gains or losses for several periods in succession. The Board believes that the ERISA requirements with respect to the frequency of determinations for gains and losses is equally appropriate for compliance with the provisions of the Standard at this time.

In addition to the foregoing, several commentators stated that the Standard should provide that the judgment of enrolled actuaries, as set forth in ERISA, should be determinate with respect to assumptions as well as other actuarial determinations. The Board recognizes the importance of the functions performed by enrolled actuaries with respect to actuarial determinations. However, contract terms are not imposed on actuaries; rather, it is the contractors who are parties to contracts with the Government and must bear the responsibility for compliance with the terms thereof.

(6)**Calculations of Normal Cost (See Note 8)**

> *Note 8: "The annual cost attributable, under the actuarial cost method in use, to years subsequent to a particular valuation date."*

The *Federal Register* proposal provided that the calculations of normal cost should be the sum of the calculations for the individual employees in the plan, except that homogeneous groupings and averages could be used if the results substantially agree with the results based on individual employee calculations. A number of commentators objected to this provision. They said that it would appear to require that two calculations be made in order to show that the use of groupings and averages gives results that agree with the results based on individual employee calculations. Some commentators stated that this requirement is unrealistic because actuaries frequently use aggregate calculations and that such aggregations can be tested against individual company or industry-wide experience. Other commentators stated that this provision would result in a single calculation for determining the assumed entry age of planned participants.

The comments received indicate that there are divergent opinions as to how normal costs shall be calculated under projected benefit cost methods. Nevertheless, the Board concludes that the methods commonly used would not materially affect the results of normal cost calculations. Accordingly, the requirement to compute normal costs on an individual basis for projected benefit cost methods has been deleted from the Standard.

The proposed Standard provided also that the calculation of normal cost shall be based on a percentage of payroll. Many commentators stated that this requirement does not recognize the fact that many pension benefits are not related to salaries. In order to accommodate these views, the Board has revised the Standard (412.50(b)(3)) to provide that the calculation of normal cost shall be based on a percentage of payroll for plans where the pension benefit is a function of salaries and wages and be based on employee service for plans where the pension benefit is not related to salaries and wages.

(7)**Pay-As-You-Go Pension Methods (See Note 9)**

> *Note 9: "A method of recognizing pension cost only when benefits are paid to retired employees or their beneficiaries."*

Several commentators apparently assumed that the *Federal Register* proposal prohibited the recognition of pension costs of plans that provide benefits on a pay-as-you-go basis. One commentator stated that the Standard prohibited the recognition of the costs of pay-as you-go plans which are qualified for Federal income tax purposes.

The Board's view, as expressed in the *Federal Register* proposal, is no to prohibit recognizing the cost of pension benefits provided on a pay-as-you-go basis. Rather, the Board's intent is to specify how the cost of such benefits shall be measured and assigned among cost accounting periods. Moreover, the accounting treatment to be afforded to the costs of pay-as-you-go plans is not dependent on the Federal income tax status of the plan.

Accordingly, the Board has revised the provisions of the Standard relative to pay-as-you-go methods (412.50(b) (4)) and has added an illustration (412.60(b)(2)) to clarify its intent.

(8)**Unallowable Pension Costs**

The *Federal Register* proposal provided that the pension costs applicable to prior years that were disallowed in accordance with then-existing Government contractual provisions should be separately identified and eliminated from any unfunded actuarial liability being amortized pursuant to the provisions of the Standard. Several commentators stated that this provision is not equitable because ERISA requires that such amounts be funded.

The Board recognizes that all elements comprising an unfunded actuarial liability, including unallowable costs included therein, are required to be amortized pursuant to the funding provisions of ERISA. However, ERISA does not deal with contract costing and therefore does not deal with unallowable contract costs. The Board believes that for contract costing purposes, pension costs which were assignable to prior periods and which were specifically determined to be unallowable under then-existing contractual provisions should not be assignable to periods subsequent to the effective date of this Standard. It should be noted that the treatment of amounts funded in excess of the pension cost for a cost accounting period is separately covered in 412.50(c)(1).

(9)**Amortization of Unfunded Actuarial Liabilities**

The *Federal Register* proposal included a provision requiring contractors to establish and consistently follow a policy for selecting specific amortization periods for any unfunded actuarial liabilities. The proposed Standard stated that such policy should give consideration to the size and nature of unfunded actuarial liabilities. Several commentators stated that they did not believe that the size and nature of such liabilities should govern the choice of amortization periods. The Board's intent was to permit contractors to establish different amortization periods for different types and sizes of unfunded actuarial liabilities. The Board still believes that contractors should be permitted to establish such different amortization periods. Accordingly, the Standard has been revised (412.50(a)(3)) to clarify that such determinations are permissive rather than mandatory.

(10)**Interest Resulting from Delayed Funding of Pension Plans**

The *Federal Register* proposal provided that if any portion of pension cost computed for a cost accounting period is not funded by the time established by the funding provisions of the plan, an interest equivalent on the amount not funded shall not be a component of pension cost of any other cost accounting period. Several commentators stated that this provision is inequitable because, in order for a pension plan to be viable, an amount equivalent to interest should be added to pension costs to compensate the fund for interest that would have been earned if the cost had been funded in a timely manner. Some commentators added that APB-8 requires that interest equivalents be added to pension accruals under such circumstances. Still others understood the proposed Standard to say that such interest equivalent is not a cost; they therefore disagreed with the proposed Standard.

The Board agrees that an interest equivalent should be recognized in order to determine whether the plan is properly funded. However, the Board believes that interest cost resulting from the delayed funding of a pension plan is a consequence of an investment decision and is, therefore, an investment cost rather than a component of pension cost. The interest was caused by a decision of management to use its funds for other purposes; in effect, management borrowed from the pension trust fund.

Several commentators stated that they compute pension cost at the beginning of a cost accounting period and add interest at the valuation rate to the normal cost to the date of funding. They questioned whether the Standard would prohibit this practice. The Standard being promulgated does not prohibit this practice: Provided, That funding is made by the end of the cost accounting period. Accordingly, the Board has amended 412.50(a)(7) to state that if any portion of the cost computed for a cost accounting period is not funded in that period an amount equivalent to interest computed on that portion beyond the end of that period shall not be a component of pension cost of the current or any future cost accounting period.

(11)**Assignment of Pension Cost**

Certain commentators expressed their disagreement with the sections of the *Federal Register* proposal dealing with the assignment of pension costs among cost accounting periods. The concept set forth in the proposal related in the assignment of costs to the validity of the liability for such costs. Commentators referred to the concept set forth in APB-8 that the accrual of pension expenses and the funding of pensions are not necessarily related. They stated that cost should be assigned to cost accounting periods irrespective of whether or when funded.

The Board believes that assigning pension costs to cost accounting periods on a cash basis is inappropriate from an accounting viewpoint and could lead to the improper assignment of pension costs among periods. The Board believes also that the concept which states that funding is unrelated to pension accruals is not appropriate for contract costing because, under such a concept, pension costs could be assigned to cost accounting periods and never be funded; yet such costs would be reimbursed by the Government.

The underlying concept of the Standard is that when a valid liability exists, the corresponding costs may he accrued irrespective of when the liability is liquidated. If the liability (to the pension fund or, for pay-as-you-go plans, to retirees) is not valid, it cannot be accrued; in order for it to be allocated to cost objectives of the current period, it must be liquidated (funded) in that period or within a reasonable period of time thereafter. In order to clarify its intent wit regard to the allocation of pension costs to cost objectives of individual cost accounting periods, the Board has revised the wording of 412.40(c) of the Standard.

In the *Federal Register* proposal, the Board noted that the requirement to fund a pension cost pursuant to ERISA made the liability valid and therefore made the cost assignable to the current period. Several commentators stated that ERISA permits such costs to be waived and funded over a 15-year period. They reasoned that under such circumstances it is no longer appropriate to assign such pension cost in the year for which such costs were computed. The Board believes that if the financial, position of a contractor is such that it requests and obtains such a waiver there is doubt as to validity of the liability and therefore of the cost incurred. Accordingly, it has amended the Standard to provide, in 412.50(c)(3), that if a contractor receives such a waiver the Pension costs shall be assigned to the cost accounting periods in which the funding of such cost takes place.

(12)**Insured Plans**

Several commentators stated that the section of the *Federal Register* proposal dealing with insured plans was confusing. They stated that the definition of a “separate insurance account” set forth in the proposed Standard conflicted with this section. Commentators stated that this section would seem to eliminate from the major requirements of this Standard various forms of insured plans such as deposit administration and immediate participation guarantee contracts.

The Board’s intent with regard to insured plans is to treat defined benefit plans[10] funded exclusively by the purchase of individual or group permanent insurance contracts as defined-contribution plan[11].

> *Note 10: ”A pension plan in which the benefits to be paid or the basis for determining such benefits are established in advance and the contributions are intended to provide the stated benefits.”*
>
> *Note 11: ”A pension plan in which the contributions to be made are established in advance and the benefits are determined thereby.*

The Board’s view relative to such plans is consistent with ERISA whose minimum funding requirements are not applicable to these plans. All other insured pension plans are subject to the provisions of this Standard. The Board has revised 412.50(a)(8) accordingly and has eliminated the definition of separate insurance account.

(13)**Definitions**

The Board has received a significant number of comments relative to the definitions used in the Standard. Some commentators stated that the Board should use the definitions contained in ERISA. Others stated that the Board should use the APB-8 definitions. Still others recommended that the Board should establish a single glossary of actuarial terms.

The Board recognizes that a major problem in the field of pension accounting has been the use of various terms which have the same meaning. For example, the term “prior service costs” used in APB-8, “past service costs” used in ASPR, “accrued liability” used in ERISA, and “supplemental liability” used by many actuaries have virtually the same meaning. In researching the definitions currently in use, the Board noted that one factor seemed to prevail: The glossaries in use were tailor-made for the particular documents which applied to the terms. For example, the definitions in APB-8 were written in the context of the way in which the words were intended for use in that Opinion. Similarly, the definitions used in ERISA were fashioned to be in consonance with the specific provision of the Act. The Board’s primary objective in developing the definitions in this Standard is similar; the definitions should help provide a clear understanding of the concept used therein, while at the same time maintaining consistency with the thrust of the definitions used in APB-8 and ERISA.

The Board received some additional comments with regard to specific definitions set forth in the *Federal Register* proposal. One commentator expressed confusion at the terms “accrued pension liability” and “unfunded accrued pension liability” because the word “accrued” has a specific meaning in an accounting sense which is different than that intended in the Standard. The Board believes that this comment has merit and, accordingly, the Standard has been revised to use the terms “actuarial liability” and “unfunded actuarial liability.”

Other commentators requested elaboration of the definition of a pension plan. Specifically, they questioned whether the definition is applicable to execute compensation plans, excess benefit plans, and other plans that may not be “qualified” for Federal income tax purposes. The Standard provides the accounting treatment for the cost of all pension plans which fall within the definition of a pension plan. Such accounting treatment is not contingent on the manner in which IRS may categorize plans for income tax purposes.

Several additional commentators questioned that portion of the definition of a pension plan which states that benefits shall be paid for life or be payable for life at the option of the employee. They questioned whether a life income settlement for an employee would fall within the meaning of this definition. The Board believes that such a settlement is, in effect, equivalent to a payment for life and thus falls within the intent of the definition.

(14)**Costs and Benefits**

The anticipated benefits of this Standard are improved cost measurement and increased consistency and uniformity in accounting for pension costs and assigning such costs to cost accounting periods, leading to increased assurance that the measured and assigned costs will be allocated to the proper cost objectives, including Government contracts.

When the preliminary draft Standard on pension cost was submitted to a wide cross-section of companies and individuals, the recipients were specifically asked to comment on the costs of implementing the Standard. The overwhelming majority of the respondents stated that the incremental costs of implementation should be small. In commenting on the proposed Standard published in the *Federal Register*, several respondents stated that the prohibition against use of an aggregate projected benefit cost method and the requirement to make annual gain or loss analyses of each actuarial assumption would involve additional administration costs of any significance. Since the Board has essentially, eliminated these problem areas in this Standard, it believes that increased administrative costs occasioned by this Standard will be minimal. In summary, the Board believes that the benefits to be derived from this Standard clearly outweigh the costs of implementation.

The Board expects that this Standard will become effective on January 1, 1976.

There is also being published today an Amendment to Part 400, Definitions, to incorporate in that part terms defined in 412.30(a) of this Cost Accounting Standard.

Part 412 -- Cost Accounting Standard for Composition and Measurement of Pension Cost is added to read as Follows:

Preambles to Cost Accounting Standard 413, Adjustment and Allocation of Pension Cost.

Preamble A
Preamble to Original Publication, 6-2-76

The following is the preamble to the original publication of Part 413, 42 FR 37191, July 20, 1977.

The cost Accounting Standard on Adjustment and Allocation of Pension Cost is one of a series being promulgated by the Cost Accounting Standards Board pursuant to section 719 of the Defense Production Act of 1950, amended, Pub.L.91-379, 50 U.S.C.App. 2168, which provides for the development of Cost Accounting Standards to be used in connection with negotiated national defense contracts.

This Standard is the second Standard dealing with pension costs. The first Standard, 4 CFR Part 412, establishes requirements covering the composition of pension cost and the bases to be used for measuring such cost. The Standard being promulgated today establishes the basis for assigning actuarial gains and losses to cost accounting periods and for allocating pension cost to segments of an organization.

As part of the Board's early research relating to the subject of pension cost, it submitted an issues paper to a large cross-section of companies, Government agencies, industry and professional associations, actuaries, and other interested individuals. On June 18, 1976, this staff draft Standard sent to those interested parties who had expressed a desire to assist the Board in its research efforts. The responses to the staff draft Standard were considered in developing a proposed Standard which was published in the *Federal Register* of February 3, 1977, with an invitation to readers to submit written views and comments to the Board. The Board also supplemented the invitation in the *Federal Register* by sending copies of the proposed Standard to over 1,000 organizations and individuals.

The Board received 67 sets of written comments from companies, Government agencies, professional associations, industry associations, public accounting firms, actuaries, universities, and others in response to the *Federal Register* proposal. All of these comments have been carefully considered by the Board. The Board's views on each of the major issues discussed by commentators are outlined below, together with explanations of the changes made to the proposed

Cost Accounting Standard.

The Board wishes to take this opportunity to express its appreciation for the helpful suggestions and constructive criticisms it has received, and for the time devoted to assisting the Board in this endeavor by the many organizations and individuals involved.

(1) *Relationship to the Employee Retirement Income Security Act of 1974 and to the Financial Accounting Standards Board.* The Board received a number of comments relative to the relationship between the proposed Standard and the Employee Retirement Income Security Act of 1974 (ERISA). Many of the respondents stated that the proposed Standard contained requirements which are either inconsistent with, more restrictive than, or in conflict with the provisions of ERISA.

The purpose of the Board in promulgating its Standards on pension cost is to establish the criteria for measuring the proper amount of pension cost to be assigned to cost accounting periods for subsequent allocation to negotiated Government contracts. ERISA establishes, among other things, minimum funding Standards for pension plans and provisions affecting deductibility of pension cost for tax purposes. Although there is some commonality between the funding provisions of ERISA and the Standard being promulgated today, ERISA does not provide for the measurement of pension costs for assignment among cost accounting periods or for the subsequent allocation of such costs to contracts.

Notwithstanding the differences in objectives between the proposed Standard and ERISA, the Board believes that compliance with the provisions of the Standard being promulgated today will not violate any provision of ERISA. The Internal Revenue Service confirmed the Board's view on this matter.

One commentator expressed concern over the issuance of a Cost Accounting Standard at this time in view of the active involvement by the Financial Accounting Standards Board in refining the accounting and reporting for both pension plans and employer pension costs. The Board is aware that the FASB may issue a Standard which could be different from the Standard being promulgated today. The Board maintains constant liaison with the FASB with regard to the two Boards' respective responsibilities for developing Standards. It also maintains liaison with the legislative and regulatory bodies responsible for developing and administering ERISA. The Board will review whatever pronouncements these bodies may issue and will consider whether revisions to this Standard are appropriate.

Preamble A
Preamble to Original Publication, 6-2-76 (Continued)

(2) *Definitions.* The Board has received a number of comments relative to the definitions used in the proposed Standard. Some commentators were concerned that the Board is developing still another glossary of actuarial terms. One of the problems in the field of pension accounting has been the words used to express concepts use. Different meanings have been ascribed to the same terms; different terms have been used to describe the same circumstances; and some terms have inferred meanings which have not been present and have not been intended. Thus, the Board's objective in developing the definitions in this Standard is to help provide a clear understanding of the concepts used therein.

With regard to the specific definitions used in the proposed Standard, a the most common problem related to the term "segment." Some commentators construed the term to mean any group of employees performing work for the Government. The definition used in the proposed Standard is the same as that set forth in 4 CFR Part 400. As defined, a segment is an organizational unit which reports directly to a home office of that organization. The designation of organizational units as segments is the responsibility of the contractor; the proposed Standard does not change such designations.

(3) *Assignment of Actuarial Gains and Losses to Cost Accounting Periods.* Section 413.50(a)(2) of the proposed Standard required that for contractors using an immediate-gain actuarial cost method, actuarial gains and losses shall be amortized over a 15-year period. Several commentators stated that immediate recognition of actuarial

gains and losses should be required when there are “abnormal forfeitures” (i.e., exceptionally large termination gains). Some commentators expressed a desire for a 10-15-year amortization period: some desired a 10-20-year period; others merely wanted sufficient flexibility to permit them to use whatever amortization (sic) period they deem appropriate.

The 15-year amortization period is the same as that set forth in the minimum funding provisions of ERISA. It is also consistent with Opinion No. 8 of the Accounting Principles Board APB-8) covering the accounting for the cost of pension plans. The Board believes that the amortization period set forth in ERISA is a reasonable basis for adjusting past pension cost accruals without creating significant distortions to current year’s accruals. The Board is opposed to the use of various amortization (sic) periods because it would be contrary to the Board’s Objective of attaining greater consistency and uniformity in the measurement of pension cost and the assignment of such costs to cost accounting periods.

The Board believes also that there is no valid basis for immediate recognition of gains or losses simply because they are exceptionally large. Recognizing gains and losses in the current year generally is not appropriate because the gains or losses are often an adjustment of costs of a number of years. In this regard, the Board notes that APB-8 states also that gains and losses should be recognized immediately only if they arise from a single occurrence not directly related to the operation of the pension plan such as the closing of a plant. The Standard is consistent with this concept. Accordingly the 15-year amortization period has been retained in the Standard being promulgated today.

(4) *Annual calculation of actuarial gains and losses.* A number of commentators objected to the requirement in 413.40(a) of the proposed Standard that actuarial gains and losses be developed annually. They pointed out that this provision, in effect, requires an annual actuarial valuation. They stated that such a requirement may impose a burden on small contractors is contrary to ERISA which requires a valuation no less frequently than once every three years, and will result in increased administrative costs.

The Board’s primary reason for requiring annual calculations of actuarial gains and losses is to assure that the proper cost is assigned to each cost accounting period. Postponing such calculations may well obscure large fluctuations in pension costs which should be recognized on a timely basis. Because many contracts begin and end within a two or three-year period, such postponements can result in incorrect costs being allocated to these contracts. The Board notes that the overwhelming majority of contractors perform annual actuarial valuations.

In addition, it should be noted that annual actuarial valuations need not be made for all pension plans. Section 412.40(a)(2) of 4 CFR Part 412 provides that for defined-contribution pension plans, the pension cost for a cost accounting period is the net contribution required to be paid for that period. Similarly, 412.50(a) of 4 CFR Part 412 provides that multiemployer plans, certain insured plans, and certain plans applicable to colleges and universities shall be considered to be defined-contribution pension plans. Accordingly, the requirement to develop actuarial gains and losses annually is not applicable to these plans.

With regard to small contractors, the Board notes that it has not received a single comment from a small contractor stating that the requirement for an annual actuarial valuation for certain pension plans will result in a financial hardship to the contractor. Every comment it has received on this point has come from a major contractor. As for increased actuarial fees, the Board was informed by several actuaries that the difference between the cost of three annual valuations and the cost of a single, three-year valuation is relatively small.

In view of these considerations, the Board has retained the requirement for annual development of actuarial gains and losses.

(5) *Valuation of pension fund assets.* A substantial number of commentators objected to the provision of 413.50(b)(2) of the proposed Standard which required that the value of pension fund assets be within 80 to 120 percent of the market value of such assets. Some commentators stated that such an approach could have a significant impact on pension cost in a year in which there is a large market fluctuation. Many of these seemed particularly concerned that a substantial drop in the market value of fund assets would cause an increase in pension costs. Other commentators stated that such a requirement is inconsistent with the fundamental requirement of the proposed Standard which stated that the method in use should minimize the effect of short-term market fluctuations. Some suggested various modifications to the proposed Standard to minimize the possible impact of this provision. For example, it was suggested that the average market value of the fund on several dates be used to determine whether an adjustment is required, or that no adjustment should be required unless the value of the fund is outside of the corridor for a period of several years. Some commentators were of the opinion that the corridor approach was reasonable and should be used except in cases where certain asset valuation methods are used; the most common method cited was the 5-year moving average. Several commentators noted that ERISA requires that, for minimum funding purposes, assets shall be valued on a basis which gives consideration to fair market values. They suggested that this provision obviates a need for a corridor. The Board notes that there is no opposition to the concept that the actuarial value of pension fund assets should take into account the market value of such assets. It recognizes that there are numerous asset valuation methods which take into account market value in varying degrees. In order to achieve an acceptable relationship between the actuarial value of pension fund assets and their market values, the Board could have restricted the use of any of these market valuation methods. In the absence of such restrictions, however, the Board believes some limits must be provided to assure that the actuarial value of fund assets on a given date gives adequate recognition to their market value. The Board reiterates its often stated concept that assignment of costs to the proper period is of paramount importance in determining contract costs. Total reliance on valuation methods which fail to produce actuarial values within the specified corridor is not acceptable for contract costing purposes. For the same reasons, the Board does not accept the suggested modifications to the use of a single asset valuation date because these modifications could defeat the objective of assuring that the value of the fund bears an appropriate relationship to current market values.

The Board notes that the requirement to adjust pension fund assets to within a certain range of market value is not a new concept with this Standard. The Armed Services Procurement Regulations (ASPR) has for many years required that appreciation in equity securities be recognized to the extent that 80 percent of their market value exceeds their adjusted book value. The requirement for upward adjustments of pension fund assets in the Standard being promulgated today is thus similar to the existing ASPR provision. No known problems with this provision for upward adjustments have come to the attention of the Board. Early research in connection with the pension cost Standards did, however, indicate widespread dissatisfaction with the existing ASPR provisions because they did not permit adjustment of pension fund assets below cost. The Standard being promulgated today will correct this apparent inequity.

The Board notes also that many of the commentators apparently did not realize that the adjustment to pension fund assets required pursuant to 413.50(b) would result in an actuarial gain or loss subject to the 15-year amortization period specified in 413.50 (a)(2). It should be recognized that the 15-year amortization period minimizes the effect of short-term market fluctuations in two ways. First, the cost impact of the actuarial gain or loss for any year is spread over 15 years. Secondly, in computing a single year’s pension cost, there could be adjustments resulting from market fluctuations in as many as 15 prior years. If, as can be expected, some of these adjustments will be increases to the year’s pension costs while others will be decreases, the effect of market fluctuations on a year’s pension cost will be further minimized. Accordingly, 413.50(b)(2), in conjunction with 413.50(a)(2), is considered to assure adequate recognition of the market value of pension fund assets while at the same time assuring that the effect of short-term market fluctuations is minimized.

In summary, the Board continues of the view that wide latitude should be provided for selecting an asset valuation method, but that such latitude should be coupled with the requirement that the assets valued under the method selected fall within a range of the market value of such assets. The requirement that assets be valued at least at 80 percent of market value is consistent with the present provision of ASPR. The requirement that assets be valued at no more than 120 percent of market value is a needed and equitable change to the ASPR concept. These requirements are not expected to result in severe pension cost fluctuations which concerned some of the commentators. Under the circumstances the Board has not adopted those recommendations aimed at deleting or revising the requirement that pension fund assets be valued within 80 to 120 percent of market value.

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(6) *Valuation of bonds in a pension fund.* Several commentators expressed their disagreement with the provision of 413.60(b) of the proposed Standard which required that, in establishing the corridor, market values must be used for all assets, including bonds. They stated that the use of amortized amounts will, over time, produce values less susceptible to short/term market fluctuations than will be produced by the use of market values. They noted also that, for minimum funding purposes, ERISA permits bonds to be valued at cost less amortization. The Board's research shows that assets of a pension fund are acquired for investment purposes and may be liquidated whenever pension fund managers believe that the proceeds therefrom can generate more income elsewhere. The Board's research shows also that the frequent turnover of pension fund assets is the rule rather than the exception. Therefore, the Board continues of the view that in establishing the corridor, all assets should be valued on the basis of market and no change has been made to 413.60(b) to provide otherwise. However, the Standard permits a contractor to use amortized values for bonds as a part of the asset valuation method.

(7) Allocation of pension cost to segments of an organization. Section 413.40(c) of the proposed Standard provided that pension costs for a segment may always be developed by separate computation. It further provided that composite pension costs for two or more segments may be computed and allocated by means of an allocation base "unless distortions are created." Section 433.50(c)(2) provide that "unless an equitable allocation of pension costs to segments can be made by means of an allocation base." Separate pension costs for the segment shall be calculated under certain specified conditions.

Some commentators were opposed to a requirement to calculate separate pension costs for a segment under any conditions. Others thought that the proposed Standard was unclear as to when separate segment pension cost calculations were required. A number of commentators concluded that separate calculations would have to be made in any event in order to prove that the use of an allocation base is acceptable. A number of these stated that such separate calculations would be costly.

Normally, pension costs are "central payments or accruals" as that term is used in 4 CFR Part 403. Therefore, where pension costs can be computed for an individual segment, 4 CFR Part 403 would ordinarily require that the amount so computed be the amount allocated to such segment. The calculation of individual segment costs is, in effect, a direct allocation which is not only consistent with CAS 403 but is also consistent with the Board's cost allocation concepts as set forth in the Board's Restatement of Objections, Policies and Concepts (May 1977). Under the circumstances, the Board does not agree with those commentators who are of the view that computation of separate segments pension costs should never be required. Nevertheless, the Board recognizes that the calculation of separate segments pension costs cannot be made without some additional cost and effort. Consistent with its long-standing concepts on materiality, the Board believes that the calculation of separate segment pension cost should be mandatory only when such separate calculations produce materially different results than would result from the use of an allocation base. Therefore the Board sought to provide, in the proposed Standard, criteria to determine when separate calculations would be required.

It is evident that many reviewers of the proposed Standard were uncertain as to when separate segment pension cost calculations would required and when an allocation base could be used. Accordingly, 413.40(c) has been revised to clearly state that a separate calculation of pension cost for a segment is required only when the conditions set forth in 413.50(c)(2) and (3) are present. Appropriate changes have also been made in these paragraphs.

The Board recognizes whether separate segment pension cost calculations are required depends in the final analysis on what is considered to be “material” for the purposes of 413.50(c)(2) and (3). The proposed Standard provided that separate segment costs are to be computed for a segment which had “significant” termination gains; “significantly” different than average benefits, eligibility criteria, or age distribution; or “significantly” different actuarial assumptions.

The concern of many commentators that they would have to make separate segment pension cost calculations in order to prove that the use of a base is acceptable apparently stemmed in part from uncertainty as to what was meant by “significant.” The Board is one record as stating that Cost Accounting Standards should be reasonable and not seek to deal with insignificant amounts of costs. The Board has previously published in its Statement of Operating Policies, Procedures and Objectives certain criteria to be considered in determining whether a transaction or a decision about an accounting practice is material. Such criteria have also been proposed for inclusion in the Board’s regulations. It is intended that these criteria be considered in determining whether separate segment pension cost calculations are required.

To clarify that the Board’s existing materiality criteria apply in this instance, 413.50(c)(2) and (3) in the Standard being promulgated today use the words “material” or “materially” in lieu of the words “significant “or “significantly” contained in the proposed Standard. More importantly, a statement has been added to 413.50(c)(2) to state that separate pension cost calculations are required when the listed conditions are present only if “such conditions materially affect the amount of pension costs allocated to the segment.” The Board believes that, in most cases, it will be obvious to the contracting parties whether the presence of one or more of these conditions for a segment will materially affect the pension cost for that segment. In cases where the impact is not obviously known, the Board contemplates that the contracting parties will rely on summary estimates as a basis for determining whether separate calculations are required. The Board believes that over time, the need for such summary estimates will diminish. The Board emphasizes that separate calculations are not routinely required, even though no two segments are likely to be identical with respect to the actuarial factors set forth in the Standard. The Board intends that separate segment calculations will be required only in those instances where they would result in a materially different pension cost allocation to a segment.

Several commentators noted that there are pension plans covering several segments that are almost completely devoted to performing work for the Government. Others noted that they had segments which perform a relatively negligible amount of Government work. In either case, according to these commentators, even significant differences in pension cost factors among segments covered by the plan would not materially affect the amount of pension costs allocated to Government contracts. Accordingly they recommended that the provisions of the Standard relative to separate computations for a segment not be applicable to such segments.

One of the Board’s primary objectives in the Standard being promulgated today is to allocate the proper amount of pension costs to each segment. This objective is appropriate irrespective of the mix of Government and commercial work of a segment or among all segments covered by a pension plan. Even if several segments are entirely devoted to performing work for the Government, the allocation of pension costs among such segments could materially affect the amount of pension costs that are allocated to particular types of contracts in a cost accounting period. The Board recognizes, however, that if a relatively immaterial amount of a segment’s work is performed for the Government, any revised allocation of pension cost for that segment would probably have little or no effect on the costs allocated to Government contracts. In such a case, the Board urges the contracting parties give due consideration to the Board’s views on materiality.

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(8) *Allocation bases.* The proposed Standard required in 413.50(c)(1) that contractors who compute a composite pension cost for two or more segments must allocate such costs on a base consisting either of the salary and

wages of the participants or the number of participants, except where the contracting parties agree to the use of a different base. A number of commentators stated that in certain cases a better beneficial or causal relationship can be obtained by the use of other than the specified bases. The most commonly listed practice was the use of one base to allocate normal cost and another base to allocate unfunded actuarial liabilities. The Board recognizes that in many cases the use of other bases or a combination of bases would provide an equitable means for allocating pension costs to segments. The Board believes that it should not preclude the use of any appropriate base. Therefore, 413.50(c)(1) of the Standard being promulgated today has been revised to provide that the base to be used for allocating composite pension costs shall be representative of the factors on which the pension benefits are based.

The Board still believes, however, that under certain circumstances, a specific base provides the best means for allocating pension cost. Accordingly, 413.50(c)(1) still requires the use of salaries and wages as an allocation base where costs are calculated as a percentage of salaries and wages, and the use of a base consisting of the number of employees where costs are calculated as an amount per employee.

(9) *Allocation of pension fund assets to segments.* When pension cost must be separately calculated for a segment, it will generally be necessary to allocate pension fund assets to such segments. Section 413.50(c)(5)(iii) of the proposed Standard provided that if contractors used different actuarial cost methods in prior years, the allocation of assets must be based on actuarial liabilities developed under the Accrued Benefit actuarial cost method. Several commentators noted that this provision could result in an allocation of assets to segments which is inconsistent with the bases used to accumulate the assets. The Board agrees with this observation. Accordingly, 413.50(c)(5) of the Standard being promulgated today provides that the allocation of assets shall be made in a manner consistent with the actuarial cost method or methods used to give rise to such assets. It should be noted, however, that such an allocation is permitted only when contributions, disbursements, income, and expenditures made by, or in behalf, of a segment are not readily determinable.

Several commentators suggested that the Standard should be clarified with regard to whether the value of the assets to be allocated shall be the cost of the assets, the actuarial value of the assets, or the market value of the assets. Accordingly, the Board has provided in 413.50(c)(5)(ii) of the Standard that the allocation shall be the actuarial value of the assets.

Several other commentators expressed concern that the Standard would require that specific assets be allocated to segments. The Board never intended an allocation of specific assets; rather, it intended that there be an initial allocation of assets for accounting purposes only. All of the assets of a pension fund remain available to provide benefit payments for participants in any segment. To clarify this point, 413.50(c)(5) of the Standard being promulgated today has been revised to state that there shall be an initial allocation of a share in the undivided pension fund assets.

During the course of the Board’s research several contractors and actuaries questioned whether the proposed asset allocation requirements prohibited contractors from establishing a separate fund for a segment. The Board does not intend such a prohibition in the Standard being promulgated today.

(10) *Pension costs of inactive participants.* The proposed Standard provided in 413.50(c)(7) that inactive pension plan participants shall be considered as constituting a separate segment. This provision was included on the basis of research indicating that the accumulation of pension costs applicable to inactive employees would facilitate the allocation of such costs. However, a large number of commentators objected to this provision, stating that it would be much simpler and less costly to merely assign inactive participants to segments. The Board continues to believe that in certain cases the use of a separate segment to accumulate costs applicable to inactive employees will facilitate cost allocation. It recognizes, however, that in other cases assignment of inactive employees to active segments will ease administrative problems. The Board believes that either technique should result in an equitable allocation of pension cost. Accordingly, the Standard being promulgated today specifically provides in 413.50(c)(9) for the use of either technique.

Section 413.50(c)(10) of the proposed Standard required that the pension cost calculated for the segment created for inactive participant shall be allocated to the active segments on the basis of the pension cost calculated for those segments. Several commentators pointed out that such a basis may be inappropriate in some cases. The Board concurs and has revised 413.50(c)(9) of the Standard to permit more flexibility in selecting an allocation base under such circumstances.

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(11) *Other cost allocation matters.* Several commentators questioned whether contractors must always allocate assets, and continue developing fund data for a segment simply for the purpose of amortizing an identified one-time actuarial gain or loss attributable to a segment. If an equitable allocation of pension cost can be achieved without allocating assets, it is not necessary to do so. For example, in the case of a one-time termination gain or loss, a contractor could isolate this gain or loss from the other composite actuarial gains or losses and separately credit or charge the former gain or loss over the next fifteen years to the segment from which it arose. The contractor could then continue using the composite cost allocation method (except for such separate adjustment) so long as there is no further unusual experience for that segment. The Board has amended the illustration in 413.60(c)(1) of the Standard to embody this concept.

Section 413.50(c)(1) of the proposed Standard contained a requirement that costs shall be calculated on a segment basis under circumstances where

(1) a pension plan for a segment was or becomes, merged with that of another segment, and

(2) the ratio of assets to actuarial liabilities for each of the merged plans are significantly different from one another after applying the benefits in effect after the merger. In illustrating this point in 413.36(c)(3), it was indicated that this provision is applicable to mergers which occurred prior to the effective date of the Standard. Several commentators expressed concern over the provision, stating that retroactivity was inequitable. They stated that it would be difficult and expensive to analyze prior years' pension cost, especially in cases where the mergers arose many years ago. The Board believes that these comments have merit. Accordingly, the Standard being promulgated today specifically provides in 413.50(c)(4) that a requirement for separate segment pension cost calculations for mergers shall have prospective impact only and that pension costs need not be adjusted for prior years. Section 413.60(c)(5) has also been revised.

One commentator noted that its segments performing Government work had different pension cost factors than did the other segments of the company. However, the commentator noted that these factors were homogeneous for the segments performing Government work. The commentator asked whether the Standard requires separate cost calculation for each segment under such circumstances. The contractor can make a composite calculation for the Government segments and allocate the cost to these segments by means of an allocation base. The contractor can, of course, do this for the other segments. To highlight this point the Board has added an illustration in 413.60(c)(4) of the Standard.

Two commentators asked whether a difference between the amount of pension cost required to be funded under ERISA, and the sum of the pension costs developed for all segments could be allocated to the various segment. The board recognizes that it is theoretically possible for the sum of a pension costs calculated for segment of an organization to be materially less than the minimum amount required to be funded pursuant to ERISA. However, such a difference may not be assigned to the period for which funding is required. The Board has previously emphasized that the amount of pension cost assignable to a cost accounting period is not necessarily the same as the amount funded for that period. If the amount required to be funded exceeds the amount calculated, the excess amount funded is subject to the provisions of 4 CFR Part 412 (412.50(c)(1)) which states that "Amounts funded in excess of the pension cost computed for a cost accounting period pursuant to the provisions of this Standard shall be applied to pension costs of future cost accounting periods."

(12) *Closing of a segment.* The proposed Standard contained a requirement in 413.50(c)(13) that when a segment is closed and a significant number of employees are terminated, the contractor shall calculate a gain or loss from the plan applicable to that segment, irrespective of whether the pension plan is terminated. A number of commentators expressed their concern over this provision. Some questioned whether the "net gain or loss" was an actuarial gain or loss and, if so, how it related to other sections of the Standard. Other commentators presumed that this section dealt with the termination of a plan; they stated that, in such an event, the provisions of ERISA and regulations of the Pension Benefit Guarantee Corporation would prevail. They suggested that this section of the Standard be made applicable only to pension plans that are being continued.

As a general rule, the Standard being promulgated today is based on the concept that material actuarial gains and losses applicable to a segment will be taken into account in future cost accounting periods in determining the costs for the segment. However, a problem arises in cases where a segment is closed. Because there are no future periods in which to adjust previously-determined pension costs applicable to that segment, a means must be developed to provide a basis for adjusting such costs. This adjustment is not an actuarial gain or loss as defined in the Standard. To clarify its intent, the Board has revised 413.50(c)(12) of the Standard and the related illustration in 413.60(c)(8). The Standard now states that when a segment is closed, the contractor shall determine the difference between the actuarial liability for the segment and the market value of the assets allocated to the segment.

The Board recognizes that, in some cases, the closing of a segment could be associated with a termination of a plan. Several commentators noted that, in such a case, the actuarial liability for that segment could be greatly influenced by regulations developed pursuant to the provisions of ERISA. The Standard specifically permits the effect of such regulations to be considered in determining the actuarial liability for the segment.

It should be noted that the provisions of this section are appropriate whenever a segment performing a material amount of Government business is closed, irrespective of whether the closing is caused by the completion of a contract or an organizational change, or whether the closing results in a complete or partial termination of the plan. The board emphasizes that the purpose of this provision is to serve as a basis for recognizing and adjusting pension costs previously allocated to the segment being terminated. Such a requirement is independent of whether employees are terminated from the plan.

(13) *Application to defined-contribution and certain other plans.* A number of commentators questioned whether the provisions of the proposed Standard are applicable to defined-contribution and multiemployer pension plans. The Board notes that Standard 412 specifically provides that, for a defined contribution pension plan, the pension cost for a cost accounting period is the net contribution required to be made for that period. Standard 412 provides also that a multiemployer pension plan established pursuant to the terms of a collective bargaining agreement shall be considered to be a defined contribution pension plan for purposes of this Standard. Thus, the only provisions of this Standard that are applicable to these plans are those dealing with the allocation of costs to segments.

Specific questions were raised with regard to the applicability of the asset valuation requirements to insured plans. Section 413.50(b)(4) of the proposed Standard provided that the asset valuation requirements therein are not applicable to insured plans whose funds are commingled with those of the insurance company. Several commentators stated that this provision was unclear; they questioned whether group deposit administration annuity contracts, immediate participation guarantee contracts, or separate accounts deposit administration contracts are subject to the asset valuation provisions of the Standard. The Board intends that such contracts be subject to these provisions of the Standard. However, the asset valuation provisions do not apply to contracts under which insurance companies guarantee a rate of return. The Board believes that, in such circumstances, the recognition of unrealized appreciation or depreciation on pension fund assets does not alter the basic contractual agreement entered into between the plan sponsor and the insurance company. Section 413.50(b)(4) of the Standard has been revised to clarify this point.

(14) *Costs and benefits.* The anticipated benefits of this Standard are increased consistency and uniformity in measuring actuarial gains and losses and assigning them to cost accounting periods, and better allocation of pension costs to segments of an organization. The Board believes that such improved measurements and allocations will result in more equitable allocation of pension costs to cost objectives, including Government contracts. By providing criteria for controversial aspects of pension cost accounting, the Standard is also expected to reduce disagreements among contracting parties.

In its research leading to the development of this Standard, the Board noted a number of disagreements between contracting parties relating to the disposition of termination gains attributable to segments performing Government contracts. The Board believes that the Standard will diminish, if not eliminate, such disagreements.

On May 19, 1977, the Comptroller General of the United States issued a report to the Congress entitled "Contractor Pension Plan Costs: More Control Could Save the Department of Defense Millions." The General Accounting Office selected, at random, nine Department of Defense prime contractors and examined the pension costs of these contractors. The report states that a substantial amount of questionable pension plan costs were, or may be, charged to Government contracts. The report attributes much of the questionable pension costs to the inequitable allocation of pension plan costs between Government and commercial business. The report states that the Standard being promulgated today deals with, and should correct, many of the problems cited. The following are examples of these problems and the provision of the Standard which deals with them.

(a) A contractor, which calculates pension cost by segment, does not equitably allocate assets to these segments each year; the amounts allocated do not recognize net annual capital contributions by the segments nor the segments shares in the capital growth of pension fund investments. Section 413.50(c)(5), (6) and (7) deals with this subject.

(b) The pension fund of a contractor which acquired a commercial subsidiary is in a surplus position. As a result, pension contributions are not being made for either the Government segments or the commercial subsidiary. Because the surplus was accumulated mainly through Government reimbursements that exceeded the amount required, the Governments proportional share of the surplus has been diluted by the annual pension plan costs of the commercial subsidiary. Section 413.50(c)(3) deals with this subject.

(c) One contractor used corporate-wide assumptions to calculate pension cost. However, the Government-oriented segments had much higher employee termination rate; than did the other segments. The cost to the Government would have been much less if separate pension cost calculations were made for the Government-oriented segments, using the appropriate termination assumptions. Section 413.50(c)(2) deals with this subject.

The Board recognizes that the implementation of this Standard may result in some increased administrative costs by defense contractors. The Board's research shows that any incremental administrative costs incurred will be predominantly related to increased actuarial fees. After discussing with actuaries the nature and scope of increased actuarial work required, the Board is confident that the increased administrative costs required to implement the proposed Standard are relatively small and do not approach the benefits that will be achieved by the proposed Standard.

As required by 719(g) of the Defense Production Act of 1950, as amended, the Board has evaluated the potential inflationary effect of this Standard. The Standard may cause a shift of pension costs from earlier periods to later periods or vice versa. It may also cause a shift of pension costs among various portions of a contractor's business. In the long run, however, total pension costs will not increase or decrease as a result of this Standard. As already noted, increased administrative costs attributable to the Standard are expected to be minimal. Accordingly, the Board concludes that this Standard will have no inflationary effect.

(15) *Effective date.* At the time of promulgation of each previous Standard, the Board followed the policy of reserving the effective date of the Standard, pending the expiration of 60 calendar days of continuous session of the Congress following the date on which the Standard was transmitted. Section 413.80 of the Standard being promulgated today specifies the effective date. The date is included at this time to afford contractors and contracting agencies the earliest possible notification so that they can begin to make implementation plans. In the event any subsequent event makes it necessary to rescind or amend that date, such action will be taken by appropriate notice in the *Federal Register*.

Preambles to Cost Accounting Standard 414, Cost of Money as an Element of the Cost of Facilities Capital

Preamble A
Preamble to Original Publication, 6-2-76

The following is the preamble to the original publication of Part 414, 41 FR 22244, June 2, 1976.

The Standard on Cost of Money as an Element of the Cost of Facilities Capital being published today is one of a series being promulgated by the Cost Accounting Standards Board (Board) pursuant to section 719 of the Defense Production Act of 1950, as amended (Pub.L.91-379, 50 U.S.C.App. 2168), which provides for the development of Cost Accounting Standards to be used in connection with negotiated national defense contracts.

Performance under negotiated contracts usually requires the use of facilities which represent significant contractor investments. Accounting principles applicable to financial reporting do not provide for any explicit recognition of the cost of capital committed to facilities. The Board has long been interested in identifying, as a contract cost, a part of the contractor's total cost of capital. The Board distributed three research papers dealing with the cost of capital in connection with negotiated contracts. These mailings were in June 1974, April 1975, and December 1975. The responses received to all three of those research mailings were useful in the development of the proposal published by the Board on March 5, 1976 (41 FR 9562).

The Board supplemented that March 5 *Federal Register* request for comments by sending copies of the *Federal Register* material directly to organizations and individuals who were expected to be interested. The Board has received 82 comments on the March 5 proposal. All of these comments have been carefully considered. The Board appreciates the helpful suggestions and criticisms which have been furnished.

The comments below summarize the major issues discussed by respondents and the significant changes which have been made from the March 5 version of the proposed Standard.

A.**-- General Comments**

(1) *Impact on Contract Prices.* Commentators who represented contractors and the accounting profession tended to favor the proposal, while those who represented some Government agencies were opposed. Government representatives were joined by some other commentators who expressed the belief that the cost of money as an element of the cost of capital committed to facilities should remain, explicit or otherwise, a consideration in determining contract profit compensation, rather than be treated as an element of cost. The Board's early research into the broad question of measurement of the costs related to capital commitment included a number of inquiries about the propriety of a change in the basic concepts of contract cost to include this element.

The cost to be measured, even though imputed, is real and is relevant for contract costing. The Board is persuaded that there has not been adequate agreement on techniques for measuring it. A Cost Accounting Standard is, therefore, appropriate.

Some commentators have expressed concern that contract profit levels may be reduced when this new element of contract cost is recognized, and that there will thus be no real financial benefit from the issuance of the Standard. Such comments are based on a misunderstanding of the Board's mission. The Standard is intended to improve contract cost measurement and understanding by the contracting parties and to provide for greater uniformity by specifying techniques appropriate to types of circumstances actually encountered. Capital as asset commitment varies widely among contracts. The Board has developed a technique that takes explicit account of such differences in capital intensity. The procurement agencies are now considering their pricing policies and the Board expects the agencies in doing this to give appropriate recognition to this Standard.

(2) *Exclusion of Working Capital.* As the Board pointed out in its publication on March 5, 1976, its staff has investigated the problems related to measurement of the costs related to investments in operating, or working capital. Most commentators, while generally favoring the Board's proposal as to the cost of facilities capital, urged that the final promulgation include explicit cost recognition based on the contractor's investment in working capital. The Board is not prepared at this time to make determinations on all the issues related to working capital. The economic impact of contractor investment in facilities is, by itself, important enough to warrant recognition as a contract cost without delay. The Board will seek to resolve the problems related to measurement of the contract cost attributable to the investment in working capital.

(3) *Withdrawal of Proposed CAS No 413.* A number of commentators expressed regret that the Board has withdrawn its proposed Cost Accounting Standard No. 413 on Adjustment of Historical Depreciation Costs for Inflation, which was published on October 9, 1975. As the Board pointed out in its March 5, 1976 publication inflation has an impact on interest rates. Research shows that over time there is a strong correlation between interest rates and the rate of change of the price level. The interest rates which were available for measuring the cost of capital would unavoidably include some allowance for inflation. Although a number of respondents denied any overlap, the promulgation of both CAS No. 413 and CAS No. 414 as proposed would have resulted in some duplication of coverage.

The accounting profession continues to consider various approaches to the financial reporting problems related to inflation. The Board will continue to observe the various efforts within the profession, and will consider the usefulness for contract costing purposes of each new statement of generally accepted accounting principles related inflation.

Should the Board consider it appropriate at some future time to measure the impact of inflation in some other way for contracts, it will, of course, reconsider the rate as well as the method selected for measurement the cost of money as an element of the cost of facilities capital.

B.**-- Content of the Standard**

(1) *The Renegotiation Board Rate.* The Board's March 5 publication specified the use of the semiannual interest rate established in accordance with Pub.L.92-41 to serve as a cost of money rate for determining the imputed cost of capital committed to facilities. That law requires that the "rate shall be determined by the Secretary of the Treasury, taking into consideration current private commercial rates of interest for new loans maturing in approximately five years." (section 2, 85 Stat. 97).

Some commentators have pointed out that the interest rate specified under Pub.L.92-41 was, during 1973-1974, less than the actually experienced rate of general inflation, and thus could not have realistically reflected the rate of inflation. The rate includes provision for the expected impacts of future inflation. In the future as in the past, inflationary expectation may indeed be less than the rate of inflation subsequently experienced; but at times it may also be greater.

Obviously the single interest rate specified under Pub.L.92-41 and used as a cost of money rate in this Standard will rarely be the precise borrowing rate of any particular contractor.

(2) *Allocation of Facilities.* For contract costing purposes, the cost of capital committed to facilities must be related to contracts. The following three subsections deal with the techniques proposed to establish this relationship.

Simplified Procedure: The Standard being promulgated today is based on allocation to negotiated contracts of an appropriate share of the total cost of money which can be identified with the facilities employees in a business unit. This allocation is made by first identifying the total facilities capital associated with each indirect cost pool. The imputed interest cost is then assigned to contracts on the basis of the same measures used to allocate other costs from those indirect cost pools.

Interested parties almost universally accepted this basic approach. A few have expressed concern, however, that the proposed procedure might entail more effort than would be warranted by the improved precision obtained as compared with a much simpler procedure to approximate the desired allocation.

The March 5 proposal included a provision for a simple allocation technique, based on the established procedure for distribution of G&A expenses. This alternative was to be used “only where the contracting parties agree that the results are not likely to differ materially from those which would be produced under the procedure (otherwise described in the proposed Standard).”

Critics of the proposal suggest that the only way the two parties could agree to use the alternative simple procedure would be to recreate the detail of an allocation using the “regular” method as a comparison. But if the “regular” method must thereby be applied in any case, then there would be no reason to pursue the alternative. The Board has confidence in the reasonableness of the contracting parties in finding ways to achieve the purpose of this Standard. Where the total amount of facilities capital is minor in relation to the estimated incurred cost, for example, the parties could be expected to agree in advance to use the simpler alternative procedure. Similarly, if the contractor has a variety of service centers and other indirect cost pools, which are generally used to serve all productive activities, and which do not individually involve significant facility investments, the alternative procedure could be expected to provide significant administrative convenience, and should probably be used. The situation would be different if a relatively significant portion of the total facilities investment were identified with a service center which is obviously not used with the same intensity for all final cost objectives of the contractor; the imputed cost related to such an investment should be assigned on the basis of the use of the facilities rather than on the basis of some overall allocation procedure.

The instructions in the Standard have been modified slightly to clarify the available flexibility. The Board expects that administrative convenience and the likelihood of significant distortion will be considered in decisions about the use of the simplified alternative procedure permitted.

Basic Allocation Technique. Some commentators criticized the complexity of the regular procedure provided in the March 5 publication. The instructions called for the identification of assets to pools “on any reasonable basis that approximates the actual absorption of depreciation and the related costs of such facilities. The basis of allocation of undistributed assets in each business unit between, for example, the engineering overhead pool and the manufacturing overhead pool, should be related to the manner in which the expenses generated by these assets are absorbed in the two overhead rates. The choice of the basis for allocation is up to the contractor within the limits stated above.” Those critics who feel that the instructions require too much detailed analysis in the case of elaborate overhead distribution systems seem not to have understood the intent of the quoted portion. Consolidation and simplification to a limited number of pools and allocation bases is justified in the typical situation where there are many service centers. Minor editorial changes have been made in the instructions, but the Board has not seen the need for any major change in this regard.

Application to Process Cost Systems. The Standard provides a means for allocating the imputed cost to final cost objectives by developing facilities capital cost factors for indirect cost pools. To determine the cost of money applicable to a given final cost objective, these factors must be multiplied by the corresponding allocation base units identified with the final cost objective. A few commentators questioned the technique for applying this procedure for process cost systems.

In a process cost system all the production costs, including overhead costs, are usually accumulated in cost pools associated with "process cost centers" and are then allocated so final cost objectives or products by means of an individual cost center "charging rate." The procedures outlined in this Standard for developing facilities capital cost of money factor for overhead and G&A expense pool are equally applicable to "process cost centers" in case of a process cost system. However, difficulties may arise in computing the appropriate amount of cost of money applicable to each cost objective or product. The difficulties will emerge where the cost record of individual contracts or other final cost objectives do not, as a matter of course, identify any amount of allocation base units related to these final cost objectives in the various "process cost centers." In those circumstance it is anticipated that the contracting parties could agree upon one of several possible acceptable courses of action. Thus it should not be difficult to develop an acceptable allocation basis using statistical methods where appropriate. In addition, the "alternative method," described in instructions to Form CASB-CMF, could be applied in suitable circumstances.

(3) *Inclusion in "Cost Input"*. A few commentators questioned whether the imputed cost of capital committed to facilities should be included in the cost input typically to be used as the basis for distribution of G&A expense under the terms of Cost Accounting Standard No. 410. This element of contract cost is indeed a part of total cost. The term "cost input" is defined as "the cost, except G&A expenses, which for contract costing purposes is allocable to the production of goods and services during a cost accounting period." In principle, the cost of capital committed to facilities, other than those facilities identified with the G&A expense pool, should be included in the total cost input base.

The Board believes that as a practical matter the allocation of the cost of money for the cost accounting period (See Col. 5 Form CASB-CMF) would not be materially affected by the inclusion or exclusion of cost of money from "cost input." The cost of money for the business unit as a whole would not change. However, to the extent that cost input is used as an allocation base some difference in the allocation to individual contracts can be anticipated. As indicated earlier, however, this difference generally should be immaterial.

In view of the amount of cost accounting data that may be affected by the introduction of cost of money as an element of contract cost and the idiosyncrasies (sic) of the systems designed to handle that data, the Board believes that administrative expedience should not be ignored. Therefore, at this time it does not prescribe whether this element of cost should be included in or excluded from the cost input allocation base. Although the imputed cost of capital committed to facilities should be included in the total cost input allocation base whenever practicable, exclusion of this element will be acceptable whenever the contractor chooses such exclusion on the basis of reasonable administrative convenience. The illustration in Appendix B is prepared showing the inclusion of this cost and also, as an alternative, showing the exclusion of this element of cost from the measure used as an allocation base for G&A expenses.

C.**-- Administration**

(1) *Accounting Records.* The Board's March 5 proposal included the acknowledgement that the imputed cost to be recognized has not been treated under the generally accepted accounting principles applicable to external financial reporting. Even so, several commentators felt the need to point out to the Board that the proposal would involve a cost not currently recognized in published corporate financial reports.

The Board has often emphasized that memorandum records, not necessarily a part of the contractor's formal accounting system, can furnish adequate accounting support for contract purposes, where these purposes differ from those for which the accounting system was developed. The imputed cost to be recognized under this Standard is no exception. The Standard provides the techniques by which this cost will be measured, starting with data already in the accounting records.

(2) *Preparation of Estimates.* The March 5 proposal included the provisions that "where the cost of money must be determined on a prospective basis the cost of money rate shall be based on the most recent available rate published * * *." Some commentators urged that the Standard make more clear the relationship of the published rate to the rate to be used in estimates. Some urged that the published rate be required, and others asked for the publication of official forecasts, which should be used for estimates.

Other commentators pointed out that the determination of the cost of money applicable to a proposed contract requires estimation of a number of asset values and allocation rates. They asked that the Board provide clear instructions as to prospective application.

The Board has never undertaken to advise the contracting parties as to techniques for estimating or for agreeing upon specific amounts of estimated costs. In the case of the imputed cost of capital committed to facilities, as for other elements of cost, the clear determination of the procedure by which "actual" cost will later be measured can eliminate confusion as to the nature of the estimate. The parties may, of course, use any techniques which seem appropriate for agreeing on the numeric values to be included in contract cost estimates.

(3) *Compliance with Standard No. 401.* The Board has earlier promulgated a Standard (4 CFR Part 401) which requires that the practices used in pricing a proposal (estimating) shall be consistent with the cost accounting practices used in accumulating and reporting costs. One of the essential features of that Standard is the requirement that any significant element of cost in the estimate can be compared with the corresponding actual cost. A number of commentators have expressed concern about the applicability of that Standard to an imputed cost.

For the purposes of complying with Standard No. 401 the Board believes that any reasonable estimating technique which establishes the cost of money as a separate amount is acceptable. It is not necessary in estimating to follow precisely the procedures, including Form CASB-CMF, incorporated in the Standard.

D.-- **Applicability**

(1) *Use Rates.* Contractors are sometimes compensated for the use of facilities by means of "use rates" authorized under Government procurement policies. These rates may cover various elements of ownership costs, including depreciation. The March 5 publication contained a proposed exemption for situations where such use charges were included in contract costs. A number of commentators criticized that proposed exemption.

The Board does not intend to interfere with the process of establishing "use rates" nor is it prepared to define at this time the factors that should be taken into account when they are formulated. The Board believes that the cost of money is a valid economic cost, and that it is as relevant to a contractor employing a use rate as it is to one using depreciation. Existing schedules of use rates have presumably include appropriate consideration of all elements of the total cost to be considered in developing such rates. The proposed exemption for those covered by use charges is accordingly retained.

(2) *Existing Covered Contracts.* Many commentators urged revision of 414.70 of the March 5 proposal to delete the exemption of contracts and subcontracts entered into prior to the effective date of the Standard. Such contracts were negotiated under the provisions of Government procurement regulations. In all such regulations, any interest costs incurred by the contractor have been specifically designated as unallowable costs. Furthermore, none of these regulations has recognized any imputed cost capital committed to facilities. The agreement of the parties, embodied in such prior contracts, has necessarily been reached in light of the cost principles existing at the time the contracts were entered into. The Board therefore concludes that this Standard should not be applied to existing contracts and the Board has consequently retained the exemption in 414.70.

E.-- **Benefits and Costs**

With respect to Cost Accounting Standards, the Board's primary goal is to issue clearly stated Standards to achieve

(1) an increased degree of uniformity in accounting practices among Government contractors and

(2) consistency in accounting treatment of costs by individual Government contractors. Increased uniformity and consistency are desirable to the extent that they improve understanding a communication.

Contract costs currently do not include any measurement of the cost of money, which is undeniably a cost related to contract performance. The result is that contract cost measurements have made no distinction between contracts with equal amounts of total incurred cost but with vast differences in amounts of facilities investment.

This Standard need have no impact in the aggregate prices paid by the Government but will reflect specific identifiable cost of money as an element of the cost of facilities capital in individual negotiated contracts. Previously, these costs presumably were reflected in nonidentifiable amounts in the profits or fees included in the total contract prices. By reflecting specific costs of money attributable to contractor investments in facilities, this Standard will provide for greater consistency in negotiating total contract prices. The Board understands that procurement agencies expect to take this Standard into account in their current reconsideration of pricing policies. The Standard also will assist the procurement agencies to discriminate more effectively between contracts in which the cost of money is significant and those in which it is not.

The Nation's mobilization base depends on its facilities. These may be more effectively modernized because of the explicit cost recognition provided by this Standard, which will help to eliminate the existing disincentives which have hampered contractor investments in facilities. Also, to the extent that the Standard results in investment in cost-reducing equipment, the Government will be able to procure goods and services at lower prices.

Some commentators have suggested that the Board's issuance of Cost Accounting Standard No. 409 caused the need for recognition of this element of cost of facilities capital, and that the Standard being promulgated should be judged in that context. The Board does not agree. The Standard on depreciation was justified by the need for improved criteria with respect to depreciation expense identified with contract performance. Some critics of that Standard argued, in effect, that it should not have been promulgated because, even though it would improve depreciation accounting, there were economic costs not yet being recognized, and that improper depreciation could be justified as an acceptable technique for meeting the economic need. The Board was not and is not persuaded by such reasoning.

The Board has considered the administrative costs related to implementation of this Standard. The most significant potential problems mentioned by commentators were related to features of the proposal which have been modified in response to those comments. The Standard as promulgated today is not expected to involve any significant administrative difficulty, either for contractors or for the Government.

In summary, the Board finds that the benefits of this Standard, which are significant, outweigh the costs, including any inflationary impact.

F.**-- Miscellaneous**

The Board expects that this Standard will become effective on October 1, 1976.

There is also being published today an amendment to Part 400, Definitions, to incorporate in that part terms defined in 414.30(a) of this Cost Accounting Standard.

Preambles to Cost Accounting Standard 415, Accounting for the Cost of Deferred Compensation

Preamble A
Preamble to Original Publication, 7-30-76

The following is the preamble to the original publication of Part 415, 41 FR 31797, July 30, 1976.

The Standard on Accounting for the Cost of Deferred Compensation being published today is one of a series being promulgated by the Cost Accounting Standards Board pursuant to section 719 of the Defense Production Act of 1950. as amended(Pub.L.91-379, 50 U.S.C.App. 2168), which provides for the development of Cost Accounting Standards to be used in connection with negotiated national defense contracts. This Standard provides criteria for the measurement of the cost of deferred compensation and the assignment of such cost to cost accounting periods.

Early research included an extensive review of available literature, the Disclosure Statements filed with the Board, and decisions of boards of contract appeals. This information was then supplemented by visits and mail solicitations to contractors in order to elicit more specific data concerning company deferred compensation plans.

In May 1975, a questionnaire/issues paper was sent to a wide mailing list soliciting responses to several basic issues identified in the Board's early research. Seventy responses to the questionnaire/issues paper were received from interested parties, the majority of whom were companies that had deferred compensation plans. Based on the responses received, a preliminary draft Standard was developed in December 1975 and sent to a large cross section of companies, Government agencies, industry and professional associations, and other interested individuals. The Board received 53 responses to the draft Standard.

After several changes were made to the draft Standard, based on consideration of the comments made by respondents, a proposed Standard was published in the *Federal Register* of April 7, 1976, with an invitation to interested parties to submit written views and comments to the Board.

The Board received 34 sets of written comments from companies, Government agencies, professional associations, industry associations, public accounting firms and others in response to the *Federal Register* proposal. All of these comments have been carefully considered by the Board. The Board's views on each of the major issues discussed by the commentators are outlined in the following sections, together with explanations of the changes made in the Cost Accounting Standard being promulgated.

The Board wishes to take this opportunity to express its appreciation for the helpful suggestions it has received and the time devoted to assisting the Board in this endeavor by the many organizations and individuals involved.

Relationship of Standard to Current Procurement Regulations

Under current procurement regulations, deferred compensation is allocable as a cost of Government contracts only to the extent that such costs are deductible for the same fiscal year for Federal income tax purposes. A few commentators expressed concern that the proposed Standard would require the assignment of the cost of deferred compensation to a cost accounting period that would be different than that determined under the Internal Revenue Code for Federal income tax purposes.

Under the Internal Revenue Code, a deduction for tax purposes for the cost of many incentive or bonus type plans is not permitted until the deferred compensation is paid to the recipient. Under the Standard, however, the cost of deferred compensation is assignable as a contract cost in the period the contractor incurs an obligation to pay such cost which, for many deferred compensation plans, will be the period in which the award is made. (See 415.40(a).)

The Board has recognized that contract costing often deals with the same expenditures as are of interest in income tax accounting. Except for differences in tax rates, shifts of income or expense from one year to another generally do not have a significant effect on total tax paid over a period of time. Similar shifts of cost, however, from one year to another could have a decided impact on the costs chargeable to Government contracts. This impact occurs because the mix of Government and commercial contracts often changes significantly from period to period. Therefore, the Board believes that application of the criteria provided in the Standard to assigns the cost of deferred compensation on an accrual basis of accounting is needed to better assure that such cost of deferred compensation will be assigned to appropriate cost accounting periods.

Allocability and Allowability of Contract Costs

Several Government agency commentators pointed out that under present procurement regulations deferred compensation is not allowable until the period in which paid. These commentators also noted that the cost of stock options, under present procurement regulations, is unallowable although these commentators generally recognized that the provisions of the Standard involve allocability, they questioned whether the Standard would encroach on the allowability prerogatives of the procurement agencies.

The Board believes that recognition of the cost accounting concept that all costs incurred in carrying on the activities of an enterprise are allocable to the cost objectives of the enterprise is essential to the maintenance of sound and consistent contract cost accounting. Cost Accounting Standards should result in determination of costs which are allocable to contracts and other cost objectives. The use of Cost Accounting Standards, however, has no direct bearing on allowability determinations.

Definition

A commentator was concerned that the proposed Standard may apply to the cost of some pension plans that are subject to Accounting Principles Board Opinion No. 8, Accounting for the Cost of Pension Plans, and that different measures of cost might result for the same plan from application of the proposed Standard and from application of APB Opinion No. 8. The commentator questioned whether an amount paid to an employee after retirement for a specified period of time, e.g., 10 years, would fall under the definition of deferred compensation as used in this Standard. If a payment for a specified period of time after retirement is, in effect, equivalent to a life income settlement, this payment falls within the definition of a pension plan as provided in Cost Accounting Standard 412, Composition and Measurement of Pension Cost. If the payment is not a life income settlement, it is not a pension plan and the award is covered under the definition of deferred compensation. The Board does not believe that the Standard being promulgated today applies to any pension plan covered under APB Opinion No. 8.

Determination of Obligation

One of the criteria contained in the Standard for determining whether a contractor has incurred an obligation for the cost of deferred compensation is whether or not there is reasonable probability that certain required conditions precedent will occur before an employee is entitled to receive the benefits (see 415.50(a)(5)). The proposed Standard stated that, in determining whether certain events are likely to occur, one of the factors to be considered was the reasonableness of the time interval between the award and the expected occurrence of the event. A few commentators suggested that the proposed Standard specify the length of time that would be reasonable. The Board does not believe that a particular time period can be specified to cover all circumstances. Each category of award must be analyzed on a case-by-case basis because there are several factors involved in determining whether employees should be entitled to receive the benefits of an award. Among the factors that should be considered, in addition to the time interval, are the employer's experience with similar awards and other restrictive terms which may be involved in the terms of the award.

Since there are numerous factors to be considered, the Board has deleted from 415.50(a)(5) of the Standard mention of two specific factors in order not to give undue weight to these factors. In addition, the Board has added 415.50(a)(6) to make clear with respect to stock options, that an obligation is deemed to have been incurred only if there is a reasonable probability that the option ultimately will be exercised.

Future Service Requirements

Section 415.50(a)(3) provides, as a condition for the assignment of deferred compensation, that the amount of future payment be capable of being measured with reasonable accuracy. In this connection, several commentators suggested that this provision should override the provision for prorating the cost if future service is required. The commentators stated that the service to be rendered after the period of award does not influence the basis for the award. These commentators believe that if there is a strong likelihood that the recipients of the awards would remain with the company for the periods of future service then the costs should be charged in the year of award.

The Board does not agree that the reasonable accuracy of measuring the cost should override the appropriate assignment of the cost to the periods of current and future service based on the facts and circumstances of the award. The Board believes that, where future service is required, such compensation related to the service rendered in those future periods and therefore the related cost should be assigned to those periods. In this regard, the Board believes that the concepts embodied in Accounting Principles Board Opinion No. 12 Omnibus Opinion, are appropriate for contract costing. This Opinion states that "If elements of both current and future service are present [for deferred compensation awards], only the portion applicable to the current service should be accrued." To make certain that this concept is clearly understood to be incorporated in the Standard being promulgated, a provision has been added to 415.50(a).

Variable Interest Rate

Several commentators expressed concern over a provision in the proposed Standard which stated that if the interest rate included in the award is not fixed at the date of award, the interest was to be assignable only to the periods in which the interest was paid. A few of these commentators stated that generally accepted accounting principles require that the estimated amount to be paid should be assigned in a systematic and rational manner. The commentators stated that, if the amount of interest is known in each period, it should be assigned in each such period.

The Board agrees that the variable interests amounts should be assigned to periods in a systematic and rational manner provided that the terms of the plan specify the basis under which variable interest amounts will be derived and the interest applied in each period is determinable at that time. Consequently, the Standard being promulgated today has been revised to provide in 415.50(d)(2), that variable interest included in awards shall be assigned in the same period as the principal of the award, provided that the rate is based on a specified index and is determinable in each applicable period. The Standard also provides that since the interest rate used at the time of the award is likely to vary from the actual rates in future periods, adjustments shall be made in any future period in which the variation in rates materially affects the cost of deferred compensation.

Section 415.50(d)(3) was added to the Standard to provide for those situations in which the interest rate was not based on a specified index or not determinable in each applicable year. In these situations, the present value of the principal amount of the award is assignable in the year of award and the interest cost is assignable to the period or periods in which the payments are made.

Forfeitures

Two commentators stated that the forfeiture provision should be expanded to recognize that losses on the initial payment for irrevocably funded plans, as well as earnings, may occur within the framework of such a plan. The Board had intended that both gains and losses be recognized and has changed the provision to clarify this point (see 415.50 (d)(7)).

Another commentator stated that the forfeiture provision should not include interest to the date of the forfeiture. The commentator stated that it seems inequitable to require that the value of the forfeiture be determined at a level which was not fully allowable as a cost during the accounting periods affected. The Board does not share the view that including interest in the credit for forfeitures is inequitable. The interest factor represents the time cost of money which the contractor should pay to the Government for having been provided with funds. The forfeiture is calculated to be the present value of the future benefit at the time of forfeiture and thus is equivalent in present value terms to the amount of deferred compensation that was originally assigned. However, as stated in the Standard, the failure of the recipient to voluntarily exercise a stock option is not considered a forfeiture.

The Standard has been amended to provide that if a recipient of an award of stock options voluntarily fails to exercise such options, such failure does not constitute a forfeiture. (See 415.50(e)(6).)

Stock and Stock Options

A few commentators cited the requirement of 415.50(a)(3) of the proposed Standard which provides that the amount of the future payment must be capable of reasonable estimation, and expressed their opinion that the value of award of contractor stock that is to be distributed in a future period or periods should not be assigned to any period prior to payment because the amount of payment to the employee cannot be reasonably estimated before that time.

The Board believes that the compensation cost of stock or stock option plans should be measured by the quoted market price of the stock at the measurement date less the amount, if any, that the employee is required to pay. Further, the measurement date for both stock awards and stock option plans should be the first date on which are known both the number of shares to be distributed and the option price, if any. These views are embodied in Accounting Principles Board Opinion No. 25, Accounting for Stock Issued to Employees, which already must be followed by contractors for financial reporting.

If the market price of the stock on the date of distribution is used, the Government, in effect, would be sharing in financial risk taking with the contractor. Subsequent fluctuations of the price of the stock should not influence the measurement of the award. However, the Board recognized that the proposed Standard was not consistent with respect to the measurement of the cost of stock and stock option. Consequently, 415.50(e)(1) has been changed to provide for the measurement of the cost of stock to be at the measurement date rather than the time an obligation was deemed to have been incurred.

In order to further clarify the Board’s intent, 415.50(e) had been revised to provide that the measurement of the award of stock, stock options, or other assets as set forth in the Standard shall be deemed to be a reasonable measure of the amount of the future payment.

Two commentators stated that the cost of stock options should be based on the value of the options on the date they are exercised.

Similar to the reasoning expressed above, the Board does not believe that it would be appropriate to base the cost of stock options on the value prevailing at the date of exercise. Stock options which are awarded at a value which equals the market value of the stock would involve no cost under the provisions of the Standard. However, if the award of stock options were based on their value at the date exercised, a cost of the award would have to be recognized by the Government even though the contractor could purchase an appropriate number of shares at the time of the award to defray any cost resulting from future increases in the market value of the stock. The Board believes, therefore, that stock options should be a measured at the date on which both the option price and the number of shares are established (see 415.50(e)(1)).

Several commentators suggested that the requirement for prorating the cost of stock options over the period of future service and taking the present value of the prorated cost should be eliminated because the price of the stock is the present value of the stock price. The Board agrees with these commentators. Consequently, the requirement for discounting the cost of stock options has been eliminated from the Standard.

Transition Provision

Several commentators suggested that a transition provision be included in the Standard to amortize costs of deferred compensation accumulated in periods prior to the promulgation of the Standard, but not previously charged to contract costs. Several of these commentators suggested various methods to amortize the recovery of all prior deferred compensation on an accelerated basis. Among the methods suggested was to charge all such prior costs in the period that the Standard became effective or to charge such costs over the remaining work life of the employee or five years, whichever is shorter. However, one commentator recommended that the Board use a suspense account, as used in Cost Accounting Standard 408, Accounting for Cost of Compensated Personal Absence. The use of a suspense account would delay recognition of the cost of deferred compensation awarded before the effective date of the Standard.

The procurement regulations for costs of deferred compensation awarded prior to the effective date of the Standard generally provide that such costs will be allocable in the period in which they are paid to recipients. The Standard being promulgated today would not disturb the contractual provisions applicable to such prior awards. The provisions of this

Standard are applicable only to new awards of deferred compensation made on or after the date that the Standard becomes applicable to each contractor. The Board recognizes that there will be a minor budgetary increase required by the Government agencies until the prior deferred compensation awards are paid. However, for the majority of deferred compensation plans, the awards previously made will be paid out over a relatively short period of time, e.g., five years. Consequently, the Board believes that a transition provision is not necessary for the Standard being promulgated today.

Other Changes

The first illustration (415.60(a)) was changed to reflect the change in the provision regarding interest rates that are not fixed at the date of award. Other changes of a minor nature were made to various sections of the Standard for clarification.

Costs and Benefits

Section 719(g) of the Defense Production Act of 1950, as amended, provides “In promulgating such standard and major rules and regulations for the implementation of such standards, the Board shall take into account, and shall report to the Congress in the transmittal required by section 719(h)(3) hereof, the probable costs of implementation, including inflationary effects, if any, compared to the probable benefits, including advantages and improvements in the pricing, administration and settlement of contracts.”

Comments received in response to the *Federal Register* publication, as well as information obtained from contractors prior thereto, indicated that there would be minimal administrative costs entailed in complying with the Standard. One Government agency stated that additional administrative burden would be placed on the Government as a result of the conversion from a cash basis to the accrual method of accounting. The Board believes that any such additional administrative costs due to this conversion will be minimal. The Governmental agencies have always had the responsibility for reviewing the reasonableness of deferred compensation plans and evaluating the payments to assure that such payments coincide with the principal and interest provisions of the plan. The Board believes the main additional administrative cost involved is in reviewing the present value calculation and determining if the contract has incurred a valid obligation at the time the award is made.

Among the benefits which the Board believes will be derived from the use of this Standard is the assignment of the costs of deferred compensation to proper periods. Under the present regulations, the assignment of much of these costs is essentially on a cash basis. As a consequence, deferred compensation costs may have been incurred in much earlier periods than the periods in which they were recognized as incurred costs; in many cases, several years after the service has been rendered by the employee. Giving full consideration to all the relevant factors discussed herein, the Board believes the benefits to be derived from this Standard clearly outweigh any costs of implementation.

As required by section 719(g), the Board has evaluated the potential inflationary effect of this Standard. The Standard requires the use of present value techniques for the assignment of cost and incorporates a forfeiture provision with interest. The use of these techniques recognizes the time cost of money. In the long run, the cost to the Government should be essentially the same as that which would be incurred under a cash basis of accounting. For a majority of deferred compensation plans, moreover, the awards previously made will be paid out over a relatively short period of time, e.g., five years. The Board has concluded that there will be only a minor budgetary increase on the Government agencies until the prior deferred compensation awards are paid. Overall, however, any inflationary effect of this Standard will be minimal.

The Board expects that this Standard will become effective January 1, 1977.

There is also being published today an Amendment to Part 400, Definitions, to incorporate in that part terms defined in 415.30 of this Cost Accounting Standard.

Preamble B
Preamble to Revision of Section, 7-30-76 and 1-8-78

The following is the preamble to the revision of 415.80, published at 42 FR 18857, Apr. 11, 1977 and correctly reprinted at 43 FR 24821, June 8, 1978.

On July 30, 1976, a Cost Accounting Standard entitled Accounting for the Cost of Deferred Compensation was published in the *Federal Register* (41 FR 31797 et seq.). The effective date of the Standard was reserved in the July 30 publication. This final rule establishes the effective date.

Preambles to Cost Accounting Standard 416, Accounting for Insurance Costs

Preamble A
Preamble to Original Publication, 9-20-78

The following is the preamble to the original publication of Part 416, 43 FR 42239, Sept. 20, 1978.

(1)**Background**

Work on a potential standard on accounting for insurance costs was initiated for a number of reasons; these included

(1) differences between armed services procurement regulation (ASPR) provisions governing self-insurance and Financial Accounting Standards Board (FASB) statement No. 5,

(2) Armed Services Board of Contract Appeals (ASBCA) cases or other disputes related to insurance accounting, and

(3) knowledge of unresolved problems obtained by discussions with contractors and audit agencies.

A statement of issues related to accounting for insurance and a preliminary draft standard were developed by the staff and circulated to contractors, agencies, and others. Responses to these staff papers and to the *Federal Register* publications of October 5, 1977, and May 15, 1978, and information obtained in subsequent meetings with respondents and other interested persons were considered in developing the standard which is being promulgated today. Twenty-nine comments were received in response to the most recent *Federal Register* publication. All comments have been considered by the Board and those addressing areas of significance are discussed below, together with explanations of the changes made in the cost accounting standard being promulgated today from the proposal published in the *Federal Register* of May 15, 1978.

Ten respondents said that the proposed standard was acceptable as written, or they suggested only minor word changes.

The Board wishes to take this opportunity to express its appreciation for the helpful suggestions and constructive criticisms it has received, and for the time devoted to assisting the Board in this endeavor by the many organizations and individuals involved.

(2)**Coverage of Standard**

One respondent said that the standard should be limited in its application to significant problem areas rather than treating all insurance and insurance-related costs in a general fashion. As stated in the prefatory remarks which accompanied the May 15, 1978, *Federal Register* publication, in its research, the Board did not find that accounting practices depended upon the type of risk or insurance. Therefore this standard, applicable to the major problems, is also appropriate for all other insurance.

One respondent suggested that the standard deal with the subject of premiums paid to “captive” insurers. The Board reiterates its belief, which it stated in the May 15, 1978, *Federal Register* publication, that the technique for accounting for premium costs should not be influenced by questions of the reasonableness of the amounts paid. Consequently, no change in this regard has been made in the May 15, 1978, proposal.

(3)**Self-Insurance as a Cost**

Three respondents suggested that the proposed standard failed to properly distinguish between self-insurance and the absence of insurance. The Board recognizes that there may indeed be differences in the amount of planning involved, but there is no difference in the principle applicable to cost measurement. “Absence of insurance” is in fact one kind of self-insurance. The respondents said that a contractor who does not purchase insurance or set up a funded reserve to cover possible losses does not incur a cost and that, in such situations, actual losses are a part of entrepreneurial risk taking and should come directly from profit. For the reasons set forth below the Board does agree.

A contractor who acquires assets is exposed to two types of risks static risks and dynamic risks. Static risks are the risks which are inherent in the ownership of the assets; dynamic risks result from the decision to utilize the assets for the production of specific goods or services. Static risks are the same for all owners of similar assets in similar circumstances; e.g., the risk that property of a given type in a given location will be destroyed or damaged. Consequently, they are normally predictable by mathematical methods and can be insured against. Dynamic risks are a function of managerial judgment, e.g., whether a Proposed product can be produced for a profit. Dynamic risks are not normally predictable or insurable; they generate a profit or loss, depending on management’s ability to forecast costs and markets; they are the true entrepreneurial risks. Static risks, because they can be measured, predicted, and quantified, are properly subject to treatment as costs rather than as entrepreneurial risks.

From a cost accounting standpoint, the decision to purchase insurance or self-insure is not one of cost versus no cost. Rather, it is one of certainty versus uncertainty. A contractor who self insures will be subject to cost variations in any short time period as compared to one who purchases insurance but in the long run their costs should be substantially the same and their product or service must be priced to cover the same long-term cost.

Whether a contractor should be required to make deposits in a fund to provide for replacement of assets in the event of loss is not a consideration in determining the costs of self-insurance.

(4)**Accounting for Self-Insurance**

When the business entity purchases insurance coverage from an underwriter, the cost to the business -- for the static risk -- is the premium. When the business entity does not purchase insurance, the best method of assignment of cost to current activities is matter of possible disagreement.

A contractor who self-insures can recognize the cost of self-insurance for product pricing purposes in either of two ways:

> (1) By recognizing actual losses as they occur and allocating them to the products of some time period, usually the cost accounting period in which the loss occurred; or
>
> (2) by estimating the long-term average loss per time period and allocating it to the products of each time period. The second method is conceptually preferable in that it allocates the costs of all losses to the products of all time periods without regard to the particular chance distribution of actual losses among time periods.

The proposals which were published in the October 5, 1977, and May 15, 1978, *Federal Register* included criteria for selecting between the two approaches to recognizing the cost of self-insurance. A charge which would represent the projected average loss was required except in those situations where the actual losses in a cost accounting period could be expected to serve as a good representative of the long-term average loss for that period. The recognition of actual losses, rather than the use of a predetermined charge, would be expected where many units are exposed to loss and the maximum loss related to any one unit would be relatively small. Examples are the losses falling within the deductible portion of the automobile collision coverage for a fleet of vehicles, the deductible portions of property and casualty coverage where the size of the deductible is nominal in relation to the total exposure to risk for that coverage, and the worker’s compensation claims of a large work force. There would be little point in calculating a special self-insurance charge in such circumstances.

The Board has decided to retain the requirement for the use of a self-insurance charge, as contained in the *Federal Register* proposal. A reasonable assignment of cost should be made to products of each period in which there is exposure to the risk. The cost of each loss should be allocated to all work accomplished in the facility where it occurred (and successor facilities over the life of the enterprise, not just to the work of the day, month, or year in which the loss happened to occur. This can be accomplished by charging each period with a self-insurance charge which is equal to the projected average loss.

The standard also retains the provision of the *Federal Register* proposals which permitted the recognition of actual losses in those limited circumstances, as described above, in which the actual losses in any cost accounting period may be expected not to differ significantly from the projected average loss for that period.

Several respondents were concerned as to the possible consequences if a self-insurance charge were to be made, and, subsequently, actual losses differed substantially from the projected average loss. The self-insurance charge is, of necessity, and estimate. If the estimate is made in a reasonable and supportable manner, then the fact that actual losses depart significantly in either direction from the projected average loss is not a basis for adjusting the costs of that cost accounting period. However, the standard provides that contractor's actual loss experience shall be reviewed regularly and that self-insurance charges for subsequent periods shall reflect experience, as would premiums for purchased insurance. Similarly, if the situation were one in which it had been determined that actual losses were to be used because they were not expected to differ significantly from the projected average loss, and actual losses did, in fact, differ significantly, the actual losses would be nonetheless the measure of the cost.

(5)**Limitation on Self-Insurance Charge**

The proposals which were published in the *Federal Register* provided that the self-insurance charge plus insurance administration expenses could be equal to, but could not exceed, the cost of comparable purchased insurance plus the associated administration expenses. Several respondents saw this as a question of allowability. It is, however, not a limit on allowability; it permits the cost of comparable purchased insurance to be used as one means of estimating the projected average loss. The provision is intended to avoid the necessity of employing actuaries to perform computations which other actuaries have already performed for the insurance company in setting the premium. The standard has been modified to express this intention more clearly.

Other respondents were concerned that a company which calculated a self-insurance charge based on, say, a 5-year moving average of its own loss experience would encounter problems if it were to incur a large loss; this would raise its average above the cost of comparable purchased insurance and thereby preclude the recovery of the excess over time. Again, the Board intended the limitation to apply only where the cost of comparable purchased insurance is used as a convenient method of estimating the projected average loss. The standard specifically requires that the contractor's own loss experience be reviewed regularly and that self-insurance charges for future periods reflect such experience in the same manner as would purchased insurance. It should be noted that the cost of future insurance premiums would also be expected to reflect, to some degree, the unfavorable loss experience of the contractor.

Several respondents were concerned that the standard would require them to obtain quotations for insurance premiums for comparison with proposed self-insurance charges, and they questioned the feasibility of obtaining such quotations. The standard only requires such a quotation if the self-insurance charge is to be estimated thereby; it would not be required if, for example, the charge were to be based only on a projection of the contractor's own experience.

(6)**Terminology**

Several respondents suggested that in the definition of "actual cash value," the phrase "replacement cost less depreciation" could lead to confusion because the type of depreciation intended thereby was not clear. The phrase was intended to imply replacement of the destroyed asset with one in the same physical condition. The definition has been modified to make this intention clearer.

One respondent suggested that the provisions of 416.50(a)(1)(v) relative to "insurance coverage on retired lives" should be applicable to all types of insurance, rather than being limited to life insurance. The Board intended that this phrase provide for all types of insurance for retired persons. The term "retired lives" has accordingly been replaced by the term "retired persons."

Two respondents asked that the standard define or prescribe criteria for determining when a loss is considered to be "catastrophic" for purposes of home-office reinsurance agreements; they were concerned about after-the-fact disagreement as to whether a particular loss was "catastrophic" and thereby to be allocated in part to the home office, or "noncatastrophic" and to be absorbed entirely by the segment. The Board believes that what constitutes "catastrophic loss" depends on the individual circumstances of each contractor. The determination should be made at the time the internal loss-sharing policy is established and should be revised, as necessary, for changes in future circumstances. Obviously, a catastrophic loss would be one which would be very large in relation to the average loss per occurrence for that exposure, and losses of that magnitude would be expected to occur infrequently.

(7)**Premiums and Refunds**

The proposed standard provided that a premium refund or dividend would become an adjustment to the pro rata premium cost for the earliest cost accounting period in which the refund or dividend is actually or constructively received. However, the standard permitted the contractor the option of using estimated net premiums instead. One respondent suggested that the standard permit the shifting of adjustments to prior years for purposes of overhead analysis. This proposed change would not assure consistent measurement of cost; it has therefore not been adopted.

(8)**Direct Charging of Premiums**

Section 416.50(a)(1)(ii) provides that where insurance is purchased specifically for, and directly allocated to, a single final cost objective, the premiums need not be prorated. One respondent was concerned that if the final cost objective included requirements for two or more customers and the insurance premium were not prorated over the policy period, the cost might be charged only to the earliest units of production. They suggested that the provision be qualified by limiting it to only those final cost objectives which include requirements for a single customer. If the need for the insurance were to be occasioned by only one customer's requirements, the cost should be allocated to only that customer's units regardless of the production sequence. If the requirement is common to all customers' units, it should be allocated to all units.

The accounting principle here is the same as the one for specialized materials, which are charged directly to a final cost objective at the time of acquisition. If costs within a final cost objective, either for materials or for purchased insurance, were to be inappropriately related among the customers whose work is accumulated in the same cost objective, the problem would not be one of allocating costs to that cost objective. Rather it would be a problem of the method of analyzing costs within that final cost objective, a subject not being dealt with here.

(9)**Deposits and Reserves**

Insurance agreements frequently provide for substantial amounts to be held by the insurer for various contingencies. Such amounts may be negotiated in advance or may represent the unrefunded excess of premiums over losses; in either event they are not arrived at by actuarial computations of known risks. The contractor typically retains a significant amount of interest in, and control over, such funds. FASB statement No. 5 provides that amounts which do not represent transfers of risk from the insured to the insurer are deposits and should be accounted for as such. The proposed standard required that anything which would be a deposit under that statement be treated as a deposit for contract costing purposes. In addition, the standard required that "reserves" held by the insurer for the account of the contractor would be regarded as deposits unless they met stated criteria.

These special criteria included a prohibition against recapture of the reserve or fund so long as any beneficiary remained alive. Two commentators urged that this test be modified. The Board intended to assure that the cost had indeed been incurred, but there was no intention to tie up excess reserves for long periods. The provision has been modified accordingly.

One respondent pointed out that group insurance carriers in recent years have required that premium stabilization reserves be established on medium-size experience-rated programs to smooth the experience so it will be similar to a large group. He said that the contractor has no more right to these reserves than the monthly premium he pays on the policy. He therefore suggested that the reserves required by the insurance carrier should not be required to be treated as deposits unless these reserves are treated as deposits for financial statement purposes. The Board does not agree; such reserves are negotiated amounts and the contractor does in fact have some influence over them. Cost measurement is improved if these amounts are treated as deposits until settled.

Some respondents previously pointed out that where a contractor changes from a pay-as-you-go program for retired persons to a pre-funded program, or initially establishes a pre-funded program, a liability arises to those employees who have already retired. The respondent suggested that the standard provide a transition mechanism to deal with the newly recognized liability. Therefore, the standard which was proposed in the May 15, 1978 *Federal Register* provided and the standard being promulgated today provides that, for a transition from a pay-as-you-go plan to a terminal funded plan, or on the initial establishment of a terminal funded plan, the actuarial present value of benefits applicable to employees already retired shall be amortized over a period of 15 years.

Two respondents inquired as to the Board's reason for not providing a similar provision for transitions to fully prefunded level-premium or entry-age-normal plans. The actuarial premium computations for such plans implicitly allow for appropriate amortization of the liability for past service; therefore, an explicit provision for this purpose is unnecessary.

Two respondents asked for some liberalization of the 15-year amortization requirement; one suggested that the period be negotiable depending upon or the circumstances which occasioned the change, as for example, when a segment is abolished and many employees take immediate retirement. The 15-year period was chosen to be comparable to the amortization period for actuarial gains and losses contained in CAS 413. To permit the amortization period to be negotiated on a case-by-case basis would reduce uniformity. It might also create an incentive to make such changes at times when one of the parties could be expected to benefit. The Board does not accept the suggestion.

(10)**Relationship to Other Standards**

One respondent was concerned about the relationship of this standard to two other cost accounting standards, CAS No. 412, composition and measurement of pension cost, and CAS No. 415, accounting for costs of deferred compensation. The respondent was concerned especially about health insurance carried for retired employees of a contractor; he felt that there might be confusion as to whether such insurance should be considered a form of deferred compensation a part of a pension plan, or a part of an insurance program.

The Board believes that these standards provide ample criteria for determining which standard is applicable to any given cost. In particular, the question of whether a benefit, such as insurance provided to retired persons is an integral part of a pension plan and thereby governed by CAS No. 412 or is a part of an insurance program and thereby governed by CAS No. 416 is a question of fact in each given instance. Moreover, application of either standard to this element would result in substantially the same amounts of allocable cost.

(11)**Amount of a Loss**

The proposal which was published in the October 5, 1977, *Federal Register* provided, in part, that "the amount of an incurred loss shall be measured by the net book value of property destroyed." A number of respondents disagreed with this provision and suggested that the proper measure of the loss was "fair value," "replacement cost," "replacement cost, net of depreciation," and "replacement cost if replaced and net book value if not replaced." After considering these comments, the Board concluded that the measure of the loss should be the economic value of the asset destroyed, and that this value was best described as "actual cash value"; consequently the May 15, 1978, *Federal Register* proposal incorporated "actual cash value".

Three respondents have again asked that the standard recognize replacement cost as the measure of the loss on the grounds that the asset would probably be replaced with a new asset and that the cost of insurance premiums which would provide for replacement cost coverage would be allowable. The Board believes that the measure of the loss is the economic value of the asset destroyed, and this may bear little relationship to the economic value of the asset which is required to replace it. In this connection it should also be noted that CAS No. 409 requires the treatment of a gain on involuntary conversion of an asset as a recovery of past depreciation or alternatively, treatment as a reduction in the cost basis of the replacement asset. The Board has, accordingly, retained the use of "actual cash value" as one of the major measures of loss.

Contract audit agencies have reported that contractors sometimes charge the maximum potential loss for contract costing purposes but report a lesser amount for published financial statements; therefore, the proposed standard provided that where the amount of the loss is uncertain, the estimate of the loss shall be the amount includable in published financial statements. Three respondents suggested that this requirement be deleted because the amount reported for financial statement purposes might be too conservative. The Board continues to believe that the guidance contained in FASB statement No. 5 and interpretation No. 14 thereto permits an objective measure of the loss. The Board, therefore, retains the requirement.

One respondent was concerned about whether use of the term "incurred loss" in 416.50(a)(3) was intended to mean something other than an actual loss. The Board did not so intend; the term "incurred loss" has been eliminated.

Two respondents asked the Board to clarify the references to "publish financial statements" contained in the previously proposed standards. One of these respondents pointed out that not all published financial statements are necessarily prepared in accordance with generally accepted accounting principles; the other pointed out that a loss may be required to be reported in a published financial statement under conditions where it is not accruable therein as a liability. In order to clarify its intent, the Board has replaced the phrase "published financial statements," whenever it appeared in the proposed standard, with the phrase "statements prepared in accordance with generally accepted accounting principles" and the standard now refers to the amount which would be "includable as an accrued liability" in such statements.

(12)**Present Value of Future Losses**

One respondent objected to the requirement for discounting amounts of losses to be paid in the future at a rate different from that contained in existing procurement regulations. As it stated in the prefatory remarks which accompanied the May 15, 1978, *Federal Register* publication, the Board believes that the additional computational effort involved in using a rate for contract costing different from that required by the various States is not warranted. Where no rate is prescribed by a State, the use of the rate determined by the Secretary of the Treasury pursuant to Pub.L.92-41, 85 Stat. 97, as required by the standard, is consistent with the Board's requirement in CAS 415 to use that rate in discounting deferred compensation awards.

(13)**Allocation of Insurance Costs From a Home Office to Segments**

The October 5, 1977, proposal contained criteria for the allocation of insurance costs from a home office to segments. Various respondents questioned the need for such additional guidance on the grounds that the provisions of CAS 403 are adequate for this purpose. The Board concurred in this belief and omitted the related provisions from the May 15, 1978, proposal. Two respondents to that proposal suggested that the provisions of CAS 403 are too general and further guidance is needed to insure that such allocations will reflect significant differences in segment loss experience.

CAS 403 requires that home office expenses shall be allocated on the basis of the beneficial or casual relationship between supporting and receiving activities. Specifically, with respect to central payments or accruals made by a home office on behalf of its segments, CAS 403 requires that these shall be allocated directly to segments to the extent that they can be identified. CAS 403 provides further that payments or accruals which cannot be identified with individual segments are to be allocated by means of an allocation base representative of the factors on which the total payment is based. If there are significant differences in segment loss experience, then these differences would be identifiable and would be required by CAS 403 to be reflected in the allocation of the related home office premium cost or refund. The

Board therefore continues to believe that additional guidance for such allocations in this standard is not necessary.

(14)**Materiality of Losses and Insurance Administration Expenses**

The standard permits a contractor to recognize immaterial amounts of self-insured losses and insurance administration expenses as part of other expense categories rather than as "insurance expense." Two respondents were concerned that what is a "material" cost will be the subject of controversy.

The Board recognizes that some contractors may elect to purchase all of their insurance services from an insurance company or outside agencies; such services as claims processing or payment, risk analysis, loss prevention activities, etc. may be billed separately or included in the premium. Other contractors may elect to provide some or all of these services themselves. The standard recognizes this diversity of practice by stating, in 416.40, that the amount of the insurance cost is the sum of the projected average loss plus the insurance administration expenses.

Where a contractor purchases substantially all of its insurance service and the cost is included in the premium, the allocation of the costs of such services automatically follows the allocation of the premium. In such situations, if immaterial amounts of in-house costs, such as portions of various individuals' salaries or allocable space costs, are not explicitly recognized as insurance administration expenses, the accuracy of cost allocation is not significantly impaired. On the other hand, if a contractor establishes a claim processing department to process group insurance claims for a large work force, and the costs of such a group are material, then the Board believes that uniformity will be better served by requiring that such costs be allocated in the same manner as the costs of the related insurance. The Board believes that its previous pronouncements on the subject of materiality will provide sufficient guidance.

(15)**Renegotiation**

One respondent was concerned that contractors will have difficulty in following the standard while reporting to the Renegotiation Board, which is bound by law to allow items in accordance with chapter 1 of the Internal Revenue Code. This concern applies both to the election to account for refunds, dividends, and additional assessments on the basis of estimated net premiums, authorized in 416.50(a)(1)(vi), and the use of a self-insurance charge in lieu of the recognition of actual losses. In both instances the standard could result in the recognition, as contract cost, of amounts which would not be recognized for tax purposes.

Other cost accounting standard have required the selection of specific cost measurement techniques from among the many which might have been available under the Internal Revenue Code. The respondent suggested that the proposal on insurance is different in that it can result in the use of a method of contract cost accounting which is not permitted for tax accounting purposes.

The Board recognizes that the Renegotiation Board is indeed bound by law to recognize those elements of cost which are identified in the Internal Revenue Code. Measurement of the amounts of such costs to be recognized in any particular period, however should be done in accordance with the best available accounting technique where this standard recognizes a self-insurance charge in lieu of actual losses, the Renegotiation Board will also obtain a better measure of contractual (sic) profits by following the standard than by following (sic) the tax measurement. The Renegotiation Board, as a relevant Federal agency can arrange for the application of the standard as it has for various others which have required reconciliation between tax reporting and contract costing. No exemption is, therefore being made for renegotiation.

(16)**Records**

A contractor who elects to make a self-insurance charge should be expected to provide sufficient documentation to support the amount of the charge. In addition, the standard requires that the contractor's own loss experience be evaluated regularly. Finally, the standard requires the identification of losses to the segment in which they occur. While the cost of losses is already reflected in the contractor's formal accounting records, the data on loss frequency, amount, and location which may be necessary to comply with the proposed standard may not be a normal part of such accounting records. The “records” provision of the standard recognizes both the need for such data and the probable memorandum nature of the records. The requirement to maintain such records was contained in the October 5, 1977, proposal but was inadvertently omitted from the May 15, 1978, *Federal Register* proposal. It has been reinstated in the standard now being promulgated.

(17)**Illustrations**

One respondent suggested that the dollar amounts used in illustrations were unrealistic and would serve as guidelines for unrealistic rulings in practice. As the Board has stated on previous occasions, the use of dollar amounts in illustrations is intended to improve the understandability of the illustration. Such dollar amounts are not intended to establish criteria for use in actual situations.

(18)**Costs and Benefits**

The Board’s objective, with respect to uniformity, is to achieve comparability among entities operating under like circumstances. As applied to the measurement of insurance costs, there should be similar reported costs where there are similar exposures to risk. The Board has recognized the need to provide guidance on the determination of contract charges under self-insurance programs, especially under circumstances where the likelihood is that actual losses in a given period will differ materially from the long-term projected average. This standard will provide for increased uniformity in this field.

Consistency pertains to the use, by any one entity, of cost accounting practices which permit comparability of contract results under similar circumstances over periods of time. The decision whether to purchase insurance or to self insure is comparable to a make or buy decision. A change in the method of providing for the risks (which risks continue unchanged) is not a change in circumstances of the sort which should destroy comparability over time. This standard provides the basis for consistency in measuring insurance costs even when there are shifts between purchased insurance and self-insurance.

Only three respondents suggested a that the implementation costs of the standard would be excessive or would exceed the benefits. One of these foresaw increased administrative costs but did not offer any specifics. The concerns of the others appeared to lie primarily in two areas -- the lack of a definition of “materiality” in relation to insurance costs and the lack of specific procedural guidance in estimating a self-insurance charge. They therefore anticipated increased disagreements. The board has provided remarks about materiality in various public pronouncements. The Board believes that these comments are sufficient and that the concerns in this regard are unwarranted.

A self-insurance charge is an estimate, and the Board has consistently refrained from dictating detailed estimating procedures. A contractor must, of necessity, estimate many costs, and the degree of sophistication and complexity of the estimating process is a matter for discussion between the contractor and procurement and audit personnel.

The standard provides for several methods of recognizing the costs of self-insurance. First, the contractor may recognize actual losses in those situations in which the distribution of actual losses may be expected to not differ significantly from the projected average loss. This is a matter which should be readily determinable from or the nature of the exposure to risk; this will normally be expected where there are many units exposed to loss and the potential loss per unit is low in relation to the total exposure, as, for example, with worker’s compensation group insurance, and deductible portion of property and casualty insurance which is nominal in relation to the total exposure. In most such cases, contractors already charge actual losses, so no change will be necessary. Second, the contractor may use the premium cost of purchased insurance for comparable coverage as the basis for the self-insurance charge. This method would be appropriate when, for example, the contractor proposed to substantially increase a deductible provision for property and casualty insurance; he might propose to make a self-insurance charge equal to the premium reduction for the decreased coverage. Only in the event that either of these two methods is appropriate would the contractor have to resort to the third method, that of actuarial review of his own or industry experience to develop a self-insurance charge. Under these circumstances, the board believes that the majority of contractors will already be in compliance with the proposed standard and the costs of compliance for the remainder should not be significant. Therefore, the standard should have no significant inflationary impact.

Four respondents suggested that, if the majority of contractors would not have to change in order to comply with the standard, then the problems were not sufficient to justify the standard. The Board recognizes that, although the insurance problems resolved by this standard are likely to be encountered only by a minority of contractors, when they are encountered they are of substantial importance and their resolution in a uniform and consistent manner will be beneficial in contract costing.

In summary, the Board finds that this standard will increase the uniformity and consistency of measurement of the cost of insurance related to negotiated defense contracts. The standard will eliminate, or materially reduce, the problems listed in the Board's prefatory remarks with the May 15, 1978 publication. The Board finds that the costs of implementation will be slight and that there will be no inflationary impact

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There is also being published today an amendment to Part 400, definitions, to incorporate in that part terms defined in 416.30(a) of this cost accounting standard.

Preambles to Cost Accounting Standard 417, Cost of Money as an Element of the Cost of Capital Assets Under Construction

Preamble A
Preamble to Original Publication, 7-21-80

The following is the preamble to the original publication of Part 417, 45 FR 48574, July 21, 1980.

Summary

The Cost Accounting Standards Board is Promulgating Cost Accounting Standard No. 417, one of the series of Standards being issued pursuant to section 719 of the Defense Production Act of 1950, as amended (Pub.L.91-379, 50 U.S.C.App. 2168).

This Standard provides for the determination of an imputed cost of money to be included in the capitalized cost of acquisition of assets developed, fabricated or constructed for contractor's own use. Application of this Standard will provide increased uniformity in accounting for the acquisition costs of assets.

Effective Date

December 15, 1980.

Supplementary Information

(1)**Background**

Cost Accounting Standard (CAS) 417 being promulgated today is based on the same concept as CAS 414, which provides criteria for the measurement and allocation of the cost of money as a part of the cost of tangible and intangible capital assets. CAS 417 provides guidance for the measurement of the cost of money as an element of the cost of capital assets under construction. A proposed Standard on this topic, designated CAS 421, was published in the *Federal Register* on January 4, 1980. The Board received 36 letters of comment on that proposal and takes this opportunity to express its appreciation for the many helpful suggestions and constructive criticisms that were received.

(2)**Need for a Standard**

Most commentators favored the January 1980 proposal. Those who opposed it did so on the basis that they did not favor Standard No. 414 and do not favor any extension of the principle of that Standard. The Board, in promulgating CAS 414, provided for an important element of contract cost, that of the cost of money related to investment in facilities used in contract performance. Contractor investments committed to facilities not yet in service involve a similar economic cost. The Board believes that this Standard is an appropriate extension of the concept.

(3)**Proposals to Amend CAS 414**

A number of contractors suggested that instead of capitalizing cost of money, it should be treated as a current cost and therefore an amendment should be made to CAS 414 to recognize this cost on current contracts. The Board believes that capitalization of cost of money, in contrast to the immediate recognition of cost of money as a contract cost, will place such costs on the same basis as other construction costs and thus provide for the total cost of new assets to be charged to output of the periods when they are used in the production of goods and services.

(4)**Capitalization of Paid Interest**

The proposed Standard No. 421 provided an option to capitalize either cost of money computed in accordance with the provisions of the Standard or the amount capitalized for financial accounting and reporting purposes pursuant to FAS No.34. This option was offered in order to simplify the record-keeping procedures as it would have enabled the contractor to avoid a duplicate set of records -- one for financial accounting and the other for Government contract costing purposes.

A number of Government agencies disagreed with this approach. It was pointed out that no true compatibility exists between FAS No. 34 and the proposed CAS 421 since the former specifically prohibits recognition of any type of imputed interest cost for capitalization purposes. It was also stated that the option to elect between the two methods of capitalization in the proposed. CAS 421 would lead to inconsistent capitalization practices among contractors. Furthermore, it was pointed out that paid interest is an unallowable cost under pertinent procurement regulations. One major agency pointed out that if the Standard were to allow the choice as proposed, any contractor making the election to capitalize interest actually paid "* * * will have such costs disallowed when included in depreciation subsequently claimed as a cost under Government contracts. Such disallowance would effectively nullify the option.

In view of these comments by Government procurement agencies the Board has concluded that it would be futile at this time to proceed with the unrestricted option that permits capitalization of the amount capitalized for financial accounting and reporting purposes. The Standard, as promulgated, permits only capitalization of cost of money computed in accordance with the provisions of this Standard, or the amount used for financial reporting where it is not a materially different amount.

(5)**One-Year Limitation**

The proposed Standard required that in order to capitalize cost of money the construction or fabrication effort must be sustained at least for one year. This provision was based on the belief that administrative costs would typically be higher than the benefits to be expected from capitalization of cost of money for minor projects. Numerous commentators pointed out that irrespective of any administrative costs the cost of money could be quite material on a project lasting less than a year. The Board agrees with this view and has eliminated the restriction on the length of the construction period. The Board expects that contractors will apply the Standard where the benefits to be derived from improved cost measurement and allocation can be expected to outweigh the costs of implementation.

(6)**Computation of the Representative Investment Amount**

Some commentators questioned whether there are any constraints imposed on the methods that may be used for determining the "representative investment amount." The Standard specifies in 417.50(a)(ii) [previously designated as 421.50(e)] only that the method selected should give appropriate consideration to the "rate at which costs of construction are incurred."

The wording in illustration 417.60(a) and (b) has been changed to demonstrate more clearly when the use of beginning and ending balances of cost accounting period is appropriate. If major fluctuations are expected in the rate of cost incurrence, averaging of balances for shorter time periods, such as months, is appropriate.

(7)**Applicability**

The proposed Standard was to be applied only to those assets on which construction began after the Standard became applicable. Several commentators pointed out the desirability of immediate application with respect to all assets under construction.

The wording in 417.80 has been changed to extend the coverage to all the assets under construction at the time when the Standard is first applied by the contractor.

(8)**Costs and Benefits**

The Board recognizes that there are economic costs related to a contractor's investment in the construction period for assets subject to this Standard. The cost, even though imputed, is real and is relevant for the contract costing. It has heretofore not been part of contract costing. This Standard provides for its measurement and therefore will improve the quality of cost ascertainment on contracts where the assets are used.

Limitation on the option to use, for contract costing, the amounts capitalized under FAS 34 may impose certain administrative costs for some contractors. The Board is persuaded that these costs, in general, will not be significant, and they are surely out weighed by the benefit of more consistent contract cost measurement which will be derived from the operation of this Standard.

Title 4 CFR Chapter III is amended by adding a new Part 417 to read as follows:

Preambles to Cost Accounting Standard 418, Allocation of Direct and Indirect Costs

Preamble A
Preamble to Original Publication, 5-15-80

The following is the preamble to the original publication of Part 418, 45 FR 31932, May 15, 1980.

Summary

The Cost Accounting Standards Board is promulgating today Cost Accounting Standard (CAS) 418, Allocation of Direct and Indirect Costs. It is one of a series of Standards the Board is issuing pursuant to Section 719 of the Defense Production Act of 1950, as amended (Pub.L.91-379, 50 U.S.C.App. 2168).

CAS 418 requires that costs be consistently classified as direct or indirect establishes criteria for accumulating indirect costs in indirect cost pools and sets forth guidance on allocating indirect cost pools. These topics are central to the Board's mission to issue Standards to achieve uniformity and consistency in the cost accounting practices followed by defense contractors in estimating, accumulating and reporting costs of defense contracts.

Effective Date

September 20, 1980.

Supplementary Information:

(1) *Background*

The present Standard stems from two proposals, published in the *Federal Register* on March 16, 1978 and July 23, 1979. The March 16, 1978 publication consisted of five proposed Standards:

• CAS 417 -- Distinguishing Between Direct and Indirect Costs.

• CAS 418 -- Allocation of Service Center Costs.

• CAS 419 -- Allocation of Material-Related Overhead Costs.

• CAS 420 -- Allocation of Manufacturing, Engineering and Comparable Overhead Costs.

• CAS 421 -- Allocation of Indirect Costs.

The Board received letters from 86 commentators on the March 16, 1978 publication. As a result of the comments and additional research performed at 10 contractor locations, the number of proposed Standards was reduced to three in the July 23, 1979 publication:

• CAS 417 -- Distinguishing Between Direct and Indirect Costs. (Continued as a separate Standard.)

• CAS 418 -- Allocation of Indirect Cost Pools. (Consolidated original CAS 418 and original CAS 421.)

• CAS 419 -- Allocation of Overhead Costs of Productive Functions and Productive Activities. (Consolidated original CAS 419 and original CAS 420.)

The Board received comments from 59 interested parties in response to the July 23, 1979 publication. In addition, representatives of three industry associations supplemented their views orally. After consideration of all views, the Board has determined that it is appropriate to reduce the degree or specificity contained in the July 23, 1979 publication. As a consequence, the Board has been able to consolidate the three proposed Standards into the one Standard being promulgated today.

The Board wishes to take this opportunity to express its appreciation for the helpful suggestions and constructive criticisms it has received and for the time devoted to assisting the Board in this endeavor by the many organizations and individuals involved.

The following sections of these prefatory comments present the Board's views on the major issues raised by the commentators in response to the July 23, 1979 publication, and explains how these views are expressed in the current Standard.

(2) *Potential Impact on Contractor Accounting Systems*

Based on staff research and the comments received on prior proposals, the Board recognizes that this Standard may have a pervasive impact on contractor accounting systems. Because of this, the Board here and in the Standard is emphasizing the necessity to evaluate any perceived need for change in cost accounting practices in terms of materiality. The need to evaluate the materiality of a change in cost accounting practice applies to all provisions of the Standard. It is not limited to those particular provisions of the Standard in which materiality is mentioned for emphasis.

In resolving questions of materiality, the Board refers the parties to the criteria found in 4 CFR 331.71. These criteria take into consideration a variety of factors including the absolute dollar amount of costs involved, whether the costs are direct or indirect, the relationship of the costs to a particular contract, and the impact on Government funding. The Board is persuaded by the comments received on prior proposals that the use of these criteria will lead to an appropriate implementation of this Standard.

Some commentators urged the Board to define materiality in terms of the net effect on the cost of the totality of Government contracts in relation to the costs of implementing any accounting change pursuant to the Standard. The Board's materiality criteria recognize the need to consider the impact of cost accounting changes on the costs of individual contracts. To reduce the probable impact on the number of pools or changes in allocation bases required under the Standard however, the Board urges the parties to give special consideration to the net effect without ignoring any of the criteria specified in 331.71(a). The Board notes that a change which has the same directional impact on most Government contracts will be more material than one in which the directional impacts on the costs of various Government contracts are mixed.

Commentators were particularly concerned that the proposed Standards would require them to establish separate indirect cost pools or the change their allocation bases even where the allocation results would be substantially the same. The Board intends that the creation of additional indirect cost pools or change of allocation base will be required only if the changes will result in materially different allocations of cost.

In those circumstances in which a change in cost accounting practice is not required because of the present immateriality of impact, the Board notes that the impact may become material if circumstances should change. In this case acceptance of the existing system based on the immateriality of the impact would no longer pertain and the other criteria in the Standard would be applied to determine the appropriate accounting in the changed circumstances.

(3) *Definition of Direct Cost*

The Standard being promulgated today includes the Board's definition of direct cost (418.30(a)(2)). The Board originally issued the definition in 1972 as part of CAS 402, Consistency in Allocating Costs Incurred for the Same Purpose. Direct cost is defined as "any cost which is specifically identified with a particular final cost objective."

Commentators have criticized the definition on conceptual grounds and on the basis that it is contrary to common understanding of the term. They contend that a proper approach would recognize that all cost objectives have direct costs. Despite these criticisms, they indicate that no practical problems have resulted from the present definition.

The definition in CAS 402 was needed because of the type of consistency the Board requires in that Standard; that is, consistency in the allocation of direct and indirect costs with respect to final cost objectives. To broaden the definition of direct cost to say that all cost objectives have direct costs, would require a substantial change in CAS 402 in order to continue to achieve the purposes of that Standard.

Furthermore, the existing definition of direct cost facilitates description of allocation bases for the purposes of the Standard being promulgate today, as well as for other Standards. A change in the definition of direct costs as recommended by the commentators would necessitate a series of new definitions or lengthy descriptions of the types of direct cost which may be used for making up bases for allocating various indirect cost pools.

The Board believes that the present definition of direct cost serves useful purposes and has not created any problems. The Board, therefore, has decided to retain the present definition.

(4) Need For Written Policies

The purpose of proposed Standard 417 was to distinguish between direct and indirect costs. Criteria were established for direct costs. Generally, cost not meeting those criteria were to be classified as indirect.

Many commentators objected to the proposed Standard. They claimed that the criteria were too restrictive and would have required the reclassification from direct to indirect of many costs that have a close relationship to final cost objectives.

The Board has considered the statements made by the commentators and has studied other information it has developed. The Board has concluded that more flexibility should be allowed concerning the classification of costs as direct than was permitted by proposed CAS 417. That proposed Standard has been eliminated, and a requirement has been added to CAS 418 (418.40(a) and 418.50(a)(1)) for a written statement, in which each contractor must set forth his policies and practices for classifying costs as direct or indirect. The degree of detail that the statement should contain is a matter for decision by the contracting parties.

(5) Average And Pre-Established Direct Labor Rates

Proposed CAS 417 provided in 417.50(b) that: “The amount of cost to be allocated as a direct cost to final cost objectives may be determined on the basis of an average cost of the resources used or applied whenever the resources are interchangeable.” Several commentators believe that the requirement that resources be “interchangeable” before their costs could be averaged was too strict.

They said that “interchangeable” would be interpreted to mean “identical.” The principal concern was with average and pre-established direct labor rates. The commentators said that few labor resources are identical or even “productively interchangeable,” and that consequently the interchangeability criterion would cause the creation of many more labor rates.

The Board believes there is no conceptual difference between average and pre-established direct labor rates and labor-rate standards, which are governed by CAS 407. Use of Standard Costs for Direct Material and Direct Labor, Retention of interchangeability as the sole criterion for average and pre-established direct labor rates would impose stricter criteria for those rates than CAS 407 imposes for labor-rate standards. Accordingly, the Board decided to apply the same criteria to average and pre-established direct labor rates that are used in CAS 407 for labor-rate standards. The Standard now permits (418.50(a)(2)(B)) two kinds of groupings in addition to those based on the principle of interchangeability. Average or pre-established direct labor rates may be set for a group of employees who

(i) are interchangeable with respect to functions performed,

(ii) produce homogeneous output, or

(iii) form an integral team. The Board believes that these changes will avoid the problems foreseen by the commentators, and will be consistent with CAS 407.

(6) *Blanket Costs*

Blanket costs are labor or material costs accumulated in intermediate cost objectives and reallocated to final cost objectives as direct costs. Many commentators objected to 417.50(c) of the proposed CAS 417, which would have permitted such costs to be classified as direct only if they were allocated from an intermediate cost objective by a measure of resource consumption or a measure of output. Commentators said that this was too restrictive. They claimed that, since most bases used to distribute blanket costs are surrogates for rather than direct measures of resource consumption, proposed CAS 417 would have required most blanket costs to be classified as indirect costs.

The Board has considered the statements made by the commentators and has removed the requirement that blanket costs in order to be classified as direct costs be allocated on the basis of direct measures of consumption or output.

(7) 5 Percent Materiality Test

A number of commentators expressed concern that the requirements of the proposed CAS 418 and 419 would lead to unnecessary proliferation of indirect cost pools. The proposed Standards would have required that a separate pool be created only where a material difference in cost allocation would result. The Board had proposed a 5 percent materiality test for this purpose. This provision drew a large number of responses. Most commentators expressed serious reservations about the practicality of such a test.

The 5 percent materiality test was included in the proposed CAS 419 for the express purpose of alleviating the concern expressed by many commentators about unnecessary proliferation of overhead pools. Many of the same commentators suggested that rather than specifying an arbitrary percentage, the Standard should rely on the materiality provision already included in the Board's rules and regulations. The Standard being promulgated today refers to 331.71 which sets forth the materiality criteria for use in the application of all Standards.

(8) *Homogeneous Indirect Cost Pools*

Some commentators stated that the requirement of the proposed 418.50(a)(1) for a homogeneous indirect cost pool could result in unnecessary proliferation of indirect cost pools. A number of commentators also characterized the requirements of the proposed 418.50(a)(2) as being redundant or in conflict with the requirements of the proposed 418.50(a)(1). The Board has revised the proposed 418.50(a)(2) to parallel the language in proposed 418.50(a)(1) to preclude any conflict between the two paragraphs. The Board continues to believe that the requirement for homogeneous pools based on the concept beneficial or causal relationship is essential. The Board has emphasized in the revised 418.50(b)(2) that a pool also is deemed to be homogeneous if the separate allocation of the costs the dissimilar activities would not result in material differences. The Board has provided reference to its guidance on materiality contained in 331.71. Some commentators stated that the proposed 418.50(a)(3), which dealt with dissimilar use of resources, was too detailed a prescription and as such would lead to unnecessary proliferation of indirect cost pools. The Board was persuaded that the coverage of this level of detail is not necessary in the single revised Standard and accordingly has removed this requirement.

(9) *Hierarchy of Allocation Bases*

The proposed CAS 418 provided, in 418.50(b), a list of alternative allocation measures. The proposal would have required the use of the "best available" representation of resource consumption. Commentators questioned the need for an expressed preference and suggested a free choice among the allocation bases listed.

The Board believes that the establishment of the hierarchy is essential to assure that the basic concept of cost allocations as expressed by the Board in its statements of policy and in other Standards promulgated to date is achieved. The Board, however, made revisions to the Standard to lessen the concerns expressed by commentators. First, instead of the "best available representation of resource consumption," the Board has substituted therefor, in 418.50(e), the phrase "an appropriate measure of resource consumption". The Board also provided that the determination of which allocation measures to be used must be made on the basis of the individual circumstances, including the availability and quality of the data on which the potential measures are based.

(10) *Use of an Allocation Base Representative of the Activity Being Managed or Supervised*

A number of commentators questioned when the fourth step of the hierarchy in the proposed CAS 418, a base representative of the activity being managed or supervised, was to be used. The Standard has been revised to provide more clearly that the type of base is to be used only to allocate indirect cost pools containing significant amounts of the costs of management or supervision of activities involving direct labor or direct material cost, which are direct costs as defined by the Board. Therefore these cost pools are those which include the costs of managing and supervising final cost objectives or other cost objectives which are accounted for in a similar manner (those listed in 418.50(d)(3)). A base representative of the activity being managed or supervised is not suitable for the allocation of the costs of management or supervision of activities involving only indirect costs. For emphasis, the fourth step of the hierarchy has been set forth in a paragraph, 418.50(d), separate and apart from the first three steps of the hierarchy (418.50(e)) which should be used for allocating other indirect cost pools such as service centers.

(11) *Cross-Allocation Among Indirect Cost Pools*

The March 16, 1978 publication provided that only a cross-allocation or a sequential method could be used. In response to that proposal, commentators suggested that any method that would give the appropriate result be permitted.

The proposed CAS 418 in the July 23, 1979 publication provided for the use of any allocation method which would not result in significantly different allocation from that which would be obtained through using cross-allocation. A number of commentators stated that this provision was too complicated and costly. The Board continues to believe that the Standard should require the use of methods which would provide a reasonable representation of the beneficial or causal relationship existing among indirect cost pools. The Board was persuaded to broaden the test so that this relationship can be achieved by the use of any method that would approximate either the cross-allocation or the sequential method. Accordingly, revisions were made to 418.50(e)(4) to permit such alternative methods.

(12) *Casual Sales*

A number of commentators suggested that the proposed CAS 418 should specifically allow casual sales of services to be costed at other than full cost. Contractor definition and classification of sales as casual sales varies considerably among contractors. The Board has found no clear and consistent criteria for distinguishing these sales activities other than on the basis of materiality. The Board is of the opinion that for sales to be characterized as casual, they must be an immaterial part of the total activities of a cost pool. The Board expresses again its position that it will not deal with insignificant items of cost. Under the circumstances, the contracting parties can determine the acceptability of the costing methods to be used. Where sales represent a material part of the total activities of a cost pool, they cannot be deemed to be casual.

(13) *Definition of Productive Activity*

In the proposed CAS 419, the term “productive activity” was important to the determination of the number of pools which would be required for the allocation of overhead costs. Commentators expressed concern that the proposal would result in unnecessary proliferation of overhead pools because of the definition which was provided. The Standard has been revised to provide for the determination of the number of pools based on the concept of homogeneity.

(14) *Accounting for the Costs of Special Facilities*

The Standard being promulgated today does not provide guidance for accounting for the costs of special facilities (e.g., space chambers, wind tunnels, reactors) accumulated in separate indirect cost pools. These assets usually do not have application to all of the work of a business unit, and this circumstance creates difficult questions concerning the appropriate cost allocation techniques to be applied. The Board recognizes a need for particular attention to the accounting for the limited number of special facilities involved and has established a project in this area to review the cost allocation issues.

(15) *Degree of Specialty in Proposed CAS 419*

As discussed previously, a large number of commentators expressed concern that the definition of “productive activity” and the 5 percent materiality test which were included in the proposed CAS 419 could result in unnecessary proliferation of overhead pools. A large number of commentators were also critical of the proposed CAS 419 because in their opinion it provided too great a degree of specificity. The requirements relative to separate overhead pools, the specific reference to the treatment of costs of special facilities, and the treatment of purchased labor and overtime premiums and shift differentials in allocation bases were considered by many commentators to be too procedural and detailed.

The Board was of the opinion that some degree of specificity would be desirable and necessary in this area to minimize differing interpretations by the contracting parties. In light of the number of criticisms on the specificity of the proposed CAS 419, however, the Board decided to remove the references to those terms and provisions. The elimination of these terms and provisions does not reflect a change in position concerning the appropriate accounting for the costs involved. Rather, in consolidating the proposed 417, 418 and 419 into a single CAS 418 being promulgated today, the Board is providing a more general Standard incorporating the basic concepts of cost allocation previously established in the Board's Restatement of Objectives, Policies and Concepts.

(16) *Evaluation of Benefits and Costs*

Many commentators asserted that the costs of implementing the proposed Standards would outweigh the benefits that would be derived from here. They were concerned that the Standards would require significant accounting changes because of the perceived detailed prescriptions in the Standard and for the potential implementation of changes in cost accounting practices where no material cost impact would result. The Board believes the Standard being promulgated today will significantly reduce the anticipated costs of implementation as compared with the prior proposals. This has been accomplished by reducing the degree of specificity and by emphasizing the importance of materiality in determining when changes in cost accounting practices are required. These revisions should minimize the potential for excessive proliferation of cost pools. The Board notes that this Standard is applicable to a significant percentage of the total costs of negotiated defense contracts. The provisions of this Standard will provide great assurance of uniformity and consistency in accounting for these costs than was previously available. The Board believes that the benefits of the increased uniformity and consistency in cost allocation which will result from the Standard outweigh the costs of implementation.

Title 4 CFR Chapter III is amended by adding a new Part 418 to read as follows:

Preambles to Cost Accounting Standard 420, Accounting for Independent Research and Development Costs and Bid and Proposal Costs

Preamble A
Preamble to Original Publication, 9-25-79

The following is the preamble to the original publication of Part 420, 44 FR 55127, Sept. 25, 1979.

(1) *Background*

Work on the development of this Standard was initiated based on the General Accounting Office Report on the Feasibility of Applying Uniform Cost Accounting Standards to Negotiated Defense Contracts. The report referenced problem areas concerned with

(1) the allocation of incurred costs to IR&D and B&P projects,

(2) the allocation of such costs to cost objectives, and

(3) the definition of IR&D and B&P work tasks. Over years, Congress has continued to press its concern about the large amount of money reimbursed to defense contractors in the area of IR&D and B&P. In 1978, the last report year, the 90 companies large enough to have advance IR&D and B&P agreements with the Government were reimbursed by the Government about $1.2 billion for this effort.

Early research conducted by the Board was directed towards obtaining information on the views, policies, definitions, accounting practices and administrative procedures followed the management of IR&D and B&P activities by the defense industry, commercial companies, and Government agencies. This research was accomplished by means of questionnaires sent to 65 defense contractors and 10 commercial companies; review of General Accounting Office reports congressional hearings, Armed Services Board of Contract Appeals cases, various technical papers; and discussion with several Government agencies. Also included in the research were evaluations of recommendations made by a study group of the Commission on Government Procurement covering IR&D costs and a Statement concerning the Accounting for Research and Development Costs (FAS No. 2) issued by the Financial Accounting Standards Board.

A research draft was distributed on April 29, 1977, to obtain comments. Comments were received from 73 respondents. The Board after considering the comments published a proposed Standard for comment in the *Federal Register* on July 28, 1978. Sixty-three commentators responded to this publication. Because significant revisions appeared appropriate after evaluation of the comments, the Board decided to publish the proposed Standard for comments a second time in the *Federal Register* on May 25, 1979. 46 responses were received from individual companies, Government agencies, professional associations, public accounting firms, industry associations and others. The Board takes this opportunity to express its appreciation for the helpful suggestions and criticisms which have been furnished. The comments furnished by organizations and individuals have resulted in a number of changes in the Standard. The comments below summarize the issues discussed in connection with both proposed Standards and explains major changes which have been made to the earlier proposals. This Standard was previously published as CAS 422. It has been renumbered to CAS 420 to accommodate changes in the work plans of the Board.

(2) *Need for a Standard*

Many commentators questioned the need for a separate Standard for IR&D and B&P. Almost all of those who raised this issue cited the other allocation Standards, 403 and 410 and proposed indirect cost Standards 417, 418 and 419 and stated that the allocation practices set forth in those Standards adequately cover the allocation of IR&D and B&P costs.

Appendix III of the General Accounting Office Cost Accounting Standards-feasibility study is entitled “Problem Areas in the Assignment of Government Contract Costs.” It contained a tabulation of problem areas. The subject of “IR&D/B&P/Economic Planning” represented the highest number of reported problems of the 23 subjects on the list. On that list also were the subjects of “allocation”, “direct vs. indirect”, depreciation, etc. An analysis of disclosure statements in the Cost Accounting Standards Board’s data bank showed a considerable divergence in accounting practices followed by Government contractors. For example, the disclosure statements revealed that contractors allocated IR&D and B&P cost pools to final cost objectives by means of such allocation bases as sales, cost of sales cost input, modified cost input, modified cost of sales, direct labor dollars man-hours, and headcount. Staff research which involved visits with over 50 defense contractors and several Government agencies confirmed this divergence of practice. DoD and NASA have similar procurement regulations covering the accounting for these costs, but other agency regulations vary substantially and, as a result, a variety of accounting practices are in use for IR&D and B&P costs.

This Standard will provide for increased uniformity and consistency of allocation among segments based on the beneficial or casual relationship between the IR&D and B&P costs and segments of a company.

The Standard will also provide for increased uniformity in the composition of these costs within contractor’s segments, especially in the segments identified as central research laboratories.

The Board recognizes that the already promulgated allocation Standards 403 and 410, and the proposed indirect cost Standards 417, 418 and 419 have general requirements which will be consistent with the requirements of this Standard. Standards 403 and 410, however, would each have to be amended to include the specific accounting provisions of this Standard. IR&D and B&P cost; are an important element of the contractor’s total costs allocated to its final cost objectives. The Board believes that the accounting practices for these costs should be centralized in a single Standard in order to clearly provide the proper guidance for their allocation to cost objectives. Neither the contractor nor the Government should have to search out the accounting requirements in various Standards in order to obtain this guidance. By providing this guidance in a single source the Board believes that the administrative and accounting complexities for these costs will be reduced for both the contractor and the Government.

(3) *Definitions*

Several commentators continue to raise questions regarding the definitions. The comments generally requested definitions to clarify the accounting for “B&P administrative costs” and “technical” effort associated with IR&D costs. The words requested to be included in the Definition of Bid and Proposal Costs are: “B&P administrative costs, when separately identified and classified B&P costs in accordance with the contractor’s normal accounting practice, are not considered B&P costs for the purpose of this Standard.” Commentators also suggested that the word “technical” be included in the definition of IR&D effort so as to determine the nature of the costs allocable IR&D effort. The commentators wanted these changes as an aid in determining what costs should be charged directly to these projects.

The definitions of IR&D costs and B&P costs are not intended to include allocation requirements. Guidance allocation is included in other sections of the Standard. Section 420.50(a)(1) of the Standard provides guidance on what costs are to be charged directly to IR&D and B&P projects. Therefore, the requested additions are not necessary.

(4) *Accumulation of IR&D Costs and B&P Costs by Project*

A few respondents commented on the requirement in the Standard to account for IR&D and B&P costs by project. One commentator stated that he believed that most contractors who will be required to comply with this requirement have the capability to accumulate IR&D and B&P costs by individual projects. The commentator noted that the Board has properly considered the concept of materiality by permitting the combining of the costs of IR&D or B&P efforts of small dollar value in a single project for inclusion in the appropriate pool without the necessity of separate cost identification.

One commentator stated that even though it accounted for IR&D and B&P costs by project, it was certain that there were small contractors who did not have systems which would be sophisticated enough to keep costs in such a way. The staff of the Board visited in excess of 50 contractors in conducting research on this project. In every instance contractors accumulated the costs of IR&D and B&P by project. The Board believes that, with the materiality consideration provided in 420.50(c), the requirement to accumulate IR&D and B&P costs by project should be retained. In further consideration of the materiality concept, overhead costs and other indirect costs allocable to individual IR&D and B&P projects need not be recorded by individual project if subsequent pool allocations of these costs yield the same results as if they had been so recorded.

It was noted that the reference to “clearly and exclusively” as the criteria for allocating costs directly to IR&D and B&P projects makes a more limited requirement for this allocation than is provided for in proposed Standard 417, Distinguishing between Direct and Indirect

Costs. The Board’s intent is to be consistent in the accounting specified for costs incurred in like circumstances, and the use of the terms “clearly and exclusively” in the fundamental requirement was intended to provide this consistent treatment. It was pointed out that the same test which is included in proposed Standard 417 is only one of three tests for making the determination of what cost shall be accounted for as a direct cost.

The Board agrees that the use of “clearly and exclusively” in this Standard without the use of the complete set of criteria would have placed a limitation on what costs should be allocated directly to IR&D and B&P projects, and this would be more restrictive than the requirement contained in proposed Standard 417. The Board believes that it would be inappropriate to restate in CAS 420 the entire fundamental requirement for the proposed Standard on Distinguishing Between Direct and Indirect Costs. It believes further that the techniques for application, 420.50(a)(1) adequately establish the allocation requirement sought for these costs. For all of these reasons, the fundamental requirement paragraph has been revised accordingly.

(5) *Allocation of Business Unit G&A Expenses to IR&D and B&P Costs*

One commentator raised the question of allocating business unit general and administrative expenses to IR&D and B&P costs. This commentator made the point that accounting for this effort by project is tantamount to treating it as a final cost objective and therefore it should have allocated to it a business unit's general and administrative expenses. Both proposals published in the *Federal Register*, July 28, 1978 and May 25, 1979, contained the provision that business unit G&A expenses should not be allocated to IR&D and B&P costs. A majority of respondents to the July 28, 1978 proposal commented favorably on that section of the proposal.

Many of these commentators in replying to an earlier draft of the Standard, which had provided for allocating G&A expenses to IR&D and B&P costs, had expressed the view that IR&D and B&P costs were of general benefit to a segment or a company and therefore similar in nature to G&A expenses. They believed that since such costs were similar in nature to G&A expenses they should not receive an allocation of G&A expenses. The Board was persuaded (sic) by this view and for that reason the Standard retains the provisions for not allocating business unit general and administrative expenses to IR&D and B&P costs.

Several commentators directed remarks to accounting for IR&D and B&P costs at organizations of a company that perform as research laboratories. Some stated the belief that G&A expenses of such segments should be allocated to its IR&D costs if the segment is a "central research laboratory." Others, including an industry association, were of the opinion that a research laboratory should be treated as any other segment and its IR&D costs should not receive an allocation of G&A expenses.

The Board for some time has been persuaded that the nature of IR&D and B&P effort is such that it should not receive an allocation of business unit G&A expenses. Nothing in the comments received from the three commentators seeking to have special IR&D or B&P costs accounted for differently than all other IR&D or B&P costs provided the Board with criteria for setting up different accounting or treatment. The Board believes that such costs should not receive an allocation of business unit G&A expenses and the Standard so provides.

(6) *Allocation of G&A Expenses Work Performed by One Segment for Another Segment or Home Office*

Many contractors in responding to the proposed Standard objected to the provisions in the proposed Standard which required that G&A expenses be allocated to work performed by one segment for another segment or home office. Some stated the belief that 420.50(c) was inconsistent with 420.40(c) in the proposed Standard, which provided that business unit G&A expenses shall not be allocated to IR&D and B&P projects. The Board sees no inconsistency. If the work performed is an IR&D or B&P project of the performing segment and also benefits the receiving segment, it must be transferred to the home office without an allocation of business unit G&A expenses in accordance with 420.50(f)(1). It will then be allocated to benefiting segments pursuant to 420.50(e). If the work is not IR&D or B&P effort of the performing segment the allocation of general and administrative expenses will be governed CAS 410.

Commentators also expressed concern that including G&A expenses in the costs of IR&D or B&P work performed by one segment for another might push total IR&D and B&P costs above the negotiated ceilings. They contended that this would make the excess cost unrecoverable from any source. Furthermore, by increasing the allocated cost of a given research effort, less research would be financed by a given research allowance.

The Board recognizes these objections, but believes that the question of whether and how G&A expenses should be allocated must be decided on other grounds. The Board believes that if work is performed at a segment and sold to or transferred to another segment directly, it should be considered a final cost objective of the performing segment. Allocating G&A expenses to such work would be consistent with CAS 410 which provides for allocating general and administrative expenses to stock or product inventory as well as to final cost objectives of the segment. This accounting treatment is consistent with previous Standards and proposals which have dealt with segments as separate units, each with their own final cost objectives. It is also consistent with proposed Standard 419.

Some commentators agreed with the concept of allocating G&A expenses to work which is part of a segment's normal product or service and therefore a final cost objective of the segment, but disagreed with the use of the phrase "project in which the performing segment has an interest." The commentators believed that the phrase was not sufficiently objective to be properly administered.

The Board recognizes that there are valid objections to the use of the descriptive phrase "has an interest (in)." This paragraph (now numbered 420.50(d)) has been revised to provide that work performed by one segment for another shall not be treated as IR&D or B&P effort of the performing segment unless the work is also part of an IR&D or B&P project of the performing segment.

(7) *Allocation of Home Office IR&D and B&P Cost Pools*

In being responsive to comments on earlier proposals, the May 1979 proposal provided for allocation of IR&D or B&P costs to a limited group of segments or to specific segments where such identification could be established between specific work and benefiting or causing segments. At the urging of most commentators, the identification requirements and the base for allocation were stated as general requirements in the proposal. Two commentators suggested language to provide that a clear and exclusive identification of work to a specific segment(s) should be required to permit this type of allocation. The Board believes that such a change would be unduly restrictive.

The Board is aware that usually not all IR&D or B&P costs could be identified to specific segments. The Board believes that such residual home office IR&D and B&P costs should be allocated on a base which is representative of the total activity of segments being managed. Cost input therefore was selected in the May 1979 proposal as a good representation of total activity.

Several commentators objected to the use of only one base. As stated previously, the Board is seeking a base that will represent the total activity of the segments reporting to the home office. It does not with the Standard to be needlessly restrictive. The base used to allocate the home office residual expense under CAS 403 is a base representing total activity. A majority of commentators to the proposed Standard suggested that, in lieu of cost input as the base, the company be allowed to allocate residual home office IR&D and B&P costs on the same base it now uses to allocate home office residual expense under CAS 403. The Standard has been revised to provide for that method of allocation, but the amount of IR&D and B&P costs so allocated is not to be added to the residual pool to determine whether use of the 3 factor formula in CAS 403 is required.

One commentator recommended that "* * * all IR&D costs be pooled at the home office level and then allocated in a consistent and uniform manner over the entire business. This policy would serve as a deterrent to contractors undertaking frivolous IR&D projects or projects of questionable military relevance in divisions where costs would otherwise be borne primarily by the Government."

Early in its research the Staff considered this approach to determine if it best represented the beneficial or causal relationship between the IR&D and B&P costs and final cost objectives. The staff found that it was not unusual to find IR&D or B&P efforts which were clearly of benefit to or caused by a single segment or a group of segments within a company. For that reason the Board believes that the beneficial or causal relationship between IR&D and B&P costs and final cost objectives can be more effectively identified at organization levels below the one encompassing the entire company.

There may be situations where the beneficial or causal relationship can best be reflected by pooling and allocating on a general basis over the entire company. In such cases, the method suggested by this commentator would be called for under the Standard.

(8) *Allocation of Segment IR&D and B&P Cost Pools*

Several commentators suggested that where IR&D or B&P effort is determined to be of benefit to or caused by more than one segment, direct transfer at IR&D or B&P costs between segments should be permitted. The Standard being promulgated today continues to provide that any IR&D and B&P project which benefits more than one segment of the organization shall have its costs transferred to the home office for allocation among benefiting segments. To avoid unnecessary recordkeeping, however, the Board has provided that the transfer can be recorded directly in the accounts of the other segments if the resulting allocation is substantially the same as it would be if passed through the home office.

One commentator was concerned that there would be confusion as to the home office to which such costs would be transferred. The suggestion was made that the Standard provide that such costs be transferred to an intermediate home office. The Board believes that such an addition is not needed. The definitions of both home office and segment in 4 CFR Part 400 make clear that the transfer of costs under this provision of the Standard could be only to the home office most immediate to the segment.

(9) *Allocation of IR&D and B&P Costs to Product Lines*

Many commentators to the proposed Standard felt strongly in their responses that the allocation of IR&D or B&P costs to product lines would be impractical. Most commentators believed that the arguments and disagreements between the parties as to what constitutes a Product Line would outweigh any possible benefits that could be received from the direct identification of cost objectives that would be achieved by such provision.

In visits made by the Staff with several commentators subsequent to the publication of the proposed Standard, the question of using the same definition of Product Line used by the Federal Trade Commission (FTC) in its Line of Business Reporting was discussed. All the commentators were of the opinion that this definition would not be suitable in determining guidance for the allocation of segment IR&D and B&P costs to product lines. The primary concern of the commentators was that the FTC definition establishes product lines within a company that cross over several segments of the company. Consequently, contractors would face considerable difficulties in attempting to allocate IR&D and B&P costs in accordance with the FTC definition.

In further considering the question of defining Product Line, the comments on the proposal by the Department of Defense were particularly pertinent. Those comments stated that “In the case of product lines, our experience with the cost principle that was in the ASPR prior to 1970 convinced us that it is not practicable to define product line. In our attempt to designate product lines, and relate development costs to them, we found ourselves in endless arguments with contractors. In our experience we found that contractors and contracting officers could seldom agree on product lines and usually resolved the matter by describing a product like that included all work in the plant. If the product line allocation provision remains in the proposed Standard, we expect these experiences will again be repeated.”

The Board has considered the problems connected with the lack of definition and the administrative effort that would accompany any attempt to allocate the costs of individual IR&D or B&P projects to product lines. These provisions are not included in the Standard being promulgated today.

(10) *Selection of Allocation Base for Segment IR&D and B&P Costs*

The majority of commentators objected to the use of only the total cost input base for the allocation of a segment’s IR&D and B&P costs to final cost objectives. Most of these commentators suggested the Standard be revised to provide that IR&D and B&P costs be allocated to final cost objectives of the business units using the same base that is used to allocate the business unit G&A expense to final cost objectives.

The Board agrees that the beneficial or causal relationship between IR&D and B&P costs and final cost objectives is similar to the relationship between G&A expenses and final cost objectives. After considering the many comments regarding this part of the Standard, it has been revised and the allocation requirement now states that the IR&D and B&P cost pools shall be allocated to final cost objectives of the business unit using the same base that the business unit uses to allocate its G&A expenses.

(11) *Deferral of Development Costs*

The proposed Standard provided for the deferral of the cost of IR&D effort which met specific criteria, and established criteria for the identification of such costs. It also noted that the composition of the costs and the allocation procedure for such costs would require further research before establishing an accounting Standard Reaction to this provision in the proposal has been extensive and varied.

Several respondents to the May 25, 1979, proposed Standard noted that the Board should not allow the allocation of deferred development costs as this would be in conflict with the Financial Accounting Standards Board's (FASB) Statement No. 2, Accounting for Research and Development Costs. One of these pointed out that the FASB in its statement set forth the position that for financial reporting purposes research and development costs should be charged as a current period cost. Another stated that his company did not and would not defer such expenses, even if the Standard permitted such action.

Although the Board has always considered the FASB to be an authoritative body and considers its statements when promulgating its own, the FASB's concern is with external financial reporting, not with contract costing. FAS Statement No. 2 therefore is not determinative for contract costing and pricing purposes.

A few commentators agreed with the provision as stated in the proposal and urged its adoption without modification. One industry commentator said, "We agree with the language as stated and believe the criteria is conceptually sound so as to permit implementation by the acquisition agencies. We do not feel that further research on behalf of the CAS Staff is necessary, and (we) encourage this language be contained in the promulgated standard as written."

The majority of commentators expressed approval of the concept provided that the act of deferral should be at the sole option and discretion of the contractor. The Board has concluded that this would be inappropriate, however, because it would not be consonant with the uniformity and consistency objectives of Pub.L.91-379.

A broad spectrum of commentators suggested that the Board not change the status quo of this category of costs of deferred development in this Standard. They suggested that the entire subject, including requirements for allocating deferred costs, should be treated in one Standard. The commentators who made this suggestion represented industry, a professional accounting association, and a Government agency.

The Board continues to believe that there are different types of development costs and that objective criteria can probably be found to identify such costs. It believes, also that an important aspect of this question is the accounting treatment, including the amortization and allocation of these costs. The existence and the allocability of

deferred IR&D and deferred development costs are recognized to some degree today in various procurement regulations. Current proposals in the Federal Acquisition Regulations (FAR) increase the recognition and allowability of such costs.

Many commentators criticized the criteria listed in the May 1979 proposed Standard, but were unable to suggest other criteria that would provide the objective tests the Board believes necessary for a Standard on this subject. The Board will undertake research on a project to determine the feasibility of a Standard which will identify and provide for the accounting treatment of deferred development costs. In the interim, the agencies may continue to exercise their authority to identify and allocate such costs. To that end the Standard covers these costs in 420.40(f)(2) which provides: "IR&D costs incurred in a cost accounting period shall not be assigned to any other cost accounting period, except as may be permitted pursuant to provisions of existing laws, regulations, and other controlling factors."

(12) *Transition From the Use of a Cost of Sales Base to a Cost Input Base*

On (sic) commentator noted that the Standard was silent in regard to its application when a contractor was required to convert his accounting system from the use of a cost of sales base to the use of a cost input base for the allocation of a segment's IR&D and B&P costs. This commentator suggested that the Standard include a provision such as was incorporated in the appendix of CAS 410 which provided the accounting to be followed during the transition period. The Board does not believe that this Standard warrants the additional complexity of a transition method. The Board notes that the contractor and the Government may negotiate an equitable adjustment for this change as provided in 331.50(a)(4)(A) of the Board's regulations.

(13) *Effective Date of Standard*

One commentator stated that the promulgation of this Standard would require reorientation of both contractor and Government personnel who are charged with the accounting and administration of contracts. The commentator noted that the Standard should provide for an extended implementation period. The primary concern of the commentator was directed towards the negotiation of advance agreements for these costs, and the impact of this Standard on such advance agreements. The Board expects that this Standard will become effective on March 15, 1980. However, to provide adequate lead time for its applicability the Standard provides that it shall be followed by contractors as of the start of the second fiscal year beginning after the receipt of a contract to which this Cost Accounting Standard is applicable.

(14) *Cost and Benefit*

The Board in taking into account the cost and benefits of the Standard being promulgated today was especially mindful of the significance, both in nature and amount, of the category of costs being considered here. In comments received regarding the proposed Standard published in the *Federal Register*, some commentators offered opinions as to the cost of implementing the Standard. One commentator stated the proposed Standard will have minimal impact on administrative costs. Some commentators state that they had not estimated the amount of increased administrative costs which would result from implementation of this Standard. Based on their experience with previously promulgated Standards, these costs depend on the interpretation and implementation requirements used by the auditors and procurement officials responsible for the administration of Cost Accounting Standards. Two commentators provided large cost estimates for implementing this Standard. One commentator based its estimate on the requirement to identify IR&D or B&P projects to product lines. This requirement has been eliminated from the Standard being promulgated.

As mentioned earlier, Congress continues to express its concern regarding the large reimbursements defense contractors receive in order to carry on their IR&D and B&P efforts. (About $1.2 billion in 1978). As many commentators pointed out, this area of cost (especially IR&D) receives much attention through the medium of advance agreements. These advance agreements contain some accounting ground rules to be followed by the contractor in determining what constitutes IR&D and B&P costs. The current acquisition regulations, however, allow significant flexibility in determining costs for these projects. One the benefits of the Standard is that provides increased uniformity and consistency in determining how IR&D and B&P costs are constituted, and how these incurred costs should be a located to cost objectives.

(15) *Amendments*

In addition to the promulgation of CFR Part 420, related amendments 4 CFR Part 400 and to Standards CFR Part 403 and 4 CFR Part 410 being promulgated.

Part II
Preambles to the Related Rules and Regulations Published by the Cost

Accounting Standards Board

Preambles to Part 331, Contract Coverage

Preamble A
Preamble to Original Publication, 2-29-72

The material set forth below is the preamble to the original publication of Part 331, February 29, 1972, at 37 FR 4139. For the preamble to the republication of Part 331 (November 7, 1973, 38 FR 37025), see preamble D of this Supplement. Portions of this preamble relating to Parts 351, 400, and 401 have been omitted; they can be found in the supplements to their respective parts. This preamble to the publication of February 29, 1972, is included as part of the administrative history of Part 331.

General comments. The purpose of the regulations promulgated today by the Cost Accounting Standards Board is to implement section 719 of the Defense Production Act of 1950, as amended, 50 U.S.C.App. 2168, which provides for development of Cost Accounting Standards to be used in connection with negotiated national defense contracts and for disclosure of cost accounting practices to be used in such contracts. The Board believes the materials being promulgated today constitute a significant initial step toward accomplishing one of its major objectives -- improved cost accounting and the proper determination of the cost of negotiated defense contracts. The regulations spell out contract coverage (Part 331), disclosure requirements (Part 351), a compilation of Definitions (Part 400), and two Cost Accounting Standards, one calling for consistency in estimating, accumulating, and reporting costs (Part 401), and the other calling for consistency in allocating costs incurred for the same purpose (Part 402).

Development of the material being promulgated today began many months ago with extensive research. It included examining publications on the subject, conferring with knowledgeable, representatives of various Government agencies, Government contractors, industry association, and professional accounting associations, and identifying and considering all available viewpoints. From this research, the initial versions of the material now being published were developed. As a part of the continuing research effort, these initial drafts were sent to 81 agencies, associations, and Government contractors which had expressed interest in assisting the Board in its work, and their comments were solicited. Some national defense contractors field-tested the material to see how it would apply to and affect their operations and advised the Board of their findings. In each step of the research process, the Board and its staff have urged and received active participation and assistance by Government, industry, and accounting organizations. Their cooperative efforts contributed in large measure to the exposure draft published in the December 30, 1971, *Federal Register* for comment.

To better assure that all who might want to comment had an opportunity to do so, the Board supplemented the *Federal Register* notice by sending copies of the *Federal Register* materials directly to about 175 organizations and individuals who had expressed interest or had provided assistance in the development of the published material. Also, a press release was distributed announcing the publication, which resulted in numerous articles in journals. The Board availed itself of all opportunities to publicize the proposals and solicit comments on them.

Written comments in response to the published material were requested by February 4, 1972. Comments were received from 105 sources, including Government agencies, professional associations, industry associations, public accounting firms, individual companies, and others. The Board appreciates the obvious care and attention devoted by commentators, and as will be seen below, the Board has greatly benefited from the comments received.

Many of the comments received or were addressed to all parts of the proposed Board rules as well as to the question of public availability of the Disclosure Statements. All of the comments received have been carefully considered by the Board taking into account the requirements of section 719. Understandably, many of the comments were addressed to issues which recur in two or more of the proposed parts while others dealt only with specific sections. Comments which dealt with 11 general issues are discussed separately below followed by a section-by-section analysis of other comments. Appropriate changes have been made in the material promulgated based on the Board's disposition of the comments received.

Those comments and suggestions received which are of particular significance are discussed below.

1. *Public availability of disclosure statement.* In a special notice in the notice of proposed rule making, the Board sought comments to assist it in redetermination of whether Disclosure Statements submitted by defense contractors and subcontractors should be available to the general public, pursuant to the Public Information Section of the Administrative Procedure Act (5 U.S.C.552) or whether such information was properly within one of the statutory exceptions to the legal requirement for public availability.

With few exceptions, both Government and industry commentators urged that the Disclosure Statements not be made available to the general public. Numerous arguments were presented. Among them were that public disclosure by a Government official would violate 18 U.S.C.1905 (a provision in the Criminal Code making it a crime for a Government official to make certain matters public in certain circumstances), thus making disclosure improper under an exception to the requirement for public availability set out in 5 U.S.C.552(b)(3); that the cost accounting practices were trade secrets or property of considerable value and that disclosure would deprive the company of their value without compensation; that disclosure would reduce competition; and that the public might be misled in that it might construe disclosures respecting the defense segment of a contractor's business as representative of his entire business organization.

An argument in favor of making the Disclosure Statements available to the public was made by a public interest group. It argued that 5 U.S.C.552 clearly applies to Disclosure Statements, which do not fall within any exception to public availability; that the public requires access to Disclosure Statements in order to consider adequately and comment intelligently on any Cost Accounting Standard proposed by the Board; that public availability would enhance competition; that Disclosure Statements which are ultimately approved will form a body of precedents to guide others in complying with future Board Standards and that public availability will enable citizens and the Congress to hold both the Board and contracting officials accountable for implementation of section 719. A few commentators stated that they favored, or could see no harm to companies from, public availability of contractors' disclosed practices.

The Board is especially impressed with arguments that cost accounting practices have never been made public, that companies have regarded and treated them as confidential, and that a company's competitive position would be damaged by public disclosure of its cost accounting practices. Since disclosure will be required of many companies or divisions of companies whose principal competitors are not subject to Board regulations, the Board recognizes there might arise competitive disadvantage to the disclosing company or division if its competitors may see its disclosure but need make none themselves. The Board has, in light of these latter arguments, concluded that information received in response to Disclosure Statements is within the exception set forth at 5 U.S.C.552(b)(4) and that the Board will not make Disclosure Statements public in any case when the company or segment files its statement specifically conditioned on the Government's agreement to treat the Disclosure Statement as confidential information.

A provision to this effect has been added at 351.4(d) of Part 351. Additionally, paragraph (a)(1) of the contract clause set forth at 331.5 has been modified to this effect, and a provision added to it so that subcontractors may submit Disclosure Statements directly to the contracting officer.

While the Board has concluded that public availability of the Disclosure Statements of identified contractors is not required, it will, nevertheless, implement its announced intention of compiling statistical summaries of disclosure data and making those studies available to the public. The Board believes that the creation of a data bank of cost accounting practices will greatly benefit the Board's own research efforts and the formulation of Cost Accounting Standards; summaries of these data or studies of them should also prove to be of great value to the public. Aggregated information not identified to particular contractors will, therefore, be made available to the public.

2. *Contractor-subcontractor relationships.* Several commentators, stating that contractors cannot dictate the cost accounting practices of their subcontractors at any tier, urged that the Board not hold contractors responsible for increased costs to the United States arising from the failure of sub-contractors to follow Cost Accounting Standards or

disclosed cost accounting practices. Several commentators also urged that the contractor not be subject to the possibility of a default termination by reason of the actions or inactions of any of its subcontractors at any tier. Finally, some commentators urged that the Board establish a novel concept of privity between the contracting agency and subcontractors with respect to any concerns stemming from Board rules, regulations, and Cost Accounting Standards.

> The Board has dealt with many of the issues touched on by these commentators in its conclusions, discussed below, respecting the phasing of applicability and the proposed termination-for-default language in the Contract Clause. The Board is also mindful of the desirability of its maintaining neutrality with respect to contracting policies outside its jurisdiction; thus it should avoid establishing a standard or policy which would influence decisions of whether work should be performed in-house or subcontracted. A Board policy permitting contractors to avoid responsibility for the actions of their subcontractors could surely have such an impact.

> The Board reaffirms the established principle that prime contractors are responsible to the Government for performance of their contracts in all required respects and urges that contractors who are fearful of deficiencies in their subcontractors' performances protect themselves by use of whatever means they currently employ under other flow-down contractual requirements.

3. *Exemptions.* Many commentators urged the Board to provide exemptions either to the requirement to file a Disclosure Statement or to both that requirement and the requirement to follow Cost Accounting Standards. Exemptions were urged for subcontractors below the first tier, subcontractors with small amounts of defense contracting business, producers of basic or raw materials, colleges and universities, construction contractors, firms which would qualify as small businesses, and others.

> The Board has long been concerned with the question of appropriate exemptions. It has specifically requested interested groups to offer suggestions for criteria for use by the Board in considering exemptions. It also requested its staff to study exemptions and has discussed the staff investigations at Board meetings. In light of these studies and the comments received, the Board has found no persuasive reasons for issuing blanket or class exemptions at this time.

> The Board recognizes, however, that individual Cost Accounting Standards may by their nature be inapplicable or inappropriate to certain classes or categories of defense contractors or contracts. The Board will continue to consider exemptions from individual proposed Cost Accounting Standards as appropriate.

> With respect to the requirement to submit a Disclosure Statement, the Board's proposed regulation provides a phasing of that requirement. The Board remains convinced that a company which together with its subsidiaries received prime contract awards of negotiated national defense contracts including supplemental awards during Federal fiscal year 1971 totaling more than $30 million should be required to submit a Disclosure Statement as soon as Part 351 of the Board's regulations becomes effective. In order to provide both to other contractors and to Government agencies adequate time within which to study the use of Disclosure Statements, however, the Board will defer determination of the date after which other affected contractors and subcontractors may be required to file Disclosure Statements. From time to time, the Board will announce the dates of applicability to other contractors and subcontractors.

4. *Applicability date of standards, rules, and regulations.* A related issue raised by many commentators is a request that Cost Accounting Standards be made applicable 90 days after issuance or at the beginning of the contractor's next fiscal year, whichever is later. In order to provide the maximum benefits from use of Cost Accounting Standards, the Board has decided not to adopt any rule which would automatically delay the effective date of Cost Accounting Standards beyond the dates contemplated in section 719(h). That section provides a minimum of 4 months notice from the date of promulgation, to contractor of the likely applicability of a Cost Accounting Standard. The Board regards this as an adequate time for companies to prepare for use of the standard. The Board nevertheless recognizes that certain standards by their nature may require deferring applicability to the beginning of a contractor's fiscal year next following the effective date, and in such cases that applicability will be stated in the standards concerned.

5. *Agency administrative responsibility.* Many commentators, noting the Board's statutory responsibility to promote uniformity and consistency in cost accounting practices used in defense contracting and subcontracting have suggested

that uniformity would be promoted by giving the Board another single Federal agency the sole implementing responsibility respecting Board regulations. Thus, some commentators recommended that the Board itself issue regulations prescribing the frequency of submission of Disclosure Statements and where they must be submitted. Other commentators urged that the Board issue a single regulation prescribing exact methods by which increased costs to the United States will be determined. Other commentators urged that the Board prescribe methods by which advance agreements affecting more than one contract shall be made, some commentators urging that the Board itself make those agreements. Others urged that the Board rule that the contracting agencies must act to approve or disapprove Disclosure Statements within a stated period of time. And finally, some commentators urged that the Board itself be the sole agency to approve the cost accounting practices disclosed through submission of a Disclosure Statement.

The Board finds these recommendations cogent. It also recognizes that to act pursuant to them would require a Board regulation directed to the administrative and contracting procedures of many Federal agencies and in some cases -- such as the recommendation for Board approval of disclosed cost accounting practices -- substitute a Board regulation for the exercise of contracting officers discretion.

The Board, therefore, has decided not to implement at this time the suggestions set forth in this connection. The Board nevertheless will watch closely during the early implementation by contracting agencies of Board rules, regulations, and Cost Accounting Standards so that it may become aware of any diversity of regulations or actions by contracting agencies. If the Board finds that an unacceptable amount of diversity has arisen, it will be prepared to reconsider the recommendations that the Board issue its own regulations in many of the areas left by Board regulations to the discretion of contracting agencies.

Many commentators have expressed concern about the problems which could arise from inconsistent actions by different Federal agencies respecting disclosed practices, changes in practices, and equitable adjustment of contract prices and costs. The Board has directed its staff to work with representatives of relevant Federal agencies with the objective of obtaining designation of a single contracting officer for each contractor or major component thereof in order to achieve consistent practices within the standards issued by the Board.

6. *Contract modifications.* Several commentators have urged that negotiated contract changes and amendments over $100,000 to contracts which are themselves not subject to Board jurisdiction should not be covered. One commentator pointed out that in a long-term contract, most changes represent “instead of” type changes with cost of price adjustments only for the incremental effect of the change. This commentator stated that there is no practical way separately to identify these incremental costs.

The Board is persuaded that for the time being it should not cover negotiated modifications to contracts exempt at their inception. It has therefore, eliminated coverage for the time being of such contract modifications. In doing so, however, the Board intends that the annual extension of existing negotiated contracts and similar contract modifications would not be exempt from the Board’s rules, regulations, and Cost Accounting Standards.

7. *Definitions.* The Board is also persuaded of the value of one commentator’s suggestion that the Board provide a compilation of definitions of the words or phases defined in individual Cost Accounting Standards, making those definitions applicable to all such standards. Consequently, a new Part 400 has been added, and all terms defined in Parts 401 and 402 have been placed in it, although they also remain in the particular standards in which they are defined. As more standards are added, any terms defined in them will also be added to Part 400. However, terms defined in Parts 331 and 351 are not included in the glossary of definitions, nor are terms used in those parts necessarily to bear the meanings ascribed to those terms in Part 400.

8. *Application to individual contracts.* Several commentators urged that the Board adopt the date of final agreement on a negotiated price as a cut-off date for the disclosure of cost accounting practices. The Board has reviewed the merits of selecting that date rather than the date of award to establish the date as of which the contractor’s Disclosure Statement must accurately reflect his cost accounting practices, at least with respect to those contracts where cost or pricing data have been submitted pursuant to Pub.L.87-653. The Board has decided to use the date of final agreement on price, as shown on the signed certificate of current cost or pricing data, with respect to contractors who have submitted cost or pricing data, and to use the date of award of the contract for all other contractors. In addition, the Board has concluded

that it is appropriate to use those dates to establish which Cost Accounting Standards shall be applicable to the proposal and to the contract at its inception. Appropriate changes in Parts 331, 351, and 401 have been made to reflect this decision.

9. *Price adjustments.* Many commentators stated that where a contractor's departure from existing disclosed practices is occasioned by the contractor's wish to adopt a newly issued Cost Accounting Standard for all contracts, the Government should be willing to provide upward price adjustment whenever an existing contract is rendered thereby more expensive to perform. The view was often expressed that contractors could not maintain one accounting practice for contracts subject to a particular Cost Accounting Standard, but a different practice for contracts not so subject; therefore, it was alleged, once a contractor had to adopt a standard for any one contract, he would of necessity adopt it for all contracts and amend his Disclosure Statement accordingly.

The Board notes in this connection that the Cost Accounting Standard at Part 402 requires consistency in the allocation of all direct and indirect costs under all covered contracts. If a Cost Accounting Standard were issued which required a company to modify its disclosed cost accounting practices with respect to its earlier practice of allocating direct and indirect costs, Part 402 would require amendment of existing disclosed practices so as to meet that requirement. In such a case, the Board believes it would be unfair to deny an equitable price adjustment arising from such amendment.

Further, the Board has been persuaded by the strong arguments from industry commentators that companies with more than one contract, subject to different Cost Accounting Standards, cannot maintain multiple records to account for each contract related to its set of standards. Another industry commentator stated that the vast majority of companies must apply any required cost accounting practice across their total business, and that it would be impractical if not impossible for companies to apply different practice to different contracts.

The Board has accommodated this view by enabling contractors to apply uniform practices to all covered contracts. Such application will also serve to improve cost accounting practices for all contracts.

The Board has consequently modified both Part 331 and Part 351 to provide three things: First, that a contractor's practices disclosed for any contract shall be the same as the practices currently disclosed and applied on all other covered contracts and subcontracts being performed by that contractor. Second, that a contractor must amend his disclosure of cost accounting practices as new standards are issued and become applicable to new contracts if a change in practices is necessary, so that, at any given time, the same practices prevail under all of the contractor's existing contracts and subcontracts subject to Board jurisdiction. Similarly, contractors must amend Disclosure Statements to reflect any change in practices disclosed under later contracts. Third, that for those amendments of disclosed practices applicable to a particular contract which are occasioned by the issuance of a new Cost Accounting Standard, the Government will suitably adjust the contract price in accordance with the changes clause in the contract or reimburse any increased costs under that contract.

In view of the phasing of the requirement to file a Disclosure Statement, the Board has adopted a contract provision that will provide equitable adjustments in appropriate cases when a contractor who has not yet filed a Disclosure Statement is required to change his established cost accounting practices to comply with newly issued Cost Accounting Standards. On the other hand, any departure from disclosed cost accounting practices which is not required by newly issued Cost Accounting Standard will not be subject to equitable price adjustment, but only to price adjustment downward in the event that departure would otherwise result in increased costs being paid by the United States. The Board wishes to emphasize that if the parties to a contractual negotiation mutually agree a price based on exclusion of Cost which are allocable under the contractor's disclosed cost accounting practices, such agreement shall not affect the requirement for conformity with Board rules, regulations, and Cost Accounting Standards in the contractor's allocation of costs between the contract being negotiated and other work.

10. *Materiality.* The Board notes that many commentators urged that a concept of materiality be incorporated in the Board's regulations, to the end that minimal or insignificant modifications of or failures to use disclosed cost accounting practices would not be subject to price adjustment.

The Board agrees that the administration of its rules, regulations, and Cost Accounting Standards should be reasonable and not seek to deal with insignificant amounts of cost. Since this rule of common sense is already practiced by the Government, the Board does not believe that there is any need to attempt to formulate and state in acceptable concept of materiality applicable to all Board rules, regulations, and standards, although the Board might consider doing so if subsequent events indicate the necessity therefor. The Board does recognize that in particular standards a "materiality" statement may be useful, and in such cases, it will include one. See for example the addition at 402.50(e).

11. *Additional requirements by agencies.* As a final general point, concern was expressed that Federal agencies might require submission of cost proposals in ways inconsistent with the cost accounting practices of some or all of the potential offerors. The Board recognizes that this has happened in the past, but it notes that Board rules, regulations, and Cost Accounting Standards are to be used by relevant Federal agencies as well as by contractors and subcontractors, and it believes that henceforth requests for proposals must be fully consistent with such rules, regulations, and standards, although of course the Federal agency may ask for supplementary information to accompany proposals if this is needed to meet the agency's requirements.

Other Comments

Section 331.2 -- Definitions.

A few commentators recommended modifying the definition of "relevant Federal agency." Their purpose was to assure that agencies such as the General Accounting Office and the Renegotiation Board were excluded from the definition of such agencies. Those recommendations have not been accepted, since the Board believes the General Accounting Office, the Renegotiation Board, and other agencies whose responsibilities include review, approval, or other action affecting national defense procurements are within the meaning of "relevant Federal agencies."

One Federal agency urged that the definition of "national defense" be supplemented at the end by adding the phrase "including R.& D. and services." The Board believes this addition unnecessary, in light of the definition at 331.2(b) of "defense contractor," and the definition of "material" set out in 50 U.S.C.App. 2152 as including "technical information." The Board, of course, agrees that contractors for research and development as well as other services are national defense contractors in light of these definitions.

Several commentators urged that the definition of "negotiated subcontract" at 331.2(f) be broadened to reflect what the commentators believed was the Board's purpose in this definition, that of precluding jurisdiction over subcontracts made after adequate price competition. That is not the Board's intention; instead, the Board intended to exclude from the term "negotiated subcontract" only a subcontract made under conditions which are as close to the conditions governing Federal advertised contracts as possible. Accordingly, the Board has not accepted these suggestions, but it has added language to clarify its intention.

In connection with this comment the Board notes that several commentators urged that the Board exempt altogether from its jurisdiction any contract made after adequate price competition. The Board believes that any such exemption would be unwarranted and undesirable in view of the legislative history of section 719.

Section 331.5 Contract clause. The major changes in the contract clause urged by commentators have already been discussed in points 2 and 9 of the discussion of general comments. Commentators raised a number of additional points with respect to this contract clause. A great many commentators objected to the provision in paragraph (e) for termination for default. Many commentators urged that the requirement to repay increased costs to the United States should be deemed the sole remedy for a refusal or failure to comply with the requirements of the contract clause. While that remedy may be adequate for almost all cases involving a failure to follow Cost Accounting Standards or disclosed cost accounting practices, it would not be adequate to meet other possible situations, where, for example, a contractor refused to make a post-award submission of a Disclosure Statement or refused to grant access to records as required by the contract clause. In view of the fact that breach of any of the requirements of this clause would be a breach of a material condition of the contract, the default clause generally applicable to performance of the contract provides adequate coverage. Consequently, the Board has deleted the specific termination language in this contract clause as requested by many commentators.

Some commentators urged deletion or modification of paragraph (c) of the contract clause, which the Board has not done, since that language is prescribed by section 719(j). Other commentators urged that the Board set forth a specific period during which contractor and subcontractor documents, papers, or records relating to compliance with Cost Accounting Standards must be retained. The Board believes that there is no need to do so, since the general records retention requirements of any particular contract will establish that period. One Federal agency requested that the disputes language in paragraph (d) be modified to accommodate that agency's practice of permitting subcontractors to bring contract disputes directly to that agency's Board of Contract Appeals. The Board has accepted this recommendation. Two Federal agencies recommended deletion of the definitions in this contract clause as unnecessarily duplicating 331.2. The Board agrees and has made the deletion, except that the definition of "negotiated subcontractor" has been retained in the contract clause for the convenience of contractors and subcontractors.

Other suggestions were received in which the Board was urged to modify other language in the contract clause which is taken directly from provisions in section 719. Preferring to use the statutory language, the Board has not accepted these suggestions. It has however, modified its proposal in paragraph (b) so as to adopt the statutory language, as urged by one commentator.

Section 331.6 Post award disclosure. Two Federal agencies urged that the contracting agencies be authorized to make awards whenever the head of the agency concluded that it was impractical to secure a Disclosure Statement from a contractor or from a subcontractor. Recognizing that any avoidable delays in making procurements are undesirable, the Board has accepted this recommendation. The Board does not expect that the authority thus provided to agency heads will be abused, and it will be informed of all actions taken pursuant to this authority.

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Effective date and application. For the convenience of readers, the following summarizes the effective dates set forth in 331.8, 351.4(e), and Parts 400, 401, and 402, which were transmitted to the Congress on February 24, 1972, pursuant to section 719(h)(3) of the Defense Production Act of 1950 as amended. After the expiration of a period of 60 calendar days of continuous session following the date of transmittal to the Congress, the regulations herein promulgated shall take effect as set forth in those regulations, unless there is passed by the two Houses a concurrent resolution stating in substance that the Congress does not favor the proposed standards, rules or regulations.

1. The provisions of 331.4 are to be included in all solicitations issued on or after July 1, 1972, which are likely to lead to contracts covered by standards, rules, and regulations of the Cost Accounting Standards Board.

2. The provisions of 331.5 are to be included in all contracts resulting from solicitations covered by 1 above. In addition, these provisions are to be included in any other contract which is within the jurisdiction of the Cost Accounting Standards Board and which is awarded after October 1, 1972.

3. The provisions of Part 351 will be applicable to any contractor who submits a proposal which results in contracts containing the clause in 331.5 and whose net awards of negotiated national defense prime contracts during Federal fiscal year 1971 totaled more than $30 million. Contractors whose net awards were less than that amount may be required to complete or submit a Disclosure Statement as the Board announces extensions of this requirement to such contractors.

4. Any contractor having a contract awarded prior to July 1, 1972, which contains a clause which already incorporates requirements governing submission of Disclosure Statements and application of Cost Accounting Standards will be required to comply with the provisions of that clause. In this connection, such contractor and the respective contracting agencies whose contracts contain such a clause should review those contracts to determine whether negotiations should be instituted to make Parts 400 through 402 applicable to them.

Preamble B
Preamble to Amendment of 6-29-72

This amendment redesignated 331.3 as 331.3(a) and added a new 331.3(b). The preamble and amendment were published on June 29, 1972, at 37 FR 12784. Although Part 331 was subsequently republished and revised on November 7, 1973 (38 FR 30725), the preamble to the amendment of June 29, 1972, is included as part of the administrative history of the regulation.

The purpose of this publication by the Cost Accounting Standards Board is to adopt a modification to 331.3. Applicability, of its rules and regulations. The modification adopted today was initially published in the *Federal Register* of May 23, 1972 (37 FR 10454). Comments regarding that notice of proposed rulemaking were invited to be submitted to the Board by June 23, 1972.

The prescribed period has passed, and no comment opposing the proposed modification has been received. In view of this and for the reasons set forth on May 23, 1972, *Federal Register*, modification to 331.3 of the Board's rules and regulations is adopted and made effective on July 1, 1972.

Preamble C
Preamble to Amendments of 2-13-73

This amendment adds a new paragraph (c) to 331.3, and deletes 331.6(c). The preamble and amendments were published on February 12, 1973, at 38 FR 4237. Although Part 331 was subsequently republished and revised on November 7, 1973 (38 FR 30725), the preamble to the amendment of February 12, 1973, is included as part of the administrative history of Part 331.

The purpose of this publication by the Cost Accounting Standards Board is to adopt a modification to Part 331, Contract Coverage, of its rules and regulations. The modification was published initially in the *Federal Register* of December 8, 1972 (37 FR 26127). Some of the material in the modification was also published in the *Federal Register* of October 6, 1972 (37 FR 21177). Comments regarding the publication on December 8 were invited to be submitted to the Board by January 15, 1973.

The Board received 14 comments from a wide range of commentators. The Board is grateful for their interest and takes this occasion to thank them for the comments.

One commentator urged the Board to require certain additional information to support waiver applications pursuant to paragraphs (1)(i), (1)(iii), and (2)(I) of 331.3(c). The Board agrees that such additional information will assist it in deciding whether to grant a waiver and therefore has adopted this proposal.

Two commentators urged that the signed, unequivocal statement by a proposed contractor or subcontractor that it refuses to accept a contract containing the Cost Accounting Standards clause might not be obtainable even when there has been such a refusal. The Board agrees and has consequently modified the requirement at 331.3(c)(1)(i) so that the agency's statement of the fact of an unequivocal refusal, and of the contractor's or subcontractor's specific reasons therefor, will be sufficient to satisfy this requirement.

A commentator suggested that the Board provide for exemption from particular portions of the Cost Accounting Standards clause, as well as providing for exemption from all of it. The Board agrees that it is helpful to spell out such authority and has modified its proposal accordingly.

The Honorable Wright Patman, Chairman of the Committee on Banking and Currency of the House of Representatives, noting that any extensive use of the Board's proposed authority could seriously weaken the objectives of section 719 of the Defense Production Act of 1950, as amended, requested that within 30 days after acting on any request for an exemption the Board transmit to him a full report of the exemption request and its action thereon. The Board is pleased to comply with this request. A similar report will also be submitted to the Chairman of the Committee on Banking, Housing, and Urban Affairs of the U.S. Senate.

Another commentator urged in the interest of assuring maximum access by the public and the Congress to the Board's actions that requests for waivers be published in the *Federal Register* and that comments on them be solicited that the

Board's action on a request and an explanation of it be published in the *Federal Register*. and, finally, that notwithstanding any prior publication, that the Board include in its annual report to Congress a listing of every request for waivers received during the year, together with an explanation of the Board's action granting or denying the request. This commentator, asserting that the Board does not have unlimited discretion to grant waivers or exceptions, urges that the standards the Board will apply in acting on requests for waivers be stated.

The Board adopts the suggestion that it include in its annual reports to Congress a listing of the requests it receives for waivers and its disposition of those requests. The Board, however, does not believe that it should publish a notice of requested waiver and solicit comments. As noted above, the Board will provide full information to the Congress and to the public through it reports on its actions on waivers. With respect to this commentator's suggestion that the Board publish the criteria which it will use in acting on requests for waivers, the Board is satisfied that those criteria clearly are implicit in the information which the Board is requiring to be submitted in support of a request for a waiver.

Several commentators urged that the Board delegate its waiver authority to the procuring agencies, stating essentially that waivers could thus be granted more expeditiously. The Board has not accepted this suggestion, since it believes that it should retain control over a matter as important as a total exemption from the requirements of section 719 of the Defense Production Act of 1950, as amended, and also because the Board is convinced that its retention of its waiver authority will not unduly delay action on waiver requests. In this connection, the Board reemphasizes its comments published in the *Federal Register* for December 8, 1972 (37 FR 26127) that, "The Board *** is prepared to act promptly in response to requests for waivers but *** the Board's ability to respond promptly will depend in very large measure on whether or not the agency's request for a waiver is in full accord with the proposed requirements." If experience shows that delegation of this authority is warranted, the Board will, however, reconsider this suggestion.

Some of these commentators also urged that the level of agency officials authorized to submit requests waivers to the Board be modified to include persons at levels of responsibility below those indicated in the Board's proposal. The Board believe that the level proposed will not unduly burden the procuring agencies and will assure that any request for a waiver of the Board's regulations will receive consideration at a very high level within the procuring agency before submission to the Board. It therefore, does not adopt this suggestion at this time, although it may reconsider this suggestion if experience warrants.

Some commentators urged the Board to expand its proposal to permit exemptions on broader bases, instead of confining the exemption authority to particular cases of demonstrated need. The Board does not accept this suggestion, since it does not anticipate wholesale or, indeed, even very numerous requests for waivers. Nevertheless, should a need for broader exemption action be justified, the Board can deal with that need under its authority in section 719(h)(2) of the Defense Production Act of 1950, as amended.

One commentator urged an outright exemption for both foreign and domestic concerns for work performed outside the United States, and other commentators urged the exemption, of all subcontracts performed in Canada. The Board has adopted neither of these proposals, since it believes that the arguments advanced for them are unpersuasive in light of the purposes of section 719. The Board believes, further, that the exemption authority being adopted today provides an adequate basis for waivers where they are appropriate.

A commentator is concerned that the phrase, "on a timely basis," in 331.3(c)(1)(iv) and 331.3(c)(2)(ii), if given a narrow interpretation, might suggest that timeliness of delivery is the only condition for granting a waiver. That commentator points out that other conditions also may warrant consideration. The Board agrees with the commentator, but it does not believe that a modification of its proposal is necessary to avoid the narrow interpretation feared.

In the interest of clarity, the waiver provision in 331.6(c) is deleted from that section and transferred to 331.3(c).

The Board has revised its proposal as discussed above and has made minor technical improvements. The revised proposal is adopted today.

Preamble D
Preamble to Republication, 11-7-73

This publication (38 FR 30725. Nov. 7, 1973) revised and republished Part 331.

The purpose of this publication by the Cost Accounting Standards Board is to amend Parts 331, 351, 400, 401, 402, 403, and 404 of its rules and regulations. The amendments, which are minor clarifications to the regulations were published in the *Federal Register* of September 5, 1973 (38 FR 23971). The amendments:

(a) Renumber Parts 331 and 351 to facilitate insertion of future modifications to those parts;

(b) clarify one section of the contract clause at 331.5; and

(c) modify certain definitions in Parts 400, 401. 402, 403. and 404 for the purposes of uniformity among the various Parts. Only one comment in response to the September publication has been received by the Board. This expressed agreement with the proposed changes.

In view of the foregoing, the following amendments to the Board's regulations are being made effective November 7, 1973:

Preamble E
Preamble to amendment of 9-19-74

This amendment revised paragraph (c)(4) of 331.30, and was published on September 19, 1974, at 39 FR 33681.

The purpose of this publication by the Cost Accounting Standards Board is to adopt a modification to Part 331, Contract Coverage, of its rules and regulations. The modification adopted today was initially published in the *Federal Register* of August 9, 1974 (39 FR 28645). Comments regarding that notice of proposed rulemaking were invited to be submitted to the Board by September 9, 1974.

The August 9, 1974, publication proposed an amendment to 331.30(c)(4) to permit, under certain circumstances, submission of waiver requests from a level below that of the agency head. No objection to the Board's proposal has been made. Therefore, the proposal has been adopted for the reasons expressed in the August 9, 1974, publication.

Preamble F
Preamble to Amendments of 12-24-74

This document amended 331.30(a), added 331.30(b)(8), and amended 331.40 and 331.50. It was published Dec. 24, 1974, at 39 FR 44389. The purpose of this publication by the Cost Accounting Standards Board is to adopt modifications to Part 331, Contract Coverage, and Part 351, Basic Requirements, of its rules and regulations. These modifications will provide an exemption from Cost Accounting Standards Board requirements for certain national defense contracts and subcontracts of $500,000 or less.

Public Law 91-379 requires that Cost Accounting Standards must be used in all negotiated prime contract and subcontract national defense procurements with the United States in excess of $100,000, with certain stated exceptions. From time to time the Board refers to contracts subject to its rules and regulations as "covered contracts". Section 719(h)(2) of Pub.L.91-379 authorizes the Cost Accounting Standard Board to prescribe rules exempting from its requirements such classes or categories of national defense contractors and subcontractors as it determines, on the basis of the size of the contracts involved or otherwise, are appropriate and consistent with the purposes sought to achieved by Pub.L.91-379. The Board has granted several exemptions to classes or categories of contractors and subcontractors and also has established a procedure under which waiver of the Board's requirements may be granted for individual contracts.

A proposed exemption increasing the minimum contract amount requiring compliance with Cost Accounting Standards Board rules, regulation, and Standards from $100,000 to $500,000 was published by the Board on September 27, 1974 (39 FR 34669). The Board received 32 responses the September 27 proposal. Comments were received from individual companies, government agencies, professional associations, industry associations, public accounting firms, and individuals. All of these comments have been carefully considered by the Board, and the Board takes this opportunity to express its appreciation for the helpful suggestions which have been furnished.

The comments below summarize the major issues discussed by respondents in connection with the initial publication and explain the Board's disposition of these issues.

Issuance of the exemption. Practically all the commentators expressed concurrence in the proposed exemption, giving either unqualified support or support with added comments that additional exemptions should also be considered. However, three commentators -- a consulting firm, a major aerospace company and a Government agency -- disagreed with the proposed exemption, stating that an increase in the threshold for compliance with CAS requirements was inconsistent with the Board's objective of establishing uniformity and consistency among contractors doing business with the Government.

The Board agrees that the adoption of the proposed regulation will exempt a substantial number of contractor and subcontractors who otherwise would be covered, and consequently will permit such companies to follow accounting practices other than those set out in Cost Accounting Standards. However, the Board is aware that compliance with its rules, regulations and standards may involve additional administrative effort, particularly on the part of small companies, which may not be commensurate with the benefit to the Government or the contractor resulting from such compliance. The Board, after considering the efforts required by both the Government and its contractors to assure compliance on all covered contracts in excess of $100,000, is persuaded that maximum benefit to the Government with minimum cost can be achieved by limiting the mandatory application of its standards to contractors who receive awards which constitute a substantial majority of the national defense procurement dollars. As was stated at the time the proposed exemption was issued for comment, some 70 percent of the prime contractors of the Department of Defense did not receive one or more negotiated awards in excess of $500,000 in Fiscal Year 1973. Thus, only 30 percent, or approximately 750 prime contractors, who received contract awards totaling $20 billion, would continue to be covered. The exemption would remove coverage from only about 10 percent of the dollar value of annual DoD awards.

In view of the foregoing, the Board considers the proposed exemption increasing the minimum contract amount requiring compliance with the Cost Accounting Standards Board rules, regulations, and standards to be in keeping with the purposes sought to be achieved by Pub.L.91-379 and to be an appropriate exercise of the authority granted to the Board by section 719(h)(2) of that law.

Increase exemption on all contracts to $500,000. A number of commentators suggested that the $500,000 single contract threshold for compliance with Board rules, regulations, and standards be changed to exempt all contracts of $500,000 or less. Those giving reasons in support of this suggestion generally based their comments on simplification of administration. These commentators felt that it would be difficult for the Government or prime contractors, when awarding a prime contract or subcontract in excess of $100,000 to determine whether the contractor or subcontractor had in existence a prior $500,000 covered contract.

The Board, in proposing the $500,000 threshold, did so with the intent of exempting those companies which do not receive contracts in excess of $500,000 from the Government. However, it was decided in the interest of consistency in cost accounting practices that once a contractor had received a covered contract of that size, compliance with CASB rules, regulations and standards on contracts at the level established in Pub.L.91-379 was appropriate. This is also consistent with the desire expressed by contractors to follow a single set of accounting practices. Further, the requirement for coverage of contracts in excess of $100,000 where the contractor already has received a covered contract in excess of $500,000 will permit the small contracts to be available for equitable adjustment if subsequently issued standards should become applicable. Moreover, once the administrative effort has been expended to comply with standards for contracts in excess of $500,000, compliance with standards on contracts above the statutory threshold of $100,000 requires little added effort.

With respect to the commentators' statements concerning the difficulties, when making an award exceeding $100,000, of determining whether a contractor or subcontractor had in existence a prior award exceeding $500,000, the Board feels that an administrative requirement can be established for obtaining this information. A similar requirement now exists concerning the disclosure statement, whereby contractors are required to submit a disclosure statement, state that they have previously filed a disclosure statement, or submit a certificate of monetary exemption. The Board feels that a similar requirement can be set concerning the $500,000 level. The Board is not persuaded that this matter would create problems of sufficient significance to eliminate coverage down to the $100,000 level.

In considering the advantages of the exemption as proposed compared to its assessment of the administrative difficulties foreseen by commentators, the Board is persuaded that its proposal relative to coverage of awards in excess of $100,000 should not be changed.

Exemption based on sales. A number of commentators urged that the Board establish an exemption based on sales, using either minimum annual dollar amount of sales to the Government, or Government sales as a percentage of total annual sales, or a combination of these two factors. The most frequently it suggested amount was $10 million of sales to the Government or Government sales amounting to 10 percent of total annual sales. The objective sought by these commentators was an exemption of those companies or business units whose sales to the Government constituted a reasonably small portion of their total annual sales and whose business was essentially commercially oriented. The Board has given lengthy consideration to the use of a sales basis for the establishment of a minimum threshold for compliance with its or rules, regulations and standards. It did not use that basis at this time due to the nature of the problems involved in administering an exemption based on sales. In either of the situations suggested by commentators, the representation concerning the amount of sales must be made by the contractor and subsequently verified by the Government. This verification would impose very substantial and time-consuming efforts on both the Government and the contractor. Particularly in the case of Government sales as a percentage of total sales, Government representatives would be placed in the position of examining a contractor's total sales to including those made in its commercial business. Examination of a company's records concerning its total sales is not presently performed by Government procurement activities and would present new and unique problems to both parties as well as requiring substantial additional effort on the part of Government representatives.

An exemption based on sales would require a measurement period during which a contractor's status with respect to compliance with standard would be determined. Contracts under which sales were recorded during this period would not be subject to standards. If the volume of sales during the measurement period exceeded a stated threshold, a contractor would then be required to comply with standards under contracts received in subsequent periods. Thus, the contracts that brought the contractor under the Board's rules would not be subject to standards, while those received at a later time would be.

The Board has decided that the administrative problems involved with an exemption based on sales should be considered before establishing such a threshold. The Board will continue to study these problems and investigate whether exemptions based on criteria other than a minimum contract amount would be appropriate and consistent with the purposes of Pub. 91-379.

Retroactivity. Several commentators requested that the Board modify proposal so as to provide retroactive exemption to existing contracts when the circumstances are such that the existing contracts would have been exempt if awarded after the effective date of the proposed regulation.

The Board has no authority to modify existing contractual agreements between the government procurement agencies and their contractors. However, the Board sees nothing inconsistent with its regulations or with Pub.L.91-379 in modification by the procurement agencies of contracts in this category, assuming of course that the Government receives adequate consideration for deletion of CAS requirements.

Increase minimum amount. A number of commentators recommended that the exemption proposed be increased to an amount greater than $500,000, the figure of $1,000,000 being frequently mentioned. The Board is not now prepared to raise further minimum contract amount required compliance with its promulgator. The Board, in studying an exemption based on minimum contract amount concluded that the $500,000 threshold was the most appropriate one for achieving its objectives, all factors considered. The Board will continue examine various limitations but considers that the threshold established in the proposed exemption best meets its requirements and obligations this time.

Effect of final payment under contracts subject to CAS clause. Several commentators urged that the exemption of contracts of $500,000 or less should not be dependent on the final payment on contracts which are subject to Board requirements, on the grounds that final payment can occur a substantial period of time after completion of work on a contract and that there are many technicalities in closing out a contract which do not involve cost accounting applications.

The Board considers this point to be well taken and has changed the requirement in 331.30(b)(8) where it first appears to "notification of final acceptance of all items or work to be delivered." At that time it is considered that all direct costs will have been charged to the contract since all work will have been completed, and any further accounting transactions would be the result of adjustments not directly related to contract performance.

Reduction of contract price by exclusion of commercial items. Some commentators, in reading the introductory comments to the Board's initial publication of this exemption, interpreted the phrase "minimum contract amount requiring compliance" in a manner not at all intended by the Board. These commentators interpreted this phrase to permit the price of a contract subject to standards to be reduced by the value of those individual contract items or subassemblies of final contract items whose prices could be considered to be "catalog" or "market" prices, if sold separately. They requested that the regulation be clarified to reflect their interpretation of the Board's introductory comments.

Those requesting this clarification misunderstood the Board's intentions. The Board does not intend that the price of a contract be adjusted to exclude the price of items or subassemblies which, if purchased separately, might be exempt from the Board's promulgation's. Consequently, the change in the regulation requested by commentators on this point would be completely inappropriate.

Definition of contractor. One commentator noted that the prefatory comments to the Board's September 27, 1974, publication specifically mentioned the fact that receipt of a contract in excess of $500,000 by one business unit of a multi-unit company would not in itself require other units of the same company to follow Board requirements. This commentator requested that the definitions of "defense contractor" and "defense subcontractor" contained in 331.20 (b) and (c) be modified to reflect this intention by the Board.

As the Board stated in its September 27 publication, its contract requirements have been applied to business units, such as a profit center, division, subsidiary, or similar unit of a company, which perform the contract, even in those cases where the contract was entered into on behalf of the overall company rather than the business unit. This application of the Board's requirements to a performing business unit is well established and unchallenged, and clarification of the definitions of "contractor" and "subcontractor" does not appear necessary.

Effective date. Several commentators raised questions concerning the effective date of the eligibility for this exemption in relation to awards received prior to January 1, 1975. Contractors who have received a prime contract or subcontract in excess $500,000 subject to cost accounting standards prior to January 1, 1975, and on which notification of final acceptance of all items or work to be delivered on that contract or subcontract has not been received, is a contractor who has "already received a contract or subcontract in excess of $500,000," as that phrase is used in 331.30(b)(8). Therefore, today's publication requires that a contractor meeting this test will be required to comply with standards on all covered prime contracts or subcontracts in excess of $100,000 received after January 1, 1975, under the provisions of 331.30.

Preamble G
Preamble to Amendments of 2-2-76

This amendment added paragraph (b)(9) to 331.30 and was published on February 2, 1976, at 41 FR 4809.

* *Purpose.* The purpose of this publication by the Cost Accounting Standards Board is to adopt a modification to Part 331, Contract Coverage, of its rules and regulations. This modification will provide a conditional exemption for contracts and subcontracts made with United Kingdom, firms for performance substantially in the United Kingdom. *

The Cost Accounting Standards Board is authorized by Pub.L.91-379 to prescribe rules and regulations exempting from its requirements such classes or categories of defense contractors or subcontractors under contracts negotiated in connection with national defense procurements as it determines, on the basis of the size of the contracts involved or otherwise are appropriate and consistent with the purposes sought to be achieved by the Act. Pursuant to this authorization the Board has issued a regulation, 331.30, Applicability, exemption and waiver, of Title 4, Code of Federal Regulations, which, among other things, establishes a procedure by which procuring agencies may request a waiver of the Board's requirements for a particular contract or subcontract.

The Board from 1972 to date has granted 45 waivers requested by procuring departments and agencies. Of that number, 23 were for contracts or subcontracts to be performed by United Kingdom firms each of which is a defense supplier to the U.K. Government and also is essentially a sole source supplier for the particular item being purchased by the U.S. Department of Defense. The waivers granted to U.K. firms have been based in general on the urgency and essentiality of the procurements, which were reported to preclude any alternative to making the proposed awards. However, the U.K. firms were reported having objections to complying with the Board's rules and regulations, on the grounds that their accounting practices have been approved by the U.K. Government, their major customer, and may not thereafter be changed without further approval. They were reported as stating that they cannot assume an obligation to comply with Cost Accounting Standards which could be in conflict with U.K. Government Accounting Conventions and the governmentally approved accounting practices for the individual firms.

In view of the recurrence of this position and the high proportion of waiver requests involving U.K. firms, the Board undertook discussions with the U.K. Ministry of Defence concerning the application of Cost Accounting Standards and the Board's rules and regulations to firms which are U.K. defense contractors. As a result of these discussions it has been determined that U.K. defense contractor do disclose their accounting practice to the Ministry of Defence and that the Ministry of Defence approves companies' practices which then cannot be changed without further approval. It has further been determined that Review Board for Government Contracts, whose chairman and member are nominated by the Government and industry and appointed by the Treasury, but which is established as an independent organization, among other duties periodically reviews and makes recommendations for change in U.K. Government Accounting Conventions. The Review Board has also issued or sponsored certain cost accounting standards for use by U.K. firms in contracting with the Ministry of Defence.

On November 17, 1975, the Board published for public comment in the *Federal Register* (40 FR 53271) a proposal for a conditional exemption for U.K. firms performing substantially in the U.K. Nine responses were received to that publication. Responses were received from government department, defense contractors, an industry association and two individuals. All of these comments have been considered by the Board, and the Board takes this opportunity to express its appreciation for the helpful suggestions which have been furnished.

The comments below summarize the major issues discussed by respondent to the initial publication and explain the Board's disposition of these issues.

U.K. Government Accounting Conventions. Two United States Government departments were concerned that the reference in the proposed conditional exemption to the obligation of U.K. firms to disclose cost accounting practices which would be in accord with U.K. Government Accounting Conventions implied or could be understood to require that when matters mandated by the Conventions were in conflict with certain requirements of the Armed Services Procurement Regulation and Energy Research and Development Administration procurement regulations, the policies of the Conventions would prevail.

One of the departments pointed out that the Conventions permit reimbursement of four kinds of costs which are either by U.S. law or by U.S. procurement policy not allowable costs in U.S. contracts. These are entertainment expenses, product advertising certain donations and certain non-incurred capital costs. The Board recognizes that the Conventions deal broadly with matters which can be regarded as relating to both allocability and allowability of costs. They do indicate that in certain circumstances, the indicated costs are allowable costs under U.K. contracts. However, cost accounting practices covered by Disclosure Statements do not deal with the allowability of costs, only with their measurement and allocation. Where appropriate, a disclosed practice must result in measurement and allocation of a cost in accord with the Conventions; whether that cost is or is not allowed as a cost under U.S. contracts is a matter for agreement by the parties to the contract and is not affected by the requirement that disclosed cost accounting practices be in accord with the Conventions.

Secondly, the department points out that the profit formula used by the U.K. Government is different from the profit formula used in U.S. negotiated procurements. The U.K. profit formula, however, is not a part of the U.K. Government Accounting Conventions governing cost accounting practices, nor does the Disclosure Statement deal with policy on which profits are determined. Consequently, a requirement that disclosed cost accounting practices be in accord with the Conventions does not impinge on the authority of U.S. officials to prescribe policy for the determination of profits under U.S. prime or subcontracts.

Thirdly, the department notes that there are differences between the U.K. Government Accounting Conventions concerning independent research and development and the provisions in ASPR Section XV which are used for compliance with Pub.L.91-441. Pub.L.91-441 makes Department of Defense appropriations unavailable for payment of a contractor's independent research and development or bid and proposal costs, unless the work which is paid for has a potential relationship to a military function or operation and unless other conditions are met. The most important of the other conditions is that there be an advance agreement with the contractor. What has been said above about the allowability of costs is applicable to this point also. Furthermore, nothing in the Board's conditional exemption in any way controls the terms and conditions upon which the Department of Defense may agree in advance with a U.K. firm for the reimbursement to it of independent research and development and bid and proposal costs.

Additionally, the department notes potential differences in the treatment of depreciation costs under the Conventions and under the applicable ASPR requirements, unmodified by the Board's Cost Accounting Standards. The comment does not specify, nor does the Board find, any significant differences at present. The Board does recognize that both the U.S. and U.K. Governments may modify their tax laws and their procurement regulations with an objective to encourage capital investment, and that differences could some day arise. In such case, the Conventions permit sufficient flexibility in individual cases to allow U.S. agencies to reach agreement with U.K. firms on appropriate annual depreciation costs.

Finally, this department has consistently requested unqualified waivers from the Board for use in its prime and subcontracts with U.K. firms. Such firms have in fact been required to follow U.K. Government Accounting Conventions on their work for the U.K. Government, and the department has been able to negotiate mutually agreeable prices for contracts with them despite this circumstance. Under the Board's conditional waiver, the department will have the advantage of a Disclosure Statement from such firms, which could not have been available when an unconditional waiver was sought and which should be of material assistance in the negotiation and audit of new contracts.

The Board is glad that these questions were raised but does not believe it is necessary to modify its proposed conditional exemption to resolve them.

It is appropriate to note here that the Board has not specifically required access to records of U.K. firms by appropriate U.S. officials, as it might have done. Such a requirement appears unnecessary in view of the standard provisions for access to records contained in U.S. defense contracts and subcontracts for performance in the U.K. Access to records through such standard provisions in those contracts will be adequate to assure contractor compliance with the consistency requirement of the conditional exemption.

Another commentator opposed the proposal largely on the basis of his belief that the proposal would require adoption by U.S. price negotiators and auditors of the pricing practices followed by the U.K. Ministry of Defence. This belief appears to have been based on the reference in the proposal to U.K. Government Accounting Conventions. The Board sees nothing in the conditional exemption which would require U.S. negotiators to accept pricing practices contrary to U.S. procurement regulations and the agreements which U.S. negotiators reach with U.K. firms in the pricing of prime or subcontracts.

This commentator also indicated that not all U.K. firms which are U.S. prime or subcontractors are also suppliers to the U.K. Government. The Board agrees that this could be the case and believes that if so, it is not appropriate for the Board to require that all U.K. firms necessarily adopt the U.K. Government Accounting Conventions. It has consequently modified its proposal to provide that disclosed practices must be in accord with the Conventions only when the disclosing contractor is already required to follow the Conventions. Thus, certain U.K. firms may be subject to neither Cost Accounting Standards nor U.K. Government Accounting Conventions. In such cases, U.S. negotiators must use that firm's Disclosure Statement in arriving at agreement on the cost accounting practices to be followed in contracts subject to the conditional exemption.

Retention of disclosure statements. A commentator pointed out that while the Board had proposed that Disclosure Statements submitted by U.K. firms be filed with the U.K. Ministry of Defence, the Board had not specified that the Statements would be retained in the Ministry. Since that was in fact the Board's intention, the Board has adopted a modification to its proposal in order to make that intention clear.

Prime contractor-subcontractor relationships. Two matters relating to prime contractor-subcontractor relationships were raised. A commentator pointed out that a U.K. subcontract might be subject to price adjustment if the subcontractor changed its disclosed cost accounting practices during contract performance. In such a case, the Government's action would presumably be to require a corresponding change in the cost or price of the prime contract. The Board agrees that this is so, and prime contractors may wish in the future, as some have done in the past, to obtain agreement with U.K. subcontractors for appropriate indemnification in the event the subcontractor's change in practices cause a modification in the cost or price of the prime contract. The Board previously discussed this situation in its original publication of 4 CFR 331.50 and does not consider that specific language addressed to this matter is required to be included in the condition all exemption.

Another commentator stated that was confident that the Board did intend that the conditional exemption apply to U.S. subcontractors under prime contracts with U.K. firms a urged the Board to address this matter specifically. The Board's proposal do not require any flow-down of the clause, "Consistency in Cost Accounting Practices", from U.K. prime contractors to first tier or lower tier subcontractors. The Board may after experience in use of that clause is gained, reconsider this matter. In that case, the Board would then have to consider whether it would be appropriate for the Board to require that U.K. prime contractor be required to pass down to any subcontractor whether or not a U.S. subcontractor, a more extensive contractual obligation than is imposed on the prime contractor. For the time being, the Board notes the likelihood that U.S. subcontractors under U.K. prime contracts will already be subject to Cost Accounting Standards by reason of other covered prime or subcontracts which that firm has entered into. If this prior coverage has not taken place, the Board believes that the value of achieving coverage through a flowdown provision in a U.K. prime contract is too insignificant to justify the administrative complexities of such a provision.

Further exemptions for foreign suppliers. A commentator, not wishing to comment on the present proposal, nevertheless recommended that the Board exempt all foreign suppliers, on the ground that problems in the administration of the CAS clause are matters of contention and, in the opinion of the commentator, pose relatively greater difficulties in the administration of foreign contracts.

The Board has announced the establishment of projects to investigate the administrative concerns of this commentator and others, and if those concerns prove to be substantial, the Board will take appropriate action. In the more than four years during which the CAS clause has been required to be included in all appropriate foreign contracts and subcontracts, absent a waiver, the Board has heard of no problem in the administration of the clause which has posed any problem in foreign contracts.

Whenever the Board believes a waiver of the CAS clause for foreign firms has been persuasively proposed by a contracting agency, it will grant such a waiver, but the Board's experience to date does not indicate to it any reason to consider a blanket waiver for all foreign prime contracts and subcontracts.

Miscellaneous comments. One commentator, from a major defense contractor, deserves note by the Board because of what the Board perceives to be major misconceptions and erroneous assumptions underlying the comment.

The comment opposed the proposal for a conditional exemption and favors an unqualified exemption. One reason given, to quote from this comment, is:

By requiring a contract clause which will provide for a penalty to be paid by the U.S. prime contractor in the event that a U.K. subcontractor fails to consistently follow disclosed cost accounting practices where such failure results in increased costs paid by the U.S. Government, is to impose on the U.S. primes an obligation so vague and impracticable as literally to be unique in the history of bilateral contracting.

The Board believes this comment is wholly inaccurate. First, the obligation to consistently follow disclosed or established cost accounting practices is not imposed by the Board's current proposal -- it has been present in every U.K. prime contract or subcontract subject to the CAS clause. Secondly, exactly the same obligation of a prime contractor has existed for years with respect to every subcontract it makes which includes the CAS clause. The Board does not believe that the obligation arising under the conditional exemption is either vague or impracticable, and it knows it is not unique.

Additionally, this commentator with respect to the same obligation stated:

For the U.S. Government to impose such alien rules on the defense contracting community in the United Kingdom * * * where neither the Government of the United Kingdom nor the contractors have determined for themselves that there are benefits to the imposition of such punitive rules regarding accounting practices seems patently absurd. Further, to impose on the procurement process such a nebulous and onesided contractual requirement by the use of the regulatory procedures which will render the clause "mandatory and non-negotiable" is to express an unwarranted contempt by the United States for the standards and practices of business accounting and contracting procedures of the United Kingdom.

Apart from the commentator's several adverse characterizations of the Board's requirements, which are discussed generally below, this portion of its comment does not appear to recognize that the Board's proposal was discussed with the U.K. Government and with representatives of the British defense industries. Through meetings in both Washington and London and through continuing, close consultations, the Board has confidence that its proposal has been carefully reviewed and discussed within the United Kingdom and that its adoption will be welcomed by the firms and governmental agencies affected by it. This careful consultation, and the Board's subsequent proposal for a conditional exemption, arose out of the Board's respect for, not its contempt of, the standards and practices of cost accounting in the United Kingdom.

Finally, this commentator expressed its view that there have been no discernible benefits whatever from the Board's regulations and its further view that the Board has abundant evidence that its regulations requiring consistency in following disclosed cost accounting practices have resulted in "substantial impairment of the economy, efficiency, and effectiveness of procurement * * *. The commentator concluded this point by stating that since it regards the Board's consistency requirement to be "unfair, unworkable and doubtfully enforceable", it would use the proposed conditional exemption for U.K. firms only "with shame and reluctance."

The Board has received reports from procurement agencies of major benefits stemming from use of its consistency requirements, and the Board believes that they have unquestionably, improved the economy, efficiency and effectiveness of procurement. The Board believes that those requirements are fair, workable and enforceable.

As noted above, the Board is currently investigating suggestions made by some U.S. defense contractors, including this commentator, to determine whether there are substantial problems in the administration of its requirements to follow disclosed accounting practices consistently. The commentator offers no information concerning any such problem, only its conclusion that the Board has acted wholly improperly in proposing the U.K. conditional exemption. The Board does not agree.

Costs and benefits. The Board discerns no significant cost or inflationary impact of the conditional exemption.

The benefits include a substantial reduction in the number of waiver requests for United Kingdom firms, while establishing a consistency requirement for all U.K. contractors which is necessarily lost when all Board requirements are waived.

A United Kingdom firm could find that its obligations to follow U.K. Government Accounting Conventions might require the firm to change a disclosed cost accounting practice. In such an event, the Board hopes the cost impact on U.S. contracts or subcontracts of any such change would be negotiated in advance of the effective date of a change to the Convention, so as to avoid the imposition of any interest charges on increased cost paid by the United States. The negotiation relating to a change in disclosed practices would be patterned on the similar negotiation required under Section (a)(4)(B) of the Cost Accounting Standards Clause.

In view of the foregoing, the following change to Part 331 of the Board's regulations is being made effective February 2, 1976.

Preamble H
Preamble to Amendments of 9-12-77

The amendments to 4 CFR Part 331, 42 FR 45625, Sept. 12, 1977 were published as a part of the document which set forth the original 4 CFR Part 332 and amendments to Parts 351 and 403. The complete Preamble appears in the supplement to Part 332.

Small Business

Several commentators urged that all businesses which qualify as small business concerns under the rules and regulations of the Small Business Administration be exempted. The February 16, 1977 proposal would have provided such an exemption only for a small business which received less than $10 million in awards during its preceding fiscal year. Modified coverage would have been provided for other small businesses. Research indicates that there are very few companies which would fall into the category of small businesses receiving awards of $10 million or more. In the interest of using a single test, i.e., whether the contractor qualifies as a small business concern, rather than a dual test which would result only in a few small businesses being subject to modified coverage, the Board has adopted the recommendation to exempt all small business concerns. Research indicates that if this action had been applied to Federal Fiscal Year 1976 it would have resulted in exemption of 196 small business concerns which were doing business with the Department of Defense and which had $460 million of contracts of the type subject to Cost Accounting Standards. Consequently, on average, each small business concern would have a relatively small amount of covered contracts.

Other Categories

Various commentators renewed previous recommendations that the Board exempt other categories of contracts and contractors. The categories included colleges, universities, non-profit organizations, hospitals, and government-owned contractor-operated facilities. The Board has considered these recommendations and concluded that none of these categories should be exempted.

Effective Date

The effective date of the regulations being published today is March 10, 1978. Pub.L.92-379 provides that regulations shall take effect not earlier than the expiration of the first period of sixty calendar days of continuous session of the Congress following the date on which a copy of the regulations is transmitted to the Congress. The calendars of the Congress indicate that the required sixty days will not pass until some time in February 1978. Accordingly, March 10, 1978, has been selected to assure sufficient time for the regulation to lie before the Congress.

Preamble I
Preamble to Amendments of 10-5-77

This document added 331.71 and was published Oct. 5, 1977, at 42 FR 54254.

Summary. This modification of the Cost Accounting Standards Board's rules and regulations provides criteria for determining the materiality of costs in given circumstances, in applying words or phrases of materiality used in Cost Accounting Standards, and to limit price adjustments to material amounts of cost.

Supplementary information. A discussion of the background and public comments received in response to the initial publication of these regulations and of the principal issues considered in preparing the final promulgation precedes the regulations.

The purpose of this publication by the Cost Accounting Standards Board is to adopt a modification to Part 331, Contract Coverage, of its rules and regulations. The modification will provide criteria for determining the materiality of amounts of cost in given circumstances. The Board initially considered publishing a definition of the terms “cost accounting practice” and “change to either a disclosed cost accounting practice or an established cost accounting practice” along with the modification dealing with materiality. That definition is being handled separately by the Board, however, and will be considered at a later date.

The Board is authorized by Pub.L.91-379 to prescribe rules and regulations for implementing Cost Accounting Standards. Pursuant to this authority, the Board is today issuing a modification to its regulations. Contractors and procurement agencies engaged in the implementation and administration of CASB rules, regulations, and Standards have recommended that the Board provide guidance concerning materiality in the administration of the Board’s rules, regulations, and Standards.

Representatives from various organizations affected by Standards have pointed out that guidance in this area will facilitate the implementation and administration of CASB pronouncements. A similar recommendation was also received by the Board at an Evaluation Conference in June 1975. The General Accounting Office’s Status Report on the Cost Accounting Standards Program -- Accomplishments and Problems (PSAD-76-154, Aug. 20, 1976), also referred to the need for guidance on this subject.

Research in this area included a review of data submitted by participants in the Evaluation Conference, an analysis of papers submitted by various contractors, professional groups, trade associations, and Government agencies, as well as a review of existing procurement regulations. and existing CASB promulgation’s. A Staff draft of an amendment dealing with materiality criteria and price adjustments was distributed on August 13, 1976. Responses from 53 sources contributed to the Board’s further consideration of the issues involved in this proposed amendment.

A proposed amendment to the Board’s regulations was published in the *Federal Register* on February 3, 1977 (42 FR 6591). A total of 45 responses were received from individual companies, Government agencies, professional associations, industry associations, universities, and others. The Board takes this opportunity to express its appreciation for the helpful suggestions and criticisms which have been furnished. The comments furnished by the organizations and individuals have resulted in a number of changes in the amendment being promulgated today. The following material summarizes the issues regarding materiality that were discussed by respondents in connection with the proposed modification and explains the changes made to the proposal published February 3, 1977. The still relevant portions of the comments which accompanied the February 3, 1977 publication have been incorporated in this material.

Materiality Criteria

Generally, commentators felt the proposed materiality criteria were a necessary, positive and useful step, However, some commentators suggested that the proposed criteria were not sufficiently specific and would not resolve the materiality questions that currently exist. Some commentator suggested that quantitative criteria be added to the proposed regulation others suggested that the criteria proposed were suitable.

At the present time, the Board is of the opinion that quantitative limits should not be established for materiality determinations. The essence of materiality criteria is to allow for the excise of judgment; and absolute dollar amount in one case may be material while in another case the same amount may be immaterial. Accordingly, quantitative limits have not been added to the proposed amendment.

The materiality criteria being promulgated are designed for use in a variety of situations and to resolve issue which have been raised by various sources, Cost Accounting Standards establish the cost accounting appropriate for the determination of contract costs. Departure from the requirements of these Standards may occur and the cost effects of such departure may be immaterial. The criteria serve to limit price adjustments to material amounts of cost. The regulation also describes the actions to be taken when immaterial amounts of cost are involved in noncompliance with Standards. The criteria for materiality are also to be used in applying words or phrases of materiality used in Cost Accounting Standards. In particular Standards, the Board will continue to give consideration to defining materiality in a specific manner as to either the entire Standard or any provision thereof, whenever it appears feasible and desirable to do so.

Administrative Costs

Commentators proposed that the administrative cost of processing a change in cost accounting practice to both the Government and the contractor should be one of the criteria used in determining materiality. The Board's initial publication did not provide for consideration of these costs in determining materiality. Generally, such costs on the part of both the Government and the contractor are absorbed as part of their routine operations. On a conceptual basis, the determination of materiality should be made considering only the amount of costs affected by the proposed changes. As a practical matter, however, the administrative cost to process a contract price adjustment is a factor in a materiality decision.

The Board is persuaded that the administrative cost of processing a change in cost accounting practice should influence a decision as to materiality. For example, if it is estimated that costs would be changed by $10,000 through processing a change at a Government contractor administrative cost of $10,000, then processing the change would be nonproductive whether or not, considering all materiality factors, the estimated change in costs of $10,000 would be judged material. Accordingly, the Board has added a provision to this modification dealing with such costs.

Measurement of Cost Impact

Commentators suggested that the Board's regulations provide that initially the determination of materiality should be done on a gross, overall, basis rather than on an in-depth cost impact study. These commentators asserted that a provision of this type would help to reduce the time and cost of evaluating and processing proposed changes which are judged to have an immaterial impact. Procedures for measuring and processing cost impact due to both changes in cost accounting practice and noncompliance's with Cost Accounting Standards have been developed by the procurement agencies, and they now require an estimate of the general dollar magnitude of the change as a first step in the process. The Board encourages the use of the materiality criteria promulgated today in conjunction with the existing two-stage cost impact evaluation procedure provided in procurement agency regulations. The Board believes that the effective use of procedures established in agency regulations will accomplish the saving in time and cost desired.

Some Government commentators proposed that 331.71(b)(2) be deleted. They expressed the view that it dealt with administrative matters and not criteria for the determination of materiality. The question of both the contractor's and the Government's responsibility in situations where noncompliance with Cost Accounting Standards resulted in a cost impact which is immaterial has frequently arisen. The Board believes that the implementation and administration of cost accounting rules, regulations, and Standards will be facilitated by a statement of the Board's position on this matter. Accordingly the Board believes that the section in question should be retained in its regulations.

Retroactive Application

Commentators expressed concern that 331.71(b)(2) would be applied retroactively to immaterial items. The language of this section requires that it be applied to the accounting period or for which the cost impact of a noncompliance becomes material and to succeeding cost accounting periods. In any cost accounting period prior to that, by reason of the provisions of this requirement, the cost impact of the noncompliance would have been determined to be immaterial. Thus, no contract modification was or is required.

Illustrations

The February 3, 1977, proposal contained two illustrations of the application of the materiality criteria. A number of commentators stated that the illustrations were too basic to be useful, and that the problems related to the determination of materiality are too numerous and too complex to be adequately illustrated in a regulation of this type. The commentators suggested that the illustrations be eliminated. The Board agrees, and has eliminated the examples in this section.

Preamble J
Preamble to Amendments of 3-10-78

The document published at 43 FR 9775, Mar. 10, 1978, added 331.20(h), (i), and (j), 331.50(a)(4)(C), 331.51, 332.50(a)(5),and 332.51, revised 331.50(a)(4)(B), and (d) introductory text and (d) (1) and (2), and amended Parts 351, 403, 406, and 409.

The purpose of this publication by the Cost Accounting Standards Board is to adopt a modification to part 331 Contract Coverage, and part 332 Modified Contract Coverage, of its rules and regulations. The Board is also withdrawing a proposal to modify 331.70. This modification being adopted will

(1) provide definitions of the terms ”cost accounting practice,” and “change to either a disclosed cost accounting practice or an established cost accounting practice,”

(2) permit the negotiation of equitable adjustments to reflect the cost impact changes agreed to by both parties to the contract, and

(3) establish the effective date for application of standards to subcontracts. The December 1976 proposal to modify the method of determining increased costs is being withdrawn.

The Board is authorized by Pub. 91-379 to prescribe rules, regulations, and modifications for implementing cost accounting standards. Pursuant to this authority, the Board is today issuing modifications to its regulations. Contractors and procurement agencies engaged in the implementation and administration of CASB rules, regulations, and standards have recommended that the Board provide guidance concerning the meaning of “cost accounting practice” and “change to either a disclosed cost accounting practice or an established cost accounting practice.”

Representatives from various organizations affected by standards have pointed out that guidance in the areas will reduce disagreement and facilitate the implementation and administration of CASB pronouncements. Similar recommendations were also received by the Board at evaluation conferences in June 1975 and October 1977. The General Accounting Office’s Status Report on the Cost Accounting Standards Program -- Accomplishments and Problems,” (PSAD-76-154, August 20, 1976), also referred to the need for guidance on these subjects.

Research in this area included review of data submitted by participants in the evaluation conference, an analysis of papers submitted various contractors, professional groups, trade associations, and Government agencies, as well as a review of existing procurement regulations, the Internal Revenue Code, Accounting Principles Board Opinion No. 20, and existing CASB promulgation’s, staff draft of amendments containing definitions of “cost accounting practice” and “change to either a disclosure cost accounting practice or an established cost accounting practice” distributed on August 13, 1976. Responses from 53 sources contributed the Board’s further consideration of the issues involved in these proposed amendments.

Proposed amendments to Board’s regulations were published the *Federal Register* on February 3, 1977 (42 FR 6591). A total of 45 responses were received from individual companies, Government agencies, professional associations, industry associations, universities and others. The proposed amendments were revise and republished for comment on October 21, 1977 (42 FR 56130) and included a proposed change to the CAS contract clause. A total of 40 responses were received to that publication.

The Board takes this opportunity to express its appreciation for the helpful suggestions and criticisms which have been furnished. These comments have resulted in a number of changes and improvements in the amendments being promulgated today. The following material summarizes the issues discussed by respondents in connection with the proposed modification and explains the changes made to the proposals published February 3 and October 21, 1977. The still relevant portions of the comments which accompanied the earlier publications have been incorporated in this material.

Definition of Cost Accounting Practice

The need for a definition of "cost accounting practice" has been raised by numerous inquiries from the field and by participants in the evaluation conferences. The Board agrees, and believes that a definition of this term can reduce disputes and contribute to increased uniformity in the administration of the CAS contract clause. A number of commentators expressed the view that the proposed definition was workable and useful as presented, would serve to reduce disagreements, and would facilitate the administration of cost accounting standards. Some said that the proposal, if adopted, would go a long way towards solving several problems identified in earlier written communications to the Board and oral presentations to the Board and its staff. Some encouraged the Board to promulgate the rule at an early date and commended the Board for taking a very significant step towards solving one of the troublesome and difficult areas of Cost Accounting Standards.

Other commentators suggested that the proposed definition went beyond the authority of the Board in that it included both the measurement of cost and the assignment of cost to cost accounting periods.

They asserted that these are financial accounting topics and are not within the realm of cost accounting. Still other commentators stated that the Board was dealing with detailed practices and procedures rather than Cost Accounting Standards and principles.

As early as March 1973, in the "Statement of Operating Policies, Procedures, and Objectives" and more recently in the May 1977, "Restatement of Objectives, Policies and Concepts," the Board stated that Cost Accounting Standards will be established to define and measure cost, determine the cost accounting periods to which costs are assigned, and determine the manner in which costs are allocated to covered contracts. The Board has spoken directly to the measurement of cost in Cost Accounting Standards 404 and 412 and to the assignment of costs to cost accounting periods in Cost Accounting Standards 403, 409, and 412. The definitions being promulgated today are consistent with the Board's authority and previously adopted view that cost accounting practices include measurements of cost, assignment of cost to cost accounting periods and allocation of costs to cost objectives. Questions have been raised as to whether the measurement of cost includes the determination of the price to be paid by the contractor for goods and services. From the beginning of the project to define a cost accounting practice, the Board has taken the position that the determination of the amount paid or a change in the amount paid for units of goods and services does not constitute a change in cost accounting practices. The definition has been revised to convey this concept more clearly.

With respect to commentators' views on the difference between Cost Accounting Standards, principles, and practices, the Board's 1973 "Statement of Operating Policies, Procedures, and Objectives" and the 1977 "Restatement" describe a Cost Accounting Standard as:

A Cost Accounting Standard is a statement formally issued by the Cost Accounting Standards Board that:

(1) Enunciates a principle or principles to be followed,

(2) establishes practices to be applied, or

(3) specifies criteria to be employed in selecting from alternative principles and practices in estimating, accumulating, and reporting costs of contracts subject to the rules of the Board. A Cost Accounting Standard may be stated in terms as general or specific as the Cost Accounting Standards Boards considers necessary to accomplish its purpose.

This position is similar to the approach the accounting profession takes in dealing with accounting principles for financial reporting. The Accounting Principles Board Opinion No of 20, Accounting Changes, states:

The term accounting principle includes not only accounting principles and practices, but also the method of applying them.

Thus, in line with previous statements, the Cost Accounting Standards Board reiterates its position that the terms "principles and practices" include methods and techniques. The Board's position is consistent with Pub.L.91-379 and reflects one of the principal purposes of setting Standards, which is to measure the full cost of supplies and services acquired by the Government in a way that is fair to both buyer and seller.

Commentators also raised the question of what should be the required level of detail of a cost accounting practice. The issue is what is the appropriate and necessary level of accounting detail for effective implementation of Pub.L.91-379. For cost allocation purposes the Board has concluded that the level of detail should include not only the type of base, e.g., direct labor, but also the composition of that base, e.g., the elements of labor costs comprising the base. Similarly, the level of detail should include the types of indirect cost pools as well as the components or items of cost which make up those pools. As to measurement of cost, the level of detail includes identification of components of a particular item of cost and the basis on which cost is measured.

Definition of Change to Either a Disclosed Cost Accounting Practice or an Established Cost Accounting Practice

With respect to the February 3, 1977, proposed definition, commentators requested expansion of those changes in cost accounting practices which would not be subject to the provisions of paragraphs (a)(4) and (a)(5 of the Cost Accounting Standards contract clause (4 CFR 331.50). Commentators recommended that changes to improve management controls, accounting changes which the Government and contractors believe would be beneficial in the long run, and change due to changed business circumstance should be added to 331.20 as action which are not considered as a change in cost accounting practice for purposes of paragraphs (a)(4) and (a)(5) of the Cost Accounting Standard Contract Clause (4 CFR 331.50).

The Board notes that in a dynamic business environment it may be desirable to make changes of many types. These changes may include organizational changes, changes in the way work is performed, and changes in the product produced. There may be a Variety of reasons for these changes such as better managerial control, new technology, or changed business conditions.

These business changes by themselves are not changes in cost accounting practices. Such changes may, however, cause a change in a contractor’s cost accounting practices. In a circumstance where there is a change in cost accounting practice, the contractor and Government must take certain action under the provisions of the CAS contract clause. Only when the contracting officer does not make the required determination under the new 331.50(a)(4)(C) would contracts be amended to insure that the Government does not pay any increased cost as a consequence of the change.

The decision as to whether there is a change in cost accounting practice is made through an analysis of the circumstances of each individual situation based on the criteria being promulgated in these regulations.

It is to be expected that the accounting system must change betterments, improvements, modifications or alterations to the system are necessary to accommodate the business changes discussed above. The Board notes that Pub.L.91-379, in its provisions relative to failure of a contractor to follow consistently his disclosed practices, makes no distinction among the causes of changes in cost accounting practices. Thus, accounting changes of the types described by the commentators, which result in a failure of a contractor to follow consistently his previously disclosed or established practices, remain subject to the CAS contract clause (4 CFR 331.50). While a number of the suggestions made have been adopted and are discussed in the following material, the suggestions that changes in cost accounting practice due to changed circumstances or to improve management control be excluded from adjustment under the CAS contract cause have not been adopted by the Board. These types of changes are subject to review and agreement by the contracting officer and the contracts may be adjusted under new 331.50(a)(4)(C).

A number of commentators urged that changes resulting from issuance’s of the Financial Accounting Standards Board should also be excluded from paragraphs (a)(4) and (a)(5) adjustments. The legislative history leading to creation of the Cost Accounting Standards Board shows that standards and principles issued for financial accounting purposes were not deemed suitable for cost accounting for negotiated Government contracts. The Cost Accounting Standards Board views its own work as relating directly to the preparation, use and review of cost accounting data in the negotiation, administration and settlement of negotiated defense contracts. The Board is the only body established by law with the specific responsibility to promulgate Cost Accounting Standards and these Standards have the force and effect of law in the negotiation, administration and settlement of defense contracts.

The Board seeks to avoid conflict and disagreement with similar organizations having other responsibilities in the area of accounting Standards and through continuous liaison makes every reasonable effort to do so. The Board will give careful consideration to the pronouncements affecting financial reporting and in the formulation of Cost Accounting Standards it will take these pronouncements into account to the extent it can do so in accomplishing its objectives. Nevertheless, the nature of the Board's statutory authority and its mission to establish Cost Accounting Standards for negotiated defense contracts is such that it must retain and exercise full responsibility for meeting its objectives. Accordingly, the Board has not adopted this suggestion.

Alterations Not Considered Changes in Cost Accounting Practices

The February 1977 proposed definitions specifically provided that certain contractor actions should not be considered as changes in cost accounting practices. These include the initial adoption of a cost accounting practice or the elimination of a cost accounting practice. A number of commentators expressed the opinion that the accounting treatment of a cost which up to a given point in time has been immaterial in amount and now becomes material in amount is a situation very similar to the establishment of a practice for the initial incurrence of a cost. They pointed out that Accounting Principles Board Opinion No. 20, Accounting Changes, treats this situation as a first time incurrence of a cost rather than a change in accounting principle or practice.

The Board has previously expressed the position that administration of the Cost Accounting Standards should be reasonable and not seek to deal with immaterial amounts of costs. In concert with this position, the Board in the October 1977 proposal modified 331.20(i) to provide that a change in its accounting for a cost which has previously been immaterial and now becomes material is not a change in cost accounting practice.

The alterations described above are not treated under the CAS contract clause as changes in cost accounting practices. They can, however, result in establishment of cost accounting practices. Where such is the case, the requirements of the CAS contract clause (4 CFR 331.50) will apply. The new practices must be followed consistently on all CAS contracts, Disclosure Statements updated where appropriate.

Subsequent Changes Under a Standard

The Board's October 1977 proposal provided that when a Standard with which the contractor has complied subsequently requires the contractor to alter a cost accounting practice in order to remain in compliance, that alteration shall not be a change in cost accounting practice for purposes of paragraphs (a)(4) and (a)(5) of the CAS clause. Some commentators said that their proposal was inconsistent with the Board's position in 4 CFR Part 403. Others said that unless a contract adjustment can be made under CAS regulations no acceptable adjustment mechanism was available. Most commentators generally felt that changes of this type should be dealt with under CAS regulations. The Board believes that this provision is not inconsistent with 4 CFR Part 403. In that Standard, the Board was limiting use of equitable adjustment to the first time that a particular allocation provision of the Standard was applied.

The Board recognizes the points made by the commentators, however, and has concluded that a change in cost accounting practice to remain in compliance with a Standard does not constitute a failure to comply with Cost Accounting Standards or to follow consistently disclosed cost accounting practices. Accordingly, the Board has deleted from the regulations being published today the provision excepting adjustments for subsequent changes under a Standard from being considered under paragraph (a)(4) of the Board's regulations, because changes of this type will be covered by new paragraph (a)(4)C) of the CAS contract clause which calls for negotiation of an equitable adjustment. The Board also notes that contractors who have filed Disclosure Statements would be required to amend such Statements to describe the practices to be followed.

Change Compelled by Law or Regulation

A number of commentators urged the Board to delete the exception in its October 1977 proposal for price adjustments under cost accounting standards for changes compelled by law or regulation 331.20(i)(3). Some contended that all changes, regardless of motivation, should be considered for adjustment under the Board's new proposed subparagraph dealing with changes agreed to by the parties. Other commentators urged the Board to remove the exception to preclude a contractor from experiencing a windfall or suffering a loss because of such changes. The Board agrees with the suggestions made to delete this paragraph, because the Board feels that all contractor proposed changes in cost accounting practice should be considered for contract adjustment. Therefore, contractor desiring to make a change in cost accounting practice for any reason must negotiate with the contracting officer under the appropriate paragraph of the CAS contract clause.

Should a situation arise where major changes in cost accounting practices would be required by contractors to comply with express provisions of law or regulation, the Board would seek to accommodate any such requirement by a change in its standards, rules or regulations.

The Board has deleted from these amendments the proposed 331.20(I)(3) which dealt with changes compelled by law or regulation.

Illustrations

Many commentators said that all or some of the illustrations should be deleted, while other commentators said they should be retained. The Board included the illustrations to demonstrate the application of the definitions in situations of the type which have been reported to the Board in the past.

The Board noted that some of the illustrations dealing with changes in organization were being misinterpreted. In effect, the commentators expanded the illustrations to include situations not set forth in the illustrations. The Board concluded that in view of the extent of misinterpretation, it would be questionable value to revise the illustrations to cover all the situations described by commentators. Accordingly, several illustrations dealing with accounting changes related to organizational changes have been deleted.

As the Board stated when the proposed definitions were published in February 1977, the accounting effects of any organizational change must be considered separately and a final decision concerning a change must be based on an evaluation of those effects. Thus, an organizational change per se is not a change in cost accounting practice. One must look at any accounting revision brought about for any reason, including one caused by a change in organization.

By including the illustrations the Board does not intend to imply that all possible situations are covered nor are the illustrations to be used as limitations for accounting changes. The Board believes that the changes made to this section are responsive to the statements made by commentators.

Contract Clause

The Board proposed in October 1977 that where the parties agree to a change in cost accounting practice they should negotiate an equitable adjustment for any cost impact on existing contracts. Most commentators agree with this proposal but some felt that the contracting officer's agreement should not be necessary. Others urged the Board to state that a contracting officer's disagreement with a change is subject to the disputes clause of the contract. Further, a number of commentators suggested that the new contract adjustment paragraph be renumbered (a)(4)(C) to avoid confusion with the preexisting numbering series. Finally, some commentators asked if the Board planned to make comparable revisions to its Part 332, Modified Contract Coverage.

The October 1977 proposal was in response to urging by both contractor and Government agency representatives to establish an alternative to paragraph (a)(4)(B) for adjusting contracts where both parties agreed that a change in cost accounting practice was desirable. Under that proposal, a method was established providing for equitable adjustment for these changes. The Board does not agree that contracting officer's agreement is not necessary and remains convinced that Government agreement to the change is essential to protect the Government's interests.

With respect to the treatment of a contracting officer's disagreement with a proposed change in cost accounting practice under the disputes clause of the contract, the Board believes this should be determined under agencies' general rules governing appeals from various types of decisions by contracting officers. Accordingly, the Board has not specifically provided for the application of the disputes clause in this situation.

The Board agrees with the suggestion concerning the renumbering of the paragraph dealing with equitable adjustments for changes in cost accounting practices agree to by the parties. The amendments being published today have that paragraph numbered (a)(4)(C). Designating the new paragraph as (a)(4)(C) eliminates the need to change citations in other subparagraphs in section 331 from those previously existing in CASB regulations.

With respect to the question concerning comparable revisions to Part 332, the new definitions and illustrations are incorporated in 332.20 by the existing cross reference to 331.20. The Board's regulation concerning changes in cost accounting practices agreed to by the contracting officer will be incorporated in 332.50(a) and 332.51 by amendments being published today.

Increased Cost Paid

Commentators at the 1977 Evaluation Conference and respondents to e the February 3 and the October 21, 1977, proposals requested that the Board remove from its regulations the prohibition against increased costs paid because of changes in cost accounting practices 331.50(a)(4)(B)) and/or that the expression "increased costs paid" (4 CFR 331.70) be redefined to exclude fixed price contracts. The Board has established a priority project to perform a comprehensive review of Part 331 of its regulations including the treatment of increased costs paid.

Contracting Officer Determination

Many commentators objected to the Board's including a requirement that contracting officers make a finding that a change is desirable and is not detrimental to the interest of the Government. Some claimed that such a requirement encroached on management's prerogative to design an accounting system to meet its needs; others said the decision concerning changes was an administrative matter better left to the agencies. Others suggested that different terms be substituted for some of the words. Finally some commentators said that the Board should require only that agencies prescribe appropriate regulations for the use of the equitable adjustment provision for accounting changes agreed to by the parties.

The Board understands the concerns expressed by the commentators on this matter. It should be recognized, however, that the Board is proposing that equitable adjustments be negotiated for accounting changes not required by Standards. This type of Provision was requested by many contractors and Government agencies in the past. These groups insist that agreed-to changes should be allowed and the contractor should not be required to pay for any increased costs on existing contracts resulting from such desirable changes. The Board is responding to these requests by providing for equitable adjustments for those proposed changes with which the contracting officer agrees if he finds them to be desirable and not detrimental to the interests of the Government.

Management certainly can propose any changes it feels desirable for its own accounting system. If a change is not desirable from the Government point of view, the Board sees no justification for permitting the contractor to realize economic benefits on existing contracts from the change.

The Board's regulation merely recognizes the contracting officer's position and does not encroach on the administrative responsibilities of the procurement agencies. A contracting officer would routinely make certain that a contractor's proposed change is not detrimental to the Government before agreeing to allow increases in contract prices.

Some suggested alternative words for "desirable" were: "Appropriate, warranted, equitable, fair or reasonable." The Board concludes that all these tests are encompassed by the Board's language. Accordingly, this statement has not been changed.

The Board expects administration agencies to publish regulations they feel necessary to define what they conclude is "desirable and is not detrimental to the interest of the Government." Thus, the Board does not agree that it is getting involved in administrative matters. The Board agrees with the commentators who suggested that the second sentence of

331.51, which required that the contracting officer document the basis for his finding, be eliminated. The Board believes that the stated documentation requirement is redundant with other language in this subparagraph, and accordingly, that sentence has been eliminated.

Withdrawal of Proposed Alternative Method of Determining *Increased costs*

On December 29, 1976, a proposal was published in the *Federal Register* to amend 331.70(b) which, if adopted, would have permitted procurement agencies to use either an estimate-to-complete approach or an original-negotiation-data approach to determine increased costs paid by the United States. As proposed, agencies would have been authorized to use the estimate-to-complete method when negotiations had not been based on cost estimates or such estimates were not readily determinable by the procuring agency.

Most of the comments received expressed opposition to all or part of the proposal. Upon reexamining the subject in light of the comments received, the Board concludes that the proposed alternative method would not provide sufficient improvement in the administration of Standards to warrant its adoption. Additionally, none of the alternatives suggested by the commentators appears likely to benefit the procurement process materially. Accordingly, the proposal to amend 331.70(b), Contract Coverage, as published in the *Federal Register* of December 29, 1976, is hereby withdrawn. This subject will be considered in the Board's comprehensive review of Part 331.

Costs and Benefits

The definitions promulgated today fill a void that had been recognized in numerous comments to the Board and the procurement agencies. The Board believes that the material being promulgated today is in keeping with its responsibility and authority as provided in Pub.L.91-379. The Board believes further that the appropriate use of the definitions can significantly reduce the time and effort involved in the administration of Cost Accounting Standards. The Board concludes, therefore, that there will be virtually no costs involved in implementing these regulations and that there will be significant benefits with no inflationary effects.

Miscellaneous Amendments

A number of miscellaneous amendments are being published today to conform language in certain paragraphs of Title 4 CFR Parts 351, 403, 406 and 409. These amendments add references to the new 331.50(a)(4)(C).

Effective Date

The following changes to the Board's regulations are being made effective today, March 10, 1978.

Preamble K
Preamble to Amendments of 6-8-78

The document published as 43 FR 24819, June 8, 1978, added 331.30(b)(3) and revised 403.70(b), 408.70. and 410.70 and 415.80. Portions of this preamble relating to Parts 401 through 410 and 415 have been omitted; they can be found in the supplements to their respective parts.

The Cost Accounting Standards Board is authorized by Pub.L.91-379 to prescribe rules and regulations exempting from its requirements such classes or categories of defense contractors or subcontractors under contracts negotiated in connection with national defense procurements as it determines on the basis of the size of the contracts involved or otherwise, are appropriate and consistent with the purposes sought to be achieved by the Act.

The Cost Accounting Standards Board has been requested by several Federal agencies and by representatives of educational institutions to consider the extent to which its standards, rules, and regulations should apply to educational institutions that are subject to Federal Management Circular 73-8 or OMB Circular A-21 and to consider whether an exemption for such institutions from Board promulgation's is appropriate. The Board had provided exemptions for them in certain specific standards where the application would not be appropriate.

On March 15, 1978, the Board published for comment in the *Federal Register* (43 FR 10699) a proposal to exempt most educational institutions. The exemption would not apply to contracts with federally funded research and development centers operated by such educational institutions. Forty-seven comments have been received, all of which favored the proposed action by the Board although some respondents requested minor changes and clarifications.

A few commentators expressed concern that an educational institution receiving a contract from the Government could apportion the contract effort between the university and the FFRDC to take advantage of differences in cost accounting required under CAS and under FMC 73-8. If this becomes a problem, the procuring agencies are able to take the necessary corrective action.

Several commentators noted that there could be some misunderstanding concerning the applicability of CAS 403 to the university which is functioning as a "home office" for an FFRDC. The Board intends that CAS 403 not be applicable to the university in this situation and minor changes have been made to the language to clarify its intent.

One commentator indicated that the definition of FFRDC is not meaningful and suggested that the Board list the criteria by which NSF designates an FFRDC. Since coverage is intended only for those organizations designated as FFRDC's by the NSF based on whatever criteria they deemed appropriate, inclusion of their current criteria would not be useful. Accordingly no changes have been made in the definition included in 331.30(b)(3).

One commentator noted that the removal of current exemptions from CAS 403, 408, and 410 for FFRDC's will require a transitional period. It is considered that the provisions of 403.70(a), 408.80, and 410.80 will furnish sufficient time for compliance by the FFRDC's with those standards. Section 403.70(a) provides that a contractor, if not exempt, shall be required to comply at the start of his first cost accounting period following receipt of the award of a negotiated national defense contract making the standard applicable. A contract awarded after August 1, 1978, will make the standard applicable to a FFRDC. Consequently, a FFRDC must comply with CAS 403 as of the start of its next cost accounting period after receipt of a contract after August 1. Standards 408 and 410 apply in the same way. It is recognized that all FFRDC's do not necessarily receive new contract each year and that annual funding may be by means of an amendment to an existing contract. Applicability would be at the start of a cost accounting period after receipt of a new contract or after receipt of the annual extension of an existing contract.

The Board having found the exemption appropriate and consistent with purposes sought to be achieved by Pub.L.91-379, is modifying its regulations as set forth below.

Preamble L
Preamble to Amendments of 11-14-78

The document published on Nov. 14, 1978 at 43 FR 52693 revised 331.30 (b)(5), (c)(1) and(c)(2).

The Cost Accounting Standards Board is today promulgating amendments to its regulations dealing with exemptions for contracts and subcontracts performed by foreign governments and foreign concerns. On July 31, 1978, the Cost Accounting Standards Board published a proposal under which contracts or subcontracts with foreign concerns could be exempted from certain individual standards if an authorized official of a relevant Federal agency determines that application of the standards to such contracts or subcontracts is inappropriate. The Board received 12 comments on the proposal.

One commentator opposed the proposal as unnecessary because the Board itself has authority to grant exemptions when such action is appropriate and asserted that delegation is undesirable because such decisions are too important to be delegated. The Board agrees that decisions concerning exemptions are important and has carefully considered the proposed action in the light of all comments and other available information. Based on that consideration the Board has concluded that it should grant a specific categoric exemption. Consequently no delegations are needed. Moreover because of the categoric exemption, the need to amend individual standards is obviated.

One government agency to whom delegation of authority was proposed noted that in implementing the delegation, one of the factors it would consider in determining whether the application of an individual standard is appropriate is the matter of sovereignty. Because of the action being taken today, there is no need to comment on the appropriate weight to be assigned to that factor.

Another commentator also discussed sovereignty and suggested that the United States has no legal right to impose the requirements of its laws and regulations on foreign contracts. To support this assertion, the commentator cited an official of the Department of Defense who attributed some of the difficulties in foreign procurements to the insistence upon contracts rather than general agreements. Whether a contract or some other instrument is used is something to be decided by other agencies of the government and not by the CASB. The Board has long recognized that its Standards are not applicable to noncontractual arrangements and agrees with the suggestion that if the procuring agencies used some noncontractual arrangement to transact business with foreign contractors, CAS would be inapplicable to the transaction. However, when the parties agree to use a negotiated national defense contract or subcontract as the vehicle for transacting business, the agreement must include the standards, rules, and regulations of the Board.

One commentator expressed the opinion that no substantial benefit would accrue to the United States under the limited exemption originally proposed but that a complete exemption from all Cost Accounting Standards Board requirements would be beneficial. Instead of the proposed exemption and delegation, that commentator recommended that all contracts and subcontracts with foreign firms and governments be exempt from all CAS requirements. The Board does not agree that a limited exemption would produce no significant benefits but that a complete exemption would. Significant benefits accrue to the United States Government from all standards, in part because each standard enhances the likelihood of achieving the goal of uniformity and consistency set forth in Pub.L.91-379. The Board believes that by exempting foreign contracts from some standards there is a detriment rather than a benefit insofar as the public law itself is concerned. Nonetheless the Board has been advised that the requirement to apply some standards has become a significant impediment to efficient, successful contracting with foreign concerns and foreign governments.

The exemption being granted today will remove that impediment while continuing to provide protection through the application of CAS 401 and 402. In addition, foreign concerns will still be required to file Disclosure Statements.

The requirements of CAS 401 and 402 are fundamental to any sound cost accounting program. In the Board’s view application of these standards is essential to provide some assurance that a contractor’s cost accounting practices are sufficient to provide reliable information on which to base the negotiation, administration, and settlement of contracts. Similarly, the requirement for disclosure which is also being continued unchanged, serves to assure that necessary information about cost accounting practices is available to the Government.

Several commentators recommended that in addition to contracts with foreign contractors, the Board should exempt contracts with foreign governments. The Board has concluded that this recommendation has merit and the exemption being promulgated today has been amended accordingly. Because the exemption established in 1972 for the Canadian Commercial Corp., an agency of the Canadian Government, is included in today’s exemption action, the 1972 exemption is being withdrawn.

One commentator suggested a need to define “foreign concerns” and another recommended that “performance” be defined. The term “foreign concern” has already been defined by the Board in 331.30(c)(2).

As to what constitutes “performance,” the Board believes that in general it encompasses the contractor’s activity under the contract up to the point of inspection and acceptance of the items called for by the contract. However, because of the complexity and variety of contracts, the Board believes that the contracting agency can best determine whether a specific contract is to be performed outside the United States.

A number of commentators suggested various changes in the delegation procedures proposed by the Board. Since the Board is withdrawing the delegation, there is no need to consider these suggestions.

One commentator suggested that the reference in 331.30(c) to the Assistant Secretary of Defense (Installations and Logistics) be changed to reflect organizational changes in the Department of Defense. This revision has been made.

Preamble M
Preamble to Revision, 9-18-80

The material set forth below is the preamble to the revision and republication of Part 331, September 18, 1980, at 45 FR 62011. This preamble to the publication of September 18, 1980, is included as part of the administrative history of Part 331.

Summary

On June 1, 1979, the Board published in the *Federal Register* proposed revisions to Parts 331, 332 and 351 of its regulations dealing with contract coverage and the filing of Disclosure Statements. Based on comments to its June 1 proposal, the Board made substantial modifications in the proposed revisions and republished the revised Parts again for comment on February 8, 1980. After considering the comments to the second publication and reviewing all suggestions from interested parties, the Board has determined that the revised regulations are ready for promulgation. It believes that the revised regulations will result in improved administration and will be more readily understood by parties subject to the regulations.

Effective Date

April 1, 1981.

Supplementary Information

In the *Federal Register* of June 1, 1979, (44 FR 31655) the CASB published for comment proposed revision to Parts 331, 332 and 351 of its regulations. The revisions were made for the purpose of simplifying these parts of the regulations and to modify them where experience indicated the changes would be desirable. Thirty-six responses were received by the Board to its request for comments.

The Board after consideration of the comments modified its proposed revisions and again published the revised parts for comment in the *Federal Register* of February 8, 1980 (45 8677). Twenty comments were received to the February publication. The Board wishes to thank all of the respondents for their constructive suggestions which were of substantial assistance to the Board in its review and revision of these parts.

In the February 8 proposal two areas of the regulations drew a substantial number of comments from the respondents, the exemption of firm fixed price contracts (FFPs) awarded without submission of cost data and the definition of “increased costs paid by the Government” as such may occur under FFPs after award. The Board’s views on these two areas and on other comments received are as follows:

1. *Exemption.* Commentators generally endorsed the Board’s proposal to exempt FFPs awarded without submission of any cost data. However, most commentators urged the exemption be expanded to require that cost data be certified or that the data have been relied on as the basis of price.

> The Board is not persuaded that the suggested modifications should be made in describing those contracts which would be subject to this exemption. Situations occur in which cost data are submitted in support of a price but are not certified because the award is designated as adequate price competition. Whether the data are used in a particular case can be difficult to establish. The Board however is satisfied that such data would not be submitted unless they were to be used. Because of this and because of the administrative simplicity of the test, the Board believes that the circumstances which would support an exemption of certain FFPs being adopted today is appropriate.
>
> One commentator opposed the establishment of this exemption on the grounds it provided a positive incentive for a potential contractor to seek to avoid submission of cost data. Controlling law and regulations establish the circumstances under which a potential contractor may be required to submit cost data to support a price proposal

in a national defense procurement. In addition Government representatives have authority to act to assure that the Government's interests are properly protected. Consequently, whether a potential contractor may or may not have an incentive to avoid submitting cost data is not determinative as to whether such data are submitted. The Board believes that Government representatives, in cases where they deem it appropriate, will obtain whatever data they are entitled to. Nonetheless, the Board acknowledges that linking application of Cost Accounting Standards to submission of cost data could result in requests for waivers from the cost data submission requirements that would not be made if cost data alone were involved. In order to preclude this result the Board has revised the exemption so that contracts on which submission of cost data was avoided by obtaining a waiver of cost or pricing data requirements nonetheless remain subject to the Cost Accounting Standards requirements.

2. *"Increased costs paid" under FFPs after contract award.* In its February 8 proposal the Board deleted certain proposed revisions contained in its June 1, 1979 proposal concerning the adjustment of FFP contracts in view of the objections of most commentators to the proposed changes. The Board in its February proposal limited changes in the regulations affecting FFPs to a clarification in 331.70(b) concerning the measurement of increased costs paid by the United States under those contracts. The modified 331.70(b) paragraph was the subject of adverse comment by a majority of industry commentators who maintain that under FFP contracts once price is agreed to, there can be no increased cost paid by the U.S. attributed to any subsequent changes the contractor may make in its cost accounting practices.

The question of adjustment of FFPs has been the subject of extensive discussions since 1972. In its original promulgation's the Board recognized that there was increased cost paid by the U.S. under a FFP contract if during the accumulating and reporting process the contractor adopted practices that reduced his cost allocations below the allocation determined during the estimating process. It is noted that in the proposed contract regulations published for comment on December 30, 1971, a provision the same in all essential aspects to the present 331.70(b) was included. At that time no commentator questioned the applicability of CAS to FFPs.

The second sentence of Section (h)(l) of Pub.L.91-379 is as follows:

Such regulations shall require * * * a contract price adjustment, with interest, for any increased cost paid because of the defense contractor's failure to comply with * * * standards or to follow consistently his disclosed cost accounting practices * * * in pricing contract proposals and in accumulating and reporting contract performance cost data.

This provision prescribes price adjustments for all contracts where there is a failure to comply in pricing proposals and in accumulating and reporting costs. Since the Congress did not exclude FFP contracts when it provided for recovery of increased cost paid to the contractor because of a failure to comply or failure to follow, it was and still is incumbent on the Board to insure that, in the absence of an exemption, such recovery is accomplished. Pub.L.87-653, Truth in Negotiations, provides that the price of a contract shall be adjusted to exclude any significant sum by which a firm fixed price was increased because the cost data furnished by the contractor, in essence, was insufficient to enable the Government to judge accurately the contractor's cost estimates used in negotiating. The Board's requirements for adjustments to firm fixed price contracts when there is a failure to follow the cost accounting practices on which price was based embody essentially the same measurement principle. The Board's requirements concerning fixed price contracts constitute a recognition of the fact that the price agreed to at the outset is higher than the price that would have been agreed to if the Government had known about the accounting change. This constitutes a constructive increase in the costs paid by the United States. In view of the foregoing, the Board's regulations will continue to require recovery of increased costs paid by the United States on FFPs. However, to emphasize that the contracting parties are the ones to determine what the contract price would have been and that there are no precise rules to be used in such determinations, further provision has been added to 331.70(b).

(3) *Modification of 331.70(f).* One commentator suggested that 331.70(f) be modified to delete reference to "all affected contracting officers" and place the authority to effect agreement in the hands of one contracting officer delegated by affected agencies to handle CAS matters. In 331.70(e) the Board urged that the contracting agencies designate such an individual and generally agencies have done so. However, this is a voluntary action of the agencies and the Board is not

in a position to make it mandatory.

Two commentators urged 331.70(f) be modified to refer to aggregate cost increases and offsets rather than deal, with adjustments to individual contracts. In 331.70 (e) and (f) the CASB has suggested techniques which it considers will permit substantially easier administration in situations in which number of covered contracts may be involved. However, basic procurement statutes and Pub.L.91-379 all deal with individual contracts and in the end adjustments must be made on an individual contract basis. Consequently, it is considered that reference to adjustments on an individual contract basis and allowance for offset among contracts where appropriate is the more precise way of discussing contract price adjustments.

(4) *Statement on Fairness.* One commentator requested the Board issue a statement on fairness in the application of its contract clause and related interpretations. The essence of the statement recommended would be that the results in any particular case arising from application of the Board's Standards, rules and regulations must be deemed "fair" in some general undefined sense by the negotiating parties or the Board's issuance may be disregarded. The Board's Restatement of Objectives, Policies and Concepts contains a statement that a Standard is fair when, in the Board's best judgment, it shows neither bias nor prejudice to either party. The Board views its rules and regulations on contract and price adjustments in the same light. In any given case, the results of contract pricing may ultimately be regarded as fair or unfair by either or both parties to the contract because, on a case-by-case basis, fairness is viewed from the personal vantage point of the particular party. It is impossible to adopt such a subjective criteria and have meaningful Standards. Consequently any attempt to define "fairness" in the context of individual contract negotiations is inappropriate.

(5) *Miscellaneous.* There were various miscellaneous comments and suggestions on the Board's proposal to which the following comments are addressed:

(a) *Application of revised regulations.* Two commentators requested that the regulations, as revised by this promulgation, be applied to existing contracts. To the extent the Board has restated its interpretations to its regulations, such restatement would apply to existing contracts. However, other modifications will become effective only on the date specified in the revised regulations. This date is established so that sufficient lead time is available to procurement agencies to develop and publish any implementing regulations or instructions. The revised regulations other than restated interpretations will only apply to contracts and events which occur after the effective date of the regulation.

(b) *Section 351.120(a), Disclosure Statement revisions.* This paragraph was modified to provide that a Disclosure Statement must be revised when a change is made by the contractor whether or not the Government has agreed to the change. One commentator objected to this revision on the grounds it would increase the contractor's workload substantially. The change was made merely to clarify an existing requirement. It does not make a substantial change in the requirements set forth in the paragraph.

(c) *Increase the threshold for contract coverage and Disclosure Statement application.* Several contractors requested that the Board increase the threshold for contract coverage so as to make the application of CASB requirements effective only on contracts of $500,000 or more. Commentators also stated that the threshold for Disclosure Statement application should be increased. The Board has recently given consideration to both of these suggestions and is of the opinion that current thresholds are appropriate and no change in threshold application has been made in the regulations published today.

(d) *Deletion of post award disclosure under 331.60.* One commentator objected to the deletion under 331.60 of the provisions for post-award submission of Disclosure Statements. The Board considers the time currently provided under 351.40 to be more than adequate for the preparation and submission of Disclosure Statements prior to award. Consequently, it considers that provisions for post-award submission is unnecessary.

(e) *"Cost to Complete" method of 331.70(b).* One commentator urged that the Board provide under 331.70(b) for the use of the "Cost of the Complete" method of determining contract adjustments. It is considered that this paragraph, as revised, gives the contracting parties sufficient guidance with respect to the measurement of price impact. Consequently, the requested change has not been made.

(f) *Deletion of submission of disclosure statement of CASB.* Since the Board was receiving copies of disclosure statements to assist in its research in developing standards and since that development has been substantially completed, receipt by the Board of disclosure statements is unnecessary. Consequently, this requirement has been deleted.

Title 4 CFR Parts 331 and 332 are revised in their entirety and Part 351 is amended by revising 351.30, 351.40, 351.60, 351.70, 351.80, and 351.120 and by deleting and reserving 351.50 and 351.110 as follows:

Preambles to Part 332,
Modified Contract Coverage

Preamble A
Preamble to Original Publication 9-12-77

The material set forth below is the preamble to the original publication of Part 332, 42 FR 45625, Sept. 12, 1977.

Contract Coverage, Modified Contract Coverage, Basic Requirements And Cost Accounting Standards

This publication adds a new Part 332 and amends Parts 331, 351 and 403 of the Cost Accounting Standards Board's rules, regulations and Standards. The proposal to add Part 332 and amend Parts 331 and 351 were published for comment in the February 16, 1977 *Federal Register* (42 FR 9389). The proposal to amend Part 403 was published for comment in the November 30, 1976 *Federal Register* (41 FR 52473). Appropriate periods for comment on the proposals were provided. Numerous and extensive comments were received concerning both proposals. The Board appreciates the interest expressed by the commentators and thanks them for their participation.

Comments of Parts 332, 331 and 351

General

Many commentators expressed general approval of the proposal to exempt certain businesses and provide modified coverage for others. Information available to the Board does not demonstrate that the benefits to be derived from applying all requirements to all contracts clearly outweigh cost of requiring such application, moreover the Board does not believe that many small companies with less sophisticated accounting systems and small accounting staffs can comply with the Board's requirements without experiencing inordinate difficulty and some cost. Under these circumstances, the Board has concluded that it is appropriate to remove completely the obligation of small businesses to comply with Standards, rules, and regulations of the Board. In reaching this conclusion the Board has also given some weight to the belief expressed by a few commentators that the prospect of having to comply with Board requirements has caused some companies to avoid Government contracts.

As noted by some commentators who opposed the Board's proposal, the granting of exemptions tends to reduce rather than increase uniformity of cost accounting practices because of the exemptions. In that sense the action may be viewed as not being in furtherance of that statutory goal which is set forth in Pub.L.91-379. It has long been recognized that uniformity is an extremely important objective of the Board's actions. It is not, however, the only consideration. If there were any doubt on this point, the fact that the Law authorizes the Board to prescribe rules and regulations exempting contractors from its requirements should dispel that doubt. The Board believes that the action being taken is consistent with its statutory duties viewed as a whole even though uniformity among some business units will be reduced.

Threshold Determinations

Several commentators noted that the $10 million threshold provided in Part 332 would be based on all contracts subject to Cost Accounting Standards rather than being limited to national defense contracts and subcontracts. They noted that Pub.L.91.379 does not apply to nondefense contracts and that such contracts are subject to Board Standards rules and regulations only to the extent that the Administrator of General Services has extended coverage to it. Because of this they urged that the calculation be made only on the basis of national defense contracts and subcontracts. This recommendation has been adopted by the Board.

The proposal to exempt all contracts under $500,000 was viewed as generally desirable by many commentators. Some recommended that $1 million or more be established as the minimum coverage level. However, some commentators opposed exempting small contracts of a contractor required to follow Standards on large contracts. They contended that once the contractor has to establish practices in compliance with Standards, there is no additional burden involved in applying those practices to its small contracts. In any case it is unlikely that application of those practices could result in burdens that would be equal to those that would result from applying one set of cost accounting practices to large contracts and another set to small contracts. For this reason the Board has not adopted the proposal to exempt all contracts under $500,000. Instead the existing provisions providing for coverage of smaller contracts awarded to a business unit which has received an award of $500,000 or more are being retained.

One commentator noted that some contractors receive contract awards of $10 million or more every other year and few, if any, covered awards in the intervening years. The large contracts would not be subject to disclosure requirements or Standards under the February 16 proposal. The Board has remedied this problem by providing that any single contract award of $10 million or more is subject to all Standards and must be covered by a Disclosure Statement.

Small Business

Several commentators urged that all businesses which qualify as small business concerns under the rules and regulations of the Small Business Administration be exempted. The February 16, 1977 proposal would have provided such an exemption only for a small business which received less than $10 million in awards during its preceding fiscal year. Modified coverage would have been provided for other small businesses. Research indicates that there are very few companies which would fall into the category of small businesses receiving awards of $10 million or more. In the interest of using a single test, i.e., whether the contractor qualifies as a small business concern, rather than a dual test which would result only in a few small businesses being subject to modified coverage, the Board has adopted the recommendation to exempt all small business concerns. Research indicates that if this action had been applied to Federal Fiscal Year 1976 it would have resulted in exemption of 196 small business concerns which were doing business with the Department of Defense and which had $460 million of contracts of the type subject to Cost Accounting Standards. Consequently, on average, each small business concern would have a relatively small amount of covered contracts.

Other Categories

Various commentators renewed previous recommendations that the Board exempt other categories of contracts and contractors. The categories included colleges, universities, non-profit organizations, hospitals, and Government-owned contractor-operated facilities. The Board has considered these recommendations and concluded that none of these categories should be exempted.

Part 332 Eligibility

The February 16 publication would require that a contractor have less than $10 million in covered contracts and that the covered contracts be less than 10% of total sales to be eligible for Part 332. In discussing this provision some commentators proposed a wide variety of tests in lieu of the tests proposed in that publication. Some suggested using only a dollar test or only a percentage test rather than both. The amounts recommended ranged up to $100 million and 50 percent of total sales. Some suggested using sliding scales to determine eligibility. None of the suggested tests appear more likely to achieve the purposes of the Board than the test originally proposed. The Board has therefore retained its initial proposal.

Scope of Part 332

A number of commentators recommended that eligibility for Part 332 should result in complete exemption. Others recommended that requirement for compliance with Parts 401 and 402 be the only requirement and that the disclosure obligation be eliminated. The Board believes that substantial benefits may be derived by continuing to require compliance with Parts 401 and 402. There is nothing which suggests that compliance with the two Standards entails any significant cost. Consequently this requirement is being retained. According to information reported to the Board, adoption of Part 332 will relieve 264 segments of 131 contractors of the requirements to comply with all Standards but will remove only $405 million of contracts from full coverage.

Disclosure Statement Requirements

Many commentators suggested that preparation of a Disclosure Statement was burdensome. They also contended that in the situation where a large commercial contractor receives only a few small contracts containing a Cost Accounting Standards clause the need for a Disclosure Statement appears to be minimal. Some asserted that adoption of the proposal to require a Disclosure Statement for all covered contracts would reduce the number of companies that would accept contracts subject to the Board's Standards, rules and regulations. The Board is persuaded that for the time being Disclosure Statements should not be required for all covered contracts. Accordingly it is not adopting the February 16 proposal. The Board is retaining the existing Disclosure Statement requirement provided in Part 351 except that a business unit will be required to submit a Disclosure Statement if it is a company or a segment of a company which received awards of national defense contracts subject to Cost Accounting Standards in excess of $10 million during its preceding cost accounting period rather than the preceding Federal fiscal year.

Revisions to Part 351

Part 332 and the amendments to Part 331 generally will result in annual determinations being made a contractor's obligation to follow Standards and to submit Disclosure Statements. The determination will be made on the basis of sales and award data from the immediately preceding cost accounting period. The requirement to continue to submit a Disclosure Statement so long as the contractor has a contract subject to Cost Accounting Standards will no longer apply. Disclosure Statements must be maintained for and applied to only those contracts which were awarded during a cost accounting period which the contractor met the filing requirements of 351.40. Sections 351.40 and 351.50 have been revised to reflect this change.

Segments of Large Companies

A number of commentators sought to have small segments of large companies treated in the same way the small businesses are treated. In the view, small segments are competing the same environment as small business and are operating with essential similar capacity and resources. Therefore, such segments, they concluded should be subject to the same rules as small business. The Board does not accept this line of reasoning. Even those cases where a segment may appear to operate as a small business its status as a segment precludes it from being regarded in the same way. It has available to its capacities and resources of the company of which it is a part. Also the policy considerations of the Small Business Act has no applicability to segments of larger company. Further, as a practical matter, the rules already exist in the Small Business Administration for identifying small business concerns. There are no comparable rules for identifying small segments.

As indicated by the February 16 proposal the Board nonetheless recognizes that segments which are engage in primarily noncovered work should be eligible for modified coverage. This coverage is provided by Part 332. It will apply to segments which according to information submitted to the Board have average covered sales of approximately $1.4 million per segment. The relatively small amount of covered contract sales by each of these segments, the limited Government interest in the total business activity of the unit and the fact that the implementation and administration involves some cost lead to the conclusion that modified coverage is appropriate and sufficient to protect the interests of the Government.

Summary

The results of the Board's adoption of Part 332 and amendment of Parts 331 and 351 are:

1. None of the Board's requirement apply to a business unit unless it has received an award of at least one covered contract of more than $500,000 Thereafter covered contracts of more than $100,000 are subject to the Board's requirements.

2. A Disclosure Statement must be submitted by any business unit receiving a covered contract if it is either a company which received net awards of negotiated national defense prime contracts and subcontracts subject to Cost Accounting Standards totaling $10 million or more in its preceding cost accounting period or a segment of such a company.

3. Contracts awarded to any business unit which received less than $10 million in awards of covered contracts in its preceding cost accounting period are subject to:

(a) Standards 401 and 402, if the dollar amount of such awards is equal to less than 10 percent of the business unit's total sales during that period; or

(b) All Standards, if the dollar amount of such awards is equal to 10 percent or more of the business unit's total sales during that period.

4. Any single award of a covered contract of $10 million or more is subject to all Standards and requires submission of a Disclosure Statement.

5. Contracts awarded to any business unit which received $10 million or more in awards of covered contracts during the preceding cost accounting period are subject to all Standards.

6. Notwithstanding the foregoing, all businesses which qualify as small business concerns under the rules and regulations of the Small Business Administration are exempt from all Cost Accounting Standards Board requirements.

Comments on Part 403

With respect to the amendment of Part 403, the November 30, 1976 proposal was to revise that Standard to make it applicable to any contract which was subject to Cost Accounting Standards generally. The amendment being promulgated today retains this concept. However, as recommended by a number of commentators, the Board deferred the promulgation of this amendment pending the amendments to Parts 331 and 351 and the addition of Part 332 discussed above.

The decision to extend the application of Part 403 to additional contractors was made on the basis of extensive research. This research included both those contractors who were already required to use Part 403 and those who were expected to use it as a result of this amendment. With respect to the current users, the Board is satisfied that this Standard has resulted in more equitable allocations, with little administrative effort in most cases. With respect to potential additional users, the research indicated that many of these would have to make few, if any, changes to comply with Part 403 and that the remainder could comply with little difficulty. The Board notes in addition, an independent study by the Conference Board which found that defense contractors who are using Part 403 for contract costing purposes are using the same allocation procedures for internal reporting purposes. According to the Conference Board, it was typical of these companies to allocate home office expenses on a blanket basis prior to the promulgation of Part of 403. (Information Bulletin No. 17, February 1977.)

A number of commentators suggested various limitations for the application of Part 403. Some of these suggestions were expressed in general terms. Some of the commentators recommended, for example, that the requirement to use Part 403 should not be extended to "small contractors." Alternatively or additionally it was recommended that Part 403 should not be required for a large contractor with little work subject to Cost Accounting Standards. More specifically, recommendations were received to exempt those contractors with less than 10 percent of their revenue from Government work. Others recommended that contractors who have less than $10 million in contracts subject to Cost Accounting Standards should be exempt. The Board believes that the recommendations of this nature have been accommodated to the extent desirable and practical by the amendments to Parts 331 and 351 and the addition of Part 332 being promulgated today. Accordingly, any further exemption from Part 403, specifically, is considered to be unnecessary.

In publishing the proposed amendment to Part 403 in the *Federal Register* of November 30, 1976, the Board stated that there is evidence that almost all contractors who were required to make significant changes in their allocation practices as a result of Part 403 did so without undue trouble or expense. Several commentators questioned the Board's conclusion in this regard. The Board's conclusion was based in part on Staff research involving 147 home offices who now use Part 403 to allocate home office expenses. This research sought to determine, among other things, the administrative problems and expense involved in making allocations pursuant to Part 403. Government auditors reported that of the 147 home offices, only 4 had problems in developing the necessary data and that there was evidence of significant administration costs at one of these four offices. In addition, evidence of significant administrative costs in making the allocations was found by the Government auditors at four other of the 147 home offices.

Some of the respondents who questioned the Board's conclusions regarding administrative problems and expense referred to an industry report on the economic impact of Cost Accounting Standards as support for this position. These respondents variously referred the Board to those sections of the report which summarized

(i) contractor's appraisal of benefits from Part 403;

(ii) the number of contractors who were required to make changes as a result of Part 403,

(iii) the number of noncompliance notices issued in connection with Part 403 and

(iv) the increase and decrease in costs allocated to Government work as a result of CAS 403. Nothing in these sections, however, specifically addresses the question of administrative problems or expense involved in comply with Part 403.

Two associations reported that, contrary to the Board's findings, their member companies had experienced trouble and expense in complying with Part 403. These associations declined to identify the companies involved, the nature of the problems, or the amount of the expenses. Under these circumstances, there is no basis to alter the conclusion that contractors have been able to make changes required as a result of Part 403 without undue trouble or expense.

One commentator stated that it would not be desirable to make more contractors subject to Part 403 because he believes it to be defective, particularly with respect to its application to the allocation of state and local taxes. With respect to the application of the Standard to the allocation of state and local taxes specifically, the Board notes that it reached its conclusion on the basis of considerable research and extensive deliberation. Moreover, it has reexamined its conclusions, even after the promulgation of Part 403. Notwithstanding the views of the commentator, the Board continues of the view that the provision in question is proper. Accordingly, the Board does not agree that this Standard should not be extended to additional contractors because of the tax allocation provision.

Effective Date

The effective date of the regulations being published today is March 10, 1978. Pub.L.91-379 provides that regulations shall take effect not earlier than the expiration of the first period of sixty calendar days of continuous session of the Congress following the date on which a copy of the regulations is transmitted to the Congress. The calendars of the Congress indicate that the required sixty days will not pass until some time in February 1978. Accordingly, March 10, 1978, has been selected to assure sufficient time for the regulation to lie before the Congress.

Preamble B

Note: For text of Preamble B to Part 332, see Preamble M to Part 331, published at 45 FR 62009, Sept. 18, 1980.

Preambles to Part 351,

Basic Requirements

Preamble A
Preamble to Original Publication, 2-29-72

The material set forth below is the preamble to the original publication of Part 351, February 29, 1972, at 37 FR 4139. For the preambles to the revision of Part 351 (October 4, 1973 and November 7, 1973), see preambles B and C. Portions of this preamble, relating to Parts 331, 400, and 401 have been omitted; they can be found in the supplements to their respective parts. This preamble to the publication of Part 351 is included as part of the administrative history of Part 351.

General comments. The purpose of the regulations promulgated today by the Cost Accounting Standards Board is to implement section 719 of the Defense Production Act of 1950, as amended, 50 U.S.C.App. 2168, which provides for development of Cost Accounting Standards to be used in connection with negotiated national defense contracts and for disclosure of cost accounting practices to be used in such contracts. The Board believes the materials being promulgated today constitute a significant initial step toward accomplishing one of its major objectives -- improved cost accounting and the proper determination of the cost of negotiated defense contracts. The regulations spell out contract coverage (Part 331), disclosure requirements (Part 351), a compilation of Definitions (Part 400), and two Cost Accounting Standards, one calling for consistency in estimating, accumulating, and reporting costs (Part 401), and the other calling for consistency in allocating costs incurred for the same purpose (Part 402).

Development of the material being promulgated today began many months ago with extensive research. It included examining publications on the subject, conferring with knowledgeable representatives or various Government agencies. Government contractors, industry associations, and professional accounting associations, and identifying and considering all available viewpoints. From this research, the initial versions of the material now being published were developed. As a part of the continuing research effort, these initial drafts were sent to 81 agencies, associations, and Government contractors which had expressed interest in assisting the Board in its work, and their comments were solicited. Some national defense contractors field-tested the material to see how it would apply to and affect their operations and advised the Board of their findings. In each step of the research process, the Board and its staff have urged and received active participation and assistance by Government, industry, and accounting organizations. Their cooperative efforts contributed in large measure to the exposure draft published in the December 30, 1971, *Federal Register* for comment.

To better assure that all who might want to comment had an opportunity to do so, the Board supplemented the *Federal Register* notice by sending copies of the *Federal Register* materials directly to about 175 organizations and individuals who had expressed interest or had provided assistance in the development of the published material. Also, a press release was distributed announcing the publication, which resulted in numerous articles in journals. The Board availed itself of all opportunities to publicize the proposals and solicit comments on them.

Written comments in response to the published material were requested by February 4, 1972. Comments were received from 105 sources, including Government agencies, professional associations, industry, associations, public accounting firms, individual companies, and others. The Board appreciates the obvious care and attention devoted by commentators, and as will be seen below, the Board has greatly benefited from the comments received.

Many of the comments received were addressed to all parts of the proposed Board rules as well as to the question of public availability of the Disclosure Statements. All of the comments received have been carefully considered by the Board taking into account the requirements of section 719. Understandably, many of the comments were addressed to issues which recur in two or more of the proposed parts while others dealt only with specific sections. Comments which dealt with 11 general issues are discussed separately below followed by a section-by-section analysis of other comments. Appropriate changes have been made in the material promulgated based on the Board’s disposition of the comments received.

Those comments and suggestions received which are of particular significance are discussed below.

1. *Public availability of disclosure statement.* In a special notice in the notice of proposed rule making, the Board sought comments to assist it in its determination of whether Disclosure Statements submitted by defense contractors and subcontractors should be available to the general public, pursuant to the Public Information Section of the Administrative Procedure Act (5 U.S.C.552) or whether such information was properly within one or the statutory exceptions to the legal requirement for public availability.

With few exceptions, both Government and industry commentator urged that the Disclosure Statements not be made available to the general public. Numerous arguments were presented. Among them were that public disclosure by a Government official would violate 18 U.S.C.1905 (a provision in the Criminal Code making it a crime for a Government official to make certain matters public in certain circumstances), thus making disclosure improper under an exception to the requirement for public availability set out in 5 U.S.C.552(b)(3); that the cost accounting practices were trade secrets or property of considerable value and that disclosure would deprive the company of their value without compensation; that disclosure would reduce competition; and that the public might be misled in that it might construe disclosures respecting the defense segment of a contractor's business as representative of his entire business organization.

An argument in favor of making the Disclosure Statements available to the public was made by a public interest group. It argued that 5 U.S.C.552 clearly applies to Disclosure Statements, which do not fall within an exception to public availability; that the public requires access to Disclosure Statements in order to consider adequately and comment intelligently on any Cost Accounting Standard proposed by the Board; that public availability would enhance competition; that Disclosure Statement which are ultimately approved will form a body of precedents to guide others in complying with future Board Standards and that public availability will enable citizens and the Congress to hold both the Board and contracting officials accountable for implementation of section 719. A few commentators stated that they favored, or could see no harm to companies from, public availability of contractors' disclosed practices.

The Board is especially impressed with arguments that cost accounting practices have never been made public, that companies have regarded and treated them as confidential, and that a company's competitive position would be damaged by public disclosure of its cost accounting practices. Since disclosure will be required of many companies or divisions of companies whose principal competitors are not subject to Board regulations, the Board recognizes there might arise competitive disadvantage to the disclosing company or division if its competitors may see its disclosure but need make none themselves. The Board has, in light of these latter arguments, concluded that information received in response to Disclosure Statements is within the exception set forth at 5 U.S.C.552(b)(4) and that the Board will not make Disclosure Statements public in any case when the company or segment files its statement specifically conditioned on the Government's agreement to treat the Disclosure Statement as confidential information.

A provision to this effect has been added at 351.4(d) of Part 351. Additionally, paragraph (a)(1) of the contract clause set forth at 331.5 has been modified to this effect, and a provision added to it so that subcontractors may submit Disclosure Statements directly to the contracting officer.

While the Board has concluded that public availability of the Disclosure Statements of identified contractors is not required, it will, nevertheless, implement its announced intention of compiling statistical summaries of disclosure data and making those studies available to the public. The Board believes that the creation of a data bank of cost accounting practices will greatly benefit the Board's own research efforts and the formulation of Cost Accounting Standards; summaries of these data or studies of them should also prove to be of great value to the public. Aggregated information not identified to particular contractors will, therefore, be made available to the public.

2. *Contractor-subcontractor Relationships.* Several commentators, stating that contractors cannot dictate the cost accounting practices of their subcontractors at any tier, urged that the Board not hold contractors responsible for increased costs to the United States arising from the failure of subcontractors to follow Cost Accounting Standards or disclosed cost accounting practices. Several commentators also urged that the contractor not be subject to the possibility of a default termination by reason of the actions or inactions of any of its subcontractors at any tier. Finally, some

commentators urged that the Board establish a novel concept of privity between the contracting agency and subcontractors with respect to any concerns stemming from Board rules, regulations, and Cost Accounting Standards.

The Board has dealt with many of the issues touched on by these commentators in its conclusions, discussed below, respecting the phasing of applicability and the proposed termination for-default language in the Contract Clause. The Board is also mindful of the desirability of its maintaining neutrality with respect to contracting policies outside its jurisdiction; thus it should avoid establishing a standard or policy which would influence decisions of whether work should be performed in-house or subcontracted. A Board policy permitting contractors to avoid responsibility for the actions of their subcontractors could surely have such an impact.

The Board reaffirms the established principle that prime contractors are responsible to the Government for performance of their contracts in all required respects and urges that contractors who are fearful of deficiencies in their subcontractors' performances protect themselves by use of whatever means they currently employ under other flow-down contractual requirements.

3. *Exemptions.* Many commentators urged the Board to provide exemptions either to the requirement to file a Disclosure Statement or to both that requirement and the requirement to follow Cost Accounting Standards Exemptions were urged for subcontractors below the first tier, subcontractors with small amounts of defense contracting business, producers of basic or raw materials, colleges and universities, construction contractors, firms which would qualify as small businesses, and others.

The Board has long been concerned with the question of appropriate exemptions. It has specifically requested interested groups to offer suggestions for criteria for use by the Board in considering exemptions. It also requested its staff to study exemptions and has discussed the staff investigations at Board meetings. In light these studies and the comments received, the Board has found no persuasive reasons for issuing blanket or class exemptions at this time.

The Board recognizes, however, that individual Cost Accounting Standards may by their nature be inapplicable or inappropriate to certain classes or categories of defense contractors or contracts. The Board will continue to consider exemptions from individual proposed Cost Accounting Standards as appropriate.

With respect to the requirement to submit a Disclosure Statement, the Board's proposed regulation provides a phasing of that requirement. The Board remains convinced that a company which together with its subsidiaries received prime contract awards of negotiated national defense contracts including supplemental awards during Federal fiscal year 1971 totaling more than $30 million should be required to submit a Disclosure Statement as soon as Part 351 of the Board's regulations becomes effective. In order to provide both to other contractors and to Government agencies adequate time within which to study the use of Disclosure Statements, however, the Board will defer determination of the date after which other affected contractors and subcontractor may be required to file Disclosure Statements. From time to time, the Board will announce the dates of applicability to other contractors and subcontractors.

4. *Applicability date of standards, and regulations.* A related issue raised by many commentators is a request that Cost Accounting Standards be made applicable 90 days after issuance or at the beginning of the contractor's next fiscal year, whichever is later. In order to provide the maximum benefits from use of Cost Accounting Standards, the Board has decided not to adopt any rule which would automatically delay the effective date of Cost Accounting Standards beyond the dates contemplated in section 719(h). That section provides a minimum of 4 months' notice from the date of promulgation, to contractor of the likely applicability of a Cost Accounting Standard. The Board regards this as an adequate time for companies to prepare for use of the standard. The Board nevertheless recognizes that certain standards by their nature may require deferring applicability to the beginning of a contractor's fiscal year next following the effective date, and in such cases that applicability will be stated in the standards concerned.

5. *Agency administrative responsibility.* Many commentators, noting the Board's statutory responsibility to promote uniformity and consistency in cost accounting practices used in defense contracting and subcontracting have suggested that uniformity would be promoted by giving the Board or another single Federal agency the sole implementing responsibility respecting Board regulations. Thus, some commentators recommended that the Board itself issue

regulations prescribing the frequency of submission Disclosure Statements and where they must be submitted. Other commentators urged that the Board issue single a regulation prescribing exact methods by which increased costs to the United States will be determined. Other commentators urged that the Board prescribe methods by which advance agreements affecting more than one contract shall be made, some commentators urging that the Board itself make those agreements. Others urged that the Board rule that the contracting agencies must act to approve or disapprove Disclosure Statements within a stated period of time. And finally, some commentators urged that the Board itself be the sole agency to approve the cost accounting practices disclosed through submission of a Disclosure Statement.

> The Board finds these recommendations cogent. It also recognizes that to act pursuant to them would require a Board regulation directed to the administrative and contracting procedures of many Federal agencies and in some cases -- such as the recommendation for Board approval of disclosed cost accounting practices -- substitute a Board regulation for the exercise of contracting officers' discretion.

> The Board, therefore, has decided not to implement at this time the suggestions set forth in this connection. The Board nevertheless will watch closely during the early implementation by contracting agencies of Board rules, regulations, and Cost Accounting Standards so that it may become aware of any diversity of regulations or actions by contracting agencies. If the Board finds that an unacceptable amount of diversity has arisen, it will be prepared to reconsider the recommendations that the Board issue its own regulations in many of the areas left by Board regulations to the discretion of contracting agencies.

> Many commentators have expressed concern about the problems which could arise from inconsistent actions by different Federal agencies respecting disclosed practices, changes in practices, and equitable adjustment of contract prices and costs. The Board has directed its staff to work with representatives of relevant Federal agencies with the objective of obtaining designation of a single contracting officer for each contractor or major component thereof in order to achieve consistent practices within the standards issued by the Board.

6. *Contract modifications.* Several commentators have urged that negotiated contract changes and amendments over $100,000 to contracts which are themselves not subject to Board jurisdiction should not be covered. One commentator pointed out that in a long-term contract, most changes represent "instead of" type changes with cost of price adjustments only for the incremental effect of the change. This commentator stated that there is no practical way separately to identify these incremental costs.

> The Board is persuaded that for the time being it should not cover negotiated modifications to contracts exempt at their inception. It has, therefore, eliminated coverage for the time being of such contract modifications. In doing so, however, the Board intends that the annual extension of existing negotiated contracts and similar contract modifications would not be exempt from the Board's rules, regulations, and Cost Accounting Standards.

7. *Definitions.* The Board is also persuaded of the value of one commentator's suggestion that the Board provide a compilation of definitions of the words or phrases defined in individual Cost Accounting Standards, making those definitions applicable to all such standards. Consequently, a new Part 400 has been added, and all terms defined in Parts 401 and 402 have been placed in it, although they also remain in the particular standards in which they are defined. As more standards are added, any terms defined in them will also be added to Part 400. However, terms defined in Parts 331 and 351 are not included in the glossary of definitions, nor are terms used in those parts necessarily to bear the meanings ascribed to those terms in Part 400.

8. *Application to individual contracts.* Several commentators urged that the Board adopt the date of final agreement on a negotiated price as a cut-off date for the disclosure of cost accounting practices. The Board has "reviewed the merits of selecting that date rather than the date of award to establish the date as of which the contractor's Disclosure Statement must accurately reflect his cost accounting practices, at least with respect to those contracts where cost or pricing data have been submitted pursuant to Pub.L.87-653. The Board has decided to use the date of final agreement on price, as shown on the signed certificate of current cost or pricing data, with respect to contractors who have submitted cost or pricing data, and to use the date of award of the contract for all other contractors. In addition, the Board has concluded that it is appropriate to use those dates to establish which Cost Accounting Standards shall be applicable to the proposal and to the contract at its inception. Appropriate changes in Parts 331, 351, and 401 have been made to reflect this

decision.

9. *Price adjustments.* Many commentators stated that where a contractor's departure from existing disclosed practices is occasioned by the contractor's wish to adopt a newly issued Cost Accounting Standard for all contracts, the Government should be willing to provide upward price adjustment whenever an existing contract is rendered thereby more expensive to perform. The view was often expressed that contractors could not maintain one accounting practice for contracts subject to a particular Cost Accounting Standard, but a different practice for contracts not so subject; therefore, it was alleged, once a contractor had to adopt a standard for any one contract, he would of necessity adopt it for all contracts and amend his Disclosure Statement accordingly.

The Board notes in this connection that the Cost Accounting Standard at Part 402 requires consistency in the allocation of all direct and indirect costs under all covered contracts. If a Cost Accounting Standard were issued which required a company to modify its disclosed cost accounting practices with respect to its earlier practice of allocating direct and indirect costs, Part 402 would require amendment of existing disclosed practices so as to meet that requirement. In such a case, the Board believes it would be unfair to deny an equitable price adjustment arising from such amendment.

Further, the Board has been persuaded by the strong arguments from industry commentators that companies with more than one contract, subject to different Cost Accounting Standards, cannot maintain multiple records to account for each contract related to its set of standards. Another industry commentator stated that the vast majority of companies must apply any required cost accounting practices across their total business, and that it, would be impractical if not impossible for companies to apply different practices to different contracts. The Board has accommodated this view by enabling contractors to apply uniform practices to all covered contracts. Such application will also serve to improve cost accounting practices for all contracts.

The Board has consequently modified both Part 331 and Part 351 to provide three things: First, that a contractor's practices disclosed for any contract shall be the same as the practice currently disclosed and applied on all other covered contracts and subcontracts being performed by that contractor. Second, that a contractor must amend his disclosure of cost accounting practices as new standards are issued and become applicable to new contracts if a change in practice is necessary, so that, at any given time, the same practices prevail under all of the contractor's existing contracts and subcontracts subject to Board jurisdiction. Similarly, contractors must amend Disclosure Statements to reflect any change in practices disclosed under later contract. Third, that for those amendments of disclosed practices applicable to a particular contract which are occasioned by the issuance of a new Cost Accounting Standard, the Government will equitably adjust the contract price in accordance with the changes clause in the contract or reimburse any increased costs under that contract.

In view of the phasing of the requirement to file a Disclosure Statement, the Board has adopted a contract provision that will provide equitable adjustments in appropriate cases when a contractor who has not filed a Disclosure Statement is required to change his established cost accounting practices to comply with newly issued Cost Accounting Standards. On the other hand, any departure from disclosed cost accounting practices which is not required by a newly issued Cost Accounting Standard will not be subject to equitable price adjustment, but only to price adjustment downward in the event that the departure would otherwise result in increased costs being paid by the United States. The Board wishes to emphasize that if the parties to a contractual negotiation mutually agree to a price based on exclusion of costs which are allocable under the contractor's disclosed cost accounting practices, such agreement shall not affect the requirement for conformity with Board rules, regulations, and Cost Accounting Standards in the contractor's allocation of costs between the contract being negotiated and other work.

10. *Materiality.* The Board notes that many commentators urged that a concept of materiality be incorporated in the Board's regulations, to the end that minimal or insignificant modifications of or failures to use disclosed cost accounting practices would not be subject to price adjustment.

The Board agrees that the administration of its rules, regulations, and Cost Accounting Standards should be reasonable and not seek to deal with insignificant amounts of cost. Since this rule of common sense is already practiced by the Government, the Board does not believe that there is any need to attempt to formulate and state in acceptable concept of materiality applicable to all Board rules, regulations, and standards, although the Board might consider doing so if subsequent events indicate the necessity therefor. The Board does recognize that in particular standards a “materiality” statement may be useful, and in such cases, it will include one. See for example the addition at 402.50(e).

11. *Additional requirements by agencies.* As a final general point, concern was expressed that Federal agencies might require submission of cost proposals in ways inconsistent with the cost accounting practices of some or all of the potential offerors. The Board recognizes that this has happened in the past, but it notes that Board rules, regulations, and Cost Accounting Standards are to be used by relevant Federal agencies as well as by contractors and subcontractors, and it believes that henceforth requests for proposals must be fully consistent with such rules, regulations, and standards, although of course the Federal agency may ask for supplementary information to accompany proposals if this is needed to meet the agency’s requirements.

Section 351.14 Disclosure Statement. Several commentators pointed out that the statement was too detailed or complex, or urged that the Statement be modified to require only a statement of cost accounting policy and philosophy. The Board believes that such generalized and unspecific statements would not assist it adequately in performance of its responsibilities. Further, in order to permit the statutory requirements of disclosure of cost accounting practices and consistency to be met, the Board concluded that the extent of detail now called for in the Disclosure Statement is necessary.

Two commentators suggested that references to ASPR, the Internal Revenue Code and financial accounting be deleted from the Disclosure Statement since the contractors stated they are irrelevant to their cost accounting practices. The Board did not agree with these suggestions for the reason’s that in most cases the regulations have been referred to in the Statement in lieu of redefining certain words, such as “Independent Research and Development Costs.” Furthermore, with particular respect to the Internal Revenue Code, the Board cannot ignore that income tax considerations often influence cost accounting practices, such as those for depreciation.

The Board has deleted the item in the Statement calling for an explanation of the difference between commercial and Government cost accounting practices since the Board agrees with several commentators that inclusion of such information in the Disclosure Statement is not needed.

An educational institution and one association pointed out that the terminology in the Disclosure Statement was not responsive to the special circumstances of educational institutions. The Board made appropriate word changes to a number of items in the Statement to accommodate educational institutions.

By far, the majority of the comments addressed to the Disclosure Statement dealt with suggestions for clarification of terminology and intent of the various items in the statement. The Board considered each comment and made appropriate revisions to the statement. The part most affected by these revisions is Part IV -- Indirect Costs. Several items in the part were rearranged in sequence to improve clarity, and instructions covering the items in Part IV were restated.

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Effective date and application. For the convenience of readers, the following summarizes the effective dates set forth in 331.8, 351.4(e), and Part 400, 401, and 402, which were transmitted to the Congress on February 24, 1972, pursuant to section 719(h)(3 of the Defense Production Act of 1950 as amended. After the expiration of a period of 60 calendar days of continuous session following the date of transmittal to the Congress, the regulations herein promulgated shall take effect as set forth in those regulations, unless there is passed by the two Houses a concurrent resolution stating in substance that the Congress does not favor the proposed standards, rules, or regulations.

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3. The provisions of Part 351 will be applicable to any contractor who submits a proposal which results in contracts

containing the clause in 331.5 and whose net awards of negotiated national defense prime contracts during Federal fiscal year 1971 totaled more than $30 million. Contractor whose net awards were less than that amount may be required to complete or submit a Disclosure Statement the Board announced extensions of this requirement to such contractors.

4. Any contractor having a contract awarded prior to July 1, 1972, which contains a clause which already incorporates requirements governing submission of Disclosure Statements an application of Cost Accounting Standards will be required to comply with the provisions of that clause. In this connection, such contractor and the respective contracting agencies whose contracts contain such a clause should review those contracts to determine whether negotiations should be instituted to make Parts 400 through 402 applicable to them.

Preamble B
Preamble to Amendments of 10-4-73

These amendments (38 FR 27507, Oct. 4, 1973) added 351.41 and 351.50(c), and amended 351.70.

The purpose of this publication by the Cost Accounting Standards Board is to modify Part 351, Basic Requirements, of its rules and regulations. A proposed modification to Part 351 was published in the *Federal Register* of July 27, 1973 (38 FR 20101). That proposal was a revision of an earlier proposal published on May 21, 1973. Thirty-three sets of comments were received in response to the July publication and after considering those comments (discussed below), the Board is today publishing an amendment to its rules relative to the requirement for the submission of Disclosure Statements by defense contractors.

The Board's July 27 proposal required that, in determining who must file Disclosure Statements, only negotiated contracts of the type which are subject to Cost Accounting Standards were to be considered. All commentators who dealt with this matter supported the proposal. The Board, therefore, in the amendments being published today, specifically limits the contract awards to be included in the computation of a contractor's volume of defense contracts in determining whether the revised filing requirement has been met, to those of the type subject to the Board's jurisdiction. The Board recognizes that Standards were not required in contracts in Fiscal Year 1972. In view of this, the amendment refers to "negotiated national defense prime contracts of the type which are subject to Cost Accounting Standards." This filing requirement, therefore, includes all negotiated defense prime contracts in excess of $100,000 except those where the negotiated price is based on

(1) established catalog or market prices of commercial items sold in substantial quantities to the general public or

(2) prices set by law or regulation, or contracts which are otherwise exempt.

The amendment being published today by the Board to reduce the dollar level above which filing of a Disclosure Statement will be required excludes from the computation the amounts of all subcontracts and those negotiated defense prime contracts not subject to Cost Accounting Standards. In view of this exclusion, the Board is providing that if the dollar volume of prime contract awards to be considered exceeds $10 million, the contractor will be required to submit a Disclosure Statement. Also, in computing the amount, the amendments require that contracts awarded in either Federal Fiscal Year 1972 or 1973 should be considered. Contractors who meet the threshold amount in either year would be required to file Disclosure Statements, effective April 1, 1974.

The Board believes that the inclusion of the amount of subcontract awards in the Disclosure Statement filing requirement would be appropriate because subcontracts, unless specifically exempt, are subject to the Board's Standards, rules and regulations. The Board recognizes, however, that there is a lack of records relative to the nature of subcontracts awarded during fiscal years 1972 and 1973. Because of this, the Board concludes that it is inappropriate to include subcontracts in the determination of the threshold amount for filing Disclosure Statements at this time.

The amendments being published today thus limit consideration to the dollar value of prime contracts only. The Board wishes to point out, however, that future levels of the threshold amount may call for inclusion of the dollar value of subcontract awards in the calculation. Contractors are hereby advised that they may be required to determine the dollar value of negotiated defense subcontract awards subject to Cost Accounting Standards beginning with July 1, 1973.

Contractors and subcontractors may find it advantageous to begin to identify and accumulate the value of such awards separately.

A major defense agency commented that reduction of the threshold at this time would be premature. It stated that a large number of Disclosure Statements would now be required from contractors less likely to have sophisticated accounting systems. Consequently, greater agency manpower efforts would be required to review them for adequacy. Also, the agency expressed concern with the upcoming work required for compliance reviews and the possibility of negotiation of price adjustments relative to Standards. Finally, it stated that a number of manpower spaces have already been provided in order to support Board requirements. The agency suggested that a threshold reduction be deferred until after July 1, 1974.

The Board believes that Disclosure Statements from “contractors less likely to have sophisticated accounting systems” would seem to be especially needed by the Government in order to know more precisely how such contractors account for their costs. Additionally, the Government has gained a great deal of experience in reviewing the Disclosure Statements already received, which should aid review of newly submitted statements on an expeditious basis. With respect to the potential workload required in compliance reviews, Government agencies have always had a responsibility for reviewing contractor accounting practices and the use of those practices for Government contract costing. The Disclosure Statement provides a benchmark which should facilitate such reviews in the future. Moreover, the Board is advised that most Disclosure Statements filed under the existing $30 million threshold have been reviewed for adequacy, and compliance reviews are now being made as a part of other routine audit work.

The need to provide manpower spaces to support Board requirements is to be expected. The advantages of the expanded disclosure requirement, however, are many. For example, another defense agency strongly endorsed the Board’s proposal to reduce the threshold because of the useful information provided in Disclosure Statements to contracting officers and auditors. Additionally, one agency previously reported to the Board that the Disclosure Statement has become a valuable tool in giving the negotiator more cost visibility while another referred to the Statement as a significant asset for use in reviewing contract proposals. After considering the agencies’ comments referred to above, the Board has concluded that a reduction in the threshold is desirable and within the capabilities of the agencies’ staffs to review the additional statements that would be submitted.

The Board’s July proposal included an effective date of January 1, 1974. The Board has concluded that additional time between the publication of these amendments and the effective date of the reduced threshold should be given to allow agencies to prepare fully to handle the additional volume of Disclosure Statements that will be submitted. Also, additional time will further assure that contractors meeting the new threshold requirement can complete the Disclosure Statement without interference with the prospective award of contracts. For these reasons, the amendments being published today require that contractors meeting the threshold must submit a Disclosure Statement in order to receive a covered contract after April 1, 1974.

Nine commentators urged the Board to provide an exemption for profit centers, divisions, etc., which are predominately commercially oriented and which have only a small dollar volume or percentage of covered defense contracts. The Board has announced that it is initiating a study to consider the establishment of a minimum dollar amount or percentage of covered contract effort below which contractors profit centers and divisions would be exempt from Board Standards, rule and regulations, including the disclosure requirement. In any case, the Board has concluded that $10 million in covered contracts on a company wide basis is a significant dollar volume and that it warrants establishment of the requirement for submission of a Disclosure Statement.

Two commentators objected to the establishment of an absolute dollar amount of awards as a basis for determining the requirement for filing a Disclosure Statement. They suggested that a percentage of overall business would be more appropriate. This kind of information is not available at the present time. In estimating the number of Disclosure Statements that would be submitted at any threshold amount, and relating that number of statements to the agency’s capability to process them, the Board uses statistics on contract awards maintained by defense agencies. Because of this, for the present the Board has retained the requirement to compute the threshold amount for filing a Disclosure Statement in terms of dollar volume of contract awards. The study discussed above may provide information to allow the Board to consider use of a percentage of covered contracts in relation to total business as a factor in setting future threshold requirements. While not specifically related to the Board's proposal of July 27, 1973, the Board has received a number of oral inquiries concerning the intent of the second sentence of 351.120(d) of the Board's regulations, which states:

Revised data for items 1.4.0 through 1.7.0, 8.1.0 and 8.2.0 must be submitted annually at the beginning of the contractor's fiscal year.

The Board did not intend that the changes to these items should be considered in counting the number of changes which would necessitate the resubmission of an entire Disclosure Statement. This information, which relates to the volume of business, should be sent to the recipients of Disclosure Statements only on an annual basis and only if the responses to the items in the Disclosure Statement on file require a change. If on a year-to-year basis, the sales data remain such that the contractor would check the same box in the Disclosure Statement, the Board's rules and regulations do not require resubmission of data concerning these particular items.

The Board's July 27 proposal included a requirement that contractors were to submit a copy of their Disclosure Statement to the Board only after a determination of adequacy has been made of the Statement. All commentators who dealt with this point supported this proposal, and it is included in the amendment being published today.

Today's publication is numbered in consonance with the new numbering system published on September 5, 1973, as part of the proposal set forth in 38 *Federal Register* 171 at page 23971 et seq. Pending adoption of the September 5, proposal, references to 331.60, 351.40, 351.50, and 351.70 refer to 331.6, 351.4, 351.5 and 351.7 respectively of the Board's current rules and regulations. The new 351.41 will be located immediately after 351.4 which will become 351.40.

Preamble C
Preamble to Revision of Part 351, 11-7-73

This publication (38 FR 30725, Nov. 7, 1973) revised Part 351 in its entirety, with the exception of 351.41. 351.50(c) and the last sentence of 351.70.

The purpose of this publication by the Cost Accounting Standards Board is to amend Parts 331, 351, 400, 401, 402, 403, and 404 of its rules and regulations. The amendments, which are minor clarifications to the regulations, were published in the *Federal Register* of September 5, 1973 (38 FR 23971). The amendments:

(a) Renumber Parts 331 and 351 to facilitate insertion of future modifications to those parts;

(b) clarify one section of the contract clause at 331.5; and

(c) modify certain definitions in Parts 400, 401, 402, 403, and 404 for the purposes of uniformity among the various parts. Only one comment in response to the September publication has been received by the Board. This expressed agreement with the proposed changes.

In view of the foregoing, the following amendments to the Board's regulations are being made effective November 7, 1973:

Preamble D
Preamble to Amendment of 12-12-73

This publication (38 FR 32460, Dec. 12, 1973) amended 351.140 and added a new 351.145.

The purpose of this publication by the Cost Accounting Standards Board is to modify Part 351, Basic Requirements, of its rules and regulations. A proposed modification to Part 351 was published in the *Federal Register* of September 17, 1973 (38 FR 26072). That proposal dealt with a Disclosure Statement form designed expressly for submission by colleges and universities. Comments were requested on that proposal from the general public.

Public Law 91-379 which applies to most negotiated defense prime contracts and subcontracts in excess of $100,000 requires that contractors shall disclose in writing their cost accounting practices. The Disclosure Statement form, CASB-DS-1 has been designed to facilitate the meeting of this requirement by contractors. Representatives of colleges and universities had expressed to the Board a desire to have a separate Disclosure Statement to cover their practices. Form CASB-DS-2, being published today, was devised for that purpose and incorporates terminology more commonly used by colleges and universities.

Comments on the September 17 proposal were received from 15 commentators, who offered suggestions for changing the proposed form to explain or further clarify the intent of the questions. Insofar as practicable, the Board has made changes to the college and university Disclosure Statement form to accommodate the suggestions made.

Colleges and universities required to submit Disclosure Statements after April 1, 1974, should use Form CASB-DS-2. Any college or university which has previously submitted a Disclosure Statement should use Form CASB-DS-2 for any amendments which are to be effective after April 1, 1974.

Preamble E
Preamble to Amendment Published 12-24-74

This publication revised 351.40(a) and amended 351.130. and was published on Dec. 24, 1974, at 39 FR 44389.

The purpose of this publication by the Cost Accounting Standards Board is to adopt modifications to Part 331, Contract Coverage, and Part 351, Basic Requirements, of its rules and regulations. These modifications will provide an exemption from Cost Accounting Standards Board requirements for certain national defense contracts and subcontracts of $500,000 or less.

Public Law 91-379 requires that Cost Accounting Standards must be used in all negotiated prime contract and subcontract national defense procurements with the United States in excess of $100,000, with certain stated exceptions. From time to time the Board refers to contracts subject to its rules and regulations as “covered contracts”. Section 719(h)(2) of Pub.L.91-379 authorizes the Cost Accounting Standard Board to prescribe rules exempting from its requirements such classes or categories of national defense contractors and subcontractors as it determines, on the basis of the size of the contracts involved or otherwise, are appropriate and consistent with the purposes sought to be achieved by Pub.L.91-379. The Board has granted several exemptions to classes or categories of contractors and subcontractors and also has established a procedure under which waiver of the Board’s requirements may be granted for individual contracts.

A proposed exemption increasing the minimum contract amount requiring compliance with Cost Accounting Standards Board rules, regulations and Standards from $100,000 to $500,000 was published by the Board on September 27, 1974 (39 FR 34669). The Board received 82 responses to the September 27 proposal. Comments were received from individual companies, government agencies, professional associations, industry associations, public accounting firms, and individuals. All of these comments have been carefully considered by the Board, and the Board takes this opportunity to express its appreciation for the helpful suggestions which have been furnished.

The comments below summarize the major issues discussed by respondents in connection with the initial publication and explain the Board’s disposition of these issues.

Issuance of the exemption. Practically all the commentators expressed concurrence in the proposed exemption, giving either unqualified support or support with added comments that additional exemptions should also be considered. However, three commentators -- a constituting firm, a major aerospace company and a Government agency -- disagreed with the proposed exemption, stating that an increase in the threshold for compliance with CAS requirements was inconsistent with the Board’s objective of establishing uniformity and consistency among contractors doing business with the Government.

The Board agrees that the adoption of the proposed regulation will exempt a substantial number of contractor and subcontractors who otherwise would be covered, and consequently will permit such companies to follow accounting practices other than those set out in Cost Accounting Standards. However, the Board is aware that compliance with its rules, regulations and standards may involve additional administrative effort, particularly on the part of small companies, which may not be commensurate with the benefit to the Government or the contractor resulting from such compliance. The Board, after considering the efforts required by both the Government and its contractors to assure compliance on all covered contracts in excess of $100,000, is persuaded that maximum benefit to the Government with minimum cost can be achieved by limiting the mandatory application of its standards to contractors who receive awards which constitute a substantial majority of the national defense procurement dollars. As was stated at the time the proposed exemption was issued for comment, some 70 percent of the prime contractors of the Department of Defense did not receive one or more negotiated awards in excess of $500,000 in Fiscal Year 1973. Thus, only 30 percent, or approximately 750 prime contractors, who received contract awards totaling $20 billion, would continue to be covered. The exemption would remove coverage from only about 10 percent of the dollar value of annual DoD awards.

In view of the foregoing, the Board considers the proposed exemption increasing the minimum contract amount requiring compliance with the Cost Accounting Standards Board rules, regulations, and standards to be in keeping with the purposes sought to be achieved by Pub.L.91379 and to be an appropriate exercise of the authority granted to the Board by section 719(h)(2) of that law.

Increase exemption on all contracts to $500,000. A number of commentators suggested that the $500,000 single contract threshold for compliance with Board rules, regulations, and standards be changed to exempt all contracts of $500,000 or less. Those giving reasons in support of this suggestion generally based their comments on simplification of administration. These commentators felt that it would be difficult for the Government or prime contractors, when awarding a prime contract or subcontract in excess of $100,000 to determine whether the contractor or subcontractor had in existence a prior $500,000 covered contract.

The Board, in proposing the $500,000 threshold, did so with the intent of exempting those companies which do not receive contracts in excess of $500,000 from the Government. However, it was decided in the interest of consistency in cost accounting practices that once a contractor had received a covered contract of that size, compliance with CASB rules, regulations and standards on contracts at the level established in Pub.L.91-379 was appropriate. This is also consistent with the desire expressed by contractors to follow a single set of accounting practices. Further, the requirement for coverage of contracts in excess of $100,000 where the contractor already has received a covered contract in excess of $500,000 will permit the small contracts to be available for equitable adjustment if subsequently issued standards should become applicable. Moreover, once the administrative effort has been expended to comply with standards for contracts in excess of $500,000, compliance with standards on contracts above the statutory threshold of $100,000 requires little added effort.

With respect to the commentators' statements concerning the difficulties, when making an award exceeding in $100,000, of determining whether a contractor or subcontractor had in existence a prior award exceeding $500,000, the Board feels that an administrative requirement can be established for obtaining this information. A similar requirement now exists concerning the disclosure statement, whereby contractors are required to submit a disclosure statement, state that they have previously filed a disclosure statement, or submit a certificate of monetary exemption. The Board feels that a similar requirement can be set concerning the $500,000 level. The Board is not persuaded that this matter would create problems of sufficient significance to eliminate coverage down to the $100,000 level.

In considering the advantages of the exemption as proposed compared to its assessment of the administrative difficulties foreseen by commentators, the Board is persuaded that its proposal relative to coverage of awards in excess of $100,000 should not be changed.

Exemption based on sales. A number of commentators urged that the Board establish an exemption based on sales, using either minimum annual dollar amount of sales to the Government, or Government sales as a percentage of total annual sales, or a combination of these two factors. The most frequently suggested amount was $10 million of sales to the Government or Government sales amounting to 10 percent of total annual sales. The objective sought by these commentators was an exemption of those companies or business units whose sales to the Government constituted a reasonably small portion of their total annual sales and whose business was essentially commercially oriented. The Board has given lengthy consideration to the use of a sales basis for the establishment of a minimum threshold for compliance with its rules, regulations and standards. It did not use that basis at this time due to the nature of the problems involved administering an exemption based on sales. In either of the situations suggested by commentators, the representation concerning the amount of sale, must be made by the contractor and subsequently verified by the Government. This verification would impose very substantial and time-consuming efforts on both the Government and the contractor. Particularly in the case of Government sales as a percentage of total sales, Government representatives would be placed in the position of examining a contractor's total sales including those made in its commercial business. Examination of a company's records concerning its total sales is not presently performed by Government procurement activities and would present new and unique problems to both parties as well as requiring substantial additional effort on the part of Government representatives.

An exemption based on sales would require a measurement period during which a contractor's status with respect to compliance with standards would be determined. Contracts under which sales were recorded during this period would not be subject to standards. If the volume of sales during the measurement period exceeded a stated threshold, a contractor would then be required to comply with standards under contracts received in subsequent periods. Thus, the contracts that brought the contractor under the Board's rules would not be subject to standards, while those received at a later time would be.

The Board has decided that the administrative problems involved with an exemption based on sales should be considered before establishing such threshold. The Board will continue to study these problems and investigate whether exemptions based on criteria other than a minimum contracting amount would be appropriate and consistent with the purposes of Pub.L.91-379.

Retroactivity. Several commentators requested that the Board modify its proposal so as to provide retroactive exemption to existing contracts where the circumstances are such that these existing contracts would have been exempt if awarded after the effective date of the proposed regulation.

The Board has no authority to modify existing contractual agreements between the government procurement agencies and their contractors. However, the Board sees nothing inconsistent with its regulations or with Pub.L.91-379 in modification by the procurement agencies of contracts in this category, assuming of course that the Government receives adequate consideration for deletion of the CAS requirement.

Increase minimum amount. A number of commentators recommended that the exemption proposed be increased to an amount greater than $500,000, the figure of $1,000,000 being frequently mentioned. The Board is not now prepared to raise further the minimum contract amount requiring compliance with its promulgation's. The Board, in studying an exemption based on minimum contract amount concluded that the $500,000 threshold was the most appropriate one for achieving its objectives, all factors considered. The Board will continue to examine various limitations but considers that the threshold established in the proposed exemption best meets its requirements and obligations at this time.

Effect of final payment under contracts subject to CAS clause. Several commentators urged that the exemption of contracts of $500,000 or less should not be dependent on the final payment on contracts which are subject to Board requirements, on the grounds that final payment can occur a substantial period of time after completion of work on a contract and that there are many technicalities in closing out a contract which do not involve cost accounting applications.

The Board considers this point to be well taken and has changed the requirement in 331.30(b)(8) where it first appears to "notification of final acceptance of all items or work to be delivered." At that time it is considered that all direct costs will have been charged to the contract since all work will have been completed, and any further accounting transactions would be the result of adjustments not directly related to contract performance.

Reduction of contract price by exclusion of commercial items. Some commentators, in reading the introductory comments to the Board's initial publication of this exemption, interpreted the phrase "minimum contract amount requiring compliance" in a manner not at all intended by the Board. These commentators interpreted this phrase to permit the price of a contract subject to standards to be reduced by the value of those individual contract items or subassemblies of final contract terms whose prices could be considered to be "catalog" or "market" prices, if sold separately. They requested that the regulation be clarified to reflect their interpretation of the Board's introductory comments.

Those requesting this clarification misunderstood the Board's intentions. The Board does not intend that the price of a contract be adjusted to exclude the price of items or subassemblies which, if purchased separately, might be exempt from the Board's promulgation's. Consequently, the change in the regulation requested by commentators on this point would be completely inappropriate.

Definition of contractor. One commentator noted that the prefatory comments to the Board's September 27, 1974, publication specifically mentioned the fact that receipt of a contract in excess of $500,000 by one business unit of a multi-unit company would not in itself require other units of the same company to follow Board requirements. This commentator requested that the definitions of "defense contractor" and "defense subcontractor" contained in 331.20 (b) and (c) be modified to reflect this intention by the Board.

As the Board stated in its September 27 publication, its contract requirements have been applied to business units, such as a profit center, division, subsidiary, or similar unit of a company, which perform the contract, even in those cases where the contract was entered into on behalf of the overall company rather than the business unit. This application of the Board's requirements to a performing business unit is well established and unchallenged, and clarification of the definitions of "contractor" and "subcontractor" does not appear necessary.

Effective date. Several commentators raised questions concerning the effective date of the eligibility for this exemption in relation to awards received prior to January 1, 1975. Contractors who have received a prime contract or subcontract in excess of $500,000 subject to cost accounting standards prior to January 1, 1975, and on which notification of final acceptance of all items or work to be delivered on that contract or subcontract has not been received, is a contractor who has "already received a contract or subcontract in excess of $500,000," as that phrase is used in 331.30(b)(8). Therefore, today's publication requires that a contractor meeting this will be required to comply with standards on all covered prime contracts or subcontracts in excess of a $100,000 received after January 1, 1975, under the provisions of 331.30.

Preamble F
Preamble to Amendments of 8-4-75

This publication (40 FR 32747, Aug. 4, 1975) amended 351.40 by revising (c) and adding (f); deleted 351.41; amended 351.50 by revising (a) and (c) and adding (d); and amended 351.120 by revising (d) and adding (e). A correction to the language which amended 351.40 appeared at 40 FR 33819, Aug. 12, 1975.

The purpose of this publication by the Cost Accounting Standards Board is to modify Part 351, Basic Requirements, of its rules and regulations and Part 403, Allocation of Home Office Expenses to Segments. A proposed modification to Part 351 was published in the *Federal Register* of April 3, 1975 (40 FR 14942). Twenty-seven sets of comments were received in response to that publication. After considering those comments, the most significant of which are discussed below, the Board is today publishing an amendment to its rules relative to the requirement for the submission of Disclosure Statements by defense contractors and subcontractors.

1. *Fiscal Year Coverage.* The Board's April 3 proposal provided that any company which, together with its subsidiaries, received more than $10 million in prime contracts subject to Cost Accounting Standards in Government fiscal years 1974 or 1975 would be required to file Disclosure Statements. Board regulations now require the filing of Disclosure Statements on the basis of prime contracts awarded in fiscal years 1971, 1972 or 1973. There were no objections voiced by commentators to the inclusion of fiscal years 1974 and 1975 in the filing requirement. Accordingly, the amendments being published today require that companies who exceeded the threshold amounts in either of those fiscal years will be required to file Disclosure Statements.

2. *Effective Date.* The Board's proposal established July 1, 1975, as the effective date for the requirement to include awards made in fiscal years 1974 and 1975. Most commentators pointed out that in view of the short time permitted between submission of comments on the proposal and the July 1 date, any company which met the new requirement would not have sufficient time to file a satisfactory Disclosure Statement to permit receipt of a covered contract. The Board agrees, and accordingly, the amendments being published today establish an effective date of January 1, 1976, for

the new requirement. Thus, any company which, together with its subsidiaries, received more than $10 million in prime contract awards subject to Cost Accounting Standards in Government fiscal years 1974 or 1975 must submit a Disclosure Statement in order to receive a covered national defense contract after January 1, 1976.

The April 3 proposal also provided for including subcontract awards in the computation to determine if a company meets the requirement for the filing of Disclosure Statements, beginning with Federal fiscal year 1976. The proposal stated that companies which met the threshold in fiscal year 1976 would be required to file Disclosure Statements as of July 1, 1976. In view of the need for a company to determine whether or not it met the filing requirement and then have sufficient time in which to prepare satisfactory Disclosure Statement, the effective date for filing a Disclosure Statement on the basis of fiscal year 1976 data has been changed to March 31, 1977. For fiscal years subsequent to 1976, companies will be required to file Disclosure Statements as a condition of receiving a contract by March 31 following the end of the fiscal year in which the threshold is met. This should permit contractors to make their eligibility determination in sufficient time to allow preparation of acceptable Disclosure Statements.

3. *Inclusion of Subcontracts.* The Board's proposal required that beginning with Federal fiscal year 1976 (July 1, 1975-June 30, 1976) companies would be required to include, in addition to prime contract awards, the value of subcontract awards received subject to Cost Accounting Standards in their computation to determine if they must file Disclosure Statements. Beginning with that fiscal year and for all subsequent fiscal years, the Board's proposal stated that any company which, together with its subsidiaries, received more than $10 million in prime contract awards and subcontract awards subject to Cost Accounting Standards would be required to file Disclosure Statements.

Some commentators questioned how the value of awards was to be considered in determining if a company met the threshold. The $10 million figure is to include both prime contract awards and subcontract awards and may, in fact, be met by companies receiving only subcontracts subject to Standards. There was no intention that companies must have received one or more prime contracts in order to be required to file a Disclosure Statement. The determination of whether or not a company has $10 million in awards subject to Cost Accounting Standards must include both prime contracts and subcontracts.

A number of commentators objected to the inclusion of subcontract awards in a requirement for filing Disclosure Statements. They argued that in many cases they do not have sufficient information to determine whether a subcontract is subject to Standards. Some commentators stated that in many cases prime contractors pass through to subcontractors all Standard Government contract clauses whether or not they are required to be included in the subcontract. They alleged that, in some cases, when the prime contractors are contacted to determine specifically whether or not a subcontract which contains the Cost Accounting Standards Clause is, in fact, subject to Standards, the prime contractor states that it is not. Because of this, the commentators claim they would be required to establish an elaborate information-gathering system to assure that they properly identify every subcontract subject to Standards.

The argument about the adequacy of information concerning coverage of subcontracts has been made to the Board on a number of occasions. In October 1973, when the Board published an earlier revision to the Disclosure Statement filing requirement it advised contractors that they may be required to determine the dollar value of defense subcontract awards subject to CAS, and encouraged them to begin to identify and accumulate the value of subcontract awards separately. Many contractors are in fact effectively identifying subcontracts subject to Standards. These facts persuade the Board that identification of covered subcontracts is feasible, although the Board recognizes that some firms may have to clarify their information exchange procedures with the prime contractors with whom they do business.

The Board believes that the inclusion of the amount of subcontract awards in the Disclosure Statement filing requirement is appropriate because subcontracts, unless specifically exempt, are legally subject to the Board's Standards, rules and regulations. Accordingly, the amendments being published today provide for the inclusion of subcontract awards subject to Standards in the determination made by a company as to whether or not it must file a Disclosure Statement. This requirement is effective with Government fiscal year 1976 and applies to all subsequent fiscal years.

4. *Change in Fiscal Year Period.* Several commentators noted that the Federal Government is changing the dates of its fiscal year following Federal fiscal year 1976. The new fiscal year period will be from October 1 through the following September 30. The period July 1, 1976, thru September 30, 1976, will be known as Federal fiscal period 197T. These commentators asked whether or not contracts awarded in that period should be included in some way with a normal fiscal year's contract awards. The Board feels that it is not desirable to upset the regular twelve-month fiscal year computation period and accordingly has concluded that contracts awarded in that three-month period need not be included by companies in determining the value of contract awards received in fiscal year 1976 or any subsequent fiscal year.

5. *Previously Announced Filing Requirements.* The Board's proposal included a requirement that any company which has submitted or was required to submit a Disclosure Statement to the Government under the previously announced filing requirements by virtue of having received a covered contract shall remain subject to those requirements so long as it has any contract subject to Cost Accounting Standards. The proposal also required that Disclosure Statements from those companies on file with the Government must be maintained in a current form by those companies. There were virtually no comments received on this requirement. The amendments being published today contain that requirement as set out in the April 3 proposal.

6. *Applicability of CAS 403.* A number of commentators noted that the April 3 proposal deleted 351.41 of the Board's regulations. This paragraph restated the requirement that only companies that met the Disclosure Statement filing requirement for Federal fiscal year 1971 were required to comply with CAS 403. Allocation of Home Office Expenses to Segments. These commentators asked that the Board's position be clarified as to whether or not any current revision to the Disclosure Statement requirement also changed the coverage of CAS 403. It was not the Board's intention to broaden the coverage of CAS 403 at this time. The possibility of extending the coverage of that Standard is the subject of a separate study currently underway. To make the Board's intention wholly clear, 403.70 of CAS 403 is being revised to state explicitly rather than by cross reference the continuing coverage of that Standard. This revision has no substantive significance whatever, but instead merely sets out specifically what was and continues to be the exemption from that Standard, which was before today accomplished by reference to 351.40 of the Board's Basic Requirements. Contractors and subcontractors which together with their subsidiaries did not receive net awards of negotiated national defense prime contracts during Federal fiscal year 1971 totaling more than $30 million continue to be exempt from Standard 403.

7. *Amendments to Disclosure Statements.* The Board's April 3 proposal also included revised procedures for handling changes to the Disclosure Statement. Contractors would be required to submit only the Disclosure Statement pages on which changes have been made. All commentators supported these revised procedures and they are being published today as part of the Board's regulations.

The Board's April 3 proposal also included a provision enabling procurement agencies to issue regulations prescribing criteria under which a contractor may be required to submit complete, updated Disclosure Statement. A number of commentators expressed concern over this provision. They felt that procuring agencies perhaps would issue regulations that were not consistent with the Board's intention and for this reason they urge that the Board prescribe criteria under which procurement agencies could make such a request.

The Board appreciates the concern expressed by the commentators. It would appear, however, that agencies would have a need for a complete, updated Disclosure Statement only where the number of amended pages submitted is so great that review of Disclosure Statement would obviously be an excessively cumbersome process. The Board urges agencies to consider these views when adopting their criteria for submittal of a complete, updated Disclosure Statement. The Board has concluded that it should not itself set criteria for this particular requirement.

8. *Computation of Dollar Amount of Contract Awards.* A number of commentators asked that the Board clarify its intent as to which contracts should be included in the computation of the dollar amounts. The Board feels that covered contracts awarded in any fiscal year in which the computation is being made should be included. This would mean that for all of fiscal year 1974, negotiated defense prime contracts in excess of $100,000 would be included by a company in determining if it met the requirement to file a Disclosure Statement. For the first six months of fiscal year 1975 all

covered contracts in excess of $100,000 would be included in the figure for that fiscal year. For the balance of fiscal year 1975 only those awards which are subject to Standards would be included. This means that if a company was not performing under a covered contract exceeding $500,000 at January 1, 1975, and did not receive an award exceeding that amount in the last six months of the fiscal year, then only the covered contracts received in the first six months would be included. Only those companies which received an award of $500,000 or more in the last six months of the year would add up their covered contracts, including those subsequently awarded in amounts of $100,000 or more, to arrive at the total amount awarded in that period, to be added to the total for the first six months.

Beginning with Federal fiscal year 1976 only companies which received at least one award exceeding $500,000 either as a prime contract or subcontract subject to Standards will be required to include the value of awards received to determine if they must file a Disclosure Statement. In essence, it is the Board's intention that contracts subject to Cost Accounting Standards shall be included in the computation to determine if the filing requirement has been met by a company for fiscal year 1974 and all subsequent fiscal years.

9. *Summary of Disclosure Statement Filing Requirements.* The Board has amended the requirement for filing Disclosure Statements a number of times. As a convenience to those affected by CAS, there follows a tabulation showing these requirements.

Fiscal Period Government Contracts to be Amount Effective
Included in Computation (Million) Date
Fiscal year 1971. Net negotiated prime defense
contracts $30 Oct. 1, 1972
Fiscal years 1972, Defense prime contracts of
1973 the type subject to CAS. 10 Jan. 1, 1974
Fiscal years 1974, Defense prime contracts
1975 subject to CAS 10 Jan. 1, 1976
Fiscal year 1976 Defense prime contracts and
subcontracts subject to CAS 10 Mar. 31, 1977
Following years. Defense prime contracts and sub-
contracts subject to CAS 10 Mar. 31
following
fiscal year.

10. *Modification.* The modifications being adopted today are limited to those areas in which the Board considers clarification or changes warranted at the present time. From time to time the Board may announce further changes in the criteria for applicability of the disclosure requirement.

The following modifications to Part 351 of the Board's regulations are being made, effective August 1, 1975, in view of the foregoing.

Preamble G
Amendment Published 9-12-77

The material set forth below is the preamble to the revision or 351.40(e) and (f). This preamble was part of a document which also set forth amendments to Parts 331, 332 and 403. The complete preamble to appears in the supplement to Part 332.

Disclosure Statement Requirements

Many commentators suggested that preparation of a Disclosure Statement was burdensome. They also contended that in the situation where a large commercial contractor receives only a few small contracts containing a Cost Accounting Standards clause the need for a Disclosure Statement appears to be minimal. Some asserted that adoption of the proposal to require a Disclosure Statement for all covered contracts would reduce the number of companies that would accept contracts subject to the Board's Standards, rules and regulations. The Board is persuaded that for the time being Disclosure Statements should not be required for all covered contracts. Accordingly it is not adopting the February 15 proposal. The Board is retaining the existing Disclosure Statement requirement provided in Part 351 except that a business unit will be required to submit a Disclosure Statement if it is a company or a segment of a company which received awards of national defense contracts subject to Cost Accounting Standards in excess of $10 million during its preceding cost accounting period rather than the preceding Federal fiscal year.

Revisions to Part 351

Part 332 and the amendments to Part 331 generally will result in annual determinations being made of a contractor's obligation to follow Standards and to submit Disclosure Statements. The determination will be made on the basis of sales and awards data from the immediately preceding cost accounting period. The requirement to continue to submit a disclosure Statement so long as the contractor has a contract subject to Cost Accounting Standards will no longer apply. Disclosure Statements must be maintained for and applied to only those contracts which were awarded during a cost accounting period in which the contractor met the filing 351.40. Sections 351.40 and 351.50 have been revised to reflect this change.

Effective Date

The effective date of the regulation being published today is March 10, 1978. Pub.L.91-379 provides that regulations shall take effect not earlier than the expiration of the first period of sixty calendar days of continuous session of the Congress following the date on which a copy of the regulations is transmitted to the Congress. The calendars of the Congress indicate that the required sixty days will not pass until some time in February 1978. Accordingly, March 10, 1978, has been selected to assure sufficient time for the regulation to lie before the Congress.

Part III
Preambles Published Under the FAR System

Preamble A to 30.404,
Capitalization of Tangible Assets

This final rule, in Federal Acquisition Circular (FAC) 84-38, revises 30.404-40(b)(1), 30.404-60(a)(1), and 30.404-60(a)(1)(i).

Summary

Section 30.404 requires that contractors have written policies for capitalization which must include a minimum acquisition cost criterion of $1000. The standard is being amended to raise the threshold to $1500. The purpose of the change is to permit contractors to adopt practices appropriate in today's economy.

Effective Date: The effective date of this modification is September 19, 1988.

Background

Supplementary Information. The CAS Board established the minimum acquisition cost criterion for capitalization at $500 when it originally promulgated CAS 404 in 1973. The Board's initial $500 limitation encompassed the practices of 97 percent of the companies whose Disclosure Statements were filed with the Board. In the promulgation comments to the Standard, the Board recommended that the special limits in the standard ". . . may need to be reviewed in the future. . . (and will be revised) promptly if developments warrant a change."

On March 3, 1980, the Board did revise the limitation upward to $1000 as it recognized that circumstances had changed significantly since the promulgation of Standard 404. The Board found that the performance of several official indices showed increases from 60 to 80 percent, and a survey of companies not influenced by the limitation of Standard 404 showed a significant number using $1000 as the minimum criterion for capitalization.

The impact of inflation has continued over the 7 years since 1980, although at a lower level. Indices from the Commerce Department for the implicit price deflators on nonresidential structures and machinery and equipment showed increases from 30 to 35 percent over the period 1979 through 1985. When applied to the current $1000 criterion, this yields values from $1300 to $1350. In addition, economic projections showed inflation levels rising slightly from 1986 through 1989. Consequently, this change increases the minimum acquisition cost criterion for capitalization of tangible capital assets to $1500 to cover both actual and projected price increases.

The amendment which is now being promulgated is derived directly from the proposed rule which was published in the *Federal Register* on July 9, 1986 (51 FR 24971), with an invitation for interested parties to submit comments.

Four letters of comment were received on the July 9, 1986, proposal. Only one letter directly addressed the appropriateness of the proposed revisions to 30.404. That comment stated that inflation should not be the motivating factor in determining significant costs for capitalization, but rather materiality of the cost should be the factor in determining significance.

The CAS Board's comments in the CAS 404 preamble and its action to increase the capitalization threshold based upon inflation, discussed above, indicate that the Board considered the materiality and significance of asset acquisition cost to be directly related to the level of prices in the economy. The Defense Acquisition Regulations Council and the Civilian Agency Acquisition Council agree with the CAS Board's outlook on this matter and expect the increase in capitalization threshold provided in this modification to 30.404 will be beneficial to Government contract costing by not requiring capitalization of assets that are of insignificant value.

Preamble A to 30.416,
Accounting for Insurance Costs

This final rule, in Federal Acquisition Circular (FAC) 84-38, revises 30.416-50(a)(3)(ii).

Summary

FAR 30.416-50(a)(3)(ii) revisions delete the requirement to use state rates in discounting certain self-insured losses to present value.

Effective Date: The effective date of this modification is September 19, 1988.

This modification shall be followed by each contractor on or after the start of its next cost accounting period, beginning after receipt of a contract to which this modification is applicable.

Background

Supplementary Information. Section 30.416 provides that the amount of insurance cost to be assigned to a cost accounting period is the projected average loss (PAL) for that period plus insurance administration expense in that period. The PAL is either the insurance premium, where the risk of loss is covered by the purchase of insurance, or a self-insurance charge, where the exposure to risk is not covered by the purchase of insurance. Where it is probable that the actual amount of losses will not differ significantly from the PAL, the actual amount of losses may be considered to represent the PAL for the period as the self-insurance charge.

In self-insurance, when the actual amount of losses is being used to represent the PAL, contractors are to discount those losses to present value, where payments to the claimant will not take place for over a year after the loss occurs. If a state provides a discount rate for computing lump-sum settlements, 30.416 requires that the state rate be used for computing present value. Otherwise, the Pub.L.92-41 Treasury rate is to be used. The differing rates specified by the states, and the lack of specified rates in some states, result in inconsistent treatment of self-insurance charges on defense contracts.

The purpose of requiring a present value computation for contract cost accounting purposes is to recognize the time value of money for funds advanced to and used by the contractor for extended periods before being disbursed. The Pub.L.92-41 Treasury rate is generally specified for this purpose. The majority of state laws covering worker's compensation insurance specify a rate in the range of 3-6 percent. The use of a low rate results in a larger settlement than would use of a current money market rate. The purpose of low state rates is to discourage lump-sum settlements. This purpose is unrelated to that of fair valuation for contract cost accounting purposes. The use of state rates may produce inaccurate measures of present values and will most certainly create inconsistencies in the pricing of contracts due to the lack of consistent determinations of present values. Consequently, the proposed rule, published in the *Federal Register* on July 8, 1986 (51 FR 24788), deleted the reference to state discount rates at 30.416-50(a)(3)(ii) and required use of the Pub.L.92-41 Treasury rate in all cases.

Four comments were received in response to the proposed rule. None of the comments directly challenged the appropriateness of the proposed revision. Therefore, no changes were made to the proposed rule as a result of the public comments.

period of performance through a significant, discrete milestone before PDR with a priced option for the effort from that milestone through PDR. The down-selection would be planned for the earlier milestone, the PDR option exercised for only the winner of the down-selection, and formal Phase C/D performance initiated at completion of the PDR option. In this scenario, the earlier milestone must be carefully chosen to ensure successful accomplishment of both program technical objectives and all activities leading to completion of the down-selection process. That is, design maturity at that point must be sufficient to accommodate an informed down-selection decision leading to successful accomplishment of Phase C/D.

(f) In other program strategies, it may be both affordable and technically desirable to have all the Phase B contractors complete PDR. In these cases, the contract should be structured as a basic effort through PDR, down-selection made at that point, and Phase C/D performance beginning thereafter.

(g) Regardless of the contract structure that is appropriate given the program objectives, the schedule leading to down-selection must also be carefully crafted and followed. This schedule must allow ample time for synopsizing the Phase C/D down-selection, responding to any other offeror's intention to submit a proposal, generation of whatever information is necessary for Phase C/D proposals (e.g., final technical requirements, proposal preparation instructions, and evaluation factors), submission and evaluation of the proposals, negotiation, and award. In some cases, the earliest of these activities will commence shortly after Phase B award. However, unless these activities are planned and executed in reasonable time periods to accommodate timely Phase C/D award, many of the benefits associated with the progressive competition technique, or any other down-selection strategy, will go unrealized.

8. Requesting Phase C/D Proposals

(a) Although a new, formal solicitation is normally not issued for Phase C/D when using the progressive competition technique, Phase C/D proposals must be formally requested and the offerors given all information necessary to submit a proposal. The preferred approach for requesting Phase C/D proposals is by letter. This letter shall include the following:

(1) A specific due date for the Phase C/D proposals along with a statement that FAR 52.215-10, Late Submissions, Modifications, and Withdrawals of Proposals, applies to this proposal due date.

(2) Complete instructions for proposal preparation, including page limitations, if any.

(3) Final evaluation factors.

(4) Any statement of work, specification, or other contract requirements that have changed since the Phase B solicitation.

(5) All required clause changes applicable to new work effective since Phase B contract award.

(6) Any representations or certifications, if required.

(7) Any other required contract updates. (E.g., Phase C/D small and small disadvantaged subcontracting goals.)

(b) Although the exception and not the rule, there are circumstances in which a new, formal solicitation must be issued for Phase C/D. Significant changes in paragraphs 8(a) (3) and (4) of this appendix, in particular, require a careful assessment as to whether a new solicitation should be issued. Determining the significance of changes is often subjective and difficult, however. These determinations should only be made after coordinated consultation among procurement, legal, and technical personnel. Some cases will be particularly clouded, and no clear resolution of the magnitude of the changes can be made. In these instances, the issue should be resolved on the side of caution and a new, formal solicitation issued.

9. Phase C/D Award

(a) As stated in paragraph 6(c) of this appendix, evaluation of Phase C/D proposals will normally be accomplished in accordance with formal SEB procedures. Phase C/D award may be made by either a new contract, or by a new work supplemental agreement to the existing Phase B contracts.

(b) Keep in mind that, no matter what is included in the original solicitation or Phase B contracts regarding the progressive competition technique, or any other alternative down-selection strategy, the Phase C/D effort is new work and not an in-scope change under the "Changes" clause, or any other clause, of the Phase B contract. If a supplemental agreement is used to implement Phase C/D, it shall cite the applicable "Phased Procurement" clause (either 1852.234-70 or 1852.234-71) included in the Phase B contracts as authority for award.

(c) Whether a new contract or new work supplemental agreement is used, the document must incorporate all applicable statutory and regulatory requirements (e.g., contract clauses) in effect as of its issuance. The Phase C/D award date is controlling and not the date of the Phase B awards.

(d) In addition, regardless of the time of Phase C/D award or the contract vehicle used to effect it, the Phase C/D period of performance should commence only upon completion of Phase B tasks.

[FR Doc. 93-26910 Filed 11-3-93; 8:45 am]
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OFFICE OF MANAGEMENT AND BUDGET

Office of Federal Procurement Policy

48 CFR Part 9903

Cost Accounting Standards Board; Applicability and Thresholds for Cost Accounting Standards Coverage

AGENCY: Cost Accounting Standards Board, Office of Federal Procurement Policy, OMB.

ACTION: Final rule.

SUMMARY: The Office of Federal Procurement Policy, Cost Accounting Standards Board, is revising applicability, thresholds and procedures for the application of the Cost Accounting Standards (CAS) to negotiated government contracts. This rulemaking is authorized pursuant to section 26 of the Office of Federal Procurement Policy Act. The Board is taking action on this topic in order to adjust CAS applicability requirements and dollar thresholds to levels reflecting experience with price inflation since the thresholds were last promulgated by the previous Board on September 12, 1977. The Board is also changing the criteria for determining which Standards apply at different threshold levels and the concept of what constitutes modified coverage, and, the criteria that trigger full CAS coverage.

EFFECTIVE DATE: November 4, 1993.

FOR FURTHER INFORMATION CONTACT: Richard C. Loeb, Executive Secretary, Cost Accounting Standards Board (telephone: 202-395-3254).

SUPPLEMENTARY INFORMATION:

A. Background

On September 12, 1977, the prior Cost Accounting Standards Board (CASB) promulgated rules that exempted certain types of government contractors from the full impact of the application of the Cost Accounting Standards (CAS) to all of their otherwise CAS covered contracts and subcontracts. The regulation issued by the prior CASB, formerly part 332 of that Board's rules (4 CFR 332), entitled "Modified Contract Coverage," was designed to partially address the problem of application of CAS to smaller government contractors, as well as the application of CAS to those contractors for whom government business represented only a relatively small share of total sales volume. The impetus for the development of the concept of modified CAS coverage was the concern expressed at the time, the some business firms (principally smaller firms and non-government segments of major contractors) were avoiding bidding on government contracts because of the perceived burdens associated with the administration of CAS requirements. See Preamble A to CAS Part 332, 42 FR 45625, Sept. 12, 1977.

The previous requirement for modified CAS coverage appearing at 48 CFR 9903.201-2, entitled "Types of CAS coverage" provided:

(b) *Modified coverage.* (1) Modified coverage requires only that the contractor comply with Standard 9904.401, Consistency in Estimating, Accumulating and Reporting Costs, and Standard 9904.402, Consistency in Allocating Costs Incurred for the Same

Purpose. Modified, rather than full, CAS coverage may be applied to a covered contract of less than $10 million awarded to a business unit that received less than $10 million in CAS-covered contracts in the immediately preceding cost accounting period if the sum of such awards was less than 10 percent of the business unit's total sales during that period * * *

Additional provisions of this section, as well as § 9903.202 of the Board's rules, entitled "Disclosure requirements," provided that certain business units that were subject to modified coverage must still file Disclosure Statements (normally required only for contractors subject to full coverage) if the business unit is a part of a larger company that has other business units that are subject to full CAS coverage. See 57 FR 14157 (Apr. 17, 1992).

The regulations providing for modified CAS coverage were originally effective on March 10, 1978. In the intervening 15 years, the dollar threshold for modified CAS coverage had not been adjusted. However, prices as measured by the consumer price index have been adjusted by over 100% during this period. Presumably the issues giving rise to the development of the concept of modified CAS coverage in 1977 have been further highlighted during this time frame. The $10 million threshold, once considered to be the mark at which a contractor had sufficient "covered" contracts to be subject to full CAS coverage, has been eroded by the effects of inflation. This dollar threshold no longer serves as an appropriate size standard that represents a fair demarcation applicable to CAS covered contractors.

The Board is now promulgating what it believes to be appropriate adjustments in the threshold for application of modified CAS coverage to covered contractors. In so doing, the CASB has been considering two principal issues: (1) The adjustment should properly reflect the effects of inflation, and (2) the adjustment should protect the interests of the Government while lessening the need to impose administrative burdens associated with CAS coverage on affected contractors.

Summary of Amendments

The Board's rule provides for a full CAS coverage threshold of $25 million (actual inflation experience rounded to the nearest five million dollar increment). This represents an increase of two-and-one-half times the previous threshold, and approximates inflation experience as measured by the consumer price index from the last quarter of calendar year 1977 through the last quarter of 1992.

In the Board's judgment, its internal study (which is based upon data available in the Federal Procurement Data System) has indicated that this threshold should provide adequate protection to the Government in the form of cumulative contract dollars remaining subject to full CAS coverage, while significantly reducing the number of contractors that will be required to comply with the full scope of the Standards and the requirement for submission of a Disclosure Statement. The results of the Board's study have also established that this increase in the threshold applicable to modified CAS coverage should result in an approximately 45–50% decrease in the number of contractors (or contractor business segments) subject to full CAS coverage, while the corresponding reduction in CAS-covered dollars will be only 5–6% from previous levels. These results would appear to indicate that a substantial reduction in the administrative requirements associated with full CAS coverage will be achieved for a significant number of contractors, and contractor segments, with only a relatively small decrease in the cumulative dollar value of contracts that are subject to the full scope of CAS coverage.

The Board is also increasing the dollar threshold associated with the so-called "trigger contract" in order to further decrease the administrative requirements associated with the application of full CAS coverage. Pursuant to this rule, the "trigger contract" will be that contract dollar threshold ($1 million) associated with the initiation of full CAS coverage, for a particular contractor, based on the award of a single negotiated government contract. Under rules previously in effect (see 4 CFR 331.30(b)(7) and 332, also 48 CFR 30.201–1(b)(7) and 30.201–2(b)), the trigger contract threshold was a single negotiated government contract exceeding $500,000. Once awarded a negotiated government contract of at least this dollar magnitude in a single cost accounting period, a government contractor's segment or business unit was subject to some form of CAS coverage (either full or modified) for all subsequently awarded negotiated contracts exceeding $100,000. Public Law 100–679 raised the threshold for individual CAS contract coverage to $500,000 (see CAS recodification, 57 FR 14148, Apr. 17, 1992), which had the effect of eliminating the $500,000 trigger concept. Without an amendment, the minimum individual CAS contract threshold and the initiating CAS "trigger contract" threshold are currently one and the same. Although the Board has reestablished the "trigger contract" concept in this rule, it has limited its application exclusively to full CAS coverage. Therefore, the application of modified CAS coverage to an individual contract or subcontract will be determined without reference to the triggering contract mechanism applicable to full CAS coverage.

B. Additional Amendments

During the past year, information came to the Board's attention, that indicated a need for redefining the concept of modified CAS coverage. Based on this information, the Board became concerned that some government contractors, particularly those who do work for certain civilian procurement agencies, may be including specifically identifiable unallowable costs in indirect cost pools which are reflected in the billings submitted to, and reimbursements received from Federal Government contracting agencies. Conformance with the requirements of CAS 9904.405 would restrict this practice. Therefore, the Board is adding CAS 9904.405 to the modified CAS coverage requirements. In the Board's view, it is fundamental that Government contractors, engaged in cost-based contracting, be able to comply with this basic cost accounting concept in the pricing and administration of contracts of any dollar value. In addition, the Board has determined that the inclusion of CAS 9904.406, "Cost Accounting Period," in the coverage criteria for modified CAS will significantly reduce the opportunity for selection of inconsistent cost accounting periods with respect to the costing and pricing of contracts. The Board believes that the principle enunciated in Standard 9904.406 is so basic as to be a reasonable requirement for all government contracts priced on the basis of cost. The Board also believes that CAS 9904.406 provides a form of protection to contractors in that it prohibits the use of inappropriate and/or inconsistent cost accounting periods in order to minimize indirect contract costs. As was noted in both the preamble to the Advance Notice of Proposed Rulemaking on this topic (see 57 FR 47438), and the preamble to the Notice of Proposed Rulemaking (see 58 FR 18363) the Board has been considering methods by which to achieve a greater degree of balance between those who would urge it to raise and/or tighten certain CAS applicability thresholds, and those who have argued that these same thresholds should not be revised. The Board's consideration of this issue has led to this rule that applies the requirements of CAS 9904.401, 9904.402, 9904.405 and 9904.406 to all otherwise non-exempt awards exceeding $500,000. This now constitutes the definition of modified CAS coverage.

In addition, through this rule, the Board is hereby eliminating the alternative "10 percent or more" sales test criterion for the initiation of full CAS coverage. The Board has taken this step in order to clarify and simplify the rules with respect to the initiation of full CAS coverage. The elimination of the percent of sales test also precludes the possibility that two contractors with the same amount of covered contracts would be subject to two different levels of coverage.

The approach to the issue of full and modified CAS coverage that is being promulgated by the Board seeks to balance cost versus benefits through an adjustment in CAS thresholds that would extend the applicability of a new definition of modified CAS coverage, while providing for higher cumulative contract dollar value thresholds applicable for so-called full CAS coverage.

The Board has also determined that the exemption paragraph appearing at § 9904.201-1(b)(15) should be expanded to eliminate the requirement for a separate Cost Accounting Standards Board waiver in circumstances where the relevant procuring agency has determined to waive the requirement for submission of certified cost or pricing data. The Board believes that adequate safeguards exist within the procuring agencies with respect to this issue so as to preclude the need for the approval of individual CAS contract waivers by the Board. The elimination of this requirement should significantly ease the administrative burdens (for both the Government and contractors/subcontractors) associated with obtaining CAS coverage exemptions in those instances where the agency has already waived the requirements of the Truth in Negotiations Act, Public Law 87-653.

Finally the Board has determined to adjust the requirements for disclosure by certain otherwise modified CAS-covered business segments that are required to disclose their cost accounting practices because they are affiliated with other business segments that are subject to full CAS coverage. The Board's final rule adopts a combined $10 million and 30% sales test for determining whether disclosure is required for these otherwise modified CAS-covered business units.

C. Paperwork Reduction Act

The Paperwork Reduction Act, Public Law 96-511, does not apply to this rule, because this rule imposes no paperwork burden on offerors, affected contractors and subcontractors, or members of the public which requires the approval of OMB under 44 U.S.C. 3501, *et seq.* The purpose of this rule is to decrease the burdens (including paperwork) associated with the administration of the Cost Accounting Standards by covered government contractors and subcontractors.

D. Executive Order 12866 and the Regulatory Flexibility Act

This rule serves to eliminate certain administrative requirements associated with the administration of the Cost Accounting Standards by covered government contractors and subcontractors. The economic impact on contractors and subcontractors is therefore expected to be minor. As a result, the Chairman has determined that this is not a "major rule" under the provisions of Executive Order 12866, and that a regulatory impact analysis is not required. Furthermore, this rule will not have a significant effect on a substantial number of small entitities because small businesses are exempt from the application of the Cost Accounting Standards. Therefore, this rule does not require a regulatory flexibility analysis under the Regulatory Flexibility Act of 1980.

E. Public Comments

This final rule is based upon the Board's Notice of Proposed Rulemaking made available for public comment in the **Federal Register** on April 9, 1993, 58 FR 18363. Thirty sets of comments were received, including twenty-five timely comments, and five late comments. The major comments received and the Board's actions taken in response thereto are summarized below:

Comment: Nineteen commenters supported the NPRM's proposal for an increased "full" CAS coverage threshold, and thirteen commenters supported elimination of the alternative "10 percent of sales" test for the initiation of full CAS coverage. Three commenters supported the addition of CAS 9904.405 to the definition of "modified" CAS coverage, and six commenters supported adding CAS 9904.406 to this definition as well. An additional seven commenters supported the Board's elimination of the need for a separate CAS waiver when an agency had already granted a waiver from the requirement to submit certified cost or pricing data pursuant to the provisions of the Truth in Negotiations Act, Public Law 87-653. Finally, three commenters supported the Board's proposed $1 million trigger contract for the application of full CAS coverage.

Response: The Board thanks the commenters for their supportive comments.

Comment: Four commenters recommended that the Board revise the rule to include counting only "net awards" in determining whether certain CAS thresholds are met.

Response: The Board does not agree with the commenters. As the Board understands the commenters' position, "net awards" refers to the total obligated value of the contract at the time of award, excluding as-yet-to-be-obligated incremental funding, and the potential value of contract options. The Board believes that CAS applicability thresholds are met when the total dollar value of the contract (including as-yet-to-be-provided incremental funding and the potential value of contract options) exceeds the appropriate thresholds. Because this appeared to be a recurring issue among some contractors, the Board is amending the definition of "net awards" in order to make it clear that incrementally-funded contracts and the potential value of contract options are to be included in determining a contractor's or subcontractor's CAS eligibility status. The Board believes that it is the value of the pricing proposal or action that gives rise to CAS applicability.

Comment: One commenter (the Department of Defense Office of Inspector General) strongly opposed increasing the dollar threshold (previously $10 million) associated with the initiation of full CAS coverage. This commenter continues to believe that the $10 million threshold was of sufficient magnitude that the requirements for full CAS coverage (including the submission of a Disclosure Statement) should continue to apply without modification. This commenter, as well as one other, also supported elimination of the "trigger contract" concept. This commenter believes that previous thresholds associated with the administration of CAS requirements (with the exception of the "10 percent of sales test") do not impose hardships or burdens on industry.

Response: The Board does not agree with all aspects of this comment. The Board continues to believe that the effects of inflation over the past fifteen years should be considered in determining CAS applicability thresholds. Moreover, the Board notes that its proposal results in an approximately 45–50% decrease in the number of contractors subject to "full" CAS coverage, while reducing the coverage of covered contract dollars by only 5–6%. In the Board's view, this will allow both contractors and administering Government agencies to better focus available resources on contracts of significant dollar value.

Comment: Two commenters, representing government contractors, endorsed a proposal to raise the "full" CAS coverage threshold to between $30–$50 million. Nine similar commenters also endorsed the reinstitution of the "trigger contract" concept, but believed that it should be applied to modified, as well as, full CAS coverage. Another two commenters recommended that the trigger contract concept be reinstated at a threshold of $2.5 million. Eight commenters further recommended the elimination of the requirement for the filling of disclosure statements for modified CAS-covered business segments that are affiliated with another business segment that is subject to full CAS coverage. Thirteen commenters opposed inclusion of CAS 9904.405 in the definition of modified coverage, and five commenters opposed including CAS 9904.406.

Response: The Board believes that CAS requirements and disclosure thresholds should generally be adjusted in accordance with inflationary experience. It does not consider the commenters proposed higher levels appropriate given the statutory objectives of the Board and the substantial amounts of public spending involved in covered contracts. In response to commenters' concerns previously made known to the Board after issuance of both its ANPRM and NPRM on this subject, the Board is reinstituting the "trigger contract" concept with respect to the initiation of full CAS coverage. The new trigger contract threshold is $1 million. The Board is also adjusting the requirements for the filing of disclosure statements for certain modified CAS-covered business segments that are affiliated with another business segment that is subject to full CAS coverage. The Board respectfully disagrees with the commenters recommendations that CAS 9904.405 and 9904.406 be excluded from the definition of modified coverage. The Board continues to have serious reservations concerning administration of cost-based contract pricing and/or reimbursement arrangements with contractors that are unable to comply with these very fundamental cost accounting concepts and/or practices.

Comment: One commenter recommended that the Board exempt from all CAS coverage, contracts that are awarded to "commercial companies."

Response: The Board continues to believe that the requirements of the Cost Accounting Standards should generally be applied to negotiated contracts that exceed certain dollar thresholds as determined by the Board, in which contract cost or price is determined through the submission of cost or pricing data. The Board does not agree that the mere existence of competition at some level of the procurement process, e.g., technical competition, should give rise to an exemption from application of the Standards, if the element of adequate price competition, as applied to the instant procurement action, is not present. The Board is amending its rules in order to modify the CAS exemption paragraph appearing at 9903.201–1(b)(15). This will serve to eliminate the requirement for a separate Cost Accounting Standards Board waiver in circumstances where the relevant procuring agency has determined to waive the requirement for submission of certified cost or pricing data. The Board believes that this amendment should assist commercial companies in cases where they would ordinarily be subject to TINA, but the requirement for submission of certified cost or pricing data has been waived by the relevant procuring agency.

List of Subjects in 48 CFR Part 9903

Cost accounting standards, Government procurement.

Allan V. Burman,

Administrator for Federal Procurement Policy and Chairman, Cost Accounting Standards Board.

For the reasons set forth in this preamble, chapter 99 of title 48 of the Code of Federal Regulations is amended as set forth below:

1. The authority citation for part 9903 of chapter 99 of title 48 continues to read as follows:

Authority: Pub. L. 100–679, 102 Stat. 4056, 41 U.S.C. 422.

PART 9903—CONTRACT COVERAGE

Subpart 9903.2—CAS Program Requirements

2. Section 9903.201–1 is amended by revising paragraph (b) introductory text and paragraph (b) to read as follows:

9903.201–1 CAS applicability.

* * * * *

(b) The following categories of contracts and subcontracts are exempt from all CAS requirements:

* * * * *

(15) Firm-fixed-price contracts and subcontracts awarded without submission of any cost data.

3. Section 9903.201–2 is amended by revising paragraphs (a) (1) and (2); removing paragraph (a)(3); and revising paragraph (b) (1) and (2) and paragraph (d) to read as follows:

9903.201–2 Types of CAS coverage.

(a) * * *

(1) Receive a single CAS-covered contract award of $25 million or more; or

(2) Received $25 million or more in net CAS-covered awards during its preceding cost accounting period, of which, at least one award exceed $1 million.

(b) *Modified coverage.* (1) Modified CAS coverage requires only that the contractor comply with Standard 9904.401, Consistency in Estimating, Accumulating, and Reporting Costs, Standard 9904.402, Consistency in Allocating Costs Incurred for the Same Purpose, Standard 9904.405, Accounting for Unallowable Costs and Standard 9904.406, Cost Accounting Standard—Cost Accounting Period. Modified, rather, than full, CAS coverage may be applied to a covered contract of less than $25 million awarded to a business unit that received less than $25 million in net CAS-covered awards in the immediately preceding cost accounting period. It also applies to covered contracts of business units that received more than $25 million in net CAS covered awards in the immediately preceding cost accounting period, wherein no single contract award exceeded $1 million.

(2) If any one contract is awarded with modified CAS coverage, all CAS-covered contracts awarded to the business unit during that cost accounting period must also have modified coverage with the following exception: if the business unit receives a single CAS-covered contract award of $25 million or more, that contract must be subject to full CAS coverage. Thereafter, any covered contract awarded in the same cost accounting period must also be subject to full CAS coverage.

* * * * *

(d) *Subcontracts.* Subcontract awards subject to CAS require the same type of CAS coverage as would prime contracts awarded to the same business unit. In measuring total net CAS-covered awards for a year, a transfer by one segment to another shall be deemed to be a subcontract award by the transferor.

* * * * *

4. Section 9903.201–3 is amended by revising the clause heading and

Preamble B - New Thresholds (58 fr 58798)

introductory text; by revising paragraphs (c) (1) and (3) in Part I of the clause; by removing Part II; by redesignating Parts III and IV as Parts II and III respectively; and revising newly designated Part II to read as follows:

9903.201–3 Solicitation provisions.

* * * * *

Cost Accounting Standards Notices and Certification (November 1993)

Note: This notice does not apply to small businesses or foreign governments.

This notice is in three parts, identified by Roman numerals I through III.

Offerors shall examine each part and provide the requested information in order to determine Cost Accounting Standards (CAS) requirements applicable to any resultant contract.

I. Disclosure Statement—Cost Accounting Practices and Certification

* * * * *

(c) Check the appropriate box below:

☐ (1) Certificate of Concurrent Submission of Disclosure Statement.

The offeror hereby certifies that, as a part of the offer, copies of the Disclosure Statement have been submitted as follows: (i) Original and one copy to the cognizant Administrative Contracting Officer (ACO), and (ii) One copy to the cognizant contract auditor.

(Disclosure must be on Form No. CASB DS–1. Forms may be obtained from the cognizant ACO or from the looseleaf version of the Federal Acquisition Regulation.)

Date of Disclosure Statement:

Name and Address of Cognizant ACO where filed:

The offeror further certifies that practices used in estimating costs in pricing this proposal are consistent with the cost accounting practices disclosed in the Disclosure Statement.

☐ (2) * * *

☐ (3) Certificate of Monetary Exemption.

The offeror hereby certifies that the offeror, together with all divisions, subsidiaries, and affiliates under common control, did not receive net awards of negotiated prime contracts and subcontracts subject to CAS totaling more than $25 million (of which at least one award exceeded $1 million) in the cost accounting period immediately preceding the period in which this proposal was submitted. The offeror further certifies that if such status changes before an award resulting from this proposal, the offeror will advise the Contracting Officer immediately.

* * * * *

II. Cost Accounting Standards—Eligibility for Modified Contract Coverage

If the offeror is eligible to use the modified provisions of 9903.201–2(b) and elects to do so, the offeror shall indicate by checking the box below. Checking the box below shall mean that the resultant contract is subject to the Disclosure and Consistency of Cost Accounting Practices clause in lieu of the Cost Accounting Standards clause.

☐ The offeror hereby claims an exemption from the Cost Accounting Standards clause under the provisions of 9903.201–2(b) and certifies that the offeror is eligible for use of the Disclosure and Consistency of Cost Accounting Practices clause because during the cost accounting period immediately preceding the period in which this proposal was submitted, the offeror received less than $25 million in awards of CAS-covered prime contracts and subcontractors, or the offeror did not receive a single CAS-covered award exceeding $1 million. The offeror further certifies that if such status changes before an award resulting from this proposal, the offeror will advise the Contracting Officer immediately.

Caution: An offeror may not claim the above eligibility for modified contract coverage if this proposal is expected to result in the award of a CAS-covered contract of $25 million or more or if, during its current cost accounting period, the offeror has been awarded a single CAS-covered prime contract or subcontract of $25 million or more.

* * * *

5. Section 9903.201–4 is amended by revising paragraph (c)(1) to read as follows:

9903.201–4 Contract clauses.

* * * * *

(c) *Disclosure and Consistency of Cost Accounting Practices.* (1) The contracting officer shall insert the clause set forth below, Disclosure and Consistency of Cost Accounting Practices, in negotiated contracts when the contract amount is over $500,000 but less than $25 million, and the offeror certifies it is eligible for and elects to use modified CAS coverage (see 9903.201–2, unless the clause prescribed in paragraph (d) of this subsection is used).

* * * * *

9903.202 Disclosure requirements.

6. Section 9903.202–1 is amended by revising paragraphs (b) (1) and (2) paragraph (c) to read as follows:

9903.202–1 General requirements.

* * * * *

(b) * * *

(1) Any business unit that is selected to receive a CAS-covered contract or subcontract of $25 million or more shall submit a Disclosure Statement before award.

(2) Any company which, together with its segments, received net awards of negotiated prime contracts and subcontracts subject to CAS totaling more than $25 million in its most recent cost accounting period, of which, at least one award exceeded $1 million, must submit a Disclosure Statement before award of its first CAS-covered contract in the immediately following cost accounting period. However, if the first CAS-covered contract is received within 90 days of the start of the cost accounting period, the contractor is not required to file until the end of 90 days.

(c) When a Disclosure Statement is required, a separate Disclosure Statement must be submitted for each segment whose costs included in the total price of any CAS-covered contract or subcontract exceed $500,000, unless (i) The contract or subcontract is of the type or value exempted by 9903.201–1 or (ii) In the most recently completed cost accounting period the segment's CAS-covered awards are less than 30 percent of total segment sales for the period and less than $10 million.

* * * * *

Subpart 9903.3—CAS Rules and Regulations

7. Section 9903.301 is amended by revising the definition for Net Awards to read as follows:

§ 9903.301 Definitions.

* * * * *

Net awards, as used in this chapter, means the total value of negotiated CAS-covered prime contract and subcontract awards, including the potential value of contract options, received during the reporting period minus cancellations, terminations, and other related credit transactions.

* * * * *

[FR Doc. 93–27111 Filed 11–3–93; 8:45 am]

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DEPARTMENT OF COMMERCE

National Oceanic and Atmospheric Administration

50 CFR Part 675

[Docket No. 921185–3021; I.D. 110193A]

Groundfish of the Bering Sea and Aleutian Islands Area

AGENCY: National Marine Fisheries Service (NMFS), National Oceanic and Atmospheric Administration (NOAA), Commerce.

ACTION: Closure.

SUMMARY: NMFS is closing the directed fishery for Atka mackerel in the Central Aleutian District (statistical area 542) of the Aleutian Islands subarea in the Bering Sea and Aleutian Islands area (BSAI). This action is necessary to prevent exceeding the Atka mackerel total allowable catch (TAC) in the Central Aleutian District.

EFFECTIVE DATE: 12 noon, Alaska local time (A.l.t.), November 1, 1993, until 12 midnight, A.l.t., December 31, 1993.

FOR FURTHER INFORMATION CONTACT: Andrew N. Smoker, Resource Management Specialist, Fisheries Management Division, NMFS, 907–586–7228.

SUPPLEMENTARY INFORMATION: The groundfish fishery in the BSAI exclusive economic zone is managed by the Secretary of Commerce according to the Fishery Management Plan for the Groundfish Fishery of the BSAI (FMP) prepared by the North Pacific Fishery Management Council under authority of the Magnuson Fishery Conservation and Management Act. Fishing by U.S. vessels is governed by regulations implementing the FMP at 50 CFR parts 620 and 675.

The Atka mackerel TAC specified for the Central Aleutian District was established by a revision to the final 1993 initial specifications of groundfish in the BSAI (58 FR 37660, July 13, 1993) and later augmented from the reserve (58 FR 50856, September 29, 1993) to 27,000 metric tons (mt). The directed fishery in the Central Aleutian District opened on August 11, 1993 (58 FR 43297, August 16, 1993).

The Director of the Alaska Region, NMFS (Regional Director), has determined, in accordance with § 675.20(a)(8), that the Atka mackerel TAC in the Central Aleutian District soon will be reached. Therefore, the Regional Director has established a directed fishing allowance of 26,500 mt, with consideration that 500 mt will be taken as incidental catch in directed fishing for other species in the Central Aleutian District. The Regional Director has determined that the directed fishing allowance has been reached. Consequently, NMFS is prohibiting directed fishing for Atka mackerel in the Central Aleutian District, effective from 12 noon, A.l.t., November 1, 1993, until 12 midnight, A.l.t., December 31, 1993.

Directed fishing standards for applicable gear types may be found in the regulations at § 675.20(h).

Classification

This action is taken under § 675.20.

List of Subjects in 50 CFR Part 675

Fisheries, Reporting and recordkeeping requirements.

Authority: 16 U.S.C. 1801 *et seq.*

Dated: November 1, 1993.

David S. Crestin,

Acting Director, Office of Fisheries Conservation and Management, National Marine Fisheries Service.

[FR Doc. 93-27075 Filed 11-1-93; 2:15 pm]

BILLING CODE 3510-22-M

Preamble C - Applicability and Thresholds (59 fr 48568)

imposition of an amount that would exceed limits imposed by the United States Constitution.

(2) The amount imposed will not be less than the approximate amount required to fully compensate the United States, or any State, for its damages and costs, tangible and intangible, including but not limited to the costs attributable to the investigation, prosecution, and administrative review of the case.

(3) Nothing in this section will limit the authority of the Department to settle any issue or case as provided by § 1003.126, or to compromise any penalty and assessment as provided by § 1003.128.

Dated: September 13, 1994.

June Gibbs Brown,

Inspector General.

[FR Doc. 94–23415 Filed 9–21–94; 8:45 am]

BILLING CODE 4150–04–P

DEPARTMENT OF THE INTERIOR

Bureau of Land Management

43 CFR Public Land Order 7086

[WY–930–4210–06; WYW–84553]

Public Land Order No. 7039, Correction; Partial Revocation of Executive Order No. 5327, as Modified, and Public Land Order No. 4522; Wyoming

AGENCY: Bureau of Land Management, Interior.

ACTION: Public land order.

SUMMARY: This order will correct an error in the land description of Public Land Order No. 7039.

EFFECTIVE DATE: September 22, 1994.

FOR FURTHER INFORMATION CONTACT: Duane Feick, BLM Wyoming State Office, P.O. Box 1828, Cheyenne, Wyoming 82003, 307–775–6127.

By virtue of the authority vested in the Secretary of the Interior by Section 204(a) of the Federal Land Policy and Management Act of 1976, 43 U.S.C. 1714 (1988), it is ordered as follows:

The land description in Public Land Order No. 7039, 59 FR 19641, April 25, 1994, is hereby corrected as follows:

On page 19641, column 2, line 39, which reads "E½NW¼, and NE¼SE¼." is hereby corrected to read "E½NW¼, and NE¼SW¼.".

Bob Armstrong,

Assistant Secretary of the Interior.

[FR Doc. 94–23404 Filed 9–21–94; 8:45 am]

BILLING CODE 4310–22–P

43 CFR Public Land Order 7087

[AK–932–4210–06; AA–58075]

Partial Revocation of Secretarial Order Dated January 22, 1940, as Modified; Alaska

AGENCY: Bureau of Land Management, Interior.

ACTION: Public Land Order.

SUMMARY: This order revokes a Secretarial order, as modified, insofar as it affects 22.12 acres of public land withdrawn for Air Navigation Site No. 134 at Willow. The land is no longer needed for the purpose for which it was withdrawn. This action also allows the conveyance of the land to the State of Alaska, if such land is otherwise available. Any land described herein that is not conveyed to the State is opened and will be subject to the terms and conditions of Public Land Order No. 5186, as amended, and any other withdrawal of record.

EFFECTIVE DATE: September 22, 1994.

FOR FURTHER INFORMATION CONTACT: Sue A. Wolf, BLM Alaska State Office, 222 W. 7th Avenue, No. 13, Anchorage, Alaska 99513–7599, 907–271–5477.

By virtue of the authority vested in the Secretary of the Interior by Section 204 of the Federal Land Policy and Management Act of 1976, 43 U.S.C. 1714 (1988), and by Section 17(d)(1) of the Alaska Native Claims Settlement Act 43 U.S.C. 1616(d)(1) (1988), it is ordered as follows:

1. The Secretarial Order dated January 22, 1940, as modified, which withdrew public land at Willow for Air Navigation Site No. 134, is hereby revoked insofar as it affects the following described land:

Seward Meridian

Located within T. 19 N., R. 1 W., described as U.S. Survey No. 5556. The area described contains 22.12 acres.

2. The State of Alaska application for selection made under Section 6(b) of the Alaska Statehood Act of July 7, 1958, 48 U.S.C. note prec. 21 (1988), and under Section 906(e) of the Alaska National Interest Lands Conservation Act, 43 U.S.C. 1635(e) (1988), becomes effective without further action by the State upon publication of this public land order in the **Federal Register**, if such land is otherwise available. Land not conveyed to the State is opened and will be subject to the terms and conditions of Public Land Order No. 5186, as amended, and any other withdrawal of record.

Bob Armstrong,

Assistant Secretary of the Interior.

[FR Doc. 94–23403 Filed 9–21–94; 8:45 am]

BILLING CODE 4310–JA–P

OFFICE OF MANAGEMENT AND BUDGET

Office of Federal Procurement Policy

48 CFR Part 9903

Cost Accounting Standards Board; Applicability and Thresholds for Cost Accounting Standards Coverage; Correction

AGENCY: Cost Accounting Standards Board, Office of Federal Procurement Policy, OMB.

ACTION: Correction to final rule.

SUMMARY: This document contains a correction to the correction notice published in the **Federal Register** on Wednesday, December 15, 1993 (58 FR 65556). The notice concerned the final rule revising applicability, thresholds and procedures for the application of Cost Accounting Standards to negotiated government contracts, which was published Thursday, November 4, 1993 (58 FR 58798).

EFFECTIVE DATE: November 4, 1993.

FOR FURTHER INFORMATION CONTACT: Richard C. Loeb, Executive Secretary, Cost Accounting Standards Board (telephone: 202–395–3254).

SUPPLEMENTARY INFORMATION: The correction notice published Wednesday, December 15, 1993, at 58 FR 65556 did not provide full text under Section 9903.201–4 and is corrected as follows.

On page 65556, in the second column, section 9903.201–4, paragraph (c)(2) and the heading and paragraph (a)(1) of the "Disclosure and Consistency of Cost Accounting Practices" clause instructions is corrected to read as follows:

9903.201–4 Contract clauses.

* * * * *

(c) * * *

(2) The clause below requires the contractor to comply with CAS 9904.401, 9904.402, 9904.405, and 9904.406, to disclose (if it meets certain requirements) actual cost accounting practices, and to follow consistently disclosed and established cost accounting practices.

Disclosure and Consistency of Costs Accounting Practices (Nov 1993)

(a) * * *

(1) Comply with the requirements of 9904.401, Consistency in Estimating, Accumulating, and Reporting Costs; 9904.402, Consistency in Allocating Costs Incurred for the Same Purpose; 9904.405, Accounting for Unallowable Costs; and 9904.406, Cost Accounting Standard—Cost Accounting Period, in effect on the date of award of this contract, as indicated in Part 9904.

* * * * *

Richard C. Loeb,
Executive Secretary, Cost Accounting Standards Board.

[FR Doc. 94-23499 Filed 9-21-94; 8:45 am]

BILLING CODE 3110-01-M

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48 CFR Part 9903

Cost Accounting Standards Board; Applicability for Cost Accounting Standards Coverage

AGENCY: Cost Accounting Standards Board, Office of Federal Procurement Policy, OMB.

ACTION: Final rule.

SUMMARY: The Office of Federal Procurement Policy, Cost Accounting Standards Board, revised the applicability, thresholds and procedures for the application of Cost Accounting Standards (CAS) to negotiated government contracts, on Thursday, November 4, 1993 (58 FR 58798). The Board is taking action to avoid confusion with CAS requirements appearing at 48 CFR 9903.201-1, CAS applicability, and 48 CFR 9903.201-2, Types of CAS coverage. The change addresses the current conflicting language that concerns contracts and subcontracts with foreign governments.

EFFECTIVE DATE: November 4, 1993.

FOR FURTHER INFORMATION CONTACT: Richard C. Loeb, Executive Secretary, Cost Accounting Standards Board (telephone: 202-395-3254).

SUPPLEMENTARY INFORMATION: On November 4, 1993, the CASB promulgated rules revising applicability, thresholds and procedures for the application of the CAS to negotiated government contracts. When the final rule was published (58 FR 58798), changes to 48 CFR 9903.201-2, Types of CAS coverage, were not transmitted.

This rule serves to modify the language as it currently appears with respect to contracts and subcontracts with foreign governments, to avoid any confusion regarding CAS requirements.

1. The authority citation for part 9903 of chapter 99 of title 48 continues to read as follows:

Authority: Pub. L. 100-679, 102 Stat. 4056, 41 U.S.C. §422.

PART 9903—CONTRACT COVERAGE

Subpart 9903.2—CAS Program Requirements

2. Section 9903.201-2 is amended by revising paragraph (e) to read as follows:

9903.201-2 Types of CAS coverage.

* * * * *

(e) *Foreign concerns.* Contracts with foreign concerns subject to CAS shall only be subject to Standard 9904.401, Consistency in Estimating, Accumulating, and Reporting Costs, and Standard 9904.402, Consistency in Allocating Costs Incurred for the Same Purpose.

Richard C. Loeb,
Executive Secretary, Cost Accounting Standards Board.

[FR Doc. 94-23500 Filed 9-21-94; 8:45 am]

BILLING CODE 3110-01-M

DEPARTMENT OF THE INTERIOR

Fish and Wildlife Service

50 CFR Part 20

RIN 1018-AA24

Migratory Bird Hunting: Migratory Bird Hunting Regulations on Certain Federal Indian Reservations and Ceded Lands for the 1994-95 Late Season

AGENCY: Fish and Wildlife Service, Interior.

ACTION: Final rule.

SUMMARY: This rule prescribes special late season migratory bird hunting regulations for certain tribes on Federal Indian reservations, off-reservation trust lands and ceded lands. This is in response to tribal requests for Service recognition of their authority to regulate hunting under established guidelines. This rule is necessary to allow establishment of season bag limits and, thus, harvest at levels compatible with populations and habitat conditions.

EFFECTIVE DATE: This rule takes effect on September 24, 1994.

ADDRESSES: Comments received on the tribal proposals and special hunting regulations are available for public inspection during normal business hours in Room 634, Arlington Square Building, 4401 N. Fairfax Drive, Arlington, VA. Communications regarding the documents should be sent to: Director (FWS/MBMO), U.S. Fish and Wildlife Service, 634 ARLSQ, 1849 C St., NW, Washington, DC 20240.

FOR FURTHER INFORMATION CONTACT: Dr. Keith A. Morehouse, Office of Migratory Bird Management, U.S. Fish and Wildlife Service, Department of the Interior, 634 ARLSQ, 1849 C St., NW, Washington, DC 20240 (703/358-1714).

SUPPLEMENTARY INFORMATION: The Migratory Bird Treaty Act of July 3, 1918 (40 Stat. 755; 16 U.S.C. 703 *et seq.*), authorizes and directs the Secretary of the Interior, having due regard for the zones of temperature and for the distribution, abundance, economic value, breeding habits, and times and lines of flight of migratory game birds, to determine when, to what extent, and by what means such birds or any part, nest or egg thereof may be taken, hunted, captured, killed, possessed, sold, purchased, shipped, carried, exported or transported.

In the August 16, 1994 **Federal Register** (59 FR 42017), the U. S. Fish and Wildlife Service (Service) proposed special migratory bird hunting regulations for the 1994-95 hunting season for certain Indian tribes, under the guidelines described in the June 4, 1985, **Federal Register** (50 FR 23467). The guidelines were developed in response to tribal requests for Service recognition of their reserved hunting rights, and for some tribes, recognition of their authority to regulate hunting by both tribal members and nonmembers on their reservations. The guidelines include possibilities for: (1) On-reservation hunting by both tribal members and nonmembers, with hunting by nontribal members on some reservations to take place within Federal frameworks but on dates different from those selected by the surrounding State(s); (2) on-reservation hunting by tribal members only, outside of usual Federal frameworks for season dates and length, and for daily bag and possession limits; and (3) off-reservation hunting by tribal members on ceded lands, outside of usual framework dates and season length, with some added flexibility in daily bag and possession limits. In all cases, the regulations established under the guidelines would have to be consistent with the March 10-September 1 closed season mandated by the 1916 Convention on the Protection of Migratory Birds Between the U.S. and Great Britain (for Canada). Tribes that desired special hunting regulations in the 1994-95 hunting season were requested in the April 7, 1994, **Federal Register** (59 FR 16762) to submit a proposal that included details on: (1) requested season dates and other regulations to be observed; (2) harvest anticipated under the requested regulations; (3) methods that will be employed to measure or monitor harvest; (4) steps that will be taken to

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OFFICE OF MANAGEMENT AND BUDGET

Office of Federal Procurement Policy

48 CFR Parts 9903, 9905

Cost Accounting Standards Board; Application of Cost Accounting Standards Board Regulations to Educational Institutions

AGENCY: Cost Accounting Standards Board, Office of Federal Procurement Policy, OMB.

ACTION: Final rule.

SUMMARY: The Cost Accounting Standards Board (CASB) hereby amends the regulatory provisions contained in Chapter 99 of Title 48. The amendments being promulgated today as a final rule apply to educational institutions receiving a negotiated Federal contract or subcontract award, in excess of $500,000 (excluding contracts awarded for the operation of Federally Funded Research and Development Centers (FFRDCs) which are already subject to CASB regulations), and require that such educational institutions comply with certain specified CASB rules, regulations and Cost Accounting Standards (CAS).

EFFECTIVE DATE: This rule is effective on January 9, 1995.

FOR FURTHER INFORMATION CONTACT: Rudolph J. Schuhbauer, Project Director, Cost Accounting Standards Board (telephone: 202–395–3254).

SUPPLEMENTARY INFORMATION:

A. Regulatory Process

The CASB's rules, regulations and Standards are codified at 48 CFR Chapter 99. Section 26(g)(1) of the Office of Federal Procurement Policy Act, 41 U.S.C. 422(g), requires that the Board, prior to the establishment of any new or revised CAS, complete a prescribed rulemaking process. The process generally consists of the following four steps:

1. Consult with interested persons concerning the advantages, disadvantages and improvements anticipated in the pricing and administration of Government contracts as a result of the adoption of a proposed Standard.
2. Promulgate an Advance Notice of Proposed Rulemaking (ANPRM).
3. Promulgate a Notice of Proposed Rulemaking (NPRM).
4. Promulgate a final rule.

This promulgation completes the four step process.

B. Background

Prior Promulgations: Based on information that some institutions of higher education were improperly allocating indirect costs to Federal research programs and charging unallowable costs to Federal awards (e.g., contracts, grants and cooperative agreements), the CASB published three Federal Register (FR) proposals requesting public comments from interested parties concerning the proposed application of the Board's rules, regulations and Standards to educational institutions. A Staff Discussion Paper was published on October 8, 1991 (56 FR 50737). After consideration of the public comments received in response to the Staff Discussion Paper, the CASB published an Advance Notice of Proposed Rulemaking (ANPRM) on June 2, 1992 (57 FR 23189). On December 21, 1992, after consideration of the public comments received in response to the ANPRM, the CASB published a Notice of Proposed Rulemaking (NPRM) (57 FR 60503) concerning proposed amendments to Chapter 99 of Title 48 that, when issued as a final rule, would require educational institutions to comply with certain specified CASB rules, regulations and Standards.

Public Comments: Seventy sets of public comments were received in response to the NPRM from educational institutions, Government agencies, public accounting firms, a professional accounting association, other associations, and an individual.

Many commenters opposed the CASB's proposal to independently promulgate CAS coverage for application to colleges and universities. The commenters' concerns centered primarily on the premise that the Board's proposal would result in a "second" set of accounting rules that may conflict with the accounting principles specified in Office of Management and Budget (OMB) Circular A–21, Cost Principles For Educational Institutions. Establishment of a "single" set of accounting requirements in Circular A–21 was recommended. In the promulgations referenced above, the Board stated that its proposed requirements are intended to be compatible with the basic requirements of Circular A–21. No conflicting provisions were specifically identified by the commenters. The Board, in its promulgations, repeatedly stated that it expected OMB to extend the CAS coverage established for contracts to grants and other forms of financial assistance by formal revision of Circular A–21.

On July 26, 1993, OMB, in the preamble comments to a Federal Register proposal making certain final revisions to Circular A–21 (58 FR 39997), stated that "Consistent with the Board's stated expectations, OMB plans to extend the CASB's regulations and Standards applicable to educational institutions to all awards (contracts and grants) made to institutions that are major recipients of Federal research funds."

Consistent with the CASB's stated expectations and independent statutory rulemaking authority, the CASB is promulgating this final rule in today's Federal Register. The Board has purposefully delayed the effective date of this final rule by 60 days so that OMB, by separate action, can amend Circular A–21 to incorporate the Board's requirements. Once promulgated, the Circular A–21 amendments incorporating CAS should mitigate the basis for the commenters' concerns regarding "two" sets of rules.

A number of commenters expressed opposition to the Board's proposal from administration and cost of implementation viewpoints, but such commenters generally did not take issue with the technical aspects of the proposed coverage. Some commenters endorsed the Board's proposal. Several commenters provided constructive editorial and technical comments which, in their opinion, would improve and clarify the Board's proposed regulatory coverage.

The commenters' overall concerns and suggestions are addressed in greater detail under Section E., Public Comments. The Board and the CASB staff express their appreciation for the constructive suggestions and criticisms provided by the commenters, particularly those offered to clarify and improve the proposed language in Parts 9903 and 9905, and the content of the proposed Disclosure Statement. Many of the commenters' suggested improvements have been incorporated into the final rule being promulgated today.

Benefits: After consideration of the public comments received, it is the Board's opinion that the application of the CAS provisions being promulgated today will improve the cost accounting practices followed by educational institutions when estimating, accumulating and reporting costs under Federal awards, and that the incremental costs of compliance with the Board's specific requirements will be minimal. Costs associated with the initial preparation and maintenance of a Disclosure Statement should be offset by reductions in the recurring administrative costs currently associated with the preparation of cost accounting data being submitted routinely to the cognizant Federal agencies for informational support, evaluation and negotiation of the institutions' indirect cost rate proposals. Use of the Disclosure Statement being promulgated today should also reduce the potential for disagreements between the contracting parties regarding an institution's cost accounting practices.

The Board believes this final rule will promote uniformity and consistency in the educational institutions' cost accounting practices. The potential benefits accruing to the Government's audit, negotiation and general contract administration processes will be substantial and will greatly outweigh any added costs.

Proposed Amendments: A brief description of the proposed amendments follows:

Part 9903, Contract Coverage: In Subpart 9903.2, CAS Program Requirements, existing subparagraph 9903.201–1(b)(10), exempting certain contracts awarded to educational institutions from CAS, is deleted. Subsections 9903.201–1 and 9903.201–2 are amended to identify which Standards shall continue to be applied to contractors other than educational institutions, and a new paragraph (9903.201–2(c)) is added to establish the particular Standards and associated contractual provisions to be applied to educational institutions. Subsection 9903.201–3 is amended to conform the prescribed solicitation notice for use by educational institutions. Subsection 9903.201–4 is amended to establish a unique contract clause for inclusion in CAS-covered contracts awarded to educational institutions. Subsection 9903.201–6 is amended to reference the new contract clause's provision permitting equitable adjustments when a change in cost accounting practice is found to be desirable and not detrimental. Section 9903.201–7 is added to specify cognizant Federal agency responsibilities for administering CAS-covered contracts. Section 9903.202 is amended to establish Disclosure Statement filing requirements for educational institutions (including temporary transition period filing requirements), prescribe the disclosure form to be submitted by educational institutions, and add new provisions requiring the cognizant Federal agency to establish policies and procedures for promptly determining the adequacy of submitted Disclosure Statements. In Subpart 9903.3, CAS Rules and Regulations, Section 9903.301 is amended to incorporate cross-references to definitions for certain new and existing terms.

Part 9905, Cost Accounting Standards For Educational Institutions: A new Part 9905 is added to incorporate four new Standards applicable to educational institutions, i.e., one requiring consistency in estimating, accumulating and reporting costs (Section 9903.501), one requiring consistency in allocating costs (Section 9903.502), one requiring contractor identification of specific unallowable costs (Section 9903.505), and one requiring consistency in the selection and use of a cost accounting period (Section 9903.506).

Summary Description of Amended CAS Coverage: As amended, Part 9903 and Part 9905 apply to educational institutions. A prescribed CAS contract clause must be incorporated in any negotiated Federal contract or subcontract awarded, in excess of $500,000, to an educational institution. An institution receiving a CAS-covered award will be contractually required to (1) consistently follow its established cost accounting practices when estimating (proposed costs), accumulating, and reporting costs under that and any subsequent CAS-covered award(s), (2) consistently allocate costs incurred for the same purpose, (3) identify unallowable costs and exclude from its billings, claims and proposals costs that are expressly unallowable or mutually agreed to be unallowable, and (4) consistently use the same cost accounting period for purposes of estimating, accumulating and reporting costs. Institutions receiving CAS-covered contracts will also be required to formally disclose, in a prescribed Disclosure Statement, and consistently follow their disclosed cost accounting practices, when a business unit of an institution:

(a) receives a CAS-covered contract or subcontract of $25 million, or more,

(b) received more than $25 million of CAS-covered contracts and subcontracts in its preceding cost accounting period, of which at least one award exceeded $1 million, or

(c) receives a CAS-covered contract or subcontract in excess of $500,000 *and* is one of the major recipients of Federal funds that is listed in Exhibit A of OMB Circular A–21.

Transition period Disclosure Statement filing requirements and temporary agency waiver authority are provided so agencies can phase-in the basic disclosure requirements in an orderly manner.

The CAS contract clause further provides for equitable price and cost adjustments in the event an institution is required to or elects to change its established or disclosed cost accounting practices (including cost accounting practice changes mandated by future amendments, if any, to Circular A–21); fails to consistently follow its established or disclosed cost accounting practices, or fails to comply with applicable Standards.

C. Paperwork Reduction Act

The information collection aspects of this rule have been approved by the Office of Management and Budget, and assigned Control Number 0348–0055.

D. Executive Order 12866 and the Regulatory Flexibility Act

This rule affects educational institutions receiving negotiated Federal contracts or subcontracts in excess of $500,000. The economic impact on educational institutions resulting from this rule is expected to be minor. Therefore, the Board has determined that this is not a "major rule" under Executive Order 12866, and that a regulatory impact analysis is not required. Furthermore, this regulation will not have a significant effect on a substantial number of small entities because small businesses are exempt from the application of the Cost Accounting Standards. Therefore, this final rule does not require a regulatory flexibility analysis under the Regulatory Flexibility Act of 1980.

E. Public Comments

This final rule is based upon the NPRM published in the **Federal Register** on December 21, 1992, 57 FR 60503, wherein public comments were invited. Seventy commenters responded. Their comments were considered. The Board's actions taken in response thereto are summarized in the paragraphs that follow:

OMB Circular A–21

Comment: Many educational institutions opposed the CASB proposal to independently promulgate regulations for application to colleges and universities. Instead, they recommended that the Board "adopt" the provisions contained in the OMB Circular A–21 which they stated is also being revised to resolve the same type of problems cited as the reason for applying the proposed CAS provisions to educational institutions. Such commenters stated:

The proposed Standards duplicate A–21 requirements.

Extra Standards are unnecessary, A–21 is adequate with planned changes, etc.

CAS will increase the potential for conflicts between the two regulations.

The Government has failed to demonstrate the need for two sets of regulations.

The Board should work with OMB to develop a mutually acceptable single A–21 rule.

Response: In the NPRM, the Board specifically responded to virtually identical concerns which were expressed by commenters in response to the ANPRM.

The Board strongly disagrees with the commenters' perceptions that the Board's proposal is duplicative of the accounting principles specified in Circular A–21 and therefore is unnecessary.

Circular A–21 does not require educational institutions to formally disclose the cost accounting practices they use to estimate, accumulate and report the costs of performing Federal awards. Information currently obtained by Federal officials concerning an institution's cost accounting practices is generally limited to data (1) indirectly reflected in an institution's individual cost proposals or reimbursement claims, (2) sampled, reviewed and reported on by auditors, and/or (3) provided in conjunction with the submission of the institution's indirect cost rate proposals to the extent specifically required by the Federal negotiator. Consequently, when such cost accounting information is obtained by Federal officials, it is acquired sporadically, in varying degrees of uniformity and thoroughness.

Circular A–21 does not contain the specific criteria and guidance provided in the four Standards under consideration. Proposed Standards 9905.501 and 9905.502 establish fundamental consistency requirements, define terms, detail techniques and provide illustrations for achieving compliance with the Standards' fundamental requirements. These two Standards constitute a significant expansion and clarification of the general consistency concepts specified in Circular A–21. Standard 9905.505 prescribes alternate methods that may be applied in meeting the fundamental requirement to identify and exclude costs that are not allowable under the terms of Federal awards. Standard 9905.506 requiring that a consistent cost accounting period be used, additionally specifies how an institution can comply with that requirement, including the use of specified transition periods in cases where a change in cost accounting periods is necessary or alternate methods where use of a twelve month period is not appropriate. Again, the specificity and detailed guidance contained in the four Standards is not contained in Circular A–21.

Accordingly, it is the Board's view that:

> The commenters general objections appear to deal more with the form of regulatory coverage rather than the substance of the coverage.
>
> Promulgation of the Board's proposal will provide for disclosure of an institution's cost accounting practices in a structured manner that is more efficient and effective than the current unspecified process.
>
> Disclosure and application of the proposed Standards will facilitate and improve the administration of Federal payments to recipients of Federal funds and provide greater assurances that the educational institutions follow their cost accounting practices in a consistent manner.
>
> The Board's statutory authority for promulgating cost accounting rules, regulations and Standards resides with the Board. Delegation of such authority to other Federal officials is not authorized under the statute.
>
> The Board's proposed provisions augment, but do not duplicate, the requirements of Circular A–21. Thus, adoption of Circular A–21 requirements in lieu of the Board's proposal would be inappropriate.

Comment: Several commenters stated that CAS should be implemented after expected OMB Circular A–21 "accounting" changes go into effect. This would avoid the necessity for filing Disclosure Statement (DS) revisions and cost impact statements.

Response: The referenced accounting principle changes were incorporated in Circular A–21 on July 15, 1993. The Circular's amended provisions are to be "* * * implemented with the establishment of indirect cost rates for all fiscal years beginning on or after January 1, 1994." It is the Board's understanding that these amendments need not be implemented during any fiscal years where predetermined indirect cost rates have already been established. Thus, the date the Circular's provisions "go into effect" will vary from institution to institution. The CASB's provisions are designed to be compatible with existing and future amended A–21 accounting principles. Whenever an OMB Circular A–21 mandated accounting principle change requiring an institution to change its cost accounting practice(s) is actually implemented, only the page(s) in the DS pertaining to the changed practice(s) need be amended and filed prior to actual implementation of the change. In such cases, the institution, pursuant to provision (a)(4)(iv) of the contract clause at 9903.201–4(e), must also resolve with their cognizant Federal agency officials whether an equitable adjustment is or is not required under existing CAS-covered contracts. Guidance for effecting equitable price adjustments is contained in 9903.305, Materiality, and 9903.306, Interpretations.

Accordingly, it is not feasible, desirable or necessary for the Board to establish a concurrent effective date as suggested for implementation of this final rule.

Administrative Costs to Implement CAS

Comment: Many of the commenters stated that the CASB rules impose an administrative cost burden.

Response: The commenters various concerns that application of the Board's proposed CAS coverage will impose an administrative cost burden generally evolved into two basic questions:

> 1. What presently constitutes an adequate cost accounting system under the terms and conditions of existing Federal awards?
>
> 2. What are the additional costs imposed by CAS?

Educational institutions are required to maintain adequate records for the accumulation and identification of allowable costs under the existing regulatory requirements incorporated in their existing Federal awards. It is not altogether clear if the cited administrative cost concerns are solely attributable to the Board's proposal or a possible indication of a lack of compliance with the existing contractual requirements concerning the maintenance of adequate estimating and cost accounting systems. Educational institutions must presently administer their Federal awards and resolve any cost accounting issues raised by Federal officials in accordance with existing administrative processes. The administrative costs that were or are currently being incurred by some of the major universities to resolve the recent Federal challenges to proposed and claimed costs were not mentioned.

When several universities were recently subjected to increased Federal audit scrutiny, millions of dollars of claimed costs were questioned and recovered by Federal agencies. The basis for such Federal challenges were attributed to (1) differing interpretations regarding the propriety of the institutions' cost allocation processes and (2) the institutions' failure to identify and exclude unallowable costs from their proposals and cost-reimbursement claims. The CASB's proposal requires formal disclosure of the major institutions' cost accounting practices; and, provides Standards for attaining consistency and for identification and exclusion of unallowable costs. The additional costs imposed by CAS are the incremental costs required to complete and maintain Disclosure Statements. The CAS consistency and unallowable cost provisions are Standards for meeting existing contractual requirements. Thus, the Board views the administrative costs associated with the latter as part of the normal costs of compliance with the basic contractual requirements that are imposed under existing regulations.

Further, the Board believes the proposal will reduce the potential for after-the-fact disagreements over the educational institutions' cost allocation processes, establish a more structured process for resolving cost accounting issues and will, in the long run, benefit both the Government and the educational institutions.

The expressed concerns did not result in modification of the Board's proposed regulatory requirements. However, the content of the proposed CASB Form DS-2 was significantly reduced to minimize Disclosure Statement preparation costs, as discussed in Paragraph F.

Civilian Agencies are Not Staffed to Administer CAS

Comments: Several commenters stated that they would be adversely impacted because agencies are not staffed to administer Disclosure Statements (DSs) and routine changes in their accounting systems. The Department of Health and Human Services confirmed that it too was concerned about its abilities to immediately implement the proposed CAS requirements for all CAS-covered entities.

Response: In consideration of the expressed concerns, the Board concluded that delayed implementation of the DS submission requirements would benefit the contracting parties. Under the NPRM, educational institutions meeting specified criteria were required to submit a DS prior to receipt of a CAS-covered contract. It is not the Board's intent to preclude the award of a contract where an institution has not yet become familiar with the Board's new disclosure requirements or been provided a reasonable opportunity to disclose its cost accounting practices. Further, the Board views an orderly phased-in implementation period as preferable to the proposed requirement which could clearly strain cognizant Federal agency resources if concurrent receipt of a significant number of DSs occurred. Accordingly, the Board has delayed implementation of the basic requirement and established transition period requirements for the filing of new DSs, applicable exclusively to educational institutions, at 9903.202-1(f).

Under the cited transition period provisions, educational institutions are authorized to file completed DSs *after* receipt of a CAS-covered contract that is placed on or before December 31, 1995. Six month filing periods ending six, twelve, and eighteen months after receipt of such contracts were established to phase-in the basic disclosure requirement in order to minimize the impact on educational institutions and Federal agencies. The twenty largest recipients of Federal funds were expected to submit completed DSs first and are, therefore, subject to the six month after award filing requirement. The next largest group of Federal funds recipients are subject to the twelve month requirement, etc.

Implementation of the basic requirement that a completed DS be provided or be on file with the cognizant Federal agency prior to award applies to CAS-covered contracts placed on or after January 1, 1996. However, where the cognizant Federal agency and the educational institution have established a DS due date falling between January 1, 1996 and June 30, 1997 pursuant to 9903.202-1(f)(3) and (4), individual awarding agencies are provided authorization to waive the preaward filing requirement for contracts placed during that period when necessary to avoid any potential due date conflicts.

For those educational institutions required to disclose their cost accounting practices, the transition provisions are intended to permit the larger recipients of Federal funds to complete and file DSs on or before June 30, 1996 and the smaller recipients to complete and file DSs no later than June 30, 1997. Earlier compliance with the basic disclosure requirement is encouraged.

The Board has also established additional provisions at 9903.201-7 and 9903.202-6 requiring Federal agencies to establish appropriate policies and procedures to administer CAS and to determine the adequacy of submitted DSs in a timely manner.

Predetermined Indirect Cost Rates (PDICRs)

Background: Predetermined fixed rates or negotiated fixed rates are used by some agencies to reimburse educational institutions for indirect costs associated with their cost-reimbursement type contracts and grants. Generally, such PDICRs are negotiated in advance, and are applied to direct base costs incurred and billed in subsequent periods. PDICRs are final rates, i.e., the indirect costs so determined and paid under Federal awards are not subsequently adjusted to reflect the actual allowable indirect costs incurred during the subsequent periods of performance. At some locations where a civilian agency is the cognizant Federal agency, an institution's PDICR proposal may be based on actual costs *extrapolated* from the institution's fund accounting records that were maintained for a completed fiscal year, i.e., a prior base year (e.g., year 1). The base year's costs may be adjusted to reflect estimated base and pool costs for future fiscal years (e.g., PDICRs negotiated in year 2 may cover years 3, 4, etc.). Under the current Federal Acquisition Regulation (FAR), FAR 42.705-3(b) only permits the use of "predetermined final indirect cost rates" for contract awards when specified conditions are met. Predetermined rates covering more than a one year period are prohibited under FAR 42.705-3(b)(6).

Comment: The Department of Health and Human Services asked the Board to "* * * explicitly state that the standards do not preclude the use of * * *" PDICRs.

Response: The use of PDICRs is subject to agency procurement regulations. Where permitted by statute and implementing agency regulations, negotiated PDICRs can continue to be used *provided* that, in the completed base year and in subsequent cost accounting periods, (1) all costs incurred for the same purpose, in like circumstances, are consistently treated as either direct costs only or as indirect costs only and (2) the allocation base costs (e.g., Modified Total Direct Costs) and allowable indirect cost pool amounts are grouped, accumulated and allocated in a consistent manner. The base costs and pool costs used to calculate predetermined or negotiated fixed rates should be estimated by using the same cost accounting practices that were used to measure, assign, and allocate actual base costs and indirect pool costs for a completed fiscal year. If different cost accounting practices are used to estimate and accumulate base or pool costs of a future period, the change in cost accounting practice must be disclosed under the terms of CAS-covered contracts. The cost accounting practices used to determine estimated (predetermined) and actual indirect costs are subject to the Board's CAS and Disclosure Statement requirements.

The use of predetermined or negotiated fixed rates, for administrative convenience or for other reasons, should not be viewed as a CAS noncompliance issue, provided the institution maintains cost accounting records which clearly demonstrate that direct and indirect costs are determined in a consistent manner, when the institution estimates, accumulates and reports costs applicable to Federal awards (See 9905.501).

Comment: One university representative requested the Board to "* * * comment on the significance of

* * *" PDICRs and compliance with CAS. The commenter believes that CAS compliance is achieved if the PDICR is "* * * multiplied by the applicable direct cost base. Any further inquiry into actual indirect costs would be inconsistent with the premise of predetermined rates * * *".

Response: The Board does not agree with the commenter's perceptions. Under existing Federal contractual audit and record keeping requirements, an institution must maintain a complete set of accounting records, supported by source documents, that adequately reflect all costs incurred and claimed under their Federal awards. Such records must also be made available for audit pursuant to applicable Federal audit requirements. Under the CAS being promulgated today, an educational institution is required to maintain cost accounting records which reflect the consistent application of the institution's established cost accounting practices, including those used to classify a cost either as a direct or indirect cost, when estimating, accumulating and reporting costs during *each cost accounting period*. Memorandum or work sheet records are acceptable.

Based on this comment, the Board is concerned that some institutions may not be maintaining annual cost accounting records that adequately identify how their total direct and indirect costs are treated during each cost accounting period. Without such annual records, the institution's internal controls and the "audit trail" (from source documents to final cost accumulation points) would be obscured. Consequently, the institution's ability to demonstrate the consist application of its established cost accounting practices when estimating, accumulating and reporting direct and indirect costs may be irreparably impaired.

Educational institutions are advised that failure to maintain adequate cost accounting records *for each cost accounting period* may be viewed as a violation of their existing contractual record keeping requirements and/or result in a determination that the institution has failed to comply with an applicable CAS or to consistently follow its established cost accounting practices.

Negotiated Fixed Rates and Carry-Forward Provisions (NFR–CFPs)

Background: OMB Circular A–21 provides that where NFR–CFPs are used, the over- or under-recovery in a particular year may be included as an adjustment to the indirect cost recognized as allowable and allocable in a subsequent year.

Comment: An accounting association expressed concerns that use of NFR-CFPs may result in significantly inaccurate measurements of cost for a particular cost accounting period.

Response: To some, this overall adjustment process may raise valid cost assignment and allocation issues. However, the carry forward provision is viewed by the Board as essentially an administrative expedient. It is the Board's understanding that the carry-forward provision is generally used where the number of Federal awards is significant but the volume of Federal activity is relatively stable and predictable. Rather than adjust the individual amounts billed for a large number of awards, necessary adjustments are effected in an overall manner by offsetting different amounts otherwise considered allowable. Such offsets made in a subsequent period for adjustments attributable to a prior period represent, in essence, the implementation of an administrative policy on how to best effect adjustments for any over- or under-payments after the actual allowable costs are determined for a prior period.

Where agency procurement regulations permit the use of NFR-CFPs, the resulting cost adjustment process should not be viewed as a CAS noncompliance issue *per se*. Necessary adjustments may be applied under CAS-covered contracts if the cost accounting practices used to initially determine forecasted or actual indirect costs and rates (exclusive of any carry forward adjustments) for each year comply with the Board's rules, regulations, and Standards. In such cases, however, a distinctive two step procedure must be followed. First, the forecasted or actual indirect expense pool(s) used to initially determine the forecasted rates and the actual prior year rates must be determined exclusive of any carry forward adjustments. The cost accounting practices used to do so must meet applicable CAS requirements. Then, after the rates are so determined, the institution and cognizant Federal negotiator may, if permitted by agency regulations, effect appropriate adjustments to a forecasted year rate to compensate for any over- or under-estimated indirect cost payments made in a prior year.

Part 9903 CAS Applicability Provisions

Comment: A commenter asked if a negotiated contract would be considered CAS-covered, where a contract initially awarded for $325,000 to cover a three year performance period were increased to $625,000 and the performance period were extended to five years.

Response: The CAS applicability threshold is determined at the time the basic contract is awarded based on the total negotiated price for the entire scope of work contemplated, including all options. If only a three year contract was contemplated, the described contract action totaling $325,000 would not incorporate a CAS contract clause. However, if the Government had initially contemplated a five year contract performance period but available funds were obligated to only cover the first three years, CAS applicability would be determined based upon the negotiated contract price for the full five year period. That is, where a negotiated contract is incrementally funded, the individual amounts of funding provided in the basic award and subsequent funding modifications are not to be used individually in determining CAS applicability. Rather, the entire estimated contract cost, plus fee, if any (for the entire period of performance), is used to determine CAS applicability.

Comment: A commenter asked if an existing negotiated contract in excess of $500,000 that is not currently CAS-covered would become CAS-covered after promulgation of this final rule if a contract modification increases the contract price by $100,000.

Response: No. The existing non-CAS-covered contract would not become CAS-covered even if the modification was in excess of $500,000.

Comment: A commenter asked if a $200,000 subcontract awarded under a CAS-covered prime contract would be CAS-covered?

Response: No. Only negotiated subcontracts in excess of $500,000 will be required to be CAS-covered.

Comment: Several commenters expressed opposition to the proposed CAS applicability provision that requires full coverage when an institution receives a single CAS-covered award in excess of $500,000 and the institution is listed in Exhibit A of OMB Circular A–21.

Response: Exhibit A of the Circular lists the 99 educational institutions that receive the preponderant amount of Federal research funds under their contracts and grants. The listed institutions receive Federal funds ranging from more than $25 million annually to amounts in excess of $250 million annually. Unlike commercial organizations, however, many of these educational institutions do not receive large individual dollar value contracts that could be used as an effective applicability threshold, e.g., to trigger a

Disclosure Statement requirement. Rather, they receive a large number of small dollar value contract and grant awards. The Board believes it would be beneficial to the contracting parties if the larger recipients of Federal research funds formally disclosed their cost accounting practices. Accordingly, use of only a $25 million contract threshold to initiate the disclosure requirement being promulgated today was not considered sufficient to meet the Board's objective.

Comment: There is an inconsistency in the proposed threshold coverage: Coverage is set at "$500,000 or more" and at "in excess of $500,000."

Response: The NPRM proposed language has been revised to consistently cite "in excess of $500,000."

Comment: If educational institutions are to be covered by CAS, whereas only their FFRDCs were covered previously, all future CAS-covered contracts awarded to educational institutions should be subject to the same coverage. The proposal to retain modified and full coverage for such FFRDCs should be eliminated.

Response: FFRDCs are generally treated as an independent segment of an educational institution and have been subject to full or modified CAS coverage prescribed by the CASB and incorporated in Part 9903 and Part 9904 by the Board. That prescribed coverage for FFRDCs is not modified or revised by this final rule.

Part 9905 Cost Accounting Standards

Standard 9905.501

Comment: If an institution installs a new accounting system with a new chart of accounts during the performance of a contract and it cannot report actual costs consistent with the way the costs were estimated, does this constitute a violation of the Fundamental Requirement at 9905.501-40(b)?

Response: Yes. Changes made in an institution's general accounting systems used for financial management and reporting purposes that result in a change in the institution's cost accounting practices or noncompliance with a Standard are subject to paragraphs (a)(4) and (a)(5), respectively, of the contract clause at 9903.201-4(e).

Comment: A commenter suggested that the Board clarify that the providing of estimated cost data in greater detail than the institution's accounting system can handle should not constitute a violation of Standard 9905.501.

Response: The Board's proposal was predicated on Standard 9904.401. However, the Interpretation at 9904.401-61 that addressed to what degree the costs for estimated scrap and shrinkage costs in a manufacturing production oriented environment should be accounted for in a contractor's cost accounting records was not included in 9905.501. Scrap and shrinkage costs were not considered a material cost item under research contracts performed by educational institution. The Board believes that the record keeping concepts expressed in the referenced Interpretation apply equally to this commenter's concern and that such guidance would facilitate implementation of 9905.501. Accordingly, the portions of the referenced Interpretation concerning the amount of detail required in accumulating and reporting costs have been incorporated at 9905.501-50(c).

Standard 9905.502

Comment: One commenter expressed difficulty in understanding the concepts of Standard 9905.502 where the university engages in cost sharing, where projects have multiple sponsors particularly in light of the university's desire to accommodate the different requirements imposed by Federal and private supporters and the different fund accounting methods it uses to account for restricted and unrestricted funds.

Response: The statements provided by this commenter infer that, in a university "fund" accounting system, direct and indirect costs for a particular project cannot always be allocated to final cost objectives on a consistent basis. Thus, the proposed Standard requires revision. If that was the commenters intent, the Board does not agree.

One of the Board's primary objectives is to prescribe rules and regulations that will result in the consistent and equitable allocation of direct and indirect costs to CAS-covered contracts. The purpose of Standard 9905.502 is to require consistency in the institution's cost accounting practices followed for determining the direct and indirect costs to be allocated to all final cost objectives. The Standard requires that the institution's cost accounting practices consistently treat costs incurred for the same purpose, in like circumstances, as either a direct cost or an indirect cost, without regard to the source or type of funds (restricted or unrestricted) involved. While multi-sponsored projects and cost-sharing arrangements are not specifically addressed, this Standard requires that direct and indirect costs be allocated to all final cost objectives established for each project on a consistent basis in the institution's cost accounting system. A project's costs may be accumulated under one final cost objective and be identified with individual sponsors on a pro rata basis, and/or project costs may be accumulated and recorded in sub-accounts or individual cost accumulation points (final cost objectives) associated with each sponsor. This Standard does not prescribe criteria for determining what constitutes a project or the number of final cost objectives required to accumulate costs for a project.

Comment: Where a large major research contract involves the management of major subcontracts, complex procurements and equipment fabrications, award and administration costs of such activities may be directly attributable to the research project and are charged directly. Conversely, procurements under smaller projects that are relatively simple to administer, may be administered by the department's general business manager, who is included in Departmental Administration indirect cost pool. The Board should recognize that this is not a violation of the Standard.

Response: Where an institution can demonstrate different circumstances, Standard 9905.502 permits the use of different allocation methods. However, the described circumstances appear identical to the illustration of costs that are incurred for the same purpose, at 9905.502-60(a)(1), where the institution elects to charge travel costs, normally treated as an indirect cost, directly to a contract. That illustration provides that similar travel costs incurred under other contracts may no longer remain in the indirect expense pool. The described subcontract administration costs appear to be incurred for the same purpose, regardless of the subcontracts' size, nature or complexity. Double counting may occur if the costs of administering other subcontracts under the smaller projects are not removed from the Departmental Administration indirect cost pool and charged directly. Determinations on whether different circumstances are or are not involved must be made on a case-by-case basis.

Comment: In 9905.502-30(a)(4), it should be made clear that the term "final cost objective" is not intended to mean each individual contract.

Response: The term "final cost objective" as defined in the Standards, applies to individual cost objectives, e.g., individually sponsored projects (contracts, grants, etc.), co-sponsored projects, in-house projects, and similar cost objectives. Normally, costs accumulated in a final cost objective are not allocated to other cost objectives.

Comment: A Federal agency recommended that, in 9905.502–60(a)(2), the proposed term "planning costs" be replaced with a more representative term such as "purchasing activity" which is a more significant cost item at universities.

Response: The illustration was appropriately revised.

Comment: A commenter suggested that certain prescribed OMB policies and procedures be illustrated as an acceptable practice in the Standard.

Response: The suggestion would result in the duplication and unnecessary proliferation of existing regulations. The commenter did not indicate if there was a potential conflict between CAS and OMB Circular A–21, accordingly the proposed Standard was not modified.

Standard 9905.505

Comment: A commenter from a major university stated that paragraph 9905.505–40(f) describes how to handle a cost overrun on a contract. However, it does not consider the way in which cost overruns must be handled in a fund accounting system. This paragraph should either be deleted or modified to recognize the requirement of a fund accounting contractor.

Response: The Board's Standards pertain to the complete set of cost accounting practices used by an institution to estimate, accumulate and report costs under negotiated Federal awards. Conceptually, the same cost accounting practices are applied to all activities of a segment performing CAS-covered contracts in order to ensure all costs are allocated on a consistent basis to all final cost objectives. The particular provision in question requires that an institution be able to identify the total costs incurred with respect to a particular contract or similar cost objective, regardless of available funding considerations. In cases of a contract cost overrun, the Standard does not prescribe how the cost overrun is to be treated in the educational institution's "fund" accounting system.

The commenter's statements remain a concern to the Board, as this issue was discussed in the preamble comments to the NPRM. The explanatory statements currently provided infer that cost overruns cannot be accumulated and reported in a university environment. Because all costs must be funded in order to be recorded in a fund accounting system, the commenter advised that the direct costs of an overrun contract must be transferred to other projects or to other indirect cost centers (e.g., from Research to Instruction). Within the set of cost accounting practices used for determining the costs of Federal awards, such transfers could result in the allocation of different indirect cost amounts to the same base costs and alter the amount of indirect costs allocated to other final cost objectives. If so, the described practices would not be in compliance with the consistency requirements being promulgated today. The commenting university is encouraged to review, and possibly modify, its cost accounting practices being followed under Federal awards to ensure that they will be in compliance with the Board's consistency requirements.

Comment: One commenter asked: After identifying an indirect cost that has been questioned by the auditor and sustained by the contracting officer, must the university also deduct it from subsequent proposals pending appeal?

Response: No. The type of costs under appeal must be identified in, but need not be excluded from, proposals and reimbursement claims. If, after the appeal is adjudicated, the Contracting Officer's final decision is not overturned and the costs remain unallowable, the Standard's identification and exclusion provisions would apply.

Comment: A commenter suggested that, in 9905.505–60(d), the phrase "interim bidding and billing rates" be replaced by a more commonly used term.

Response: The phrase was replaced by the generic term "indirect cost rates."

Standard 9905.506

Comment: Under paragraph 9905.506–50(a)(2), a commenter suggested adding the words "or cost group" after the words "indirect cost pool." By way of explanation, the commenter advised the only way one could handle a situation of an indirect cost function which exists for only part of a year is to set up a separate cost group *within* one of the A–21 specified indirect cost pools.

Response: This suggestion was partially adopted. The term "expense pool" was added instead of the suggested term.

The commenter's suggestion and rationale could be erroneously interpreted by some to mean that a separate pool and allocation base applicable to the partial period need not be established. This Standard requires the use of a full cost accounting period, e.g., normally the institution's fiscal year. An exception provision permits the use of a shorter period for the allocation of indirect costs that only exist during a portion of the cost accounting period. In such cases, 9905.506–50(a) requires the establishment of a separate allocation base, during the partial period, that is representative of the short term function. That provision also requires that the indirect costs associated with the unique short term function be accumulated in a separate indirect cost pool. The resultant allocation to final cost objectives of the short term period would generally be independent of the normal A–21 allocation process that is predicated on allocation bases and indirect cost pools applicable to all work performed during a full cost accounting period. The Board believes incorporation of the term "expense pool" will clarify that unique indirect costs that only exist during a portion of the cost accounting period may be accumulated in a separate pool and allocated to final cost objectives of that shorter period.

Comment: A commenter stated that, in the illustration at 9905.506–60(a), the proposed phrase "estimated amount of the Organized Research expense pool" was unclear and suggested use of the phrase "estimated amount of indirect costs allocated to Organized Research."

Response: The suggested change was adopted.

Disclosure Statement (DS)

Comment: One commenter recommended that the Board clarify that the different and special handling of direct vs. indirect costs of an FFRDC contract from all other CAS-covered contracts does not constitute a violation of Standard 9905.502.

Response: When the cost accounting practices of the FFRDC activity and other institutional activities differ, the FFRDC should be treated as a separate "segment" and file its own DS. Where costs of the institution are allocated to both FFRDC and non-FFRDC activities, the segments' DSs should appropriately detail how institution-wide costs are allocated to the segments. Each segment must then disclose its particular cost accounting practices.

Likewise, if two departments at a campus location follow different cost accounting practices, the institution must decide if the two departments should be treated as separate segments and file separate DSs for each or if the cost accounting practices of the two departments should be conformed.

Comment: A Federal agency and other commenters advised that the level of detailed cost accounting records maintained by educational institutions to accumulate costs may vary depending upon the indirect cost category or functional activity involved.

Response: In determining the costs of performing Federal awards, an institution's cost accounting records must be able to first identify and accumulate the total costs of each indirect cost category to be allocated to all major functions and activities of the institution. The accounting records maintained for this purpose must be sufficiently detailed to enable the contracting parties to reasonably establish base costs and indirect pool costs, applicable to all functions and activities, in a consistent manner. However, decisions on the level of detailed accounting records to be maintained should be influenced by the materiality of the costs being allocated to Federal awards. Reasonable approximations of costs may be used when the costs are immaterial or the resultant allocations to intermediate and final cost objectives will not differ materially from the amounts that would be obtained if more precise and detailed records were maintained. The level of accounting detail considered necessary in the circumstances must, therefore, be determined on a case-by-case basis and remains a matter subject to review and approval by the cognizant Federal agency.

In light of the commenter's statements, Item 3.1.0. of the Disclosure Statement was expanded to require disclosure of how the costs of the individual indirect cost categories are identified and accumulated. Where the costs associated with a particular indirect cost category are not formally accumulated and recorded in the institution's formal accounting system, the cost accounting practices followed to identify such costs for allocation to the major functions and activities of the institution must be fully described on a continuation sheet.

F. Additional Revisions—Disclosure Statement (DS) Form CASB DS–2

By memorandum dated February 1, 1994, the Deputy Administrator, Office of Information and Regulatory Affairs (OIRA), advised the Board that some representatives from OMB and the Department of Health and Human Services (HHS) had recently informed OIRA that the Board's proposed DS Form CASB DS–2 could be improved. The Board advised OIRA that in order to meet its primary objective, the promulgation of a useful DS Form, it would consider any additional OMB suggestions or Federal agency elaborations regarding their previously submitted responses to the Board's NPRM. Representatives from OMB's Office of Federal Financial Management, HHS and the Department of Defense proceeded to develop a list of suggested changes which, in their view, would further clarify the proposed disclosure requirements or curtail the amount of disclosure needed for certain cost elements that were not considered to be significant or problematic. The list was informally coordinated with the CASB's staff. A revised CASB Form DS–2 was then prepared by the CASB staff and submitted to the Board. Most of the suggested changes were adopted by the Board and are reflected in the CASB Form DS–2 being promulgated today.

Essentially, a number of DS items contained in the NPRM were deleted and/or restated to facilitate disclosure. Consequently, the Board believes the DS being promulgated today is more useful and cost effective than that proposed in the NPRM. To that end, the Board expresses its appreciation for the assistance provided by OMB and agency representatives.

On July 21, 1994, OMB promulgated a Notice in the **Federal Register** (59 FR 37276) for paperwork clearance purposes and copies of the revised Form CASB DS–2 were made available to interested parties. Based on the public comments received, the promulgated Form CASB DS–2 was further revised as follows:

Item 2.4.0 was revised to clarify that the term "direct personal service costs" may include applicable fringe benefits costs consistent with OMB Circular A–21 provisions.

Item 3.1.0 was revised to include the word "other" to clarify that costs from one indirect cost category may be allocated to "other" indirect cost categories.

In Part VI, the instructions were expanded to provide the reporting unit with the option of completing the form for any costs incurred by another organizational entity where it has access to the necessary data or of requesting that entity to complete the pertinent items.

The Federal Acquisition Streamlining Act of 1994, in Section 2191 titled "Travel Expenses of Government Contractors" repealed Section 24 of the Office of Federal Procurement Policy Act (41 U.S.C. 420). Since proposed item 2.7.1. was predicated on the repealed statutory provisions, it was deleted.

In the General Instructions to the Disclosure Statement, Instruction Number 8, was modified to permit incorporation of written cost accounting polices and procedures by specific reference or alternatively by incorporation as appendices. As promulgated today, Instruction 8 is intended to facilitate full disclosure and minimize Disclosure Statement preparation costs whenever an established cost accounting practice is adequately described in an institution's formal accounting system.

List of Subjects in 48 CFR Parts 9903, 9905

Cost accounting standards, Government procurement.

Richard C. Loeb,
Executive Secretary, Cost Accounting Standards Board.

For the reasons set forth in this preamble, chapter 99 of title 48 of the Code of Federal Regulations is amended as set forth below:

1. The authority citation for Part 9903 continues to read as follows:

Authority: Public Law 100–679, 102 Stat. 4056, 41 U.S.C. 422.

PART 9903—CONTRACT COVERAGE

Subpart 9903.1—General

2. Section 9903.102 is amended by revising the last sentence of this paragraph to read as follows:

9903.102 OMB Approval Under the Paperwork Reduction Act.

* * * OMB has assigned Control Numbers 0348–0051 and 0348–0055 to the paperwork, recordkeeping and forms associated with this regulation.

Subpart 9903.2—CAS Program Requirements

3. Section 9903.201–1 is amended by revising paragraph (a) and removing and reserving paragraph (b)(10) to read as follows:

9903.201–1 CAS applicability.

(a) This subsection describes the rules for determining whether a proposed contract or subcontract is exempt from CAS. (See 9904 or 9905, as applicable.) Negotiated contracts not exempt in accordance with 9903.201–1(b) shall be subject to CAS. A CAS-covered contract may be subject to full, modified or other types of CAS coverage. The rules for determining the applicable type of CAS coverage are in 9903.201–2.

(b) * * *

(7)–(10) [Reserved]

* * * * *

4. Section 9903.201–2 is amended by revising the first sentence in paragraph (a) and adding a new paragraph (c) to read as follows:

9903.201–2 Types of CAS coverage.

(a) *Full coverage.* Full coverage requires that the business unit comply with all of the CAS specified in Part 9904 that are in effect on the date of the contract award and with any CAS that become applicable because of later award of a CAS-covered contract. * * *

* * * * *

(c) *Coverage for educational institutions*—(1) Regulatory requirements. Parts 9903 and 9905 apply to educational institutions except as otherwise provided in this paragraph (c) and at 9903.202–1(f).

(2) *Definitions.* (i) The following term is prominent in Parts 9903 and 9905. Other terms defined elsewhere in this Chapter 99 shall have the meanings ascribed to them in those definitions unless paragraph (c)(2)(ii) of this subsection below requires otherwise.

Educational institution means a public or nonprofit institution of higher education, e.g., an accredited college or university, as defined in section 1201(a) of Public Law 89–329, November 8, 1965, Higher Education Act of 1965; (20 U.S.C. 1141(a)).

(ii) The following modifications of terms defined elsewhere in this Chapter 99 are applicable to educational institutions:

Business unit means any segment of an educational institution, or an entire educational institution which is not divided into segments.

Segment means one of two or more divisions, campus locations, or other subdivisions of an educational institution that operate as independent organizational entities under the auspices of the parent educational institution and report directly to an intermediary group office or the governing central system office of the parent educational institution. Two schools of instruction operating under one division, campus location or other subdivision would not be separate segments unless they follow different cost accounting practices, for example, the School of Engineering should not be treated as a separate segment from the School of Humanities if they both are part of the same division's cost accounting system and are subject to the same cost accounting practices. The term includes Government-owned contractor-operated (GOCO) facilities, Federally Funded Research and Developments Centers (FFRDCs), and joint ventures and subsidiaries (domestic and foreign) in which the institution has a majority ownership. The term also includes those joint ventures and subsidiaries (domestic and foreign) in which the institution has less than a majority of ownership, but over which it exercises control.

(3) *Applicable Standards.* Coverage for educational institutions requires that the business unit comply with all of the CAS specified in Part 9905 that are in effect on the date of the contract award and with any CAS that become applicable because of later award of a CAS-covered contract. This coverage applies to business units that receive negotiated contracts in excess of $500,000, except for CAS-covered contracts awarded to FFRDCs operated by an educational institution.

(4) *FFRDCs.* Negotiated contracts awarded to an FFRDC operated by an educational institution are subject to the full or modified CAS coverage prescribed in paragraphs (a) and (b) of this subsection. CAS-covered FFRDC contracts shall be excluded from the institution's universe of contracts when determining CAS applicability and disclosure requirements for contracts other than those to be performed by the FFRDC.

(5) *Contract Clauses.* The contract clause at 9903.201–4(e) shall be incorporated in each negotiated contract and subcontract awarded to an educational institution when the negotiated contract or subcontract price exceeds $500,000. For CAS-covered contracts awarded to a FFRDC operated by an educational institution, however, the full or modified CAS contract clause specified at 9903.201–4 (a) or (c), as applicable, shall be incorporated.

(6) *Continuity in Fully CAS-Covered Contracts.* Where existing contracts awarded to an educational institution incorporate full CAS coverage, the contracting officer may continue to apply full CAS coverage, as prescribed at 9903.201–2(a), in future awards made to that educational institution.

* * * * *

5. Section 9903.201–3 is amended by redesignating the introductory heading as the heading of paragraph (a); redesignating the existing introductory text and paragraphs (a) through (d) as paragraph (a)(1) introductory text and paragraphs (a)(1) (i) through (iv) respectively; adding a new paragraph (a)(2); revising the heading of the solicitation notice; adding a new paragraph at the end of the introductory "Note;" amending Part I of the basic provision by revising paragraph (a), the first and second sentences in paragraph (b) and paragraphs (c)(1) and (c)(2); and adding a new Alternate I at the end of the basic provision to read as follows:

9903.201–3 Solicitation provisions.

(a) Cost Accounting Standards Notices and Certifications.

(1) * * *

(2) If an award to an educational institution is contemplated prior to July 1, 1997, the contracting officer shall use the basic provision set forth below with its Alternate I, unless the contract is to be performed by an FFRDC (see 9903.201(c)(5)), or the provision at 9903.201(c)(6) applies.

Cost Accounting Standards Notices and Certification (Oct 1994)

Note: * * *

If the offeror is an educational institution, Part II does not apply unless the contemplated contract will be subject to full or modified CAS-coverage pursuant to 9903.201–2(c)(5) or 9903.201–2(c)(6).

I. Disclosure Statement—Cost Accounting Practices and Certification

(a) Any contract in excess of $500,000 resulting from this solicitation, except contracts in which the price negotiated is based on (1) established catalog or market prices of commercial items sold in substantial quantities to the general public, or (2) prices set by law or regulation, will be subject to the requirements of the Cost Accounting Standards Board (48 CFR, Chapter 99), except for those contracts which are exempt as specified in 9903.201–1.

(b) Any offeror submitting a proposal which, if accepted, will result in a contract subject to the requirements of 48 CFR, Chapter 99 must, as a condition of contracting, submit a Disclosure Statement as required by 9903.202. When required, the Disclosure Statement must be submitted as a part of the offeror's proposal under this solicitation unless the offeror has already submitted a Disclosure Statement disclosing the practices used in connection with the pricing of this proposal. * * *

(c) Check the appropriate box below:

☐ (1) Certificate of Concurrent Submission of Disclosure Statement.

The offeror hereby certifies that, as a part of the offer, copies of the Disclosure Statement have been submitted as follows: (i) Original and one copy to the cognizant Administrative Contracting Officer (ACO) or cognizant Federal agency official authorized to act in that capacity, as applicable, and (ii) one copy to the cognizant Federal auditor.

(Disclosure must be on Form No. CASB DS–1 or CASB DS–2, as applicable. Forms may be obtained from the cognizant ACO or cognizant Federal agency official acting in that capacity and/or from the looseleaf version of the Federal Acquisition Regulation.)

Date of Disclosure Statement: __________

Name and Address of Cognizant ACO or Federal Official where filed: __________

The offeror further certifies that the practices used in estimating costs in pricing this proposal are consistent with the cost accounting practices disclosed in the Disclosure Statement.

☐ (2) Certificate of Previously Submitted Disclosure Statement. The offeror hereby certifies that the required Disclosure Statement was filed as follows:

Date of Disclosure Statement: __________

Name and Address of Cognizant ACO or Federal Official where filed: __________

The offeror further certifies that the practices used in estimating costs in pricing this proposal are consistent with the cost accounting practices disclosed in the applicable Disclosure Statement.

* * * * *

(End of basic provision)

Alternate I (OCT 1994) Insert the following subparagraph (5) at the end of Part I of the basic clause:

☐ (5) Certificate of Disclosure Statement Due Date by Educational Institution. If the offeror is an educational institution that, under the transition provisions of 9903.202-1(f), is or will be required to submit a Disclosure Statement after receipt of this award, the offeror hereby certifies that (check one and complete):

☐ (a) A Disclosure Statement filing Due Date of ___________ has been established with the cognizant Federal agency.

☐ (b) The Disclosure Statement will be submitted within the six month period ending ___________ months after receipt of this award.

Name and Address of Cognizant ACO or Federal Official where Disclosure Statement is to be filed: ___________________________

____

(End of Alternate I)

6. Section 9903.201-4 is amended by revising the text of paragraphs (a)(1) and (a)(2) preceding the clause and by adding a new paragraph (e) including a new clause to read as follows:

9903.201-4 Contract clauses.

(a) *Cost Accounting Standards.* (1) The contracting officer shall insert the clause set forth below, Cost Accounting Standards, in negotiated contracts, unless the contract is exempted (see 9903.201-1), the contract is subject to modified coverage (see 9903.201-2), or the clause prescribed in paragraphs (d) or (e) of this section is used.

(2) The clause below requires the contractor to comply with all CAS specified in Part 9904, to disclose actual cost accounting practices (applicable to CAS-covered contracts only), and to follow disclosed and established cost accounting practices consistently.

* * * * *

(e) *Cost Accounting Standards—Educational Institutions.* (1) The contracting officer shall insert the clause set forth below, Cost Accounting Standards—Educational Institution, in negotiated contracts awarded to educational institutions, unless the contract is exempted (see 9903.201-1), the contract is to be performed by an FFRDC (see 9903.201-2(c)(5)), or the provision at 9903.201-2(c)(6) applies.

(2) The clause below requires the educational institution to comply with all CAS specified in Part 9905, to disclose actual cost accounting practices as required by 9903.202-1(f), and to follow disclosed and established cost accounting practices consistently.

Cost Accounting Standards—Educational Institution (Oct 1994)

(a) Unless the contract is exempt under 9903.201-1 and 9903.201-2, the provisions of 9903 are incorporated herein by reference and the Contractor in connection with this contract, shall—

(1) (CAS-covered Contracts Only) If a business unit of an educational institution required to submit a Disclosure Statement, disclose in writing the Contractor's cost accounting practices as required by 9903.202-1 through 9903.202-5 including methods of distinguishing direct costs from indirect costs and the basis used for accumulating and allocating indirect costs. The practices disclosed for this contract shall be the same as the practices currently disclosed and applied on all other contracts and subcontracts being performed by the Contractor and which contain a Cost Accounting Standards (CAS) clause. If the Contractor has notified the Contracting Officer that the Disclosure Statement contains trade secrets, and commercial or financial information which is privileged and confidential, the Disclosure Statement shall be protected and shall not be released outside of the Government.

(2) Follow consistently the Contractor's cost accounting practices in accumulating and reporting contract performance cost data concerning this contract. If any change in cost accounting practices is made for the purposes of any contract or subcontract subject to CAS requirements, the change must be applied prospectively to this contract and the Disclosure Statement, if required, must be amended accordingly. If an accounting principle change mandated under Office of Management and Budget (OMB) Circular A-21, Cost Principles for Educational Institutions, requires that a change in the Contractor's cost accounting practices be made after the date of this contract award, the change must be applied prospectively to this contract and the Disclosure Statement, if required, must be amended accordingly. If the contract price or cost allowance of this contract is affected by such changes, adjustment shall be made in accordance with subparagraph (a)(4) or (a)(5) of this clause, as appropriate.

(3) Comply with all CAS, including any modifications and interpretations indicated thereto contained in 48 CFR 9905, in effect on the date of award of this contract or, if the Contractor has submitted cost or pricing data, on the date of final agreement on price as shown on the Contractor's signed certificate of current cost or pricing data. The Contractor shall also comply with any CAS (or modifications to CAS) which hereafter become applicable to a contract or subcontract of the Contractor. Such compliance shall be required prospectively from the date of applicability to such contract or subcontract.

(4)(i) Agree to an equitable adjustment as provided in the Changes clause of this contract if the contract cost is affected by a change which, pursuant to subparagraph (a)(3) of this clause, the Contractor is required to make to the Contractor's established cost accounting practices.

(ii) Negotiate with the Contracting Officer to determine the terms and conditions under which a change may be made to a cost accounting practice, other than a change made under other provisions of subparagraph (a)(4) of this clause; provided that no agreement may be made under this provision that will increase costs paid by the United States.

(iii) When the parties agree to a change to a cost accounting practice, other than a change under subdivision (a)(4)(i) or (a)(4)(iv) of this clause, negotiate an equitable adjustment as provided in the Changes clause of this contract.

(iv) Agree to an equitable adjustment as provided in the Changes clause of this contract, if the contract cost is materially affected by an OMB Circular A-21 accounting principle amendment which, on becoming effective after the date of contract award, requires the Contractor to make a change to the Contractor's established cost accounting practices.

(5) Agree to an adjustment of the contract price or cost allowance, as appropriate, if the Contractor or a subcontractor fails to comply with an applicable Cost Accounting Standard, or to follow any cost accounting practice consistently and such failure results in any increased costs paid by the United States. Such adjustment shall provide for recovery of the increased costs to the United States, together with interest thereon computed at the annual rate established under section 6621 of the Internal Revenue Code of 1986 (26 U.S.C. 6621) for such period, from the time the payment by the United States was made to the time the adjustment is effected. In no case shall the Government recover costs greater than the increased cost to the Government, in the aggregate, on the relevant contracts subject to the price adjustment, unless the Contractor made a change in its cost accounting practices of which it was aware or should have been aware at the time of price negotiations and which it failed to disclose to the Government.

(b) If the parties fail to agree whether the Contractor or a subcontractor has complied with an applicable CAS or a CAS rule or regulation in 9903 and as to any cost adjustment demanded by the United States, such failure to agree will constitute a dispute under the Contract Disputes Act (41 U.S.C. 601).

(c) The Contractor shall permit any authorized representatives of the Government to examine and make copies of any documents, papers, or records relating to compliance with the requirements of this clause.

(d) The Contractor shall include in all negotiated subcontracts which the Contractor enters into, the substance of this clause, except paragraph (b), and shall require such inclusion in all other subcontracts, of any tier, including the obligation to comply with all applicable CAS in effect on the subcontractor's award date or if the subcontractor has submitted cost or pricing data, on the date of final agreement on price as shown on the subcontractor's signed Certificate of Current Cost or Pricing Data, except that—

(1) If the subcontract is awarded to a business unit which pursuant to 9903.201-2

is subject to other types of CAS coverage, the substance of the applicable clause set forth in 9903.201–4 shall be inserted; and

(2) This requirement shall apply only to negotiated subcontracts in excess of $500,000 where the price negotiated is not based on—

(i) Established catalog or market prices of commercial items sold in substantial quantities to the general public; or

(ii) Prices set by law or regulation, and except that the requirement shall not apply to negotiated subcontracts otherwise exempt from the requirement to include a CAS clause as specified in 9903.201–1.

(End of clause)

7. Section 9903.201–6 is amended by revising paragraph (a) to read as follows:

9903.201–6 Findings.

(a) Prior to making any equitable adjustment under the provisions of paragraph (a)(4)(iii) of the contract clause set forth in 9903.201–4(a) or 9903.201–4(e), the Contracting Officer shall make a finding that the change is desirable and is not detrimental to the interests of the Government.

* * * * *

8. A new section 9903.201–7 is added to read as follows:

9903.201–7 Cognizant Federal Agency Responsibilities.

(a) The requirements of Part 9903 shall, to the maximum extent practicable, be administered by the cognizant Federal agency responsible for a particular contractor organization or location, usually the Federal agency responsible for negotiating indirect cost rates on behalf of the Government. The cognizant Federal agency should take the lead role in administering the requirements of Part 9903 and coordinating CAS administrative actions with all affected Federal agencies. When multiple CAS-covered contracts or more than one Federal agency are involved, agencies should discourage Contracting Officers from individually administering CAS on a contract-by-contract basis. Coordinated administrative actions will provide greater assurances that individual contractors follow their cost accounting practices consistently under all their CAS-covered contracts and that changes in cost accounting practices or CAS noncompliance issues are resolved, equitably, in a uniform overall manner.

(b) Federal agencies shall prescribe regulations and establish internal policies and procedures governing how agencies will administer the requirements of CAS-covered contracts, with particular emphasis on inter-agency coordination activities. Procedures to be followed when an agency is and is not the cognizant Federal agency should be clearly delineated. Internal agency policies and procedures shall provide for the designation of the agency office(s) or officials responsible for administering CAS under the agency's CAS-covered contracts at each contractor business unit and the delegation of necessary contracting authority to agency individuals authorized to administer the terms and conditions of CAS-covered contracts, e.g., Administrative Contracting Officers (ACOs) or other agency officials authorized to perform in that capacity. Agencies are urged to coordinate on the development of such regulations.

9. Section 9903.202–1 is amended by adding a new paragraph (f) to read as follows:

9903.202–1 General Requirements.

* * * * *

(f) *Educational institutions—disclosure requirements.* (1) Educational institutions receiving contracts subject to the CAS specified in Part 9905 are subject to the requirements of 9903.202, except that completed Disclosure Statements are required in the following circumstances.

(2) *Basic requirement.* For CAS-covered contracts placed on or after January 1, 1996, completed Disclosure Statements are required as follows:

(i) Any business unit of an educational institution that is selected to receive a CAS-covered contract or subcontract in excess of $500,000 and is part of a college or university location listed in Exhibit A of Office of Management and Budget (OMB) Circular A–21 shall submit a Disclosure Statement before award. A Disclosure Statement is not required, however, if the listed entity can demonstrate that the net amount of Federal contract and financial assistance awards received during its immediately preceding cost accounting period was less than $25 million.

(ii) Any business unit that is selected to receive a CAS-covered contract or subcontract of $25 million or more shall submit a Disclosure Statement before award.

(iii) Any educational institution which, together with its segments, received net awards of negotiated prime contracts and subcontracts subject to CAS totaling $25 million or more in its most recent cost accounting period, of which, at least one award exceeded $1 million, must submit a Disclosure Statement before award of its first CAS-covered contract in the immediately following cost accounting period. However, if the first CAS-covered contract is received within 90 days of the start of the cost accounting period, the institution is not required to file until the end of 90 days.

(3) *Transition period requirement.* For CAS-covered contracts placed on or before December 31, 1995, completed Disclosure Statements are required as follows:

(i) For business units that are selected to receive a CAS-covered contract or subcontract in excess of $500,000 and are part of the first 20 college or university locations (i.e., numbers 1 through 20) listed in Exhibit A of OMB Circular A–21, Disclosure Statements shall be submitted within six months after the date of contract award.

(ii) For business units that are selected to receive a CAS-covered contract or subcontract in excess of $500,000 and are part of a college or university location that is listed as one of the institutions numbered 21 through 50, in Exhibit A of OMB Circular A–21, Disclosure Statements shall be submitted during the six month period ending twelve months after the date of contract award.

(iii) For business units that are selected to receive a CAS-covered contract or subcontract in excess of $500,000 and are part of a college or university location that is listed as one of the institutions numbered 51 through 99, in Exhibit A of OMB Circular A–21, Disclosure Statements shall be submitted during the six month period ending eighteen months after the date of contract award.

(iv) For any other business unit that is selected to receive a CAS-covered contract or subcontract of $25 million or more, a Disclosure Statement shall be submitted within six months after the date of contract award.

(4) *Transition period due dates.* The educational institution and cognizant Federal agency should establish a specific due date within the periods prescribed in 9903.202–1(f)(3) when a Disclosure Statement is required under a CAS-covered contract placed on or before December 31, 1995.

(5) *Transition period waiver authority.* For a CAS-covered contract to be awarded during the period January 1, 1996 through June 30, 1997, the awarding agency may waive the preaward Disclosure Statement submission requirement specified in 9903.202–1(f)(2) when a due date for the submission of a Disclosure Statement has previously been established by the cognizant Federal agency and the educational institution under the provisions of 9903.202–1(f) (3) and (4). **CAUTION:** This waiver authority is not available unless the cognizant Federal agency and the educational institution have established a disclosure statement due date pursuant to a written agreement executed prior to January 1, 1996, and award is made prior to the established disclosure statement due date.

10. Section 9903.202–5 is revised to read as follows:

9903.202–5 Filing Disclosure Statements.

(a) Disclosure must be on Form Number CASB DS–1 or CASB DS–2, as applicable. Forms may be obtained from the cognizant Federal agency (cognizant ACO or cognizant Federal agency official authorized to act in that capacity) or from the looseleaf version of the Federal Acquisition Regulation. When requested in advance by a contractor, the cognizant Federal agency may authorize contractor disclosure based on computer generated reproductions of the applicable Disclosure Statement Form.

(b) Offerors are required to file Disclosure Statements as follows:

(1) Original and one copy with the cognizant ACO or cognizant Federal agency official acting in that capacity, as applicable; and

(2) One copy with the cognizant Federal auditor.

(c) Amendments and revisions shall be submitted to the ACO or agency official acting in that capacity, as applicable, and the Federal auditor of the currently cognizant Federal agency.

11. Section 9903.202–6 is added to read as follows:

9903.202–6 Adequacy of Disclosure Statement.

Federal agencies shall prescribe regulations and establish internal procedures by which each will promptly determine on behalf of the Government, when serving as the cognizant Federal agency for a particular contractor location, that a Disclosure Statement has adequately disclosed the practices required to be disclosed by the Cost Accounting Standards Board's rules, regulations and Standards. The determination of adequacy shall be distributed to all affected agencies. Agencies are urged to coordinate on the development of such regulations.

12. Section 9903.202–10 is added to read as follows:

9903.202–10 Illustration of Disclosure Statement Form, CASB DS–2.

The data which are required to be disclosed by educational institutions are set forth in detail in the Disclosure Statement Form, CASB DS–2, which is illustrated below:

BILLING CODE 3110–01–P

FORM APPROVED OMB NUMBER
0348-0055

COST ACCOUNTING STANDARDS BOARD
DISCLOSURE STATEMENT
REQUIRED BY PUBLIC LAW 100-679
EDUCATIONAL INSTITUTIONS

INDEX

FORM CASB DS-2 (REV 10/94)

COST ACCOUNTING STANDARDS BOARD
DISCLOSURE STATEMENT
REQUIRED BY PUBLIC LAW 100-679
EDUCATIONAL INSTITUTIONS

GENERAL INSTRUCTIONS

1. This Disclosure Statement has been designed to meet the requirements of Public Law 100-679, and persons completing it are to describe the educational institution and its cost accounting practices. For complete regulations, instructions and timing requirements concerning submission of the Disclosure Statement, refer to Section 9903.202 of Chapter 99 of Title 48 CFR (48 CFR 9903).

2. Part I of the Statement provides general information concerning each reporting unit (e.g., segments, business units, and central system or group (intermediate administration) offices). Parts II through VI pertain to the types of costs generally incurred by the segment or business unit directly performing under Federally sponsored agreements (e.g., contracts, grants and cooperative agreements). Part VII pertains to the types of costs that are generally incurred by a central or group office and are allocated to one or more segments performing under Federally sponsored agreements.

3. Each segment or business unit required to disclose its cost accounting practices should complete the Cover Sheet, the Certification, and Parts I through VI.

4. Each central or group office required to disclose its cost accounting practices for measuring, assigning and allocating its costs to segments performing under Federally sponsored agreements should complete the Cover Sheet, the Certification, Part I and Part VII of the Disclosure Statement. Where a central or group office incurs the types of cost covered by Parts IV, V and VI, and the cost amounts allocated to segments performing under Federally sponsored agreements are material, such office(s) should complete Parts IV, V, or VI for such material elements of cost. While a central or group office may have more than one reporting unit submitting Disclosure Statements, only one Statement needs to be submitted to cover the central or group office operations.

5. The Statement must be signed by an authorized signatory of the reporting unit.

6. The Disclosure Statement should be answered by marking the appropriate line or inserting the applicable letter code which describes the segment's (reporting unit's) cost accounting practices.

7. A number of questions in this Statement may need narrative answers requiring more space than is provided. In such instances, the reporting unit should use the attached continuation sheet provided. The continuation sheet may be reproduced locally as needed. The number of the question involved should be indicated and the same coding required to answer the questions in the Statement should be used in presenting the answer on the continuation sheet. Continuation sheets should be inserted at the end of the pertinent Part of the Statement. On each continuation sheet, the reporting unit should enter the next sequential page number for that Part and, on the last continuation sheet used, the words "End of Part" should be inserted after the last entry.

FORM CASB DS-2 (REV 10/94) (i)

COST ACCOUNTING STANDARDS BOARD DISCLOSURE STATEMENT REQUIRED BY PUBLIC LAW 100-679 EDUCATIONAL INSTITUTIONS	GENERAL INSTRUCTIONS

8. Where the cost accounting practice being disclosed is clearly set forth in the Institution's existing written accounting policies and procedures, such documents may be cited on a continuation sheet and incorporated by reference. In such cases, the reporting unit should provide the date of issuance and effective date for each accounting policy and/or procedures document cited. Alternatively, copies of the relevant parts of such documents may be attached as appendices to the pertinent Disclosure Statement Part. Such continuation sheets and appendices should be labeled and cross-referenced with the applicable Disclosure Statement item number. Any supplementary comments needed to fully describe the cost accounting practice being disclosed should also be provided.

9. Disclosure Statements must be amended when disclosed practices are changed to comply with a new CAS or when practices are changed with or without agreement of the Government (Also see 48 CFR 9903.202-3).

10. Amendments shall be submitted to the same offices to which submission would have to be made were an original Disclosure Statement being filed.

11. Each amendment should be accompanied by an amended cover sheet (indicating revision number and effective date of the change) and a signed certification. For all resubmissions, on each page, insert "Revision Number ____" and "Effective Date ____" in the Item Description block; and, insert "Revised" under each Item Number amended. Resubmitted Disclosure Statements must be accompanied by similar notations identifying the items which have been changed.

ATTACHMENT - Blank Continuation Sheet

FORM CASB DS-2 (REV 10/94) (ii)

COST ACCOUNTING STANDARDS BOARD DISCLOSURE STATEMENT REQUIRED BY PUBLIC LAW 100-679 EDUCATIONAL INSTITUTIONS	CONTINUATION SHEET
	NAME OF REPORTING UNIT

Item No.	Item Description

FORM CASB DS-2 (REV 10/94)

COST ACCOUNTING STANDARDS BOARD DISCLOSURE STATEMENT REQUIRED BY PUBLIC LAW 100-679 EDUCATIONAL INSTITUTIONS	COVER SHEET AND CERTIFICATION

0.1 Educational Institution

(a) Name

(b) Street Address

(c) City, State and ZIP Code

(d) Division or Campus of (if applicable)

0.2 Reporting Unit is: (Mark one.)

A. ____ Independently Administered Public Institution
B. ____ Independently Administered Nonprofit Institution
C. ____ Administered as Part of a Public System
D. ____ Administered as Part of a Nonprofit System
E. ____ Other (Specify) ____________

0.3 Official to Contact Concerning this Statement:

(a) Name and Title

(b) Phone Number (include area code and extension)

0.4 Statement Type and Effective Date:

A. (Mark type of submission. If a revision, enter number)

(a) ____ Original Statement
(b) ____ Amended Statement; Revision No. ______

B. Effective Date of this Statement: (Specify) ____________

0.5 Statement Submitted To (Provide office name, location and telephone number, include area code and extension):

A. Cognizant Federal Agency: ____________

B. Cognizant Federal Auditor: ____________

FORM CASB DS-2 (REV 10/94) C-1

COST ACCOUNTING STANDARDS BOARD DISCLOSURE STATEMENT REQUIRED BY PUBLIC LAW 100-679 EDUCATIONAL INSTITUTIONS	COVER SHEET AND CERTIFICATION

CERTIFICATION

I certify that to the best of my knowledge and belief this Statement, as amended in the case of a Revision, is the complete and accurate disclosure as of the date of certification shown below by the above-named organization of its cost accounting practices, as required by the Disclosure Regulations (48 CFR 9903.202) of the Cost Accounting Standards Board under 41 U.S.C. § 422.

Date of Certification: ____________

____
(Signature)

____
(Print or Type Name)

____
(Title)

THE PENALTY FOR MAKING A FALSE STATEMENT IN THIS DISCLOSURE IS PRESCRIBED IN 18 U.S.C. § 1001

FORM CASB DS-2 (REV 10/94) C-2

COST ACCOUNTING STANDARDS BOARD
DISCLOSURE STATEMENT
REQUIRED BY PUBLIC LAW 100-679
EDUCATIONAL INSTITUTIONS

PART I - GENERAL INFORMATION
NAME OF REPORTING UNIT

Item No.	Item Description
	Part I
1.1.0	Description of Your Cost Accounting System for recording expenses charged to Federally sponsored agreements (e.g., contracts, grants and cooperative agreements). (Mark the appropriate line(s) and if more than one is marked, explain on a continuation sheet.) A. ____ Accrual B. ____ Modified Accrual Basis 1/ C. ____ Cash Basis Y. ____ Other 1/
1.2.0	Integration of Cost Accounting with Financial Accounting. The cost accounting system is: (Mark one. If B or C is marked, describe on a continuation sheet the costs which are accumulated on memorandum records.) A. ____ Integrated with financial accounting records (Subsidiary cost accounts are all controlled by general ledger control accounts.) B. ____ Not integrated with financial accounting records (Cost data are accumulated on memorandum records.) C. ____ Combination of A and B
1.3.0	Unallowable Costs. Costs that are not reimbursable as allowable costs under the terms and conditions of Federally sponsored agreements are: (Mark one) A. ____ Specifically identified and recorded separately in the formal financial accounting records. 1/ B. ____ Identified in separately maintained accounting records or workpapers. 1/ C. ____ Identifiable through use of less formal accounting techniques that permit audit verification. 1/ D. ____ Combination of A, B or C 1/ E. ____ Determinable by other means. 1/
	1/ Describe on a Continuation Sheet.

FORM CASB DS-2 (REV 10/94) I-1

COST ACCOUNTING STANDARDS BOARD
DISCLOSURE STATEMENT
REQUIRED BY PUBLIC LAW 100-679
EDUCATIONAL INSTITUTIONS

PART I - GENERAL INFORMATION
NAME OF REPORTING UNIT

Item No.	Item Description
1.3.1	Treatment of Unallowable Costs. (Explain on a continuation sheet how unallowable costs and directly associated costs are treated in each allocation base and indirect expense pool, e.g., when allocating costs to a major function or activity; when determining indirect cost rates; or, when a central office or group office allocates costs to a segment.)
1.4.0	Cost Accounting Period: ____________ (Specify the twelve month period used for the accumulation and reporting of costs under Federally sponsored agreements, e.g., 7/1 to 6/30. If the cost accounting period is other than the institution's fiscal year used for financial accounting and reporting purposes, explain circumstances on a continuation sheet.)
1.5.0	State Laws or Regulations. Identify on a continuation sheet any State laws or regulations which influence the institution's cost accounting practices, e.g., State administered pension plans, and any applicable statutory limitations or special agreements on allowance of costs.
	1/ Describe on a Continuation Sheet.

FORM CASB DS-2 (REV 10/94) I-2

COST ACCOUNTING STANDARDS BOARD DISCLOSURE STATEMENT REQUIRED BY PUBLIC LAW 100-679 EDUCATIONAL INSTITUTIONS	PART II- DIRECT COSTS NAME OF REPORTING UNIT

Item No.	Item Description

Instructions for Part II

Institutions should disclose what costs are, or will be, charged directly to Federally sponsored agreements or similar cost objectives as Direct Costs. It is expected that the disclosed cost accounting practices (as defined at 48 CFR 9903.302-1) for classifying costs either as direct costs or indirect costs will be consistently applied to all costs incurred by the reporting unit.

2.1.0 Criteria for Determining How Costs are Charged to Federally Sponsored Agreements or Similar Cost Objectives. (For all major categories of cost under each major function or activity such, as instruction, organized research, other sponsored activities and other institutional activities, describe on a continuation sheet, your criteria for determining when costs incurred for the same purpose, in like circumstances, are treated either as direct costs only or as indirect costs only with respect to final cost objectives. Particular emphasis should be placed on items of cost that may be treated as either direct or indirect costs (e.g., Supplies, Materials, Salaries and Wages, Fringe Benefits, etc.) depending upon the purpose of the activity involved. Separate explanations on the criteria governing each direct cost category identified in this Part II are required. Also, list and explain if there are any deviations from the specified criteria.)

2.2.0 Description of Direct Materials. All materials and supplies directly identified with Federally sponsored agreements or similar cost objectives. (Describe on a continuation sheet the principal classes of materials which are charged as direct materials and supplies.)

2.3.0 Method of Charging Direct Materials and Supplies. (Mark the appropriate line(s) and if more than one is marked, explain on a continuation sheet.)

2.3.1 Direct Purchases for Projects are Charged to Projects at:

A. ____ Actual Invoiced Costs
B. ____ Actual Invoiced Costs Net of Discounts Taken
Y. ____ Other(s) 1/
Z. ____ Not Applicable

2.3.2 Inventory Requisitions from Central or Common, Institution-owned Inventory. (Identify the inventory valuation method used to charge projects):

A. ____ First In, First Out
B. ____ Last In, First Out
C. ____ Average Costs 1/
D. ____ Predetermined Costs 1/
Y. ____ Other(s) 1/
Z. ____ Not Applicable

1/ Describe on a Continuation Sheet.

COST ACCOUNTING STANDARDS BOARD DISCLOSURE STATEMENT REQUIRED BY PUBLIC LAW 100-679 EDUCATIONAL INSTITUTIONS	PART II- DIRECT COSTS NAME OF REPORTING UNIT

Item No.	Item Description

2.4.0 Description of Direct Personal Services. All personal services directly identified with Federally sponsored agreements or similar cost objectives. (Describe on a continuation sheet the personal services compensation costs, including applicable fringe benefits costs, if any, within each major institutional function or activity that are charged as direct personal services.)

2.5.0 Method of Charging Direct Salaries and Wages. (Mark the appropriate line(s) for each Direct Personal Services Category to identify the method(s) used to charge direct salary and wage costs to Federally sponsored agreements or similar cost objectives. If more than one line is marked in a column, fully describe on a continuation sheet, the applicable methods used.)

	Direct Personal Services Category			
	Faculty (1)	Staff (2)	Students (3)	Other 1/ (4)
A. Payroll Distribution Method (Individual time card/actual hours and rates)	____	____	____	____
B. Plan - Confirmation (Budgeted, planned or assigned work activity, updated to reflect significant changes)	____	____	____	____
C. After-the-fact Activity Records (Percentage Distribution of employee activity)	____	____	____	____
D. Multiple Confirmation Records (Employee Reports prepared each academic term, to account for employee's activities, direct and indirect charges are certified separately.)	____	____	____	____
Y. Other(s) 1/	____	____	____	____

1/ Describe on a Continuation Sheet.

COST ACCOUNTING STANDARDS BOARD DISCLOSURE STATEMENT REQUIRED BY PUBLIC LAW 100-679 EDUCATIONAL INSTITUTIONS	PART II- DIRECT COSTS NAME OF REPORTING UNIT

Item No.	Item Description
2.5.1	Salary and Wage Cost Distribution Systems. Within each major function or activity, are the methods marked in Item 2.5.0 used by all employees compensated by the reporting unit? (If "NO", describe on a continuation sheet, the types of employees not included and describe the methods used to identify and distribute their salary and wage costs to direct and indirect cost objectives.) ___ Yes ___ No
2.5.2	Salary and Wage Cost Accumulation System. (Within each major function or activity, describe, on a continuation sheet, the specific accounting records or memorandum records used to accumulate and record the share of the total salary and wage costs attributable to each employee's direct (Federally sponsored projects, non-sponsored projects or similar cost objectives) and indirect activities. Indicate how the salary and wage cost distributions are reconciled with the payroll data recorded in the institution's financial accounting records.)
2.6.0	Description of Direct Fringe Benefits Costs. All fringe benefits that are attributable to direct salaries and wages and are charged directly to Federally sponsored agreements or similar cost objectives. (Describe on a continuation sheet all of the different types of fringe benefits which are classified and charged as direct costs, e.g., actual or accrued costs of vacation, holidays, sick leave, sabbatical leave, premium pay, social security, pension plans, post-retirement benefits other than pensions, health insurance, training, tuition, tuition remission, etc.)
2.6.1	Method of Charging Direct Fringe Benefits. (Describe on a continuation sheet, how each type of fringe benefit cost identified in item 2.6.0. is measured, assigned and allocated (for definitions, See 9903.302-1); first, to the major functions (e.g., instruction, research); and, then to individual projects or direct cost objectives within each function.)
2.7.0	Description of Other Direct Costs. All other items of cost directly identified with Federally sponsored agreements or similar cost objectives. (List on a continuation sheet the principal classes of other costs which are charged directly, e.g., travel, consultants, services, subgrants, subcontracts, malpractice insurance, etc.)

FORM CASB DS-2 (REV 10/94) II-3

COST ACCOUNTING STANDARDS BOARD DISCLOSURE STATEMENT REQUIRED BY PUBLIC LAW 100-679 EDUCATIONAL INSTITUTIONS	PART II- DIRECT COSTS NAME OF REPORTING UNIT

Item No.	Item Description
2.8.0	Cost Transfers. When Federally sponsored agreements or similar cost objectives are credited for cost transfers to other projects, grants or contracts, is the credit amount for direct personal services, materials, other direct charges and applicable indirect costs always based on the same amount(s) or rate(s) (e.g., direct labor rate, indirect costs) originally used to charge or allocate costs to the project (Consider transactions where the original charge and the credit occur in different cost accounting periods). (Mark one, If "No", explain on a continuation sheet how the credit differs from original charge.) ___ Yes ___ No
2.9.0	Interorganizational Transfers. This item is directed only to those materials, supplies, and services which are, or will be transferred to you from other segments of the educational institution. (Mark the appropriate line(s) in each column to indicate the basis used by you as transferee to charge the cost or price of interorganizational transfers or materials, supplies, and services to Federally sponsored agreements or similar cost objectives. If more than one line is marked in a column, explain on a continuation sheet.)

	Materials (1)	Supplies (2)	Services (3)
A. At full cost excluding indirect costs attributable to group or central office expenses.	___	___	___
B. At full cost including indirect costs attributable to group or central office expenses.	___	___	___
C. At established catalog or market price or prices based on adequate competition.	___	___	___
Y. Other(s) 1/	___	___	___
Z. Interorganizational transfers are not applicable	___	___	___

1/ Describe on a Continuation Sheet.

FORM CASB DS-2 (REV 10/94) II-4

COST ACCOUNTING STANDARDS BOARD DISCLOSURE STATEMENT REQUIRED BY PUBLIC LAW 100-679 EDUCATIONAL INSTITUTIONS	PART III- INDIRECT COSTS NAME OF REPORTING UNIT

Item No.	Item Description

Instructions for Part III

Institutions should disclose how the segment's total indirect costs are identified and accumulated in specific indirect cost categories and allocated to applicable indirect cost pools and service centers within each major function or activity, how service center costs are accumulated and "billed" to users, and the specific indirect cost pools and allocation bases used to calculate the indirect cost rates that are used to allocate accumulated indirect costs to Federally sponsored agreements or similar final cost objectives. A continuation sheet should be used wherever additional space is required or when a response requires further explanation to ensure clarity and understanding.

The following Allocation Base Codes are provided for use in connection with Items 3.1.0 and 3.3.0.

A. Direct Charge or Allocation
B. Total Expenditures
C. Modified Total Cost Basis
D. Modified Total Direct Cost Basis
E. Salaries and Wages
F. Salaries, Wages and Fringe Benefits
G. Number of Employees (head count)
H. Number of Employees (full-time equivalent basis)
I. Number of Students (head count)
J. Number of Students (full-time equivalent basis)
K. Student Hours -- classroom and work performed
L. Square Footage
M. Usage
N. Unit of Product
O. Total Production
P. More than one base (Separate Cost Groupings) 1/
Y. Other(s) 1/
Z. Category or Pool not applicable

1/ List on a continuation sheet, the category and subgrouping(s) of expense involved and the allocation base(s) used.

FORM CASB DS-2 (REV 10/94) III-1

COST ACCOUNTING STANDARDS BOARD DISCLOSURE STATEMENT REQUIRED BY PUBLIC LAW 100-679 EDUCATIONAL INSTITUTIONS	PART III- INDIRECT COSTS NAME OF REPORTING UNIT

Item No.	Item Description

3.1.0 Indirect Cost Categories - Accumulation and Allocation. This item is directed at the identification, accumulation and allocation of all indirect costs of the institution. (Under the column heading, "Accumulation Method," insert "Yes" or "No" to indicate if the cost elements included in each indirect cost category are identified, recorded and accumulated in the institution's formal accounting system. If "No," describe on a continuation sheet, how the cost elements included in the indirect cost category are identified and accumulated. Under the column heading "Allocation Base," enter one of the allocation base codes A through P, Y, or Z, to indicate the basis used for allocating the accumulated costs of each indirect cost category to other applicable indirect cost categories, indirect cost pools, other institutional activities, specialized service facilities and other service centers. Under the column heading "Allocation Sequence," insert 1, 2, or 3 next to each of the first three indirect cost categories to indicate the sequence of the allocation process. If cross-allocation techniques are used, insert "CA." If an indirect cost category listed in this section is not used, insert "NA.")

Indirect Cost Category	Accumulation Method	Allocation Base Code	Allocation Sequence
(a) Depreciation/Use Allowances/Interest			___
Building	___	___	
Equipment	___	___	
Capital Improvements to Land 1/	___	___	
Interest 1/	___	___	
(b) Operation and Maintenance	___	___	___
(c) General Administration and General Expense	___	___	___
(d) Departmental Administration	___	___	
(e) Sponsored Projects Administration	___	___	
(f) Library	___	___	
(g) Student Administration and Services	___	___	
(h) Other 1/	___	___	

1/ Describe on a Continuation Sheet.

FORM CASB DS-2 (REV 10/94) III-2

COST ACCOUNTING STANDARDS BOARD DISCLOSURE STATEMENT REQUIRED BY PUBLIC LAW 100-679 EDUCATIONAL INSTITUTIONS	PART III- INDIRECT COSTS NAME OF REPORTING UNIT
Item No.	**Item Description**
3.2.0	Service Centers. Service centers are departments or functional units which perform specific technical or administrative services primarily for the benefit of other units within a reporting unit. Service Centers include "recharge centers" and the "specialized service facilities" defined in Section J of Circular A-21. (The codes identified below should be inserted on the appropriate line for each service center listed. The column numbers correspond to the paragraphs listed below that provide the codes. Explain on a Continuation Sheet if any of the services are charged to users on a basis other than usage of the services. Enter "Z" in Column 1, if not applicable.)

		(1)	(2)	(3)	(4)	(5)	(6)
(a)	Scientific Computer Operations	___	___	___	___	___	___
(b)	Business Data Processing	___	___	___	___	___	___
(c)	Animal Care Facilities	___	___	___	___	___	___
(d)	Other Service Centers with Annual Operating Budgets exceeding $1,000,000 or that generate significant charges to Federally sponsored agreements either as a direct or indirect cost. (Specify below; use a Continuation Sheet, if necessary)						
	___________	___	___	___	___	___	___
	___________	___	___	___	___	___	___

(1) Category Code: Use code "A" if the service center costs are billed only as direct costs of final cost objectives; code "B" if billed only to indirect cost categories or indirect cost pools; code "C" if billed to both direct and indirect cost objectives.

(2) Burden Code: Code "A" -- center receives an allocation of all applicable indirect costs; Code "B" -- partial allocation of indirect costs; Code "C" -- no allocation of indirect costs.

(3) Billing Rate Code: Code "A" -- billing rates are based on historical costs; Code "B" -- rates are based on projected costs; Code "C" -- rates are based on a combination of historical and projected costs; Code "D" -- billings are based on the actual costs of the billing period; Code "Y" -- other (explain on a Continuation Sheet).

(4) User Charges Code: Code "A" -- all users are charged at the same billing rates; Code "B" -- some users are charged at different rates than other users (explain on a Continuation Sheet).

(5) Actual Costs vs. Revenues Code: Code "A" -- billings (revenues) are compared to actual costs (expenditures) at least annually; Code "B" -- billings are compared to actual costs less frequently than annually.

(6) Variance Code: Code "A" -- Annual variances between billed and actual costs are prorated to users (as credits or charges); Code "B" -- variances are carried forward as adjustments to billing rate of future periods; Code "C" -- annual variances are charged or credited to indirect costs; Code "Y" -- other (explain on a Continuation Sheet).

COST ACCOUNTING STANDARDS BOARD DISCLOSURE STATEMENT REQUIRED BY PUBLIC LAW 100-679 EDUCATIONAL INSTITUTIONS	PART III- INDIRECT COSTS NAME OF REPORTING UNIT
Item No.	**Item Description**
3.3.0	Indirect Cost Pools and Allocation Bases (Identify all of the indirect cost pools established for the accumulation of indirect costs, excluding service centers, and the allocation bases used to distribute accumulated indirect costs to Federally sponsored agreements or similar cost objectives within each major function or activity. For all applicable indirect cost pools, enter the applicable Allocation Base Code A through P, Y, or Z, to indicate the basis used for allocating accumulated pool costs to Federally sponsored agreements or similar cost objectives.)

Indirect Cost Pools	Allocation Base Code
A. Instruction	
___ On-Campus	___
___ Off-Campus	___
___ Other 1/	___
B. Organized Research	
___ On-Campus	___
___ Off-Campus	___
___ Other 1/	___
C. Other Sponsored Activities	
___ On-Campus	___
___ Off-Campus	___
___ Other 1/	___
D. Other Institutional Activities 1/	___

3.4.0 Composition of Indirect Cost Pools. (For each pool identified under Items 3.1.0 and 3.2.0, describe on a continuation sheet the major organizational components, subgoupings of expenses, and elements of cost included.)

1/ Describe on a Continuation Sheet.

COST ACCOUNTING STANDARDS BOARD DISCLOSURE STATEMENT REQUIRED BY PUBLIC LAW 100-679 EDUCATIONAL INSTITUTIONS	PART III- INDIRECT COSTS NAME OF REPORTING UNIT

Item No.	Item Description
3.5.0	Composition of Allocation Bases. (For each allocation base code used in Items 3.1.0 and 3.3.0, describe on a continuation sheet the makeup of the base. For example, if a modified total direct cost base is used, specify which of the elements of direct cost identified in Part II, Direct Costs, that are included, e.g., materials, salaries and wages, fringe benefits, travel costs, and excluded, e.g., subcontract costs over first $25,000. Where applicable, explain if service centers are included or excluded. Specify the benefitting functions and activities included. If any cost objectives are excluded from the allocation base, such cost objectives and the alternate allocation method used should be identified. If an indirect cost allocation is based on Cost Analysis Studies, identify the study, and fully describe the study methods and techniques applied, the composition of the specific allocation base used, and the frequency of each recurring study .
3.6.0	Allocation of Indirect Costs to Programs That Pay Less Than Full Indirect Costs. Are appropriate direct costs of all programs and activites included in the indirect cost allocation bases, regardless of whether allocable indirect costs are fully reimbursed by the sponsoring organizations? A. ____ Yes B. ____ No 1/ 1/ Describe on a Continuation Sheet.

FORM CASB DS-2 (REV 10/94) III-5

COST ACCOUNTING STANDARDS BOARD DISCLOSURE STATEMENT REQUIRED BY PUBLIC LAW 100-679 EDUCATIONAL INSTITUTIONS	PART IV- DEPRECIATION AND USE ALLOWANCES NAME OF REPORTING UNIT

Item No. | Item Description

Part IV

4.1.0 Depreciation Charged to Federally Sponsored Agreements or Similar Cost Objectives. (For each asset category listed below, enter a code from A through C in Column (1) describing the method of depreciation; a code from A through D in Column (2) describing the basis for determining useful life; a code from A through C in Column (3) describing how depreciation methods or use allowances are applied to property units; and Code A or B in Column (4) indicating whether or not the estimated residual value is deducted from the total cost of depreciable assets. Enter Code Y in each column of an asset category where another or more than one method applies. Enter Code Z in Column (1) only, if an asset category is not applicable.)

	Asset Category	Depreciation Method (1)	Useful Life (2)	Property Unit (3)	Residual Value (4)
(a)	Land Improvements	____	____	____	____
(b)	Buildings	____	____	____	____
(c)	Building Improvements	____	____	____	____
(d)	Leasehold Improvements	____	____	____	____
(e)	Equipment	____	____	____	____
(f)	Furniture and Fixtures	____	____	____	____
(g)	Automobiles and Trucks	____	____	____	____
(h)	Tools	____	____	____	____
(i)	Enter Code Y on this line if other asset categories are used and enumerate on a continuation sheet each such asset category and the applicable codes. (Otherwise enter Code Z.)	____	____	____	____

Column (1)--Depreciation Method Code

A. Straight Line
B. Expensed at Acquisition
C. Use Allowance
Y. Other or more than one method 1/

Column (2)--Useful Life Code

A. Replacement Experience
B. Term of Lease
C. Estimated service life
D. As prescribed for use allowance by Office of Management and Budget Circular No. A-21
Y. Other or more than one method 1/

Column (3)--Property Unit Code

A. Individual units are accounted for separately
B. Applied to groups of assets with similar service lives
C. Applied to groups of assets with varying service lives
Y. Other or more than one method 1/

Column (4)--Residual Value Code

A. Residual value is deducted
B. Residual value is not deducted
Y. Other or more than one method 1/

1/ Describe on a Continuation Sheet.

FORM CASB DS-2 (REV 10/94) IV-1

COST ACCOUNTING STANDARDS BOARD
DISCLOSURE STATEMENT
REQUIRED BY PUBLIC LAW 100-679
EDUCATIONAL INSTITUTIONS

PART IV- DEPRECIATION AND USE ALLOWANCES

NAME OF REPORTING UNIT

Item No.	Item Description
4.1.1	Asset Valuations and Useful Lives. Are the asset valuations and useful lives used in your indirect cost proposal consistent with those used in the institution's financial statements? (Mark one.) A. ____ Yes B. ____ No 1/
4.2.0	Fully Depreciated Assets. Is a usage charge for fully depreciated assets charged to Federally sponsored agreements or similar cost objectives? (Mark one. If yes, describe the basis for the charge on a continuation sheet.) A. ____ Yes B. ____ No
4.3.0	Treatment of Gains and Losses on Disposition of Depreciable Property. Gains and losses are: (Mark the appropriate line(s) and if more than one is marked, explain on a continuation sheet.) A. ____ Excluded from determination of sponsored agreement costs B. ____ Credited or charged currently to the same pools to which the depreciation of the assets was originally charged C. ____ Taken into consideration in the depreciation cost basis of the new items, where trade-in is involved D. ____ Not accounted for separately, but reflected in the depreciation reserve account Y. ____ Other(s) 1/ Z. ____ Not applicable
4.4.0	Criteria for Capitalization. (Enter (a) the minimum dollar amount of expenditures which are capitalized for acquisition, addition, alteration, donation and improvement of capital assets, and (b) the minimum number of expected life years of assets which are capitalized. If more than one dollar amount or number applies, show the information for the majority of your capitalized assets, and enumerate on a continuation sheet the dollar amounts and/or number of years for each category or subcategory of assets involved which differs from those for the majority of assets.) A. Minimum Dollar Amount ____ B. Minimum Life Years ____
4.5.0	Group or Mass Purchase. Are group or mass purchases (initial complement) of similar items, which individually are less than the capitalization amount indicated above, capitalized? (Mark one.) A. ____ Yes 1/ B. ____ No 1/ Describe on a Continuation Sheet.

FORM CASB DS-2 (REV 10/94) IV-2

COST ACCOUNTING STANDARDS BOARD
DISCLOSURE STATEMENT
REQUIRED BY PUBLIC LAW 100-679
EDUCATIONAL INSTITUTIONS

PART V- OTHER COSTS AND CREDITS

NAME OF REPORTING UNIT

Item No.	Item Description
	Part V
5.1.0	Method of Charging Leave Costs. Do you charge vacation, sick, holiday and sabbatical leave costs to sponsored agreements on the cash basis of accounting (i.e., when the leave is taken or paid), or on the accrual basis of accounting (when the leave is earned)? (Mark applicable line(s)) A. ____ Cash B. ____ Accrual 1/
5.2.0	Applicable Credits. This item is directed at the treatment of "applicable credits" as defined in Section C of OMB Circular A-21 and other incidental receipts (e.g., purchase discounts, insurance refunds, library fees and fines, parking fees, etc.). (Indicate how the principal types of credits and incidental receipts the institution receives are usually handled.) A. ____ The credits/receipts are offset against the specific direct or indirect costs to which they relate. B. ____ The credits/receipts are handled as a general adjustment to the indirect pool. C. ____ The credits/receipts are treated as income and are not offset against costs. D. ____ Combination of methods 1/ Y. ____ Other 1/ 1/ Describe on a Continuation Sheet.

FORM CASB DS-2 (REV 10/94) V-1

COST ACCOUNTING STANDARDS BOARD
DISCLOSURE STATEMENT
REQUIRED BY PUBLIC LAW 100-679
EDUCATIONAL INSTITUTIONS

PART VI- DEFERRED COMPENSATION AND INSURANCE COSTS

NAME OF REPORTING UNIT

Item No.	Item Description
	Instructions for Part VI
	This part covers the measurement and assignment of costs for employee pensions, post retirement benefits other than pensions (including post retirement health benefits) and insurance. Some organizations may incur all of these costs at the main campus level or for public institutions at the governmental unit level, while others may incur them at subordinate organization levels. Still others may incur a portion of these costs at the main campus level and the balance at subordinate organization levels.
	Where the segment (reporting unit) does not directly incur such costs, the segment should, on a continuation sheet, identify the organizational entity that incurs and records such costs. When the costs allocated to Federally sponsored agreements are material, and the reporting unit does not have access to the information needed to complete an item, the reporting unit should require that entity to complete the applicable portions of this Part VI. (See item 4, page (i), General Instructions)
6.1.0	Pension Plans.
6.1.1	Defined-Contribution Pension Plans. Identify the types and number of pension plans whose costs are charged to Federally sponsored agreements. (Mark applicable line(s) and enter number of plans.)

Type of Plan		Number of Plans
A. ____	Institution employees participate in State/Local Government Retirement Plan(s)	____
B. ____	Institution uses TIAA/CREF plan or other defined contribution plan that is managed by an organization not affiliated with the institution	____
C. ____	Institution has its own Defined-Contribution Plan(s) 1/	____

6.1.2 Defined-Benefit Pension Plan. (For each defined-benefit plan (other than plans that are part of a State or Local government pension plan) describe on a continuation sheet the actuarial cost method, the asset valuation method, the criteria for changing actuarial assumptions and computations, the amortization periods for prior service costs, the amortization periods for actuarial gains and losses, and the funding policy.)

1/ Describe on a Continuation Sheet.

FORM CASB DS-2 (REV 10/94) VI-1

COST ACCOUNTING STANDARDS BOARD
DISCLOSURE STATEMENT
REQUIRED BY PUBLIC LAW 100-679
EDUCATIONAL INSTITUTIONS

PART VI- DEFERRED COMPENSATION AND INSURANCE COSTS

NAME OF REPORTING UNIT

Item No.	Item Description
6.2.0	Post Retirement Benefits Other Than Pensions (including post retirement health care benefits) (PRBs). (Identify on a continuation sheet all PRB plans whose costs are charged to Federally sponsored agreements. For each plan listed, state the plan name and indicate the approximate number and type of employees covered by each plan.)
	Z. [ ] Not Applicable
6.2.1	Determination of Annual PRB Costs. (On a continuation sheet, indicate whether PRB costs charged to Federally sponsored agreements are determined on the cash or accrual basis of accounting. If costs are accrued, describe the accounting practices used, including actuarial cost method, the asset valuation method, the criteria for changing actuarial assumptions and computations, the amortization periods for prior service costs, the amortization periods for actuarial gains and losses, and the funding policy.)
6.3.0	Self-Insurance Programs (Employee Group Insurance). Costs of the self-insurance programs are charged to Federally sponsored agreements or similar cost objectives: (Mark one.)
	A. ____ When accrued (book accrual only)
	B. ____ When contributions are made to a nonforfeitable fund
	C. ____ When contributions are made to a forfeitable fund
	D. ____ When the benefits are paid to an employee
	E. ____ When amounts are paid to an employee welfare plan
	Y. ____ Other or more than one method 1/
	Z. ____ Not Applicable
6.4.0	Self-Insurance Programs (Worker's Compensation, Liability and Casualty Insurance.)
6.4.1	Worker's Compensation and Liability. Costs of such self-insurance programs are charged to Federally sponsored agreements or similar cost objectives: (Mark one.)
	A. ____ When claims are paid or losses are incurred (no provision for reserves)
	B. ____ When provisions for reserves are recorded based on the present value of the liability
	C. ____ When provisions for reserves are recorded based on the full or undiscounted value, as contrasted with present value, of the liability
	D. ____ When funds are set aside or contributions are made to a fund
	Y. ____ Other or more than one method 1/
	Z. ____ Not Applicable

1/ Describe on a Continuation Sheet.

FORM CASB DS-2 (REV 10/94) VI-2

COST ACCOUNTING STANDARDS BOARD DISCLOSURE STATEMENT REQUIRED BY PUBLIC LAW 100-679 EDUCATIONAL INSTITUTIONS	PART VI- DEFERRED COMPENSATION AND INSURANCE COSTS NAME OF REPORTING UNIT
Item No.	Item Description
6.4.2	Casualty Insurance. Costs of such self-insurance programs are charged to Federally sponsored agreements or similar cost objectives: (Mark one.) A. ____ When losses are incurred (no provision for reserves) B. ____ When provisions for reserves are recorded based on replacement costs C. ____ When provisions for reserves are recorded based on reproduction costs new less observed depreciation (market value) excluding the value of land and other indestructibles. D. ____ Losses are charged to fund balance with no charge to contracts and grants (no provision for reserves) Y ____ Other or more than one method 1/ Z. ____ Not Applicable 1/ Describe on a Continuation Sheet.

COST ACCOUNTING STANDARDS BOARD DISCLOSURE STATEMENT REQUIRED BY PUBLIC LAW 100-679 EDUCATIONAL INSTITUTIONS	PART VII- CENTRAL SYSTEM OR GROUP EXPENSES NAME OF REPORTING UNIT
Item No.	Item Description
	DISCLOSURE BY CENTRAL SYSTEM OFFICE, OR GROUP (INTERMEDIATE ADMINISTRATION) OFFICE, AS APPLICABLE. Instructions for Part VII This part should be completed only by the central system office or a group office of an educational system when that office is responsible for administering two or more segments, where it allocates its costs to such segments and where at least one of the segments is required to file Parts I through VI of the Disclosure Statement. The reporting unit (central system or group office) should disclose how costs of services provided by the reporting unit are, or will be, accumulated and allocated to applicable segments of the institution. For a central system office, disclosure should cover the entire institution. For a group office, disclosure should cover all of the subordinate organizations administered by that group office.
7.1.0	Organizational Structure. On a continuation sheet, list all segments of the university or university system, including hospitals, Federally Funded Research and Development Centers (FFRDC's), Government-owned Contractor-operated (GOCO) facilities, and lower-tier group offices serviced by the reporting unit.
7.2.0	Cost Accumulation and Allocation. On a continuation sheet, provide a description of: A. The services provided to segments of the university or university system (including hospitals, FFRDC's, GOCO facilities, etc.), in brief. B. How the costs of the services are identified and accumulated. C. The basis used to allocate the accumulated costs to the benefitting segments. D. Any costs that are transferred from a segment to the central system office or the intermediate administrative office, and which are reallocated to another segment(s). If none, so state. E. Any fixed management fees that are charged to a segment(s) in lieu of a prorata or allocation basis and the basis of such charges. If none, so state.

BILLING CODE 3110-01-C

Subpart 9903.3—CAS Rules and Regulations

13. Section 9903.301 is amended by redesignating the existing introductory text and definitions as paragraph (a) and by adding a new paragraph (b) to read as follows:

9903.301 Definitions.

* * * * *

(b) The definitions set forth below are applicable exclusively to educational institutions and apply to this chapter 99.

Business unit. See 9903.201–2(c)(2)(ii).

Educational institution. See 9903.201–2(c)(2)(i).

Intermediate cost objective. See 9905.502–30(a)(7).

Segment. See 9903.201–2(c)(2)(ii).

14. A new Part 9905 is added to read as follows:

PART 9905—COST ACCOUNTING STANDARDS FOR EDUCATIONAL INSTITUTIONS

Authority: Public Law 100–679, 102 Stat. 4056, 41 U.S.C. 422.

9905.501 Cost accounting standard—consistency in estimating, accumulating and reporting costs by educational institutions.

9905.501–10 [Reserved]

9905.501–20 Purpose.

The purpose of this Cost Accounting Standard is to ensure that each educational institution's practices used in estimating costs for a proposal are consistent with cost accounting practices used by the institution in accumulating and reporting costs. Consistency in the application of cost accounting practices is necessary to enhance the likelihood that comparable transactions are treated alike. With respect to individual contracts, the consistent application of cost accounting practices will facilitate the preparation of reliable cost estimates used in pricing a proposal and their comparison with the costs of performance of the resulting contract. Such comparisons provide one important basis for financial control over costs during contract performance and aid in establishing accountability for costs in the manner agreed to by both parties at the time of contracting. The comparisons also provide an improved basis for evaluating estimating capabilities.

9905.501–30 Definitions.

(a) The following are definitions of terms which are prominent in this Standard. Other terms defined elsewhere in this Chapter 99 shall have the meanings ascribed to them in those definitions unless paragraph (b) of this subsection requires otherwise.

(1) *Accumulating costs* means the collecting of cost data in an organized manner, such as through a system of accounts.

(2) *Actual cost* means an amount determined on the basis of cost incurred (as distinguished from forecasted cost), including standard cost properly adjusted for applicable variance.

(3) *Estimating costs* means the process of forecasting a future result in terms of cost, based upon information available at the time.

(4) *Indirect cost pool* means a grouping of incurred costs identified with two or more objectives but not identified specifically with any final cost objective.

(5) *Pricing* means the process of establishing the amount or amounts to be paid in return for goods or services.

(6) *Proposal* means any offer or other submission used as a basis for pricing a contract, contract modification or termination settlement or for securing payments thereunder.

(7) *Reporting costs* means the providing of cost information to others.

(b) The following modifications of terms defined elsewhere in this Chapter 99 are applicable to this Standard: None.

9905.501–40 Fundamental requirement.

(a) An educational institution's practices used in estimating costs in pricing a proposal shall be consistent with the institution's cost accounting practices used in accumulating and reporting costs.

(b) An educational institution's cost accounting practices used in accumulating and reporting actual costs for a contract shall be consistent with the institution's practices used in estimating costs in pricing the related proposal.

(c) The grouping of homogeneous costs in estimates prepared for proposal purposes shall not *per se* be deemed an inconsistent application of cost accounting practices under paragraphs (a) and (b) of this subsection when such costs are accumulated and reported in greater detail on an actual cost basis during contract performance.

9905.501–50 Techniques for application.

(a) The standard allows grouping of homogeneous costs in order to cover those cases where it is not practicable to estimate contract costs by individual cost element. However, costs estimated for proposal purposes shall be presented in such a manner and in such detail that any significant cost can be compared with the actual cost accumulated and reported therefor. In any event, the cost accounting practices used in estimating costs in pricing a proposal and in accumulating and reporting costs on the resulting contract shall be consistent with respect to:

(1) The classification of elements of cost as direct or indirect;

(2) The indirect cost pools to which each element of cost is charged or proposed to be charged; and

(3) The methods of allocating indirect costs to the contract.

(b) Adherence to the requirement of 9905.501–40(a) of this standard shall be determined as of the date of award of the contract, unless the contractor has submitted cost or pricing data pursuant to 10 U.S.C. 2306(a) or 41 U.S.C. 254(d) (Pub. L. 87–653), in which case adherence to the requirement of 9905.501–40(a) shall be determined as of the date of final agreement on price.

as shown on the signed certificate of current cost or pricing data. Notwithstanding 9905.501–40(b), changes in established cost accounting practices during contract performance may be made in accordance with Part 9903 (48 CFR part 9903).

(c) The standard does not prescribe the amount of detail required in accumulating and reporting costs. The basic requirement which must be met, however, is that for any significant amount of estimated cost, the contractor must be able to accumulate and report actual cost at a level which permits sufficient and meaningful comparison with its estimates. The amount of detail required may vary considerably depending on how the proposed costs were estimated, the data presented in justification or lack thereof, and the significance of each situation. Accordingly, it is neither appropriate nor practical to prescribe a single set of accounting practices which would be consistent in all situations with the practices of estimating costs. Therefore, the amount of accounting and statistical detail to be required and maintained in accounting for estimated costs has been and continues to be a matter to be decided by Government procurement authorities on the basis of the individual facts and circumstances.

9905.501–60 Illustration. [Reserved]

9905.501–61 Interpretation. [Reserved]

9905.501–62 Exemption.

None for this Standard.

9905.501–63 Effective date.

This Standard is effective as of January 9, 1995.

9905.502 Cost accounting standard—consistency in allocating costs incurred for the same purpose by educational institutions.

9905.502–10 [Reserved]

9905.502–20 Purpose.

The purpose of this Standard is to require that each type of cost is allocated only once and on only one basis to any contract or other cost objective. The criteria for determining the allocation of costs to a contract or other cost objective should be the same for all similar objectives. Adherence to these cost accounting concepts is necessary to guard against the overcharging of some cost objectives and to prevent double counting. Double counting occurs most commonly when cost items are allocated directly to a cost objective without eliminating like cost items from indirect cost pools which are allocated to that cost objective.

9905.502–30 Definitions.

(a) The following are definitions of terms which are prominent in this Standard. Other terms defined elsewhere in this Chapter 99 shall have the meanings ascribed to them in those definitions unless paragraph (b) of this subsection requires otherwise.

(1) *Allocate* means to assign an item of cost, or a group of items of cost, to one or more cost objectives. This term includes both direct assignment of cost and the reassignment of a share from an indirect cost pool.

(2) *Cost objective* means a function, organizational subdivision, contract, or other work unit for which cost data are desired and for which provision is made to accumulate and measure the cost of processes, products, jobs, capitalized projects, etc.

(3) *Direct cost* means any cost which is identified specifically with a particular final cost objective. Direct costs are not limited to items which are incorporated in the end product as material or labor. Costs identified specifically with a contract are direct costs of that contract. All costs identified specifically with other final cost objectives of the educational institution are direct costs of those cost objectives.

(4) *Final cost objective* means a cost objective which has allocated to it both direct and indirect costs, and in the educational institution's accumulation system, is one of the final accumulation points.

(5) *Indirect cost* means any cost not directly identified with a single final cost objective, but identified with two or more final cost objectives or with at least one intermediate cost objective.

(6) *Indirect cost pool* means a grouping of incurred costs identified with two or more cost objectives but not identified with any final cost objective.

(7) *Intermediate cost objective* means a cost objective that is used to accumulate indirect costs or service center costs that are subsequently allocated to one or more indirect cost pools and/or final cost objectives.

(b) The following modifications of terms defined elsewhere in this Chapter 99 are applicable to this Standard: None.

9905.502–40 Fundamental requirement.

All costs incurred for the same purpose, in like circumstances, are either direct costs only or indirect costs only with respect to final cost objectives. No final cost objective shall have allocated to it as an indirect cost any cost, if other costs incurred for the same purpose, in like circumstances, have been included as a direct cost of that or any other final cost objective. Further, no final cost objective shall have allocated to it as a direct cost any cost, if other costs incurred for the same purpose, in like circumstances, have been included in any indirect cost pool to be allocated to that or any other final cost objective.

9905.502–50 Techniques for application.

(a) The Fundamental Requirement is stated in terms of cost incurred and is equally applicable to estimates of costs to be incurred as used in contract proposals.

(b) The Disclosure Statement to be submitted by the educational institution will require that the institution set forth its cost accounting practices with regard to the distinction between direct and indirect costs. In addition, for those types of cost which are sometimes accounted for as direct and sometimes accounted for as indirect, the educational institution will set forth in its Disclosure Statement the specific criteria and circumstances for making such distinctions. In essence, the Disclosure Statement submitted by the educational institution, by distinguishing between direct and indirect costs, and by describing the criteria and circumstances for allocating those items which are sometimes direct and sometimes indirect, will be determinative as to whether or not costs are incurred for the same purpose. Disclosure Statement as used herein refers to the statement required to be submitted by educational institutions as a condition of contracting as set forth in Subpart 9903.2.

(c) In the event that an educational institution has not submitted a Disclosure Statement, the determination of whether specific costs are directly allocable to contracts shall be based upon the educational institution's cost accounting practices used at the time of contract proposal.

(d) Whenever costs which serve the same purpose cannot equitably be indirectly allocated to one or more final cost objectives in accordance with the educational institution's disclosed accounting practices, the educational institution may either use a method for reassigning all such costs which would provide an equitable distribution to all final cost objectives, or directly assign all such costs to final cost objectives with which they are specifically identified. In the event the educational institution decides to make a change for either purpose, the Disclosure Statement shall be amended to reflect the revised accounting practices involved.

(e) Any direct cost of minor dollar amount may be treated as an indirect cost for reasons of practicality where the accounting treatment for such cost is consistently applied to all final cost objectives, provided that such treatment produces results which are substantially the same as the results which would have been obtained if such cost had been treated as a direct cost.

9905.502–60 Illustrations.

(a) Illustrations of costs which are incurred for the same purpose:

(1) An educational institution normally allocates all travel as an indirect cost and previously disclosed this accounting practice to the Government. For purposes of a new proposal, the educational institution intends to allocate the travel costs of personnel whose time is accounted for as direct labor directly to the contract. Since travel costs of personnel whose time is accounted for as direct labor working on other contracts are costs which are incurred for the same purpose, these costs may no longer be included within indirect cost pools for purposes of allocation to any covered Government contract. The educational institution's Disclosure Statement must be amended for the proposed changes in accounting practices.

(2) An educational institution normally allocates purchasing activity costs indirectly and allocates this cost to instruction and research on the basis of modified total costs. A proposal for a new contract requires a disproportionate amount of subcontract administration to be performed by the purchasing activity. The educational institution prefers to continue to allocate purchasing activity costs indirectly. In order to equitably allocate the total purchasing activity costs, the educational institution may use a method for allocating all such costs which would provide an equitable distribution to all applicable indirect cost pools. For example, the institution may use the number of transactions processed rather than its former allocation base of modified total costs. The educational institution's Disclosure Statement must be amended for the proposed changes in accounting practices.

(b) Illustrations of costs which are not incurred for the same purpose:

(1) An educational institution normally allocates special test equipment costs directly to contracts. The costs of general purpose test equipment are normally included in the indirect cost pool which is allocated to contracts. Both of these accounting practices were previously disclosed to the Government. Since both types of costs involved were not incurred for the same purpose in accordance with the criteria set forth in the educational institution's Disclosure Statement, the allocation of general purpose test equipment costs from the indirect cost pool to the contract, in addition to the directly allocated special test equipment costs, is not considered a violation of the Standard.

(2) An educational institution proposes to perform a contract which will require three firemen on 24-hour duty at a fixed-post to provide protection against damage to highly inflammable materials used on the contract. The educational institution presently has a firefighting force of 10 employees for general protection of its facilities. The educational institution's costs for these latter firemen are treated as indirect costs and allocated to all contracts; however, it wants to allocate the three fixed-post firemen directly to the particular contract requiring them and also allocate a portion of the cost of the general firefighting force to the same contract. The institution may do so but only on condition that its disclosed practices indicate that the costs of the separate classes of firemen serve different purposes and that it is the institution's practice to allocate the general firefighting force indirectly and to allocate fixed-post firemen directly.

9905.502–61 Interpretation.

(a) 9905.502, Cost Accounting Standard—Consistency in Allocating Costs Incurred for the Same Purpose by Educational Institutions, provides, in 9905.502–40, that "* * * no final cost objective shall have allocated to it as a direct cost any cost, if other costs incurred for the same purpose, in like circumstances, have been included in any indirect cost pool to be allocated to that or any other final cost objective."

(b) This interpretation deals with the way 9905.502 applies to the treatment of costs incurred in preparing, submitting, and supporting proposals. In essence, it is addressed to whether or not, under the Standard, all such costs are incurred for the same purpose, in like circumstances.

(c) Under 9905.502, costs incurred in preparing, submitting, and supporting proposals pursuant to a specific requirement of an existing contract are considered to have been incurred in different circumstances from the circumstances under which costs are incurred in preparing proposals which do not result from such a specific requirement. The circumstances are different because the costs of preparing proposals specifically required by the provisions of an existing contract relate only to that contract while other proposal costs relate to all work of the educational institution.

(d) This interpretation does not preclude the allocation, as indirect costs, of costs incurred in preparing all proposals. The cost accounting practices used by the educational institution, however, must be followed consistently and the method used to reallocate such costs, of course, must provide an equitable distribution to all final cost objectives.

9905.502–62 Exemption.

None for this Standard.

9905.502–63 Effective date.

This Standard is effective as of January 9, 1995.

9905.505 Accounting for unallowable costs—Educational institutions.

9905.505–10 [Reserved]

9905.505–20 Purpose.

(a)(1) The purpose of this Cost Accounting Standard is to facilitate the negotiation, audit, administration and settlement of contracts by establishing guidelines covering:

(i) Identification of costs specifically described as unallowable, at the time such costs first become defined or authoritatively designated as unallowable, and

(ii) The cost accounting treatment to be accorded such identified unallowable costs in order to promote the consistent application of sound cost accounting principles covering all incurred costs.

(2) The Standard is predicated on the proposition that costs incurred in carrying on the activities of an educational institution—regardless of the allowability of such costs under Government contracts—are allocable to the cost objectives with which they are identified on the basis of their beneficial or causal relationships.

(b) This Standard does not govern the allowability of costs. This is a function of the appropriate procurement or reviewing authority.

9905.505–30 Definitions.

(a) The following are definitions of terms which are prominent in this Standard. Other terms defined elsewhere in this Chapter 99 shall have the meanings ascribed to them in those definitions unless paragraph (b) of this subsection requires otherwise.

(1) *Directly associated cost* means any cost which is generated solely as a result of the incurrence of another cost, and which would not have been incurred had the other cost not been incurred.

(2) *Expressly unallowable cost* means a particular item or type of cost which,

under the express provisions of an applicable law, regulation, or contract, is specifically named and stated to be unallowable.

(3) *Indirect cost* means any cost not directly identified with a single final cost objective, but identified with two or more final cost objectives or with at least one intermediate cost objective.

(4) *Unallowable cost* means any cost which, under the provisions of any pertinent law, regulation, or contract, cannot be included in prices, cost reimbursements, or settlements under a Government contract to which it is allocable.

(b) The following modifications of terms defined elsewhere in this Chapter 99 are applicable to this Standard: None.

9905.505–40 Fundamental requirement.

(a) Costs expressly unallowable or mutually agreed to be unallowable, including costs mutually agreed to be unallowable directly associated costs, shall be identified and excluded from any billing, claim, or proposal applicable to a Government contract.

(b) Costs which specifically become designated as unallowable as a result of a written decision furnished by a contracting officer pursuant to contract disputes procedures shall be identified if included in or used in the computation of any billing, claim, or proposal applicable to a Government contract. This identification requirement applies also to any costs incurred for the same purpose under like circumstances as the costs specifically identified as unallowable under either this paragraph or paragraph (a) of this subsection.

(c) Costs which, in a contracting officer's written decision furnished pursuant to contract disputes procedures, are designated as unallowable directly associated costs of unallowable costs covered by either paragraph (a) or (b) of this subsection shall be accorded the identification required by paragraph (b) of this subsection.

(d) The costs of any work project not contractually authorized, whether or not related to performance of a proposed or existing contract, shall be accounted for, to the extent appropriate, in a manner which permits ready separation from the costs of authorized work projects.

(e) All unallowable costs covered by paragraphs (a) through (d) of this subsection shall be subject to the same cost accounting principles governing cost allocability as allowable costs. In circumstances where these unallowable costs normally would be part of a regular indirect-cost allocation base or bases, they shall remain in such base or bases. Where a directly associated cost is part of a category of costs normally included in an indirect-cost pool that will be allocated over a base containing the unallowable cost with which it is associated, such a directly associated cost shall be retained in the indirect-cost pool and be allocated through the regular allocation process.

(f) Where the total of the allocable and otherwise allowable costs exceeds a limitation-of-cost or ceiling-price provision in a contract, full direct and indirect cost allocation shall be made to the contract cost objective, in accordance with established cost accounting practices and Standards which regularly govern a given entity's allocations to Government contract cost objectives. In any determination of unallowable cost overrun, the amount thereof shall be identified in terms of the excess of allowable costs over the ceiling amount, rather than through specific identification of particular cost items or cost elements.

9905.505–50 Techniques for application.

(a) The detail and depth of records required as backup support for proposals, billings, or claims shall be that which is adequate to establish and maintain visibility of identified unallowable costs (including directly associated costs), their accounting status in terms of their allocability to contract cost objectives, and the cost accounting treatment which has been accorded such costs. Adherence to this cost accounting principle does not require that allocation of unallowable costs to final cost objectives be made in the detailed cost accounting records. It does require that unallowable costs be given appropriate consideration in any cost accounting determinations governing the content of allocation bases used for distributing indirect costs to cost objectives. Unallowable costs involved in the determination of rates used for standard costs, or for indirect-cost bidding or billing, need be identified only at the time rates are proposed, established, revised or adjusted.

(b)(1) The visibility requirement of paragraph (a) of this subsection, may be satisfied by any form of cost identification which is adequate for purposes of contract cost determination and verification. The Standard does not require such cost identification for purposes which are not relevant to the determination of Government contract cost. Thus, to provide visibility for incurred costs, acceptable alternative practices would include:

(i) The segregation of unallowable costs in separate accounts maintained for this purpose in the regular books of account,

(ii) The development and maintenance of separate accounting records or workpapers, or

(iii) The use of any less formal cost accounting techniques which establishes and maintains adequate cost identification to permit audit verification of the accounting recognition given unallowable costs.

(2) Educational institutions may satisfy the visibility requirements for estimated costs either:

(i) By designation and description (in backup data, workpapers, etc.) of the amounts and types of any unallowable costs which have specifically been identified and recognized in making the estimates, or

(ii) By description of any other estimating technique employed to provide appropriate recognition of any unallowable costs pertinent to the estimates.

(c) Specific identification of unallowable costs is not required in circumstances where, based upon considerations of materiality, the Government and the educational institution reach agreement on an alternate method that satisfies the purpose of the Standard.

9905.505–60 Illustrations.

(a) An auditor recommends disallowance of certain direct labor and direct material costs, for which a billing has been submitted under a contract, on the basis that these particular costs were not required for performance and were not authorized by the contract. The contracting officer issues a written decision which supports the auditor's position that the questioned costs are unallowable. Following receipt of the contracting officer's decision, the educational institution must clearly identify the disallowed direct labor and direct material costs in the institution's accounting records and reports covering any subsequent submission which includes such costs. Also, if the educational institution's base for allocation of any indirect cost pool relevant to the subject contract consists of direct labor, direct material, total prime cost, total cost input, etc., the institution must include the disallowed direct labor and material costs in its allocation base for such pool. Had the contracting officer's decision been against the auditor, the educational institution would not, of course, have been required to account separately for the costs questioned by the auditor.

(b) An educational institution incurs, and separately identifies, as a part of a service center or expense pool, certain costs which are expressly unallowable under the existing and currently effective regulations. If the costs of the service center or indirect expense pool are regularly a part of the educational institution's base for allocation of other indirect expenses, the educational institution must allocate the other indirect expenses to contracts and other final cost objectives by means of a base which includes the identified unallowable indirect costs.

(c) An auditor recommends disallowance of certain indirect costs. The educational institution claims that the costs in question are allowable under the provisions of Office Of Management and Budget Circular A–21, Cost Principles For Educational Institutions; the auditor disagrees. The issue is referred to the contracting officer for resolution pursuant to the contract disputes clause. The contracting officer issues a written decision supporting the auditor's position that the total costs questioned are unallowable under the Circular. Following receipt of the contracting officer's decision, the educational institution must identify the disallowed costs and specific other costs incurred for the same purpose in like circumstances in any subsequent estimating, cost accumulation or reporting for Government contracts, in which such costs are included. If the contracting officer's decision had supported the educational institution's contention, the costs questioned by the auditor would have been allowable and the educational institution would not have been required to provide special identification.

(d) An educational institution incurred certain unallowable costs that were charged indirectly as general administration and general expenses (GA&GE). In the educational institution's proposals for final indirect cost rates to be applied in determining allowable contract costs, the educational institution identified and excluded the expressly unallowable GA&GE costs form the applicable indirect cost pools. In addition, during the course of negotiation of indirect cost rates to be used for bidding and billing purposes, the educational institution agreed to classify as unallowable cost, various directly associated costs of the identifiable unallowable costs. On the basis of negotiations and agreements between the educational institution and the contracting officer's authorized representatives, indirect cost rates were established, based on the net balance of allowable GA&GE. Application of the rates negotiated to proposals, and to billings, for covered contracts constitutes compliance with the Standard.

(e) An employee, whose salary, travel, and subsistence expenses are charged regularly to the general administration and general expenses (GA&GE), an indirect cost category, takes several business associates on what is clearly a business entertainment trip. The entertainment costs of such trips is expressly unallowable because it constitutes entertainment expense prohibited by OMB Circular A–21, and is separately identified by the educational institution. In these circumstances, the employee's travel and subsistence expenses would be directly associated costs for identification with the unallowable entertainment expense. However, unless this type of activity constituted a significant part of the employee's regular duties and responsibilities on which his salary was based, no part of the employee's salary would be required to be identified as a directly associated cost of the unallowable entertainment expense.

9905.505–61 Interpretation. [Reserved]

9905.505–62 Exemption.

None for this Standard.

9905.505–63 Effective date.

This Standard is effective as of January 9, 1995.

9905.506 Cost accounting period—Educational institutions.

9905.506–10 [Reserved]

9905.506–20 Purpose.

The purpose of this Cost Accounting Standard is to provide criteria for the selection of the time periods to be used as cost accounting periods for contract cost estimating, accumulating, and reporting. This Standard will reduce the effects of variations in the flow of costs within each cost accounting period. It will also enhance objectivity, consistency, and verifiability, and promote uniformity and comparability in contract cost measurements.

9905.506–30 Definitions.

(a) The following are definitions of terms which are prominent in this Standard. Other terms defined elsewhere in this Part 99 shall have the meanings ascribed to them in those definitions unless paragraph (b) of this subsection requires otherwise.

(1) *Allocate* means to assign an item of cost, or a group of items of cost, to one or more cost objectives. This term includes both direct assignment of cost and the reassignment of a share from an indirect cost pool.

(2) *Cost objective* means a function, organizational subdivision, contract, or other work unit for which cost data are desired and for which provision is made to accumulate and measure the cost of processes, products, jobs, capitalized projects, etc.

(3) *Fiscal year* means the accounting period for which annual financial statements are regularly prepared, generally a period of 12 months, 52 weeks, or 53 weeks.

(4) *Indirect cost pool* means a grouping of incurred costs identified with two or more cost objectives but not identified specifically with any final cost objective.

(b) The following modifications of terms defined elsewhere in this Chapter 99 are applicable to this Standard: None.

9905.506–40 Fundamental requirement.

(a) Educational institutions shall use their fiscal year as their cost accounting period, except that:

(1) Costs of an indirect function which exists for only a part of a cost accounting period may be allocated to cost objectives of that same part of the period as provided in 9905.506–50(a).

(2) An annual period other than the fiscal year may, as provided in 9905.506–50(d), be used as the cost accounting period if its use is an established practice of the institution.

(3) A transitional cost accounting period other than a year shall be used whenever a change of fiscal year occurs.

(b) An institution shall follow consistent practices in the selection of the cost accounting period or periods in which any types of expense and any types of adjustment to expense (including prior-period adjustments) are accumulated and allocated.

(c) The same cost accounting period shall be used for accumulating costs in an indirect cost pool as for establishing its allocation base, except that the contracting parties may agree to use a different period for establishing an allocation base as provided in 9905.506–50(e).

9905.506–50 Techniques for application.

(a) The cost of an indirect function which exists for only a part of a cost accounting period may be allocated on the basis of data for that part of the cost accounting period if the cost is:

(1) Material in amount,

(2) Accumulated in a separate indirect cost pool or expense pool, and

(3) Allocated on the basis of an appropriate direct measure of the activity or output of the function during that part of the period.

(b) The practices required by 9905.506–40(b) of this Standard shall include appropriate practices for deferrals, accruals, and other adjustments to be used in identifying the cost accounting periods among which any types of expense and any types of adjustment to expense are distributed. If an expense, such as insurance or employee leave, is identified with a fixed, recurring; annual period which is different from the institution's cost accounting period, the Standard permits continued use of that different period. Such expenses shall be distributed to cost accounting periods in accordance with the institution's established practices for accruals, deferrals, and other adjustments.

(c) Indirect cost allocation rates, based on estimates, which are used for the purpose of expediting the closing of contracts which are terminated or completed prior to the end of a cost accounting period need not be those finally determined or negotiated for that cost accounting period. They shall, however, be developed to represent a full cost accounting period, except as provided in paragraph (a) of this subsection.

(d) An institution may, upon mutual agreement with the Government, use as its cost accounting period a fixed annual period other than its fiscal year, if the use of such a period is an established practice of the institution and is consistently used for managing and controlling revenues and disbursements, and appropriate accruals, deferrals or other adjustments are made with respect to such annual periods.

(e) The contracting parties may agree to use an annual period which does not coincide precisely with the cost accounting period for developing the data used in establishing an allocation base: Provided,

(1) The practice is necessary to obtain significant administrative convenience,

(2) The practice is consistently followed by the institution,

(3) The annual period used is representative of the activity of the cost accounting period for which the indirect costs to be allocated are accumulated, and

(4) The practice can reasonably be estimated to provide a distribution to cost objectives of the cost accounting period not materially different from that which otherwise would be obtained.

(f)(1) When a transitional cost accounting period is required under the provisions of 9905.506–40(a)(3), the institution may select any one of the following: (i) The period, less than a year in length, extending from the end of its previous cost accounting period to the beginning of its next regular cost accounting period,

(ii) A period in excess of a year, but not longer than 15 months, obtained by combining the period described in paragraph (f)(1) of this subsection with the previous cost accounting period, or

(iii) A period in excess of a year, but not longer than 15 months, obtained by combining the period described in subparagraph (f)(1) of this subsection with the next regular cost accounting period.

(2) A change in the institution's cost accounting period is a change in accounting practices for which an adjustment in the contract price may be required in accordance with subdivision (a)(4)(ii) or (iii) of the contract clause set out at 9903.201–4(e).

9905.506–60 Illustrations.

(a) An institution allocates indirect expenses for Organized Research on the basis of a modified total direct cost base. In a proposal for a covered contract, it estimates the allocable expenses based solely on the estimated amount of indirect costs allocated to Organized Research and the amount of the modified total direct cost base estimated to be incurred during the 8 months in which performance is scheduled to be commenced and completed. Such a proposal would be in violation of the requirements of this Standard that the calculation of the amounts of both the indirect cost pools and the allocation bases be based on the contractor's cost accounting period.

(b) An institution whose cost accounting period is the calendar year, installs a computer service center to begin operations on May 1. The operating expense related to the new service center is expected to be material in amount, will be accumulated in an intermediate cost objective, and will be allocated to the benefiting cost objectives on the basis of measured usage. The total operating expenses of the computer service center for the 8-month part of the cost accounting period may be allocated to the benefiting cost objectives of that same 8-month period.

(c) An institution changes its fiscal year from a calendar year to the 12-month period ending May 31. For financial reporting purposes, it has a 5-month transitional "fiscal year." The same 5-month period must be used as the transitional cost accounting period; it may not be combined as provided in 9905.506–50(f), because the transitional period would be longer than 15 months. The new fiscal year must be adopted thereafter as its regular cost accounting period. The change in its cost accounting period is a change in accounting practices; adjustments of the contract prices may thereafter be required in accordance with subdivision (a)(4) (ii) or (iii) of the contract clause at 9903.201–4(e).

(d) Financial reports are prepared on a calendar year basis on a university-wide basis. However, the contracting segment does all internal financial planning, budgeting, and internal reporting on the basis of a twelve month period ended June 30. The contracting parties agree to use the period ended June 30 and they agree to overhead rates on the June 30 basis. They also agree on a technique for prorating fiscal year assignment of the university's central system office expenses between such June 30 periods. This practice is permitted by the Standard.

(e) Most financial accounts and contract cost records are maintained on the basis of a fiscal year which ends November 30 each year. However, employee vacation allowances are regularly managed on the basis of a "vacation year" which ends September 30 each year. Vacation expenses are estimated uniformly during each "vacation year." Adjustments are made each October to adjust the accrued liability to actual, and the estimating rates are modified to the extent deemed appropriate. This use of a separate annual period for determining the amounts of vacation expense is permitted under 9905.506–50(b).

9905.506–61 Interpretation. [Reserved]

9905.506–62 Exemption.

None for this Standard.

9905.506–63 Effective date.

This Standard is effective as of January 9, 1995. For institutions with no previous CAS-covered contracts, this Standard shall be applied as of the start of its next fiscal year beginning after receipt of a contract to which this Standard is applicable.

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OFFICE OF MANAGEMENT AND BUDGET

Office of Federal Procurement Policy

48 CFR Parts 9903, 9904

Cost Accounting Standards Board; Cost Accounting Standards for Composition, Measurement, Adjustment, and Allocation of Pension Costs

AGENCY: Cost Accounting Standards Board, Office of Federal Procurement Policy, OMB.

ACTION: Final rule.

SUMMARY: The Office of Federal Procurement Policy, Cost Accounting Standards Board (CASB), is revising the Cost Accounting Standards relating to accounting for pension costs under negotiated government contracts. Section 26(g)(1) of the Office of Federal Procurement Policy Act, 41 U.S.C. 422(g)(1), requires that the Board, when promulgating any new or revised Cost Accounting Standard, publish a final rule. This final rule addresses certain problems that have emerged since the original promulgation (in the 1970's) of the pension Standards: CAS 9904.412—''Cost Accounting Standard for composition and measurement of pension cost,'' and CAS 9904.413, ''Adjustment and allocation of pension cost.'' The changes address pension cost recognition for qualified pension plans subject to the tax-deductibility limits of the Federal Tax Code, problems associated with pension plans that are not qualified plans under the Federal Tax Code, and problems associated with overfunded pension plans.

EFFECTIVE DATE: March 30, 1995.

FOR FURTHER INFORMATION CONTACT: Richard C. Loeb, Executive Secretary, Cost Accounting Standards Board (telephone: 202–395–3254).

SUPPLEMENTARY INFORMATION:

A. Regulatory Process

The Cost Accounting Standards Board's rules and regulations are codified at 48 CFR Chapter 99. Section 26(g)(1) of the Office of Federal Procurement Policy Act, 41 U.S.C. 422(g)(1), requires that the Board, prior to the establishment of any new or revised Cost Accounting Standard, complete a prescribed rulemaking process. This process consists of the following four steps:

1. Consult with interested persons concerning the advantages, disadvantages and improvements anticipated in the pricing and administration of government contracts as a result of a proposed Standard.
2. Promulgate an Advance Notice of Proposed Rulemaking.
3. Promulgate a Notice of Proposed Rulemaking.
4. Promulgate a final rule.

This final rule is step four in the four step process.

B. Background

Prior Promulgations: The previous CASB published CAS 9904.412—''Cost Accounting Standard for Composition and Measurement of Pension Cost'' on September 24, 1975 and CAS 9904.413—''Adjustment and Allocation of Pension Cost'' on July 20, 1977. The effective dates of these Standards were January 1, 1976 and March 10, 1978, respectively. These Standards were developed in the early years of the applicability of the Employee Retirement Income Security Act (ERISA). At that time, the problems on which this final rule focuses were not significant. Adequate or minimum, rather than excess funding, concerned pension managers of that era. Over the intervening years, government contractors' pension plans have become more adequately funded. At the same time, limits on the maximum amount of benefits that can be provided by a qualified pension plan have been considerably constrained in real terms. At the time the previous coverage was promulgated, there was little or no inconsistency between an orderly method of accruing pension costs and a contractor's ability to concurrently fund those accruals.

The Tax Reform Act of 1986 amended the Federal Tax Code to impose an excise tax on contributions in excess of the maximum tax-deductible amount for qualified pension plans. Immediately thereafter, the Omnibus Budget Reconciliation Act of 1987 (OBRA 87) added a second, often more restrictive full-funding limitation on the determination of the tax-deductible amount. To avoid the incurrence of an unallowable excise tax, government contractors generally did not fund any accrued pension cost in excess of the maximum tax-deductible pension contribution. However, portions of accrued pension costs that were not funded were not allowable. Furthermore, because the Standards prohibited the reassignment of accrued but unfunded pension costs, contractors could not allocate such costs to contracts when funded in future periods. On April 8, 1991, the Board issued a ''Memorandum for Agency Senior Procurement Executives'' which granted temporary authority to reassign to future periods pension costs that were not funded in the year of accrual because they lacked tax-deductibility.

An overwhelming majority of respondents to the Board's November 1990 solicitation of agenda items gave a high priority to the problems associated with fully-funded qualified plans and those connected with the growing universe of nonqualified pension plans. The Board sought public comments with a set of Staff Discussion Papers. A Paper addressing the ''pay-as-you-go'' or unfunded plan issue was published by the Board on June 17, 1991. See 56 FR 27780. A Paper seeking views on the ''full funding'' problem was published on August 19, 1991. See 56 FR 41151. On January 26, 1993, after consideration of the public comments received on these Staff Discussion Papers, the CASB published an Advance Notice of Proposed Rulemaking (ANPRM) in the **Federal Register**, 58 FR 6103. The ANPRM set forth proposed amendments to deal with both the unfunded pension plan issue related to nonqualified pension plans and the ''full-funding'' problem of qualified plans.

In the public comments to the ANPRM, the Board found two areas of concern particularly persuasive. These dealt with the ANPRM lacking any full-funding limitation, and the complexities and problems introduced by drastic revisions to the amortization period for actuarial gains and losses.

The ANPRM was premised on the idea that, by reducing such amortization periods, there would be only a relatively short time lag between cost/price recognition and the eventual funding. This premise, as pointed out by the commenters, was unsound. Because the ANPRM lacked any full-funding limitation, it could result in recognition of pension costs in years in which surplus assets existed. This is of particular concern to the Board because of the number of contractors that now have overfunded plans.

The Board also determined that changing amortization periods, in order to improve cost predictability, was unnecessary. Most commenters believed that a satisfactory degree of predictability could be achieved under the existing Standards' amortization rules.

On November 5, 1993, after consideration of the public comments received on the ANPRM, the CASB published a Notice of Proposed Rulemaking (NPRM), 58 FR 58999. The NPRM set forth proposed amendments to resolve the regulatory conflict for qualified pension plans by incorporating into the Standards the ERISA full-funding limitation, while maintaining the current amortization rules. To address questions concerning overfunded pension plans, the Board added coverage to CAS 9904.413 defining what constitutes a segment closing and providing greater specificity regarding accounting for pension costs when segments are closed or pension plans are terminated. The NPRM retained the accounting approach for nonqualified pension plans included in the ANPRM.

The public comments received in response to the NPRM raised some new issues. In the final rule, the Board addresses these issues focusing on three areas in particular. These deal with the restriction of accrual accounting by an outside limit, incomplete and unclear coverage for segment closings and pension plan terminations, and the lack of accounting for differences between accrued and funded pension costs. A majority of public comments expressed strong opinions, which were divided between support for accrual accounting and support for funding as the basis for determining allocable contract costs. In addition, numerous public comments were submitted concerning specific actuarial and technical issues.

The final rule reflects these and other concerns expressed by commenters to the NPRM. In addition, certain pension actuaries and the Pension Committee of the American Academy of Actuaries submitted suggestions to address the actuarial soundness of the final rule.

Termination of Temporary Waiver Authority

The final rule removes the regulatory conflict between the funding limits of ERISA and the period assignment provisions of CAS 9904.412–40(c). Therefore, the Board terminates the temporary waiver authority granted in the ‘‘Memorandum for Agency Senior Procurement Executives’’ issued on April 8, 1991.

Summary of Proposed Amendments

The Board's final rule provides for accrual accounting to initially compute the pension cost for a cost accounting period. The Board also recognizes that funding of such cost serves to substantiate the cost and adds to the verifiability of the measurement of cost. For assignment purposes, the computed cost is subject to a corridor with zero as the floor and the maximum tax-deductible amount, where applicable, as the ceiling. The computed cost is also subject to an assignable cost limitation so that cost will not be assigned to an overfunded pension plan. The cost assigned to the period must be funded as specified in the Standard to be allocable to final cost objectives. This four-step process of computing, assigning, funding, and allocating pension cost applies to both qualified and nonqualified defined-benefit pension plans.

This final rule affirms the complementary funding approach for nonqualified plans that takes into account Federal income tax deductibility. The Board views the complementary funding approach as a reasonable compromise addressing the Government's concern that claimed cost be substantiated by funding while providing contractors with relief from adverse cash flow consequences of funding a cost that is not tax-deductible. The Board decided that tax-exempt entities do not experience such cash flow disadvantages, and therefore, they are required to fund all pension cost that is assigned to the period.

For nonqualified defined-benefit plans that do not meet the communication, nonforfeiture, or funding criteria, or for which the contractor chooses to use the pay-as-you-go method, the assigned cost is equal to the amount of benefits paid in that period. To promote consistency between periods, this final rule requires that any lump sum settlements or annuity purchases be amortized.

For qualified defined-benefit pension plans, the conflict between the Standards and ERISA is removed. The cost assigned to a period is limited to the accrued cost that can be funded without penalizing a contractor. A $0 floor was added to the corridor to eliminate any inequity between a requirement to credit negative costs to contracts and the contractor's inability to make withdrawal from the funding agency.

By not requiring the assignment of negative pension cost, the Board has deferred the Government's recovery of excess assets in overfunded plans. This delay is appropriate for on-going pension plans when no assets have reverted or inured to the contractor. The effect of this delay has been mitigated by clarifying and strengthening the Government's rights or obligations for a cost adjustment when there is a segment closing, plan termination, or freezing of benefits.

Portions of pension costs computed for a period that fall outside of the assignable cost corridor ($0 floor and a ceiling based on tax-deductibility) are reassigned to future periods, together with an interest adjustment, as portions of unfunded actuarial liability and are identified as assignable cost deficits or assignable cost credits, respectively. Unfunded portions of assigned cost continue to be separately identified and eliminated from future cost computations.

For nonqualified plans, a clarification in the final rule is made by the addition of the concept of ‘‘permitted unfunded accruals’’; the portion of the computed and assigned cost of a nonqualified plan exempted from current funding based on the tax rate offset. These amounts are updated and described as the accumulated value of permitted unfunded accruals. All such previously assigned and allocated costs, adjusted for earnings, expenses, and benefit payments, are treated as plan assets retained by the contractor for purposes of assessing the funding status of the plan.

The fundamental requirement for assignment of pension cost has been expanded to include a ‘‘CAS balance test’’ modeled after the Internal Revenue Service ‘‘equation of balance’’. The CAS balance test requires that the entire actuarial accrued liability be accounted for by the assets or the portions of unfunded actuarial liability identified under subparagraphs 9904.412–50(a) (1) and (2). For the CAS balance test to function, the definition of unfunded actuarial liability is revised to clarify that an actuarial surplus exists whenever the actuarial value of assets exceeds the actuarial accrued liability. The accumulated value of prepayment credits, that is, funds that have yet to be applied to assigned costs, is excluded from the assets.

Technical corrections have been made to enhance the actuarial completeness of the final rule. Consistent with recent changes in ERISA and Generally Accepted Accounting Principles, as embodied in Statement 87 of the Financial Accounting Standards Board, and reflecting the sophistication of modern actuarial valuations, this final rule requires the use of explicit actuarial assumptions that are individually reasonable. Revisions have been made to distinguish the actuarial value of assets used for computations of on-going pension costs from the market value of assets used for current period adjustments. In addition, Generally Accepted Actuarial Principles and Practices as promulgated by the Actuarial Standards Board were considered in the drafting of this final rule.

Finally, this rule implements an amendment to the CAS applicability and exemption requirements contained in Section 9903.201–1(b)(11). This amendment is made necessary due to recent statutory changes contained in the Federal Acquisition Streamlining Act, Public Law 103–355.

Transition

The Board is aware that contracting officers and contractors have negotiated many pragmatic agreements while awaiting the promulgation of this final rule. The transition methods and illustrations of 9904.412–64 and 9904.413–64 are presented as model solutions. The Board expects that modifications of these methods and alternate approaches may be necessary to ensure equity for both the Government and contractors. Cognizant Federal officials are encouraged to ratify existing agreements that comport with the concepts of this final rule. For prior agreements or interim solutions based on a ''fresh-start'' amortization of the unfunded actuarial liability of qualified defined-benefit pension plans, the cognizant Federal official should verify that no portion of unfunded actuarial liability for prior unfunded costs that could have been funded, or, for other previously disallowed costs, have in fact been inadvertently included in pension costs.

The transition rules are constructed on a few basic concepts. Prior assigned costs of qualified plans, which were neither funded nor allocated to contracts because they lacked tax-deductibility, may be assigned, with interest, to periods beginning on or after the effective date of this rule. Conversely, unfunded accrued costs of nonqualified plans allocated to contracts should be treated as assets, updated for earnings and benefit payments, and applied against either the actuarial accrued liability used to compute cost accruals or the benefits paid under the pay-as-you-go method.

C. Paperwork Reduction Act

The Paperwork Reduction Act, Public Law 96–511, does not apply to this final rule, because this rule imposes no paperwork burden on offerors, affected contractors and subcontractors, or members of the public which requires the approval of OMB under 44 U.S.C. 3501, *et seq*.

D. Executive Order 12866 and the Regulatory Flexibility Act

The economic impact of this final rule on contractors and subcontractors is expected to be minor. As a result, the Board has determined that this final rule does not result in the promulgation of a ''major rule'' under the provisions of Executive Order 12866, and that a regulatory impact analysis will not be required. Furthermore, this final rule does not have a significant effect on a substantial number of small entities because small businesses are exempt from the application of the Cost Accounting Standards. Therefore, this rule does not require a regulatory flexibility analysis under the Regulatory Flexibility Act of 1980.

E. Public Comments

Public Comments: This final rule is based upon the Board's Notice of Proposed Rulemaking made available for public comment on November 5, 1993, 58 FR 58999. Thirty sets of public comments were received from contractors, Government agencies, professional associations, actuarial firms, law firms, public accounting firms, and individuals. The comments received and the Board's actions taken in response thereto are summarized below:

Comment: Twelve commenters expressed concern that the introduction of a funding limit on accrual accounting was a significant departure from the full accrual accounting approach of the ANPRM. Some commenters were also concerned with the complexity inherent in any rule governing pension costs. For these reasons the commenters supported the promulgation of a second NPRM.

Response: The Staff Discussion Papers, the ANPRM, and the NPRM each addressed the role of accrual accounting and the role of funding. The Staff Discussion Paper on fully-funded defined-benefit pension plans requested comments on the relative weights the Board should assign to accrual accounting, funding, and predictability as a basis for cost determination. The Staff Discussion Paper on unfunded nonqualified defined-benefit pension plans balanced its avoidance of a funding requirement with a very constrained method of accrual accounting for so-called ''accruable'' plans.

In response to the comments on the Staff Discussion Papers, the ANPRM adopted accrual accounting for both qualified plans and accruable nonqualified plans, which permitted certain portions of computed pension costs to be unfunded. Because the Board supported the need to substantiate the accrual with funding, the ANPRM required that the accrued costs for qualified plans be funded as soon as practicable. The ANPRM presumed there would not be a lengthy delay between accrual and funding, and so it did not link the period assignment of the accrual to current period funding. For nonqualified plans, the assignment of accrued costs was tied to funding, but the ANPRM introduced an exception for the effect of taxes on contractor cashflows. As with the Staff Discussion Paper, non-accruable plans, and accruable plans that so elect, were limited to the pay-as-you-go method.

The NPRM kept the same accounting approach for nonqualified plans as the ANPRM. Comments from the Government and contractors persuaded the Board that the conflict between full accrual accounting and ERISA funding, not predictability, was the significant problem. Finding that there could be indefinitely extended delays in the funding of the accruals of overfunded plans, the Board determined that it was necessary to link the period assignment of costs to current period funding in order to assure the verifiability of the accrued amounts. To resolve the conflict with ERISA's funding limits, the ERISA full-funding limitation was incorporated into the NPRM. Furthermore, aware of the need to address overfunded plans, the Board added clarity and specificity to the current period adjustment required when a segment closes. The Board explicitly included an adjustment for plan terminations because there has been some uncertainty as to the prior Board's intent.

With this final rule, the Board affirms the accounting approaches of the NPRM. Throughout the four-step promulgation process, accrual accounting consistently has been the starting point for the recognition of pension costs. The period assignment rule is tied to ERISA's tax-deductible maximum to prevent conflict with any of ERISA's funding limits. This final rule retains the complementary funding rule for nonqualified plans. The Board adopted many technical corrections suggested in public comments from actuaries and other professionals. To ensure that the technical corrections did not alter the conceptual approach of the NPRM, the Board sought and received input from certain pension actuaries and the American Academy of Actuaries.

Besides continuing support for either unrestricted accrual accounting or cost recognition based solely on funding, the public comments on the NPRM generally addressed details of the coverage requiring clarification or correction. This final rule does not deviate from the conceptual construct of the NPRM. As intended by the four-step promulgation process, this rule has evolved and the Board has found an informed balance between the advantages of accrual accounting and funding. Further public exposure would not alter the conceptual approach exposed in the NPRM and expressed in this final rule.

Comment: Thirteen commenters expressed their opposition to the adoption of the ERISA full-funding limitation. These commenters supported full accrual accounting as the only method that provides true matching of the incurrence of pension costs with the periods during which benefits were earned. They contend that tax law is not good accrual accounting and that the Board should make accounting rules independently of the concerns of taxability.

Response: The Board continues to recognize that one of the primary benefits of accrual accounting, and one of the stated goals of the Board, is the proper matching of benefiting contracts with the incurrence of expense. The Board also continues to support accrual accounting as the most effective means to promote consistency between cost accounting periods.

This final rule is based on the use of accrual accounting to initially compute the pension cost for a period. The assignable cost is then determined by comparing the computed pension cost accrual to a minimum of $0 and to the maximum tax-deductible amount. The Board has determined that funding is needed to substantiate the cost allocation because of the magnitude of the liability and the extended delay between the accrual of the cost and the settlement of the liability. This final rule has not adopted ERISA as an accounting method, but has modified accrual accounting to fit within the confines of practicable funding.

Comment: Eleven other commenters supported the imposition of the full-funding limit. Two commenters recommended that the cost accrual be subject to a $0 minimum because contractors are prohibited from withdrawing funds from a qualified trust.

Response: In this final rule, the Board refines the NPRM concept of a full-funding limitation. The full-funding limitation of the final rule is implemented through the definition and operation of the ''assignable cost limitation'' which defines the point when the plan is overfunded for cost recognition purposes. When a pension plan is overfunded, the Government would be violating its fiduciary duty to the taxpayers by advancing any further reimbursements to the contractor. The assignable cost limitation is similar to ERISA's pre-OBRA 87 full funding limitation, but uniquely defined to avoid confusion with ERISA terminology. As with the NPRM, whenever a plan is determined to be overfunded, that is, the actuarial value of assets exceeds the liability, all existing amortization bases are deemed fully amortized and eliminated.

The Board concurs that there should be a $0 floor imposed on the assignable pension cost for the period. The Standard requires the funding agency to be established for the ''exclusive benefit'' of the participants so that withdrawals by the contractor are prohibited, absent a plan termination. To be internally consistent, this final rule eliminates the assignment of negative costs to a period and the allocation of such credit to contracts, except when either assets revert or inure to the contractor or the segment is no longer continuing.

However, when a contractor makes a voluntary investment decision to not fund the assigned cost of its qualified pension plan, which is otherwise allocable to and payable as cost or price under Government contracts, the contractor has knowingly accepted the consequences of its decision. In this case, because there is no conflict between ERISA and the Standards, there is no reason to alter the cost computation and assignment for the period. Permitting arbitrary reassignment of the cost to other periods would be contrary to the Board's stated goal of enhancing the consistency of costs between periods and could create a potential for gaming.

Comment: A major concern of thirteen commenters was that the full-funding limitation is difficult to predict. Some commenters opined that the emphasis on funding made the rule unnecessarily complex.

Response: In this final rule, full-funding, which is measured by the assignable cost limitation based on the actuarial value of assets and the actuarial accrued liability, is reasonably predictable. Through the smoothing techniques of an asset valuation method, large swings in assets values are dampened. In a relatively stable population, the actuarial accrued liability can be fairly well predicted using actuarial projection techniques for forward pricing purposes. Other events that dramatically affect the liability are addressed in the provisions on cost method changes, segmentation, segment closings, plan terminations, and frozen plans. Finally, contractors have some flexibility in determining the timing of certain other events, such as assumption changes or plan amendments, that affect the size of the actuarial accrued liability.

When pension plan assets and liabilities are sufficiently different in amount, the impact of the tax-deductible limits of ERISA can be forecast with a fair degree of certainty. The tax-deductible limit, computed without regard to the full-funding limitation, is generally based on the normal cost and 10 year amortization of the unfunded actuarial liability and is also relatively predictable.

A predictability problem does arise when a plan is near the threshold of ERISA's full-funding limitations. The impact of these limits is sensitive to small changes in the market value of assets, the actuarial accrued liability, and prevailing Treasury rates. The Board believes that the ''all or nothing'' nature and the magnitude of the impact are beyond the normal assumption of risk inherent in firm fixed-priced contracting. However, the Board believes that this is a forward-pricing problem that may be addressed by the contracting officer through the negotiation of an advance agreement reflecting the contractor's unique facts, circumstances, and expected level and mix of Government contracting. Such advance agreements could provide a method for achieving equity in the forecasting of pension costs for contractors whose pension plans are close to entering or emerging from the funding limits of ERISA.

While the special problems of forward-pricing will continue to require attention by the contracting officer, this final rule does not add more complication. The concepts of assignable cost limitation, assignable cost deficit, and assignable cost credit contained in this final rule are simply the accounting and actuarial mechanisms necessary to assign computed costs that fall outside of the funding corridor to future periods.

Comment: Twelve commenters noted that, despite the full-funding limitation, the cost assigned under the NPRM could still be greater than the tax-deductible maximum. Seven commenters remarked that ERISA requires amortizations to continue, and a new base be established, when the contribution is affected by the OBRA 87 full-funding limitation only. Seven commenters recommended that subparagraph 9904.412–50(b)(1) be clarified.

Response: This has been corrected in the final rule by using the maximum tax-deductible amount, however determined, as the limit on assignable cost for qualified plans. The accrued pension cost not assigned to the current period is reassigned to future periods as an assignable cost deficit. This final rule also specifies that any negative accrued cost be reassigned to future periods as an assignable cost credit.

This final rule specifies that all existing amortization bases are deemed fully amortized when the accrued cost is affected by the assignable cost limitation. This rule provides that any unfunded actuarial liability, including an actuarial surplus, existing in the next accounting period is deemed to be an actuarial gain or loss unless it is attributable to a change in assumptions, plan amendment, or separately identified portions of unfunded actuarial liability attributable to unfunded and/or disallowed pension costs.

Comment: Fifteen commenters stated that funding would not be needed to validate the liability of nonqualified defined-benefit plans if the Board retained the existing requirement that the benefits be ''compelled''.

Response: The Board believes it is reasonable for the Government to require that pension cost of both qualified and nonqualified pension plans allocated to contracts, which the Government pays for through cost or price, be subject to funding. This final rule ensures that any unfunded portion of assigned cost is isolated from the computation of future cost accruals. To prevent windfall gains or losses and to minimize the need for advance agreements discussed above, costs allocated to fixed-priced contracts must be funded to the extent possible.

The Board notes that the excess funding, which occurs when a contractor funds more than the assigned pension cost for the period, is carried forward to future periods with interest. This final rule retains the premature funding provisions of the original Standard through the definition and operation of prepayment credits.

Comment: Five commenters stated that current period funding of assigned costs for nonqualified pension plans is necessary to enhance the verifiability of all costs allocated to contracts and to reduce the risk that the promised benefits might never be paid.

Response: As already discussed, the Board is persuaded that funding of the assigned cost is necessary to substantiate the liability. The Board is also persuaded that requiring a taxable contractor to fund 100% of the pension cost could impose a cash flow penalty to the extent the amount funded may not be tax-deductible. The Board has modified the funding requirement accordingly. However, the Board does not wish to provide a cash flow advantage to tax-exempt contractors for whom no such cash flow penalty exists. Accordingly, the complementary funding rule is restricted to taxable entities only.

This final rule addresses the risk that unfunded costs will not be verified by providing for an accounting of all assigned costs. Funded costs are captured and accounted for within the assets of the funding agency. Amounts exempted from funding based on the tax-rate are retained in the general assets of the contractor and accounted for within the accumulated value of permitted unfunded accruals. Portions of assigned cost not substantiated by complementary funding must be separately identified and accounted for pursuant to 9904.412–50(a)(2). This final rule ensures that all portions of assigned cost and allocated cost are tracked and accounted for, and thereby removes much of the risk.

Comment: Eight commenters were concerned that a ''Rabbi'' trust would not satisfy the ''exclusive benefit'' requirement in the definition of a funding agency since creditors might have superior rights to those of the plan participants. Other commenters asked if other nonqualified trust arrangements could qualify as a funding agency under the Standard.

Response: The Board's intention when revising the definition of a funding agency was to prohibit the use of bookkeeping reserves, escrow accounts, or any other arrangement under which the rights of the plan participants were not clearly superior to those of the plan sponsor. The basic test of ''exclusive benefit'' is whether the contractor has relinquished all rights to the funds and that, except for the extraordinary event of bankruptcy, the participants have primary rights to the funds. The solvency of a contractor is always a concern to the Government that is not restricted merely to pension costs.

The Board does not intend that a ''Rabbi trust'' be the only funding arrangement that satisfies the funding agency definition. Other arrangements such as so-called secular trusts can be satisfactory. The Board expects that as tax law changes and as qualified plan benefit limits possibly become more or less restrictive, other funding arrangements may become more effective and more widely adopted.

The Board does not intend for the ''exclusive benefit'' clause to prohibit asset reversions where, after settling all benefit obligations to plan participants, the residual assets of the trust revert or inure to a contractor. The funding agency coverage in the pension Standards is intended to be consistent with the coverage for funded insurance reserves found at 9904.416–50(a)(1)(v)(B), which permits a reversion of assets only after all benefit obligations have been satisfied through insurance.

Comment: Nine commenters were concerned that taxes and administrative costs associated with Rabbi trusts will increase pension costs. Five commenters believe that the NPRM (and prior ANPRM) complementary funding rule for nonqualified plans creates an administrative burden.

Response: The Board recognizes that there will be some additional expenses associated with the use of complementary funding and the use of nonqualified trust funds. The specificity of the final rule gives contractors clear rules under which they can choose to compute, assign, and allocate the costs of a nonqualified plan. The benefits of an accurate accounting of all assigned costs will offset any increased administrative expense to the Government and contractors.

There will be an increase in the cost of such plans for the taxes on the earnings of the nonqualified trust fund that are directly paid by or reimbursed from the fund. These taxes are a valid expense of the pension plan incurred in response to the final rule's requirement that a portion of the assigned cost be funded. The Board notes that, in fact, such increased costs are being returned to the Government through the payment of the tax.

The rule specifies that income taxes on the earnings of a nonqualified trust are treated as administrative expenses and not as decrements to the assumed investment earning rate. This technical correction clarifies that the interest assumption used to compute actuarial values is not reduced to reflect taxes on fund earnings. This rule is not intended to prevent contractors from expressing the actuarial assumption for administrative expenses as a percentage of the earnings.

Comment: Two commenters suggested that the final rule address how ERISA's funding limits are allocated to segments.

Response: Only the maximum tax-deductible amount and the contribution to the funding agency are determined for the pension plan in its entirety. Under segmented accounting, all other aspects of period cost; i.e., normal cost, unfunded actuarial liability, assignable cost limitation, are measured at the segment level. This final rule requires that the tax-deductible maximum, determined for the plan as a whole, must be apportioned to segments using a basis that considers the assignable costs or the funding levels of the segments. Illustrations of how plan-wide values are apportioned to segments have been added.

In addition, to ease the funding of costs attributable to Government contracts, this final rule allows contractors with predominantly commercial business to apportion contributions for qualified defined-benefit plans to their Government segments first, but only if the contractor uses segmented accounting. Unfunded assigned costs, whether attributable to Government contracts or commercial business, will be separately identified under 9904.412–50(a)(2) and thereby isolated from future cost computations and future allocation. This provision allows the contractor to determine when to fund costs of its qualified defined-benefit plan for segments that are associated solely with commercial business.

Although the assets of a pension plan are subject to the claims of all plan participants, the Board believes the funding requirements and protections of ERISA will prevent any untenable differences in funding levels of segments from arising. Because nonqualified plans lack the funding requirement protection of ERISA, the funding of such plans must be apportioned across all segments.

Comment: Four commenters suggested that the definition of a segment closing should be clarified. Concerns were raised that an internal reorganization would require a current period adjustment for a segment closing even though neither the segment's nor the contractor's relationship to the Government had changed.

Response: The definition has been revised to delineate three conditions requiring a current period adjustment. The first condition occurs when there is a change in ownership of the segment, not just a simple reorganization within the contractor's internal structure. The second event is the one addressed in the NPRM; that is, when the contractual relationship ends because the segment operationally ceases to exist. The third case addresses the end of the contractual relationship with the Government, whether the segment continues in operation or not.

Comment: Two commenters opposed using the accrued benefit cost method (ABCM) to determine the actuarial liability for a segment closing or plan termination adjustment. These commenters believe the ABCM understates the liability. Four commenters supported limiting the actuarial assumptions used to determine the segment closing and plan termination adjustment. These commenters also supported a phase-in of benefit improvements adopted within 5 years of a segment closing or plan termination.

Response: In this final rule, the actuarial accrued liability, used for determining the adjustment for a segment closing or curtailment of benefits, is determined using the accrued benefit cost method. For a curtailment of benefits or for plan participants who are terminated from employment in a segment closing, the accrued benefit is the appropriate measure of the ultimate benefit that will be paid under the plan. If plan participants remain employed by the contractor, whether in the same or another segment, the Board believes the responsibility for future salary increases, which are attributable to future productivity, merit, and inflation, belongs to the future customers that benefit from the participants' continued employment. The Board notes that the ABCM does recognize the cost of vesting earned by the participants' future service.

The Board also believes that when there is an immediate period liquidation of the liability through the payment of lump sum settlements or the purchase of annuities, the cost of such settlements and annuities is an exact measure of the liability, although the Government does have a right to share in any future dividends or refunds. This final rule has been revised accordingly.

Consistent with the requirement that actuarial assumptions be individual best-estimates of future long-term economic and demographic trends, this final rule requires that the assumptions used to determine the actuarial liability be consistent with the assumptions that have been in use. This is consistent with the fact that the pension plan is continuing even though the segment has closed or the earning of future benefits has been curtailed. The Board does not intend this rule to prevent contractors from using assumptions that have been revised based on a persuasive actuarial experience study or a change in a plan's investment policy.

This final rule does include a sixty-month phase-in of voluntary benefit improvements to forestall an increase in the liability in contemplation of a segment closing or plan termination. Improvements mandated by law or granted though collective bargaining negotiations are not considered voluntary. A plan termination or curtailment of benefits is viewed as negating the intent of any recent voluntary benefit improvements.

Under the revised definition of a segment closing, some employees may remain in a segment performing non-Government work while other employees may be transferred to other segments. For consistency, the provisions for transfers of either active or retired participants specify that the assets transferred must equal the actuarial accrued liability determined under the accrued benefit cost method.

Comment: One commenter asked if a contractor must determine whether a termination of plan gain or loss has occurred before an adjustment is required. Another commenter asked if a termination of plan gain or loss occurs when a pension plan is ''frozen.''

Response: The definition has been changed to refer to an event; that is, the termination of a pension plan. Any resultant gain or loss for Government contracting purposes is determined by the 9904.413–50(c)(12) adjustment. The ''freezing'' of a pension plan is addressed by the addition of a definition for a ''Curtailment of Benefits.''

Comment: Two commenters supported the amortization of any segment closing adjustment, rather than an immediate period adjustment.

Response: Under this final rule, the 9904.413–50(c)(12) adjustment is determined as a current period adjustment, whether or not assets actually revert from the trust. The Board believes a current period adjustment is appropriate when there is a disruption of the contracting relationship, a discontinuance of the operational segment, or a discontinuance of the pension plan. When such events occur, pension costs can no longer be computed and adjusted on an on-going basis since there are either no future accounting periods in which credits or charges can be allocated to contracts or no future periods in which benefits will be earned.

If a contractor will continue to have a contracting relationship with the Government, the final rule does permit the cognizant Federal official and the contractor to negotiate an amortization schedule. This provision will allow a contractor to allocate an adjustment credit to future years during which it can recover the amount of credited assets either through decreased pension costs or through prices charged to other customers benefiting from the future work performed by plan participants.

Comment: Eleven commenters requested that the Board clarify that the 9904.413–50(c)(12) adjustment could result in a charge to final cost objectives if the liabilities exceeded the assets.

Response: The final rule refers to the ''difference'' between assets and liabilities without prejudice towards either adjustment credits or adjustment charges. An illustration of the adjustment when liabilities exceed assets has been added.

Comment: Four commenters asked the Board to clarify how the Government's share of the adjustment was to be determined. Five commenters opposed the inclusion of fixed-price contracts in any formula used to determine the Government's share.

Response: The asset value used to determine the adjustment amount is the market value of the assets, including permitted unfunded accruals, plus portions of unfunded liability identified pursuant to 9904.412–50(a)(2), i.e., plan assets retained by the contractor due to allocated but unfunded costs. The asset value is reduced for the accumulated value of any prepayment credits since such assets have never been assigned to past periods nor allocated to Government contracts. Because this asset value represents the current value of assigned costs of prior periods, the sum of previously assigned pension costs is the denominator of the fraction. The portion of these assets attributable to the Government's participation in the funding of the pension plan through cost or price is measured by the sum of costs allocated to Government contracts. The fraction is determined based on data from years that are representative of the Government's participation, which is a factual determination best made by the contracting officer.

Costs allocated to fixed-price contracts subject to CAS 9904.412 and 9904.413 are included since the Government has participated in the funding of the plan through the payment of the estimated pension cost considered in the pricing of the contract. A risk/reward of a fixed-price contract is the deviation of actual costs from the estimated cost considered in the price. If a single period event, e.g., segment closing, plan termination, or benefit curtailment, alters the on-going nature of the pension plan or segment, the effect on fixed-price contracts should be similar to that of an accounting practice change.

Comment: Four commenters supported amending the NPRM coverage to explicitly state that the 9904.413–50(c)(12) adjustment is determined net of the excise tax on pension plan asset reversions.

Response: The Board agrees. Before applying the fraction that determines the Government's share, subdivision 9904.413–50(c)(12)(vi) reduces the adjustment amount for any excise taxes assessed on assets that revert to the contractor as part of a pension plan termination. The excise tax is intended to discourage plan sponsors from terminating their qualified pension plans, and under this final rule, Government contractors are subject to the same termination penalty as their commercial counterparts. Since the excise tax is returned to the Government, albeit the Internal Revenue Service, the Board believes equity warrants determining the Government's share based on the net adjustment amount.

While the Board believes the Government's allocable share of any adjustment should be net of any reversion excise tax, the allowability of such excise taxes continues to be determined by the applicable cost principles. Income taxes, which are paid to the Internal Revenue Service as an offset against prior tax deductions, continue not to be allocable.

Comment: Six commenters suggested that a segment closing adjustment is not necessary if the assets and liabilities of the segment were transferred to the successor contractor.

Response: The Board agrees. The appropriate coverage and illustrations have been added.

List of Subjects in 48 CFR Parts 9903 and 9904

Cost accounting standards, Government procurement.

Richard C. Loeb,

Executive Secretary, Cost Accounting Standards Board.

PART 9903—CONTRACT COVERAGE

1. The authority citations for Parts 9903 and 9904 continue to read as follows:

Authority: Public Law 100–679, 102 Stat 4056, 41 U.S.C. 422.

9903.201 [Amended]

2. Subsection 9903.201–1 is amended by removing and reserving paragraph (b)(11).

PART 9904—COST ACCOUNTING STANDARDS

3. Subsection 9904.412–30 is amended by revising paragraph (a) to read as follows:

9904.412–30 Definitions.

(a) The following are definitions of terms which are prominent in this Standard. Other terms defined elsewhere in this chapter 99 shall have the meanings ascribed to them in those definitions unless paragraph (b) of this subsection requires otherwise.

(1) *Accrued benefit cost method* means an actuarial cost method under which units of benefits are assigned to each cost accounting period and are valued as they accrue; that is, based on the services performed by each employee in the period involved. The measure of normal cost under this method for each cost accounting period is the present value of the units of benefit deemed to be credited to employees for service in that period. The measure of the actuarial accrued liability at a plan's inception date is the present value of the units of benefit credited to employees for service prior to that date. (This method is also known as the Unit Credit cost method without salary projection.)

(2) *Actuarial accrued liability* means pension cost attributable, under the actuarial cost method in use, to years prior to the current period considered by a particular actuarial valuation. As of such date, the actuarial accrued liability represents the excess of the present value of future benefits and administrative expenses over the present value of future normal costs for all plan participants and beneficiaries. The excess of the actuarial accrued liability over the actuarial value of the assets of a pension plan is the Unfunded Actuarial Liability. The excess of the actuarial value of the assets of a pension plan over the actuarial accrued liability is an actuarial surplus and is treated as a negative unfunded actuarial liability.

(3) *Actuarial assumption* means an estimate of future conditions affecting pension cost; for example, mortality rate, employee turnover, compensation levels, earnings on pension plan assets, changes in values of pension plan assets.

(4) *Actuarial cost method* means a technique which uses actuarial assumptions to measure the present value of future pension benefits and pension plan administrative expenses, and which assigns the cost of such benefits and expenses to cost accounting periods. The actuarial cost method includes the asset valuation method used to determine the actuarial value of the assets of a pension plan.

(5) *Actuarial gain and loss* means the effect on pension cost resulting from differences between actuarial assumptions and actual experience.

(6) *Actuarial valuation* means the determination, as of a specified date, of the normal cost, actuarial accrued liability, actuarial value of the assets of a pension plan, and other relevant values for the pension plan.

(7) *Assignable cost credit* means the decrease in unfunded actuarial liability that results when the pension cost computed for a cost accounting period is less than zero.

(8) *Assignable cost deficit* means the increase in unfunded actuarial liability that results when the pension cost computed for a qualified defined-benefit pension plan exceeds the maximum tax-deductible amount for the cost accounting period determined in accordance with the Employee Retirement Income Security Act of 1974

(ERISA), 29 U.S.C. 1001 *et seq.*, as amended.

(9) *Assignable cost limitation* means the excess, if any, of the actuarial accrued liability plus the current normal cost over the actuarial value of the assets of the pension plan.

(10) *Defined-benefit pension plan* means a pension plan in which the benefits to be paid or the basis for determining such benefits are established in advance and the contributions are intended to provide the stated benefits.

(11) *Defined-contribution pension plan* means a pension plan in which the contributions are established in advance and the benefits are determined thereby.

(12) *Funded pension cost* means the portion of pension cost for a current or prior cost accounting period that has been paid to a funding agency.

(13) *Funding agency* means an organization or individual which provides facilities to receive and accumulate assets to be used either for the payment of benefits under a pension plan, or for the purchase of such benefits, provided such accumulated assets form a part of a pension plan established for the exclusive benefit of the plan participants and their beneficiaries. The fair market value of the assets held by the funding agency as of a specified date is the Funding Agency Balance as of that date.

(14) *Immediate-gain actuarial cost method* means any of the several cost methods under which actuarial gains and losses are included as part of the unfunded actuarial liability of the pension plan, rather than as part of the normal cost of the plan.

(15) *Market value of the assets* means the sum of the funding agency balance plus the accumulated value of any permitted unfunded accruals belonging to a pension plan. The Actuarial Value of the Assets means the value of cash, investments, permitted unfunded accruals, and other property belonging to a pension plan, as used by the actuary for the purpose of an actuarial valuation.

(16) *Multiemployer pension plan* means a plan to which more than one employer contributes and which is maintained pursuant to one or more collective bargaining agreements between an employee organization and more than one employer.

(17) *Nonforfeitable* means a right to a pension benefit, either immediate or deferred, which arises from an employee's service, which is unconditional, and which is legally enforceable against the pension plan or the contractor. Rights to benefits that do not satisfy this definition are considered forfeitable. A right to a pension benefit is not forfeitable solely because it may be affected by the employee's or beneficiary's death, disability, or failure to achieve vesting requirements. Nor is a right considered forfeitable because it can be affected by the unilateral actions of the employee.

(18) *Normal cost* means the annual cost attributable, under the actuarial cost method in use, to current and future years as of a particular valuation date, excluding any payment in respect of an unfunded actuarial liability.

(19) *Pay-as-you-go cost method* means a method of recognizing pension cost only when benefits are paid to retired employees or their beneficiaries.

(20) *Pension plan* means a deferred compensation plan established and maintained by one or more employers to provide systematically for the payment of benefits to plan participants after their retirement, provided that the benefits are paid for life or are payable for life at the option of the employees. Additional benefits such as permanent and total disability and death payments, and survivorship payments to beneficiaries of deceased employees may be an integral part of a pension plan.

(21) *Pension plan participant* means any employee or former employee of an employer, or any member or former member of an employee organization, who is or may become eligible to receive a benefit from a pension plan which covers employees of such employer or members of such organization who have satisfied the plan's participation requirements, or whose beneficiaries are receiving or may be eligible to receive any such benefit. A participant whose employment status with the employer has not been terminated is an active participant of the employer's pension plan.

(22) *Permitted unfunded accrual* means the amount of pension cost for nonqualified defined-benefit pension plans that is not required to be funded under 9904.412–50(d)(2). The Accumulated Value of Permitted Unfunded Accruals means the value, as of the measurement date, of the permitted unfunded accruals adjusted for imputed earnings and for benefits paid by the contractor.

(23) *Prepayment credit* means the amount funded in excess of the pension cost assigned to a cost accounting period that is carried forward for future recognition. The Accumulated Value of Prepayment Credits means the value, as of the measurement date, of the prepayment credits adjusted for interest at the valuation rate and decreased for amounts used to fund pension costs or liabilities, whether assignable or not.

(24) *Projected benefit cost method* means either (i) any of the several actuarial cost methods which distribute the estimated total cost of all of the employees' prospective benefits over a period of years, usually their working careers, or (ii) a modification of the accrued benefit cost method that considers projected compensation levels.

(25) *Qualified pension plan* means a pension plan comprising a definite written program communicated to and for the exclusive benefit of employees which meets the criteria deemed essential by the Internal Revenue Service as set forth in the Internal Revenue Code for preferential tax treatment regarding contributions, investments, and distributions. Any other plan is a Nonqualified Pension Plan.

(b) * * *

4. Subsection 9904.412–40 is revised to read as follows:

9904.412–40 Fundamental requirement.

(a) *Components of pension cost.* (1) For defined-benefit pension plans, except for plans accounted for under the pay-as-you-go cost method, the components of pension cost for a cost accounting period are (i) the normal cost of the period, (ii) a part of any unfunded actuarial liability, (iii) an interest equivalent on the unamortized portion of any unfunded actuarial liability, and (iv) an adjustment for any actuarial gains and losses.

(2) For defined-contribution pension plans, the pension cost for a cost accounting period is the net contribution required to be made for that period, after taking into account dividends and other credits, where applicable.

(3) For defined-benefit pension plans accounted for under the pay-as-you-go cost method, the components of pension cost for a cost accounting period are:

(i) The net amount of periodic benefits paid for that period, and

(ii) An amortization installment, including an interest equivalent on the unamortized settlement amount, attributable to amounts paid to irrevocably settle an obligation for periodic benefits due in current and future cost accounting periods.

(b) *Measurement of pension cost.* (1) For defined-benefit pension plans other than those accounted for under the pay-as-you-go cost method, the amount of pension cost of a cost accounting period shall be determined by use of an immediate-gain actuarial cost method.

(2) Each actuarial assumption used to measure pension cost shall be separately identified and shall represent the contractor's best estimates of anticipated experience under the plan, taking into account past experience and reasonable expectations. The validity of each assumption used shall be evaluated solely with respect to that assumption. Actuarial assumptions used in calculating the amount of an unfunded actuarial liability shall be the same as those used for other components of pension cost.

(c) *Assignment of pension cost.* Except costs assigned to future periods by 9904.412–50(c) (2) and (5), the amount of pension cost computed for a cost accounting period is assignable only to that period. For defined-benefit pension plans other than those accounted for under the pay-as-you-go cost method, the pension cost is assignable only if the sum of (1) the unamortized portions of assignable unfunded actuarial liability developed and amortized pursuant to 9904.412–50(a) (1), and (2) the unassignable portions of unfunded actuarial liability separately identified and maintained pursuant to 9904.412–50(a)(2) equals the total unfunded actuarial liability.

(d) *Allocation of pension cost.* Pension costs assigned to a cost accounting period are allocable to intermediate and final cost objectives only if they meet the requirements for allocation in 9904.412–50(d). Pension costs not meeting these requirements may not be reassigned to any future cost accounting period.

5. Subsection 9904.412–50 is revised to read as follows:

9904.412–50 Techniques for application.

(a) *Components of pension cost.* (1) The following portions of unfunded actuarial liability shall be included as a separately identified part of the pension cost of a cost accounting period and shall be included in equal annual installments. Each installment shall consist of an amortized portion of the unfunded actuarial liability plus an interest equivalent on the unamortized portion of such liability. The period of amortization shall be established as follows:

(i) If amortization of an unfunded actuarial liability has begun prior to the date this Standard first becomes applicable to a contractor, no change in the amortization period is required by this Standard.

(ii) If amortization of an unfunded actuarial liability has not begun prior to the date this Standard first becomes applicable to a contractor, the amortization period shall begin with the period in which the Standard becomes applicable and shall be no more than 30 years nor less than 10 years. However, if the plan was in existence as of January 1, 1974, the amortization period shall be no more than 40 years nor less than 10 years.

(iii) Each increase or decrease in unfunded actuarial liability resulting from the institution of new pension plans, from the adoption of improvements, or other changes to pension plans subsequent to the date this Standard first becomes applicable to a contractor shall be amortized over no more than 30 years nor less than 10 years.

(iv) If any assumptions are changed during an amortization period, the resulting increase or decrease in unfunded actuarial liability shall be separately amortized over no more than 30 years nor less than 10 years.

(v) Actuarial gains and losses shall be identified separately from unfunded actuarial liabilities that are being amortized pursuant to the provisions of this Standard. The accounting treatment to be afforded to such gains and losses shall be in accordance with Cost Accounting Standard 9904.413.

(vi) Each increase or decrease in unfunded actuarial liability resulting from an assignable cost deficit or credit, respectively, shall be amortized over a period of 10 years.

(vii) Each increase or decrease in unfunded actuarial liability resulting from a change in actuarial cost method, including the asset valuation method, shall be amortized over a period of 10 to 30 years. This provision shall not affect the requirements of 9903.302 to adjust previously priced contracts.

(2) Except as provided in 9904.412–50(d)(2), any portion of unfunded actuarial liability attributable to either (i) pension costs applicable to prior years that were specifically unallowable in accordance with then existing Government contractual provisions or (ii) pension costs assigned to a cost accounting period that were not funded in that period, shall be separately identified and eliminated from any unfunded actuarial liability being amortized pursuant to paragraph (a)(1) of this subsection. Such portions of unfunded actuarial liability shall be adjusted for interest at the valuation rate of interest. The contractor may elect to fund, and thereby reduce, such portions of unfunded actuarial liability and future interest adjustments thereon. Such funding shall not be recognized for purposes of 9904.412–50(d).

(3) A contractor shall establish and consistently follow a policy for selecting specific amortization periods for unfunded actuarial liabilities, if any, that are developed under the actuarial cost method in use. Such policy may give consideration to factors such as the size and nature of the unfunded actuarial liabilities. Except as provided in 9904.412–50(c)(2) or 9904.413–50(c)(12), once the amortization period for a portion of unfunded actuarial liability is selected, the amortization process shall continue to completion.

(4) Any amount funded in excess of the pension cost assigned to a cost accounting period shall be accounted for as a prepayment credit. The accumulated value of such prepayment credits shall be adjusted for interest at the valuation rate of interest until applied towards pension cost in a future accounting period. The accumulated value of prepayment credits shall be reduced for portions of the accumulated value of prepayment credits used to fund pension costs or to fund portions of unfunded actuarial liability separately identified and maintained in accordance with 9904.412–50(a)(2). The accumulated value of any prepayment credits shall be excluded from the actuarial value of the assets used to compute pension costs for purposes of this Standard and Cost Accounting Standard 9904.413.

(5) An excise tax assessed pursuant to a law or regulation because of excess, inadequate, or delayed funding of a pension plan is not a component of pension cost. Income taxes paid from the funding agency of a nonqualified defined-benefit pension plan on earnings or other asset appreciation of such funding agency shall be treated as an administrative expense of the fund and not as a reduction to the earnings assumption.

(6) For purposes of this Standard, defined-benefit pension plans funded exclusively by the purchase of individual or group permanent insurance or annuity contracts, and thereby exempted from ERISA's minimum funding requirements, shall be treated as defined-contribution pension plans. However, all other defined-benefit pension plans administered wholly or in part through insurance company contracts shall be subject to the provisions of this Standard relative to defined-benefit pension plans.

(7) If a pension plan is supplemented by a separately-funded plan which provides retirement benefits to all of the participants in the basic plan, the two plans shall be considered as a single plan for purposes of this Standard. If the effect of the combined plans is to provide defined-benefits for the plan participants, the combined plans shall

be treated as a defined-benefit plan for purposes of this Standard.

(8) A multiemployer pension plan established pursuant to the terms of a collective bargaining agreement shall be considered to be a defined-contribution pension plan for purposes of this Standard.

(9) A pension plan applicable to a Federally-funded Research and Development Center (FFRDC) that is part of a State pension plan shall be considered to be a defined-contribution pension plan for purposes of this Standard.

(b) *Measurement of pension cost.* (1) For defined-benefit pension plans other than those accounted for under the pay-as-you-go cost method, the amount of pension cost assignable to cost accounting periods shall be measured by an immediate-gain actuarial cost method.

(2) Where the pension benefit is a function of salaries and wages, the normal cost shall be computed using a projected benefit cost method. The normal cost for the projected benefit shall be expressed either as a percentage of payroll or as an annual accrual based on the service attribution of the benefit formula. Where the pension benefit is not a function of salaries and wages, the normal cost shall be based on employee service.

(3) For defined-benefit plans accounted for under the pay-as-you-go cost method, the amount of pension cost assignable to a cost accounting period shall be measured as the sum of:

(i) The net amount for any periodic benefits paid for that period, and

(ii) The level annual installment required to amortize over 15 years any amounts paid to irrevocably settle an obligation for periodic benefits due in current or future cost accounting periods.

(4) Actuarial assumptions shall reflect long-term trends so as to avoid distortions caused by short-term fluctuations.

(5) Pension cost shall be based on provisions of existing pension plans. This shall not preclude contractors from making salary projections for plans whose benefits are based on salaries and wages, or from considering improved benefits for plans which provide that such improved benefits must be made.

(6) If the evaluation of the validity of actuarial assumptions shows that any assumptions were not reasonable, the contractor shall:

(i) Identify the major causes for the resultant actuarial gains or losses, and

(ii) Provide information as to the basis and rationale used for retaining or revising such assumptions for use in the ensuing cost accounting period(s).

(c) *Assignment of pension cost.* (1) Amounts funded in excess of the pension cost computed for a cost accounting period pursuant to the provisions of this Standard shall be accounted for as a prepayment credit and carried forward to future accounting periods.

(2) For qualified defined-benefit pension plans, the pension cost computed for a cost accounting period is assigned to that period subject to the following adjustments, in order of application:

(i) Any amount of computed pension cost that is less than zero shall be assigned to future accounting periods as an assignable cost credit. The amount of pension cost assigned to the period shall be zero.

(ii) When the pension cost equals or exceeds the assignable cost limitation:

(A) The amount of computed pension cost, adjusted pursuant to paragraph (c)(2)(i) of this subsection, shall not exceed the assignable cost limitation,

(B) All amounts described in 9904.412–50(a)(1) and 9904.413–50(a), which are required to be amortized, shall be considered fully amortized, and

(C) Except for portions of unfunded actuarial liability separately identified and maintained in accordance with 9904.413–50(a)(2), any portion of unfunded actuarial liability, which occurs in the first cost accounting period after the pension cost has been limited by the assignable cost limitation, shall be considered an actuarial gain or loss for purposes of this Standard. Such actuarial gain or loss shall exclude any increase or decrease in unfunded actuarial liability resulting from a plan amendment, change in actuarial assumptions, or change in actuarial cost method effected after the pension cost has been limited by the assignable cost limitation.

(iii) Any amount of computed pension cost of a qualified pension plan, adjusted pursuant to paragraphs (c)(2)(i) and (ii) of this subsection that exceeds the sum of (A) the maximum tax-deductible amount, determined in accordance with ERISA, and (B) the accumulated value of prepayment credits shall be assigned to future accounting periods as an assignable cost deficit. The amount of pension cost assigned to the current period shall not exceed the sum of the maximum tax-deductible amount plus the accumulated value of prepayment credits.

(3) The cost of nonqualified defined-benefit pension plans shall be assigned to cost accounting periods in the same manner as qualified plans (with the exception of paragraph (c)(2)(iii) of this subsection) under the following conditions:

(i) The contractor, in disclosing or establishing his cost accounting practices, elects to have a plan so accounted for;

(ii) The plan is funded through the use of a funding agency; and,

(iii) The right to a pension benefit is nonforfeitable and is communicated to the participants.

(4) The costs of nonqualified defined-benefit pension plans that do not meet all of the requirements in 9904.412–50(c)(3) shall be assigned to cost accounting periods using the pay-as-you-go cost method.

(5) Any portion of pension cost computed for a cost accounting period that exceeds the amount required to be funded pursuant to a waiver granted under the provisions of ERISA shall not be assigned to the current period. Rather, such excess shall be treated as an assignable cost deficit, except that it shall be assigned to future cost accounting periods using the same amortization period as used for ERISA purposes.

(d) *Allocation of pension costs.* The amount of pension cost assigned to a cost accounting period allocated to intermediate and final cost objectives shall be limited according to the following criteria:

(1) Except for nonqualified defined-benefit plans, the costs of a pension plan assigned to a cost accounting period are allocable to the extent that they are funded.

(2) For nonqualified defined-benefit pension plans that meet the criteria set forth at 9904.412–50(c)(3), pension costs assigned to a cost accounting period are fully allocable if they are funded at a level at least equal to the percentage of the complement (i.e., 100%-tax rate % = percentage of assigned cost to be funded) of the highest published Federal corporate income tax rate in effect on the first day of the cost accounting period. If the contractor is not subject to Federal income tax, the assigned costs are allocable to the extent such costs are funded. Funding at other levels and benefit payments of such plans are subject to the following:

(i) Funding at less than the foregoing levels shall result in proportional reductions of the amount of assigned cost that can be allocated within the cost accounting period.

(ii) (A) Payments to retirees or beneficiaries shall contain an amount drawn from sources other than the funding agency of the pension plan that is, at least, proportionately equal to the accumulated value of permitted unfunded accruals divided by an amount that is the market value of the assets of the pension plan excluding any accumulated value of prepayment credits.

(B) The amount of assigned cost of a cost accounting period that can be allocated shall be reduced to the extent that such payments are drawn in a higher ratio from the funding agency.

(iii) The permitted unfunded accruals shall be identified and accounted for year to year, adjusted for benefit payments directly paid by the contractor and for interest at the actual annual earnings rate on the funding agency balance.

(3) For nonqualified defined-benefit pension plans accounted for under the pay-as-you-go method, pension costs assigned to a cost accounting period are allocable in that period.

(4) Funding of pension cost shall be considered to have taken place within the cost accounting period if it is accomplished by the corporate tax filing date for such period including any permissible extensions thereto.

6. Subsection 9904.412–60 is revised to read as follows:

9904.412–60 Illustrations.

(a) *Components of pension cost.* (1) Contractor A has insured pension plans for each of two small groups of employees. One plan is exclusively funded through a group permanent life insurance contract and is exempt from the minimum funding requirements of ERISA. The other plan is funded through a deposit administration contract, which is a form of group deferred annuity contract that is not exempt from ERISA's minimum funding requirements. Both plans provide for defined benefits. Pursuant to 9904.412–50(a)(6), for purposes of this Standard the plan financed through a group permanent insurance contract shall be considered to be a defined-contribution pension plan; the net premium required to be paid for a cost accounting period (after deducting dividends and any credits) shall be the pension cost for that period. However, the deposit administration contract plan is subject to the provisions of this Standard that are applicable to defined-benefit plans.

(2) Contractor B provides pension benefits for certain hourly employees through a multiemployer defined-benefit plan. Under the collective bargaining agreement, the contractor pays six cents into the fund for each hour worked by the covered employees. Pursuant to 9904.412–50(a)(8), the plan shall be considered to be a defined-contribution pension plan. The payments required to be made for a cost accounting period shall constitute the assignable pension cost for that period.

(3) Contractor C provides pension benefits for certain employees through a defined-contribution pension plan. However, the contractor has a separate fund that is used to supplement pension benefits for all of the participants in the basic plan in order to provide a minimum monthly retirement income to each participant. Pursuant to 9904.412–50(a)(7), the two plans shall be considered as a single plan for purposes of this Standard. Because the effect of the supplemental plan is to provide defined-benefits for the plan's participants, the provisions of this Standard relative to defined-benefit pension plans shall be applicable to the combined plan.

(4) Contractor D provides supplemental benefits to key management employees through a nonqualified defined-benefit pension plan funded by a so-called ''Rabbi Trust.'' The trust agreement provides that Federal income taxes levied on the earnings of the Rabbi trust may be paid from the trust. The contractor's actuarial cost method recognizes the administrative expenses of the plan and trust, such as broker and attorney fees, by adding the prior year's expenses to the current year's normal cost. The income taxes paid by the trust on trust earnings shall be accorded the same treatment as any other administrative expense in accordance with 9904.412–50(a)(5).

(5) (i) Contractor E has been using the entry age normal actuarial cost method to compute pension costs. The contractor has three years remaining under a firm fixed price contract subject to this Standard. The contract was priced using the unfunded actuarial liability, normal cost, and net amortization installments developed using the entry age normal method. The contract was priced as follows:

ENTRY AGE NORMAL VALUES

Cost component	Year 1	Year 2	Year 3
Normal cost	$100,000	$105,000	$110,000
Amortization	50,000	50,000	50,000
Pension cost	150,000	155,000	160,000

(ii) The contractor, after notifying the cognizant Federal official, switches to the projected unit credit actuarial cost method. The unfunded actuarial liability and normal cost decreased when redetermined under the projected unit credit method. Pursuant to 9904.412–50(a)(1)(vii), the contractor determines that an annual installment credit of $20,000 will amortize the decrease in unfunded actuarial liability (UAL) over ten years. The following pension costs are determined under the projected unit credit method:

PROJECTED UNIT CREDIT VALUES

Cost component	Year 1	Year 2	Year 3
Normal cost	$80,000	$85,000	$90,000
Amortization:			
Prior method	50,000	50,000	50,000
UAL decrease	(20,000)	(20,000)	(20,000)
Pension cost	110,000	115,000	120,000

(iii) The change in cost method is a change in accounting method that decreased previously priced pension costs by $40,000 per year. In accordance with 9903.302, Contractor E shall adjust the cost of the firm fixed-price contract for the remaining three years by $120,000 ($40,000×3 years).

(6) Contractor F has a defined-benefit pension plan for its employees. Prior to being subject to this Standard the contractor's policy was to compute and fund as annual pension cost normal cost plus only interest on the unfunded actuarial liability. Pursuant to 9904.412–40(a)(1), the components of pension cost for a cost accounting period must now include not only the normal cost for the period and interest on the unfunded actuarial liability, but also an amortized portion of the unfunded actuarial liability. The amortization of the liability and the interest equivalent on the unamortized portion of the liability must be computed in equal annual installments.

(b) *Measurement of pension cost.* (1) Contractor G has a pension plan whose costs are assigned to cost accounting periods by use of an actuarial cost method that does not separately identify actuarial gains and losses or the effect on pension cost resulting from changed actuarial assumptions. Contractor G's method is not an immediate-gain cost method and does not comply with the provisions of 9904.412–50(b)(1).

(2) For several years Contractor H has had an unfunded nonqualified pension plan which provides for payments of $200 a month to employees after retirement. The contractor is currently making such payments to several retired employees and recognizes those payments as its pension cost. The contractor paid monthly annuity benefits totaling $24,000 during the current year. During the prior year, Contractor H made lump sum payments to irrevocably settle the benefit liability of several participants with small benefits. The annual installment to amortize these lump sum payments over fifteen years at the valuation interest rate assumption is $5,000. Since the plan does not meet the criteria set forth in 9904.412–50(c)(3)(ii), pension cost must be accounted for using the pay-as-you-go cost method. Pursuant to 9904.412–50(b)(3), the amount of assignable cost allocable to cost objectives of that period is $29,000, which is the sum of the amount of benefits actually paid in that period ($24,000) plus the second annual installment to amortize the prior year's lump sum settlements ($5,000).

(3) Contractor I has two qualified defined-benefit pension plans that provide for fixed dollar payments to hourly employees. Under the first plan, the contractor's actuary believes that the contractor will be required to increase the level of benefits by specified percentages over the next several years. In calculating pension costs, the contractor may not assume future benefits greater than that currently required by the plan. With regard to the second plan, a collective bargaining agreement negotiated with the employees' labor union provides that pension benefits will increase by specified percentages over the next several years. Because the improved benefits are required to be made, the contractor can consider such increased benefits in computing pension costs for the current cost accounting period in accordance with 9904.412–50(b)(5).

(4) In addition to the facts of 9904.412–60(b)(3), assume that Contractor I was required to contribute at a higher level for ERISA purposes because the plan was underfunded. To compute pension costs that are closer to the funding requirements of ERISA, Contractor I decides to ''fresh start'' the unfunded actuarial liability being amortized pursuant to 9904.412–50(a)(1); i.e., treat the entire amount as a newly established portion of unfunded actuarial liability, which is amortized over 10 years in accordance with 9904.412–50(a)(1)(ii). Because the contractor has changed the periods for amortizing the unfunded actuarial liability established pursuant to 9904.412–50(a)(3), the contractor has made a change in accounting practice subject to the provisions of Cost Accounting Standard 9903.302.

(c) *Assignment of pension cost.* (1) Contractor J maintains a qualified defined-benefit pension plan. The actuarial value of the assets of $18 million is subtracted from the actuarial accrued liability of $20 million to determine the total unfunded actuarial liability of $2 million. Pursuant to 9904.412–50(a)(1), Contractor J has identified and is amortizing twelve separate portions of unfunded actuarial liabilities. The sum of the unamortized balances for the twelve separately maintained portions of unfunded actuarial liability equals $1.8 million. In accordance with 9904.412–50(a)(2), the contractor has separately identified, and eliminated from the computation of pension cost, $200,000 attributable to a pension cost assigned to a prior period that was not funded. The sum of the twelve amortization bases maintained pursuant to 9904.412–50(a)(1) and the amount separately identified under 9904.412–50(a)(2) equals $2 million ($1,800,000+200,000). Because the sum of all identified portions of unfunded actuarial liability equals the total unfunded actuarial liability, the plan is in actuarial balance and Contractor J can assign pension cost to the current cost accounting period in accordance with 9904.412–40(c).

(2) Contractor K's pension cost computed for 1996, the current year, is $1.5 million. This computed cost is based on the components of pension cost described in 9904.412–40(a) and 9904.412–50(a) and is measured in accordance with 9904.412–40(b) and 9904.412–50(b). The assignable cost limitation, which is defined at 9904.412–30(a)(9), is $1.3 million. In accordance with the provisions of 9904.412–50(c)(2)(ii)(A), Contractor K's assignable pension cost for 1996 is limited to $1.3 million. In addition, all amounts that were previously being amortized pursuant to 9904.412–50(a)(1) and 9904.413–50(a) are considered fully amortized in accordance with 9904.412–50(c)(2)(ii)(B). The following year, 1997, Contractor K computes an unfunded actuarial liability of $4 million. Contractor K has not changed his actuarial assumptions nor amended the provisions of his pension plan. Contractor K has not had any pension costs disallowed or unfunded in prior periods. Contractor K must treat the entire $4 million of unfunded actuarial liability as an actuarial loss to be amortized over fifteen years beginning in 1997 in accordance with 9904.412–50(c)(2)(ii)(C).

(3) Assume the same facts shown in illustration 9904.412–60(c)(2), except that in 1995, the prior year, Contractor K's assignable pension cost was $800,000, but Contractor K only funded and allocated $600,000. Pursuant to 9904.412–50(a)(2), the $200,000 of unfunded assignable pension cost was separately identified and eliminated from other portions of unfunded actuarial liability. This portion of unfunded actuarial liability was adjusted for 8% interest, which is the interest assumption for 1995 and 1996, and was brought forward to 1996 in accordance with 9904.412–50(a)(2). Therefore, $216,000 ($200,000×1.08) is excluded from the amount considered fully amortized in 1996. The next year, 1997, Contractor K must eliminate $233,280 ($216,000×1.08) from the $4 million so that only $3,766,720 is treated as an actuarial loss in accordance with 9904.412–50(c)(2)(ii)(C).

(4) Assume, as in 9904.412–60(c)(2), the 1996 pension cost computed for Contractor K's qualified defined-benefit pension plan is $1.5 million and the assignable cost limitation is $1.7

million. However, because of the ERISA limitation on tax-deductible contributions, Contractor K cannot fund more than $1 million without incurring an excise tax, which 9904.412–50(a)(5) does not permit to be a component of pension cost. In accordance with the provisions of 9904.412–50(c)(2)(iii), Contractor K's assignable pension cost for the period is limited to $1 million. The $500,000 ($1.5 million − $1 million) of pension cost not funded is reassigned to the next ten cost accounting periods beginning in 1997 as an assignable cost deficit in accordance with 9904.412–50(a)(1)(vi).

(5) Assume the same facts for Contractor K in 9904.412–60(c)(4), except that the accumulated value of prepayment credits equals $700,000. Therefore, in addition to the $1 million, Contractor K can apply $500,000 of the accumulated value of prepayment credits towards the pension cost computed for the period. In accordance with the provisions of 9904.412–50(c)(2)(iii), Contractor K's assignable pension cost for the period is the full $1.5 million ($1 million+$500,000) computed for the period. The $200,000 of remaining accumulated value of prepayment credits ($700,000 − $500,000) is adjusted for interest at the valuation rate and carried forward until needed in future accounting periods in accordance with 9904.412–50(a)(4).

(6) Assume the same facts for Contractor K in 9904.412–60(c)(4), except that the 1996 assignable cost limitation is $1.3 million. Pension cost of $1.5 million is computed for the cost accounting period, but the assignable cost is limited to $1.3 million in accordance with 9904.412–50(c)(2)(ii)(A). Pursuant to 9904.412–50(c)(2)(ii)(B), all existing amortization bases maintained in accordance with subparagraph 9904.412–50(a)(1) are considered fully amortized. The assignable cost of $1.3 million is then compared to the maximum tax-deductible amount of $1 million. Pursuant to 9904.412–50(c)(2)(iii), Contractor K's assignable pension cost for the period is limited to $1 million. The $300,000 ($1.3 million − $1 million) excess of the assignable cost limitation over the tax-deductible maximum is assigned to future periods as an assignable cost deficit.

(7) Contractor L is currently amortizing a large decrease in unfunded actuarial liability over a period of ten years. A similarly large increase in unfunded actuarial liability is being amortized over 30 years. The absolute value of the resultant net amortization credit is greater than the normal cost so that the pension cost computed for the period is a negative $200,000. Contractor L first applies the provisions of 9904.412–50(c)(2)(i) and determines the assignable pension cost is $0. The negative pension cost of $200,000 is assigned to the next ten cost accounting periods as an assignable cost credit in accordance with 9904.412–50(a)(1)(vi). However, when Contractor L applies the provisions of 9904.412–50(c)(2)(ii), the assignable cost limitation is also $0. Because the assignable cost of $0 determined under 9904.412–50(c)(2)(i) is equal to the assignable cost limitation, the assignable cost credit of $200,000 is considered fully amortized along with all other portions of unfunded actuarial liability being amortized pursuant to 9904.412–50(a)(1). Conversely, if the assignable cost limitation had been greater than zero, the assignable cost credit of $200,000 would have carried-forward and amortized in future periods.

(8) Contractor M has a qualified defined-benefit pension plan which is funded through a funding agency. It computes $1 million of pension cost for a cost accounting period. However, pursuant to a waiver granted under the provisions of ERISA, Contractor M is required to fund only $800,000. Under the provisions of 9904.412–50(c)(5), the remaining $200,000 shall be accounted for as an assignable cost deficit and assigned to the next five cost accounting periods in accordance with the terms of the waiver.

(9) Contractor N has a company-wide defined-benefit pension plan, wherein benefits are calculated on one consistently applied formula. That part of the formula defining benefits within ERISA limits is administered and reported as a qualified plan and funded through a funding agency. The remainder of the benefits are considered to be a supplemental or excess plan which, while it meets the criteria at 9904.412–50(c)(3)(iii) as to nonforfeitability and communication, is not funded. The costs of the qualified portion of the plan shall be comprised of those elements of costs delineated at 9904.412–40(a)(1), while the supplemental or excess portion of the plan shall be accounted for and assigned to cost accounting periods under the pay-as-you-go cost method provided at 9904.412–40(a)(3) and 9904.412–50(c)(4).

(10) Assuming the same facts as in 9904.412–60(c)(9), except that Contractor N funds its supplemental or excess plan using a so-called ''Rabbi Trust'' vehicle. Because the nonqualified plan is funded, the plan meets the criteria set forth at 9904.412–50(c)(3)(ii). Contractor N may account for the supplemental or excess plan in the same manner as its qualified plan, if it elects to do so pursuant to 9904.412–50(c)(3)(i).

(11) Assuming the same facts as in 9904.412–60(c)(10), except that under the nonqualified portion of the pension plan a former employee will forfeit his pension benefit if the employee goes to work for a competitor within three years of terminating employment. Since the right to a benefit cannot be affected by the unilateral action of the contractor, the right to a benefit is considered to be nonforfeitable for purposes of 9904.412–30(a)(17). The nonqualified plan still meets the criteria set forth at 9904.412–50(c)(3)(iii), and Contractor N may account for the supplemental or excess plan in the same manner as its qualified plan, if it elects to do so.

(12) Assume the same facts as in 9904.412–60(c)(11), except that Contractor N, while maintaining a ''Rabbi Trust'' funding vehicle elects to have the plan accounted for under the pay-as-you-go cost method so as to have greater latitude in annual funding decisions. It may so elect pursuant to 9904.412–50(c)(3)(i).

(13) The assignable pension cost for Contractor O's qualified defined-benefit plan is $600,000. For the same period Contractor O contributes $700,000, which is the minimum funding requirement under ERISA. In addition, there exists $75,000 of unfunded actuarial liability that has been separately identified pursuant to 9904.412–50(a)(2). Contractor O may use $75,000 of the contribution in excess of the assignable pension cost to fund this separately identified unfunded actuarial liability, if he so chooses. The effect of the funding is to eliminate the unassignable $75,000 portion of unfunded actuarial liability that had been separately identified and thereby eliminated from the computation of pension costs. Contractor O shall then account for the remaining $25,000 of excess contribution as a prepayment credit in accordance with 9904.412–50(a)(4).

(d) *Allocation of pension cost.* (1) Assume the same set of facts for Contractor M in 9904.412–60(c)(8) except there was no ERISA waiver; i.e., only $800,000 was funded against $1 million of assigned pension cost for the period. Under the provisions of 9904.412–50(d)(1), only $800,000 may be allocated to Contractor M's intermediate and final cost objectives. The remaining $200,000 of assigned cost, which has not been funded, shall be separately identified and maintained in accordance with 9904.412–50(a)(2) so that it will not be reassigned to any future accounting periods.

(2) Contractor P has a nonqualified defined-benefit pension plan which covers benefits in excess of the ERISA limits. Contractor P has elected to account for this plan in the same manner as its qualified plan and, therefore, has established a ''Rabbi Trust'' as the funding agency. For the current cost accounting period, the contractor computes and assigns $100,000 as pension cost. The contractor funds $65,000, which is equivalent to a funding level equal to the complement of the highest published Federal corporate income tax rate of 35%. Under the provisions of 9904.412–50(d)(2), the entire $100,000 is allocable to cost objectives of the period.

(3) Assume the set of facts in 9904.412–60(d)(2), except that Contractor P's contribution to the Trust is $59,800. In that event, the provisions of 9904.412–50(d)(2)(i) would limit the amount of assigned cost allocable within the cost accounting period to the percentage of cost funded (i.e., $59,800/ $65,000 = 92%). This results in allocable cost of $92,000 (92% of $100,000) for the cost accounting period. Under the provisions of 9904.412–40(c) and 9904.412–50(d)(2)(i), respectively, the unallocable $8,000 may not be assigned to any future cost accounting period. In addition, in accordance with 9904.412–50(a)(2), the $8,000 must be separately identified and no amount of interest on such separately identified $8,000 shall be a component of pension cost in any future cost accounting period.

(4) Again, assume the set of facts in 9904.412–60(d)(2) except that, Contractor P's contribution to the Trust is $105,000 based on a valuation interest assumption of 8%. Under the provisions of 9904.412–50(d)(2) the entire $100,000 is allocable to cost objectives of the period. In accordance with the provisions of 9904.412–50(c)(1) Contractor P has funded $5,000 ($105,000—$100,000) in excess of the assigned pension cost for the period. The $5,000 shall be accounted for as a prepayment credit. Pursuant to 9904.412–50(a)(4), the $5,000 shall be adjusted for interest at the 8% valuation rate of interest and excluded from the actuarial value of assets used to compute the next year's pension cost computations. The accumulated value of prepayment credits of $5,400 (5,000 × 1.08) may be used to fund the next year's assigned pension cost, if needed.

(5) Contractor Q maintains a nonqualified defined-benefit pension plan which satisfies the requirements of 9904.412–50(c)(3). As of the valuation date, the reported funding agency balance is $3.4 million excluding any accumulated value of prepayment credits. When the adjusted funding agency balance is added to the accumulated value of permitted unfunded accruals of $1.6 million, the market value of assets equals $5.0 million ($3.4 million + $1.6 million) in accordance with 9904.412–30(a)(13). During the plan year, retirees receive monthly benefits totalling $350,000. Pursuant to 9904.412–50(d)(2)(ii)(A), at least 32% ($1.6 million divided by $5 million) of these benefit payments shall be made from sources other than the funding agency. Contractor Q, therefore, draws $238,000 from the funding agency assets and pays the remaining $112,000 using general corporate funds.

(6) Assume the same facts as 9904.412–60(d)(5), except that by the time Contractor Q receives its actuarial valuation it has paid retirement benefits equalling $288,000 from funding agency assets. The contractor has made deposits to the funding agency equal to the tax complement of the $500,000 assignable pension cost for the period. Pursuant to 9904.412–50(d)(2)(ii)(B), the assignable $500,000 shall be reduced by the $50,000 ($288,000—$238,000) of benefits paid from the funding agency in excess of the permitted $238,000, unless the contractor makes a deposit to replace the $50,000 inadvertently drawn from the funding agency. If this corrective action is not taken within the time permitted by 9904.412–50(d)(4), Contractor Q shall allocate only $450,000 ($500,000–$50,000) to final cost objectives. Furthermore, the $50,000, which was thereby attributed to benefit payments instead of funding, must be separately identified and maintained in accordance with 9904.412–50(a)(2).

(7) Contractor R has a nonqualified defined-benefit plan that meets the criteria of 9904.412–50(c)(3). For 1996, the funding agency balance was $1,250,000 and the accumulated value of permitted unfunded accruals was $600,000. During 1996 the earnings and appreciation on the assets of the funding agency equalled $125,000, benefit payments to participants totalled $300,000, and administrative expenses were $60,000. All transactions occurred on the first day of the period. In accordance with 9904.412–50(d)(2)(ii)(A), $200,000 of benefits were paid from the funding agency and $100,000 were paid directly from corporate assets. Pension cost of $400,000 was assigned to 1996. Based on the current corporate tax rate of 35%, $260,000 ($400,000 × (1–35%)) was deposited into the funding agency at the beginning of 1996. For 1997 the funding agency balance is $1,375,000 ($1,250,000 + $260,000 + $125,000—$200,000—$60,000). The actual annual earnings rate of the funding agency was 10% for 1996. Pursuant to 9904.412–50(d)(2)(iii), the accumulated value of permitted unfunded accruals is updated from 1996 to 1997 by: (i) adding $140,000 (35% × $400,000), which is the unfunded portion of the assigned cost; (ii) subtracting the $100,000 of benefits paid directly by the contractor; and (iii) increasing the value of the assets by $64,000 for imputed earnings at 10% (10% × ($600,000 + $140,000—$100,000)). The accumulated value of permitted unfunded accruals for 1997 is $704,000 ($600,000 + $140,000—$100,000 + $64,000).

7. Subsection 9904.412–63 is revised to read as follows:

9904.412–63 Effective date.

(a) This Standard is effective as of March 30, 1995.

(b) This Standard shall be followed by each contractor on or after the start of its next cost accounting period beginning after the receipt of a contract or subcontract to which this Standard is applicable.

(c) Contractors with prior CAS-covered contracts with full coverage shall continue to follow the Standard in 9904.412 in effect prior to March 30, 1995, until this Standard, effective March 30, 1995, becomes applicable following receipt of a contract or subcontract to which this Standard applies.

8. A new subsection 9904.412–64 is added to read as follows:

9904.412–64 Transition method.

To be acceptable, any method of transition from compliance with Standard 9904.412 in effect prior to March 30, 1995, to compliance with the Standard effective March 30, 1995, must follow the equitable principle that costs, which have been previously provided for, shall not be redundantly provided for under revised methods. Conversely, costs that have not previously been provided for must be provided for under the revised method. This transition subsection is not intended to qualify for purposes of assignment or allocation, pension costs which have previously been disallowed for reasons other than ERISA tax-deductibility limitations. The sum of all portions of unfunded actuarial liability identified pursuant to Standard 9904.412, effective March 30, 1995, including such portions of unfunded actuarial liability determined for transition purposes, is subject to the provisions of 9904.412–40(c) on requirements for assignment. The method, or methods, employed to achieve an equitable transition shall be consistent with the provisions of Standard 9904.412, effective March 30, 1995, and shall be approved by the contracting officer. Examples and illustrations of such transition methods include, but are not limited to, the following:

(a) *Reassignment of certain prior unfunded accruals.*

(1) Any portion of pension cost for a qualified defined-benefit pension plan, assigned to a cost accounting period prior to [insert date of publication in the **Federal Register**], which was not funded because such cost exceeded the maximum tax-deductible amount, determined in accordance with ERISA, shall be assigned to subsequent accounting periods, including an adjustment for interest, as an assignable cost deficit. However, such costs shall be assigned to periods on or after March 30, 1995, only to the extent that such costs have not previously been allocated as cost or price to contracts subject to this Standard.

(2) Alternatively, the transition method described in paragraph (d) of this subsection may be applied separately to costs subject to paragraph (a)(1) of this subsection.

(b) *Reassignment of certain prior unallocated credits.*

(1) Any portion of pension cost for a defined-benefit pension plan, assigned to a cost accounting period prior to March 30, 1995, which was not allocated as a cost or price credit to contracts subject to this Standard because such cost was less than zero, shall be assigned to subsequent accounting periods, including an adjustment for interest, as an assignable cost credit.

(2) Alternatively, the transition method described in paragraph (d) of this subsection may be applied separately to costs subject to paragraph (b)(1) of this subsection.

(c) *Accounting for certain prior allocated unfunded accruals.* Any portion of unfunded pension cost for a nonqualified defined-benefit pension plan, assigned to a cost accounting period prior to March 30, 1995, that was allocated as cost or price to contracts subject to this Standard, shall be recognized in subsequent accounting periods, including adjustments for imputed interest and benefit payments, as an accumulated value of permitted unfunded accruals.

(d) *''Fresh start'' alternative transition method.* The transition methods of paragraphs (a)(1), (b)(1), and (c) of this subsection may be implemented using the so-called ''fresh start'' method whereby a portion of the unfunded actuarial liability of a defined-benefit pension plan, which occurs in the first cost accounting period after March 30, 1995, shall be treated in the same manner as an actuarial gain or loss. Such portion of unfunded actuarial liability shall exclude any portion of unfunded actuarial liability that must continue to be separately identified and maintained in accordance with 9904.412–50(a)(2), including interest adjustments. If the contracting officer already has approved a different amortization period for the fresh start amortization, then such amortization period shall continue.

(e) *Change to pay-as-you-go method.* A change in accounting method subject to 9903.302 will have occurred whenever costs of a nonqualified defined-benefit pension plan have been accounted for on an accrual basis prior to March 30, 1995, and the contractor must change to the pay-as-you-go cost method because the plan does not meet the requirement of 9904.412–50(c)(3), either by election or otherwise. In such case, any portion of unfunded pension cost, assigned to a cost accounting period prior to March 30, 1995 that was allocated as cost or price to contracts subject to this Standard, shall be assigned to future accounting periods, including adjustments for imputed interest and benefit payments, as an accumulated value of permitted unfunded accruals. Costs computed under the pay-as-you-go cost method shall be charged against such accumulated value of permitted unfunded accruals before such costs may be allocated to contracts.

(f) *Actuarial assumptions.* The actuarial assumptions used to calculate assignable cost deficits, assignable cost credits, or accumulated values of permitted unfunded accruals for transition purposes shall be consistent with the long term assumptions used for valuation purposes for such prior periods unless the contracting officer has previously approved the use of other reasonable assumptions.

(g) *Transition illustrations.* Unless otherwise noted, paragraphs (g) (1) through (9) of this subsection address pension costs and transition amounts determined for the first cost accounting period beginning on or after the date this revised Standard becomes applicable to a contractor. For purposes of these illustrations an interest assumption of 7% is presumed to be in effect for all periods.

(1) For the cost accounting period immediately preceding the date this revised Standard was applicable to a contractor, Contractor S computed and assigned pension cost of $1 million for a qualified defined-benefit pension plan. The contractor made a contribution equal to the maximum tax-deductible amount of $800,000 for the period leaving $200,000 of assigned cost unfunded for the period. Except for this $200,000, no other assigned pension costs have ever been unfunded or otherwise disallowed. Using the transition method of paragraph (a)(1) of this subsection, the contractor shall establish an assignable cost deficit equal to $214,000 ($200,000 × 1.07), which is the prior unfunded assigned cost plus interest. If this assignable cost deficit amount, plus all other portions of unfunded actuarial liability identified in accordance with 9904.412–50(a) (1) and (2), equal the total unfunded actuarial liability, pension cost may be assigned to the current period.

(2) Assume that Contractor S in 9904.412–64(g)(1) priced the entire $1 million into firm fixed-price contracts. In this case, no assignable cost deficit amount may be established. In addition, the $214,000 ($200,000 × 1.07) shall be separately identified and maintained in accordance with 9904.412–50(a)(2). If all portions of unfunded actuarial liability identified in accordance with 9904.412–50(a) (1) and (2), equal the total unfunded actuarial liability, pension cost may be assigned to the period.

(3) Assume the same facts as in 9904.412–64(g)(1), except Contractor S only funded and allocated $500,000. The $300,000 of assigned cost that was not funded, but could have been funded without exceeding the tax-deductible maximum, may not be recognized as an assignable cost deficit. Instead, the $300,000 must be separately identified and maintained in accordance with 9904.412–50(a)(2). If the $321,000 ($300,000 × 1.07) plus the $214,000 already identified as an assignable cost deficit plus all other portions of unfunded actuarial liability identified in accordance with 9904.412–50(a) (1) and (2), equal the total unfunded actuarial liability, pension cost may be assigned to the period.

(4) Assume that, for Contractor S in 9904.412–64(g)(3), the only portion of unfunded actuarial liability that must be identified under 9904.412–50(a)(2) is the $321,000. If Contractor S chooses to use the ''fresh start'' transition method, the $321,000 of unfunded assigned cost must be subtracted from the total unfunded actuarial liability in accordance with 9904.412–63(d). The net amount of unfunded actuarial liability shall then be amortized over a

period of fifteen years as an actuarial loss in accordance with 9904.412–50(a)(1)(v) and Cost Accounting Standard 9904.413.

(5) For the cost accounting period immediately preceding the date this revised Standard becomes applicable to a contractor, Contractor T computed and assigned pension cost of negative $400,000 for a qualified defined-benefit plan. Because the contractor could not withdraw assets from the trust fund, the contracting officer agreed that instead of allocating a current period credit to contracts, the negative costs would be carried forward, with interest, and offset against future pension costs allocated to the contract. Using the transition method of paragraph (b)(1) of this subsection, the contractor shall establish an assignable cost credit equal to $428,000 ($400,000 × 1.07). If this assignable cost credit amount, plus all other portions of unfunded actuarial liability identified in accordance with 9904.412–50(a) (1) and (2), equals the total unfunded actuarial liability, pension cost may be assigned to the period.

(6) Assume that in 9904.412–64(g)(5), following guidance issued by the contracting agency the contracting officer had deemed the cost for the prior period to be $0. In order to satisfy the requirements of 9904.412–40(c) and assign pension cost to the current period, Contractor S must account for the prior period negative accruals that have not been specifically identified. Following the transition method of paragraph (b)(1) of this subsection, the contractor shall identify $428,000 as an assignable cost credit.

(7) Assume the facts of 9904.412–64(g)(5), except Contractor S uses the ‘‘fresh start’’ transition method. In addition, for the current period the plan is overfunded since the actuarial value of the assets is greater than the actuarial accrued liability. In this case, an actuarial gain equal to the negative unfunded actuarial liability; i.e., actuarial surplus, is recognized since there are no portions of unfunded actuarial liability that must be identified under 9904.412–50(a)(2).

(8) Since March 28, 1989 Contractor U has computed, assigned, and allocated pension costs for a nonqualified defined-benefit plan on an accrual basis. The value of these past accruals, increased for imputed interest at 7% and decreased for benefits paid by the contractor, is equal to $2 million as of the beginning of the current period. Contractor U elects to establish a ‘‘Rabbi trust’’ and the plan meets the other criteria at 9904.412–50(c)(3). Using the transition method of paragraph (c) of this subsection, Contractor U shall recognize the $2 million as the accumulated value of permitted unfunded accruals, which will then be included in the market value and actuarial value of the assets. Because the accumulated value of permitted unfunded accruals is exactly equal to the current period market value of the assets, 100% of benefits for the current period must be paid from sources other than the funding agency in accordance with 9904.412–50(d)(2)(ii).

(9) Assume that Contractor U in 9904.412–64(g)(8) establishes a funding agency, but elects to use the pay-as-you-go method for current and future pension costs. Furthermore, plan participants receive $500,000 in benefits on the last day of the current period. Using the transition method of paragraph (e) of this subsection to ensure prior costs are not redundantly provided for, the contractor shall establish assets; i.e., an accumulated value of permitted unfunded accruals, of $2 million. Since these assets are sufficient to provide for the current benefit payments, no pension costs can be allocated in this period. Furthermore, previously priced contracts subject to this Standard shall be adjusted in accordance with 9903.302. The accumulated value of permitted unfunded accruals shall be carried forward to the next period by adding $140,000 (7% x $2 million) of imputed interest, and subtracting the $500,000 of benefit payments made by the contractor. The accumulated value of permitted unfunded accruals for the next period equals $1,640,000 ($2 million + $140,000—$500,000).

9904.413 [Amended]

9. Subsection 9904.413–30 is amended by revising paragraph (a) to read as follows:

9904.413–30 Definitions.

(a) The following are definitions of terms which are prominent in this Standard. Other terms defined elsewhere in this chapter 99 shall have the meaning ascribed to them in those definitions unless paragraph (b) of this subsection requires otherwise.

(1) *Accrued benefit cost method* means an actuarial cost method under which units of benefits are assigned to each cost accounting period and are valued as they accrue; that is, based on the services performed by each employee in the period involved. The measure of normal cost under this method for each cost accounting period is the present value of the units of benefit deemed to be credited to employees for service in that period. The measure of the actuarial accrued liability at a plan's inception date is the present value of the units of benefit credited to employees for service prior to that date. (This method is also known as the Unit Credit cost method without salary projection.)

(2) *Actuarial accrued liability* means pension cost attributable, under the actuarial cost method in use, to years prior to the current period considered by a particular actuarial valuation. As of such date, the actuarial accrued liability represents the excess of the present value of future benefits and administrative expenses over the present value of future normal costs for all plan participants and beneficiaries. The excess of the actuarial accrued liability over the actuarial value of the assets of a pension plan is the Unfunded Actuarial Liability. The excess of the actuarial value of the assets of a pension plan over the actuarial accrued liability is an actuarial surplus and is treated as a negative unfunded actuarial liability.

(3) *Actuarial assumption* means an estimate of future conditions affecting pension cost; for example, mortality rate, employee turnover, compensation levels, earnings on pension plan assets, changes in values of pension plan assets.

(4) *Actuarial cost method* means a technique which uses actuarial assumptions to measure the present value of future pension benefits and pension plan administrative expenses, and which assigns the cost of such benefits and expenses to cost accounting periods. The actuarial cost method includes the asset valuation method used to determine the actuarial value of the assets of a pension plan.

(5) *Actuarial gain and loss* means the effect on pension cost resulting from differences between actuarial assumptions and actual experience.

(6) *Actuarial valuation* means the determination, as of a specified date, of the normal cost, actuarial accrued liability, actuarial value of the assets of a pension plan, and other relevant values for the pension plan.

(7) *Curtailment of benefits* means an event; e.g., a plan amendment, in which the pension plan is frozen and no further material benefits accrue. Future service may be the basis for vesting of nonvested benefits existing at the time of the curtailment. The plan may hold assets, pay benefits already accrued, and receive additional contributions for unfunded benefits. Employees may or may not continue working for the contractor.

(8) *Funding agency* means an organization or individual which provides facilities to receive and

accumulate assets to be used either for the payment of benefits under a pension plan, or for the purchase of such benefits, provided such accumulated assets form a part of a pension plan established for the exclusive benefit of the plan participants and their beneficiaries. The fair market value of the assets held by the funding agency as of a specified date is the Funding Agency Balance as of that date.

(9) *Immediate-gain actuarial cost method* means any of the several cost methods under which actuarial gains and losses are included as part of the unfunded actuarial liability of the pension plan, rather than as part of the normal cost of the plan.

(10) *Market value of the assets* means the sum of the funding agency balance plus the accumulated value of any permitted unfunded accruals belonging to a pension plan. The Actuarial Value of the Assets means the value of cash, investments, permitted unfunded accruals, and other property belonging to a pension plan, as used by the actuary for the purpose of an actuarial valuation.

(11) *Normal cost* means the annual cost attributable, under the actuarial cost method in use, to current and future years as of a particular valuation date, excluding any payment in respect of an unfunded actuarial liability.

(12) *Pension plan* means a deferred compensation plan established and maintained by one or more employers to provide systematically for the payment of benefits to plan participants after their retirement, provided that the benefits are paid for life or are payable for life at the option of the employees. Additional benefits such as permanent and total disability and death payments, and survivorship payments to beneficiaries of deceased employees may be an integral part of a pension plan.

(13) *Pension plan participant* means any employee or former employee of an employer, or any member or former member of an employee organization, who is or may become eligible to receive a benefit from a pension plan which covers employees of such employer or members of such organization who have satisfied the plan's participation requirements, or whose beneficiaries are receiving or may be eligible to receive any such benefit. A participant whose employment status with the employer has not been terminated is an active participant of the employer's pension plan.

(14) *Pension plan termination* means an event; i.e., plan amendment, in which either the pension plan ceases to exist and all benefits are settled by purchase of annuities or other means, or the trusteeship of the plan is assumed by the Pension Benefit Guarantee Corporation or other conservator. The plan may or may not be replaced by another plan.

(15) *Permitted unfunded accruals* means the amount of pension cost for nonqualified defined-benefit pension plans that is not required to be funded under 9904.412–50(d)(2). The Accumulated Value of Permitted Unfunded Accruals means the value, as of the measurement date, of the permitted unfunded accruals adjusted for imputed earnings and for benefits paid by the contractor.

(16) *Prepayment credit* means the amount funded in excess of the pension cost assigned to a cost accounting period that is carried forward for future recognition. The Accumulated Value of Prepayment Credits means the value, as of the measurement date, of the prepayment credits adjusted for interest at the valuation rate and decreased for amounts used to fund pension costs or liabilities, whether assignable or not.

(17) *Projected benefit cost method* means either (i) any of the several actuarial cost methods which distribute the estimated total cost of all of the employees' prospective benefits over a period of years, usually their working careers, or (ii) a modification of the accrued benefit cost method that considers projected compensation levels.

(18) *Qualified pension plan* means a pension plan comprising a definite written program communicated to and for the exclusive benefit of employees which meets the criteria deemed essential by the Internal Revenue Service as set forth in the Internal Revenue Code for preferential tax treatment regarding contributions, investments, and distributions. Any other plan is a nonqualified pension plan.

(19) *Segment* means one of two or more divisions, product departments, plants, or other subdivisions of an organization reporting directly to a home office, usually identified with responsibility for profit and/or producing a product or service. The term includes Government-owned contractor-operated (GOCO) facilities, and joint ventures and subsidiaries (domestic and foreign) in which the organization has a majority ownership. The term also includes those joint ventures and subsidiaries (domestic and foreign) in which the organization has less than a majority ownership, but over which it exercises control.

(20) *Segment closing* means that a segment has (i) been sold or ownership has been otherwise transferred, (ii) discontinued operations, or (iii) discontinued doing or actively seeking Government business under contracts subject to this Standard.

(21) *Termination of employment gain or loss* means an actuarial gain or loss resulting from the difference between the assumed and actual rates at which plan participants separate from employment for reasons other than retirement, disability, or death.

(b) * * *

10. Subsection 9904.413–40 is amended by revising paragraphs (b) and (c) to read as follows:

9904.413–40 Fundamental requirement.

(a) * * *

(b) *Valuation of the assets of a pension plan.* The actuarial value of the assets of a pension plan shall be determined under an asset valuation method which takes into account unrealized appreciation and depreciation of the market value of the assets of the pension plan, including the accumulated value of permitted unfunded accruals, and shall be used in measuring the components of pension costs.

(c) *Allocation of pension cost to segments.* Contractors shall allocate pension costs to each segment having participants in a pension plan. A separate calculation of pension costs for a segment is required when the conditions set forth in 9904.413–50(c)(2) or (3) are present. When these conditions are not present, allocations may be made by calculating a composite pension cost for two or more segments and allocating this cost to these segments by means of an allocation base. When pension costs are separately computed for a segment or segments, the provisions of Cost Accounting Standard 9904.412 regarding the assignable cost limitation shall be based on the assets and liabilities for the segment or segments for purposes of such computations. In addition, the amount of pension cost assignable to a segment or segments shall not exceed the maximum tax-deductible amount computed for the plan as a whole and apportioned among the segment(s).

11. Subsection 9904.413–50 is revised to read as follows:

9904.413–50 Techniques for application.

(a) *Assignment of actuarial gains and losses.* (1) In accordance with the provisions of Cost Accounting Standard 9904.412, actuarial gains and losses shall be identified separately from other unfunded actuarial liabilities.

(2) Actuarial gains and losses determined under a pension plan whose

costs are measured by an immediate-gain actuarial cost method shall be amortized over a 15 year period in equal annual installments, beginning with the date as of which the actuarial valuation is made. The installment for a cost accounting period shall consist of an element for amortization of the gain or loss plus an element for interest on the unamortized balance at the beginning of the period. If the actuarial gain or loss determined for a cost accounting period is not material, the entire gain or loss may be included as a component of the current or ensuing year's pension cost.

(3) Pension plan terminations and curtailments of benefits shall be subject to adjustment in accordance with 9904.413–50(c)(12).

(b) *Valuation of the assets of a pension plan.* (1) The actuarial value of the assets of a pension plan shall be used:

(i) In measuring actuarial gains and losses, and

(ii) For purposes of measuring other components of pension cost.

(2) The actuarial value of the assets of a pension plan may be determined by the use of any recognized asset valuation method which provides equivalent recognition of appreciation and depreciation of the market value of the assets of the pension plan. However, the actuarial value of the assets produced by the method used shall fall within a corridor from 80 to 120 percent of the market value of the assets, determined as of the valuation date. If the method produces a value that falls outside the corridor, the actuarial value of the assets shall be adjusted to equal the nearest boundary of the corridor.

(3) The method selected for valuing pension plan assets shall be consistently applied from year to year within each plan.

(4) The provisions of paragraphs (b)(1) through (3) of this subsection are not applicable to plans that are treated as defined-contribution plans in accordance with 9904.412–50(a)(6).

(5) The market and actuarial values of the assets of a pension plan shall not be adjusted for any fee, reserve charge, or other investment charge for withdrawals from or termination of an investment contract, trust agreement, or other funding arrangement, unless such fee is determined in an arm's length transaction, and actually incurred and paid.

(c) *Allocation of pension cost to segments.* (1) For contractors who compute a composite pension cost covering plan participants in two or more segments, the base to be used for allocating such costs shall be representative of the factors on which the pension benefits are based. For example, a base consisting of salaries and wages shall be used for pension costs that are calculated as a percentage of salaries and wages; a base consisting of the number of participants shall be used for pension costs that are calculated as an amount per participant. If pension costs are separately calculated for one or more segments, the contractor shall make a distribution among the segments for the maximum tax-deductible amount and the contribution to the funding agency as follows:

(i) When apportioning the maximum tax-deductible amount, which is determined for a qualified defined-benefit pension plan as a whole pursuant to the Employee Retirement Income Security Act of 1974 (ERISA), 29 U.S.C. 1001 *et seq.*, as amended, to segments, the contractor shall use a base that considers the otherwise assignable pension costs or the funding levels of the individual segments.

(ii) When apportioning amounts deposited to a funding agency to segments, contractors shall use a base that is representative of the assignable pension costs, determined in accordance with 9904.412–50(c) for the individual segments. However, for qualified defined-benefit pension plans, the contractor may first apportion amounts funded to the segment or segments subject to this Standard.

(2) Separate pension cost for a segment shall be calculated whenever any of the following conditions exist for that segment, provided that such condition(s) materially affect the amount of pension cost allocated to the segment:

(i) There is a material termination of employment gain or loss attributable to the segment,

(ii) The level of benefits, eligibility for benefits, or age distribution is materially different for the segment than for the average of all segments, or

(iii) The appropriate actuarial assumptions are, in the aggregate, materially different for the segment than for the average of all segments. Calculations of termination of employment gains and losses shall give consideration to factors such as unexpected early retirements, benefits becoming fully vested, and reinstatements or transfers without loss of benefits. An amount may be estimated for future reemployments.

(3) Pension cost shall also be separately calculated for a segment under circumstances where—

(i) The pension plan for that segment becomes merged with that of another segment, or the pension plan is divided into two or more pension plans, and in either case,

(ii) The ratios of market value of the assets to actuarial accrued liabilities for each of the merged or separated plans are materially different from one another after applying the benefits in effect after the pension plan merger or pension plan division.

(4) For a segment whose pension costs are required to be calculated separately pursuant to paragraphs (c) (2) or (3) of this subsection, such calculations shall be prospective only; pension costs need not be redetermined for prior years.

(5) For a segment whose pension costs are either required to be calculated separately pursuant to paragraph (c)(2) or (c)(3) of this subsection or calculated separately at the election of the contractor, there shall be an initial allocation of a share in the undivided market value of the assets of the pension plan to that segment, as follows:

(i) If the necessary data are readily determinable, the funding agency balance to be allocated to the segment shall be the amount contributed by, or on behalf of, the segment, increased by income received on such assets, and decreased by benefits and expenses paid from such assets. Likewise, the accumulated value of permitted unfunded accruals to be allocated to the segment shall be the amount of permitted unfunded accruals assigned to the segment, increased by interest imputed to such assets, and decreased by benefits paid from sources other than the funding agency; or

(ii) If the data specified in paragraph (c)(5)(i) of this subsection are not readily determinable for certain prior periods, the market value of the assets of the pension plan shall be allocated to the segment as of the earliest date such data are available. Such allocation shall be based on the ratio of the actuarial accrued liability of the segment to the plan as a whole, determined in a manner consistent with the immediate gain actuarial cost method or methods used to compute pension cost. Such assets shall be brought forward as described in paragraph (c)(7) of this subsection.

(iii) The actuarial value of the assets of the pension plan shall be allocated to the segment in the same proportion as the market value of the assets.

(6) If, prior to the time a contractor is required to use this Standard, it has been calculating pension cost separately for individual segments, the amount of assets previously allocated to those segments need not be changed.

(7) After the initial allocation of assets, the contractor shall maintain a record of the portion of subsequent

contributions, permitted unfunded accruals, income, benefit payments, and expenses attributable to the segment and paid from the assets of the pension plan: Income and expenses shall include a portion of any investment gains and losses attributable to the assets of the pension plan. Income and expenses of the pension plan assets shall be allocated to the segment in the same proportion that the average value of assets allocated to the segment bears to the average value of total pension plan assets for the period for which income and expenses are being allocated.

(8) If plan participants transfer among segments, contractors need not transfer assets or actuarial accrued liabilities unless a transfer is sufficiently large to distort the segment's ratio of pension plan assets to actuarial accrued liabilities determined using the accrued benefit cost method. If assets and liabilities are transferred, the amount of assets transferred shall be equal to the actuarial accrued liabilities, determined using the accrued benefit cost method, transferred.

(9) Contractors who separately calculate the pension cost of one or more segments may calculate such cost either for all pension plan participants assignable to the segment(s) or for only the active participants of the segment(s). If costs are calculated only for active participants, a separate segment shall be created for all of the inactive participants of the pension plan and the cost thereof shall be calculated. When a contractor makes such an election, assets shall be allocated to the segment for inactive participants in accordance with paragraphs (c) (5), (6), and (7) of this subsection. When an employee of a segment becomes inactive, assets shall be transferred from that segment to the segment established to accumulate the assets and actuarial liabilities for the inactive plan participants. The amount of assets transferred shall be equal to the actuarial accrued liabilities, determined under the accrued benefit cost method, for these inactive plan participants. If inactive participants become active, assets and liabilities shall similarly be transferred to the segments to which the participants are assigned. Such transfers need be made only as of the last day of a cost accounting period. The total annual pension cost for a segment having active employees shall be the amount calculated for the segment plus an allocated portion of the pension cost calculated for the inactive participants. Such an allocation shall be on the same basis as that set forth in paragraph (c)(1) of this subsection.

(10) Where pension cost is separately calculated for one or more segments, the actuarial cost method used for a plan shall be the same for all segments. Unless a separate calculation of pension cost for a segment is made because of a condition set forth in paragraph (c)(2)(iii) of this subsection, the same actuarial assumptions may be used for all segments covered by a plan.

(11) If a pension plan has participants in the home office of a company, the home office shall be treated as a segment for purposes of allocating the cost of the pension plan. Pension cost allocated to a home office shall be a part of the costs to be allocated in accordance with the appropriate requirements of Cost Accounting Standard 9904.403.

(12) If a segment is closed, if there is a pension plan termination, or if there is a curtailment of benefits, the contractor shall determine the difference between the actuarial accrued liability for the segment and the market value of the assets allocated to the segment, irrespective of whether or not the pension plan is terminated. The difference between the market value of the assets and the actuarial accrued liability for the segment represents an adjustment of previously-determined pension costs.

(i) The determination of the actuarial accrued liability shall be made using the accrued benefit cost method. The actuarial assumptions employed shall be consistent with the current and prior long term assumptions used in the measurement of pension costs. If there is a pension plan termination, the actuarial accrued liability shall be measured as the amount paid to irrevocably settle all benefit obligations or paid to the Pension Benefit Guarantee Corporation.

(ii) In computing the market value of assets for the segment, if the contractor has not already allocated assets to the segment, such an allocation shall be made in accordance with the requirements of paragraphs (c)(5) (i) and (ii) of this subsection. The market value of the assets shall be reduced by the accumulated value of prepayment credits, if any. Conversely, the market value of the assets shall be increased by the current value of any unfunded actuarial liability separately identified and maintained in accordance with 9904.412–50(a)(2).

(iii) The calculation of the difference between the market value of the assets and the actuarial accrued liability shall be made as of the date of the event (e.g., contract termination, plan amendment, plant closure) that caused the closing of the segment, pension plan termination, or curtailment of benefits. If such a date is not readily determinable, or if its use can result in an inequitable calculation, the contracting parties shall agree on an appropriate date.

(iv) Pension plan improvements adopted within 60 months of the date of the event which increase the actuarial accrued liability shall be recognized on a prorata basis using the number of months the date of adoption preceded the event date. Plan improvements mandated by law or collective bargaining agreement are not subject to this phase-in.

(v) If a segment is closed due to a sale or other transfer of ownership to a successor in interest in the contracts of the segment and all of the pension plan assets and actuarial accrued liabilities pertaining to the closed segment are transferred to the successor segment, then no adjustment amount pursuant to this paragraph (c)(12) is required. If only some of the pension plan assets and actuarial accrued liabilities of the closed segment are transferred, then the adjustment amount required under this paragraph (c)(12) shall be determined based on the pension plan assets and actuarial accrued liabilities remaining with the contractor. In either case, the effect of the transferred assets and liabilities is carried forward and recognized in the accounting for pension cost at the successor contractor.

(vi) The Government's share of the adjustment amount determined for a segment shall be the product of the adjustment amount and a fraction. The adjustment amount shall be reduced for any excise tax imposed upon assets withdrawn from the funding agency of a qualified pension plan. The numerator of such fraction shall be the sum of the pension plan costs allocated to all contracts and subcontracts (including Foreign Military Sales) subject to this Standard during a period of years representative of the Government's participation in the pension plan. The denominator of such fraction shall be the total pension costs assigned to cost accounting periods during those same years. This amount shall represent an adjustment of contract prices or cost allowance as appropriate. The adjustment may be recognized by modifying a single contract, several but not all contracts, or all contracts, or by use of any other suitable technique.

(vii) The full amount of the Government's share of an adjustment is allocable, without limit, as a credit or charge during the cost accounting period in which the event occurred and contract prices/costs will be adjusted accordingly. However, if the contractor continues to perform Government contracts, the contracting parties may negotiate an amortization schedule, including interest adjustments. Any amortization agreement shall consider the magnitude of the adjustment credit or charge, and the size and nature of the continuing contracts.

12. Subsection 9904.413–60 is revised to read as follows:

9904.413–60 Illustrations.

(a) *Assignment of actuarial gains and losses.* Contractor A has a defined-benefit pension plan whose costs are measured under an immediate-gain actuarial cost method. The contractor makes actuarial valuations every other year. In the past, at each valuation date, the contractor has calculated the actuarial gains and losses that have occurred since the previous valuation date and has merged such gains and losses with the unfunded actuarial liabilities that are being amortized. Pursuant to 9904.413–40(a), the contractor must make an actuarial valuation annually. Any actuarial gains or losses measured must be separately amortized over a 15-year period beginning with the period for which the actuarial valuation is made in accordance with 9904.413–50(a) (1) and (2).

(b)(1) *Valuation of the assets of a pension plan.* Contractor B has a qualified defined-benefit pension plan, the assets of which are invested in equity securities, debt securities, and real property. The contractor, whose cost accounting period is the calendar year, has an annual actuarial valuation of the pension plan assets in June of each year; the effective date of the valuation is the beginning of that year. The contractor's method for valuing the assets of the pension plan is as follows: debt securities expected to be held to maturity are valued on an amortized basis running from initial cost at purchase to par value at maturity; land and buildings are valued at cost less depreciation taken to date; all equity securities and debt securities not expected to be held to maturity are valued on the basis of a five-year moving average of market values. In making an actuarial valuation, the contractor must compare the values reached under the asset valuation method used with the market value of all the assets as required by 9904.413–40(b). In this case, the assets are valued as of January 1 of that year. The contractor established the following values as of the valuation date.

	Asset valuation method	Market
Cash	$100,000	100,000
Equity securities	6,000,000	7,800,000
Debt securities, expected to be held to maturity	550,000	600,000
Other debt securities	600,000	750,000
Land and Buildings, net of depreciation ...	400,000	750,000
Total	7,650,000	10,000,000

(2) Section 9904.413–50(b)(2) requires that the actuarial value of the assets of the pension plan fall within a corridor from 80 to 120 percent of market. The corridor for the plan's assets as of January 1 is from $12 million to $8 million. Because the asset value reached by the contractor, $7,650,000, falls outside that corridor, the value reached must be adjusted to equal the nearest boundary of the corridor: $8 million. In subsequent years the contractor must continue to use the same method for valuing assets in accordance with 9904.413–50(b)(3). If the value produced falls inside the corridor, such value shall be used in measuring pension costs.

(c) *Allocation of pension costs to segments.* (1) Contractor C has a defined-benefit pension plan covering employees at five segments. Pension cost is computed by use of an immediate-gain actuarial cost method. One segment (X) is devoted primarily to performing work for the Government. During the current cost accounting period, Segment X had a large and unforeseeable reduction of employees because of a contract termination at the convenience of the Government and because the contractor did not receive an anticipated follow-on contract to one that was completed during the period. The segment does continue to perform work under several other Government contracts. As a consequence of this termination of employment gain, a separate calculation of the pension cost for Segment X would result in materially different allocation of costs to the segment than would a composite calculation and allocation by means of a base. Accordingly, pursuant to 9904.413–50(c)(2), the contractor must calculate a separate pension cost for Segment X. In doing so, the entire termination of employment gain must be assigned to Segment X and amortized over fifteen years. If the actuarial assumptions for Segment X continue to be substantially the same as for the other segments, the termination of employment gain may be separately amortized and allocated only to Segment X; all other Segment X computations may be included as part of the composite calculation. After the termination of employment gain is amortized, the contractor is no longer required to separately calculate the costs for Segment X unless subsequent events require each separate calculation.

(2) Contractor D has a defined-benefit pension plan covering employees at ten segments, all of which have some contracts subject to this Standard. The contractor's calculation of normal cost is based on a percentage of payroll for all employees covered by the plan. One of the segments (Segment Y) is entirely devoted to Government work. The contractor's policy is to place junior employees in this segment. The salary scale assumption for employees of the segment is so different from that of the other segments that the pension cost for Segment Y would be materially different if computed separately. Pursuant to 9904.413–50(c)(2)(iii), the contractor must compute the pension cost for Segment Y as if it were a separate pension plan. Therefore, the contractor must allocate a portion of the market value of pension plan's assets to Segment Y in accordance with 9904.413–50(c)(5). Memorandum records may be used in making the allocation. However, because the necessary records only exist for the last five years, 9904.413–50(c)(5)(ii) permits an initial allocation to be made as of the earliest date such records are available. The initial allocation must be made on the basis of the immediate gain actuarial cost method or methods used to calculate prior years' pension cost for the plan. Once the assets have been allocated, they shall be brought forward to the current period as described in 9904.413–50(c)(7). A portion of the undivided actuarial value of assets shall then be allocated to the segment based on the segment's proportion of the market value of assets in accordance with 9904.413–50(c)(5)(iii). In future cost accounting periods, the contractor shall make separate pension cost calculations for Segment Y based on the appropriate salary scale assumption. Because the factors comprising pension cost for the other nine segments are relatively equal, the contractor may compute pension cost for these nine segments by using composite factors. As required by 9904.413–50(c)(1), the base to be used for allocating such costs shall be representative of the factors on which the pension benefits are based.

(3) Contractor E has a defined-benefit pension plan which covers employees at twelve segments. The contractor uses composite actuarial assumptions to

develop a pension cost for all segments. Three of these segments primarily perform Government work; the work at the other nine segments is primarily commercial. Employee turnover at the segments performing commercial work is relatively stable. However, employment experience at the Government segments has been very volatile; there have been large fluctuations in employment levels and the contractor assumes that this pattern of employment will continue to occur. It is evident that separate termination of employment assumptions for the Government segments and the commercial segments will result in materially different pension costs for the Government segments. Therefore, the cost for these segments must be separately calculated, using the appropriate termination of employment assumptions for these segments in accordance with 9904.413–50(c)(2)(iii).

(4) Contractor F has a defined-benefit pension plan covering employees at 25 segments. Twelve of these segments primarily perform Government work; the remaining segments perform primarily commercial work. The contractor's records show that the termination of employment experience and projections for the twelve segments are so different from that of the average of all of the segments that separate pension cost calculations are required for these segments pursuant to 9904.413–50(c)(2). However, because the termination of employment experience and projections are about the same for all twelve segments, Contractor F may calculate a composite pension cost for the twelve segments and allocate the cost to these segments by use of an appropriate allocation base in accordance with 9904.413–50(c)(1).

(5) After this Standard becomes applicable to Contractor G, it acquires Contractor H and makes it Segment H. Prior to the merger, each contractor had its own defined-benefit pension plan. Under the terms of the merger, Contractor H's pension plan and plan assets were merged with those of Contractor G. The actuarial assumptions, current salary scale, and other plan characteristics are about the same for Segment H and Contractor G's other segments. However, based on the same benefits at the time of the merger, the plan of Contractor H had a disproportionately larger unfunded actuarial liability than did Contractor G's plan. Any combining of the assets and actuarial liabilities of both plans would result in materially different pension cost allocation to Contractor G's segments than if pension cost were computed for Segment H on the basis that it had a separate pension plan. Accordingly, pursuant to 9904.413–50(c)(3), Contractor G must allocate to Segment H a portion of the assets of the combined plan. The amount to be allocated shall be the market value of Segment H's pension plan assets at the date of the merger determined in accordance with 9904.413–50(c)(5), and shall be adjusted for subsequent receipts and expenditures applicable to the segment in accordance with 9904.413–50(c)(7). Pursuant to 9904.413–40(b)(1) and 9904.413–50(c)(5)(iii), Contractor G must use these amounts of assets as the basis for determining the actuarial value of assets used for calculating the annual pension cost applicable to Segment H.

(6) Contractor I has a defined-benefit pension plan covering employees at seven segments. The contractor has been making a composite pension cost calculation for all of the segments. However, the contractor determines that, pursuant to this Standard, separate pension costs must be calculated for one of the segments. In accordance with 9904.413–50(c)(9), the contractor elects to allocate pension plan assets only for the active participants of that segment. The contractor must then create a segment to accumulate the assets and actuarial accrued liabilities for the plan's inactive participants. When active participants of a segment become inactive, the contractor must transfer assets to the segment for inactive participants equal to the actuarial accrued liabilities for the participants that become inactive.

(7) Contractor J has a defined-benefit pension plan covering employees at ten segments. The contractor makes a composite pension cost calculation for all segments. The contractor's records show that the termination of employment experience for one segment, which is performing primarily Government work, has been significantly different from the average termination of employment experience of the other segments. Moreover, the contractor assumes that such different experience will continue. Because of this fact, and because the application of a different termination of employment assumption would result in significantly different costs being charged the Government, the contractor must develop separate pension cost for that segment. In accordance with 9904.413–50(c)(2)(ii), the amount of pension cost must be based on an acceptable termination of employment assumption for that segment; however, as provided in 9904.413–50(c)(10), all other assumptions for that segment may be the same as those for the remaining segments.

(8) Contractor K has a five-year contract to operate a Government-owned facility. The employees of that facility are covered by the contractor's overall qualified defined-benefit pension plan which covers salaried and hourly employees at other locations. At the conclusion of the five-year period, the Government decides not to renew the contract. Although some employees are hired by the successor contractor, because Contractor K no longer operates the facility, it meets the 9904.413–30(a)(20)(i) definition of a segment closing. Contractor K must compute the actuarial accrued liability for the pension plan for that facility using the accrued benefit cost method as of the date the contract expired in accordance with 9904.413–50(c)(12)(i). Because many of Contractor K's employees are terminated from the pension plan, the Internal Revenue Service considers it to be a partial plan termination, and thus requires that the terminated employees become fully vested in their accrued benefits to the extent such benefits are funded. Taking this mandated benefit improvement into consideration in accordance with 9904.413–50(c)(12)(iv), the actuary calculates the actuarial accrued liability to be $12.5 million. The contractor must then determine the market value of the pension plan assets allocable to the facility, in accordance with 9904.413–50(c)(5), as of the date agreed to by the contracting parties pursuant to 9904.413–50(c)(12)(iii), the date the contract expired. In making this determination, the contractor is able to do a full historical reconstruction of the market value of the assets allocated to the segment. In this case, the market value of the segment's assets amounted to $13.8 million. Thus, for this facility the value of pension plan assets exceeded the actuarial accrued liability by $1.3 million. Pursuant to 9904.413–50(c)(12)(vi), this amount indicates the extent to which the Government over-contributed to the pension plan for the segment and, accordingly, is the amount of the adjustment due to the Government.

(9) Contractor L operated a segment over the last five years during which 80% of its work was performed under Government CAS-covered contracts. The Government work was equally divided each year between fixed-price and cost-type contracts. The employees of the facility are covered by a funded nonqualified defined-benefit pension plan accounted for in accordance with 9904.412–50(c)(3). For each of the last five years the highest Federal corporate income tax rate has been 30%. Pension costs of $1 million per year were

computed using a projected benefit cost method. Contractor L funded at the complement of the tax rate ($700,000 per year). The pension plan assets held by the funding agency earned 8% each year. At the end of the five-year period, the funding agency balance; i.e., the market value of invested assets, was $4.4 million. As of that date, the accumulated value of permitted unfunded accruals; i.e., the current value of the $300,000 not funded each year, is $1.9 million. As defined by 9904.413–30(a)(20)(i), a segment closing occurs when Contractor L sells the segment at the end of the fifth year. Thus, for this segment, the market value of the assets of the pension plan determined in accordance with 9904.413–30(a)(10) is $6.3 million, which is, the sum of the funding account balance ($4.4 million) and the accumulated value of permitted unfunded accruals ($1.9 million). Pursuant to 9904.413–50(c)(12)(i), the contractor uses the accrued benefit cost method to calculate an actuarial accrued liability of $5 million as of that date. There is no transfer of plan assets or liabilities to the buyer. The difference between the market value of the assets and the actuarial accrued liability for the segment is $1.3 million ($6.3 million—$5 million). Pursuant to 9904.413–50(c)(12)(vi), the adjustment due the Government for its 80% share of previously-determined pension costs for CAS-covered contracts is $1.04 million (80% times $1.3 million). Because contractor L has no other Government contracts the $1.04 million is a credit due to the Government.

(10) Assume the same facts as in 9904.413–60(c)(9), except that Contractor L continues to perform substantial Government contract work through other segments. After considering the amount of the adjustment and the current level of contracts, the contracting officer and the contractor establish an amortization schedule so that the $1.04 million is recognized as credits against ongoing contracts in five level annual installments, including an interest adjustment based on the interest assumption used to compute pension costs for the continuing contracts. This amortization schedule satisfies the requirements of 9904.413–50(c)(12))(vii).

(11) Assume the same facts as in 9904.413–60(c)(9). As part of the transfer of ownership, Contractor L also transfers all pension liabilities and assets of the segment to the buyer. Pursuant to 9904.413–50(c)(12)(v), the segment closing adjustment amount for the current period is transferred to the buyer and is subsumed in the future pension cost accounting of the buyer. If the transferred liabilities and assets of the segment are merged into the buyer's pension plan which has a different ratio of market value of pension plan assets to actuarial accrued liabilities, then pension costs must be separately computed in accordance with 9904.413–50(c)(3).

(12) Contractor M sells its only government segment. Through a contract novation, the buyer assumes responsibility for performance of the segment's government contracts. Just prior to the sale, the actuarial accrued liability under the actuarial cost method in use is $18 million and the market value of assets allocated to the segment of $22 million. In accordance with the sales agreement, Contractor M is required to transfer $20 million of assets to the new plan. In determining the segment closing adjustment under 9904.413–12(c)(12) the actuarial accrued liability and the market value of assets are reduced by the amounts transferred to the buyer by the sale. The adjustment amount, which is the difference between the remaining assets ($2 million) and the remaining actuarial liability ($0), is $2 million.

(13) Contractor N has three segments that perform primarily government work and has been separately calculating pension costs for each segment. As part of a corporate reorganization, the contractor closes the production facility for Segment A and transfers all of that segment's contracts and employees to Segments B and C, the two remaining government segments. The pension assets from Segment A are allocated to the remaining segments based on the actuarial accrued liability of the transferred employees. Because Segment A has discontinued operations, a segment closing has occurred pursuant to 9904.413–30(a)(20)(ii). However, because all pension assets and liabilities have been transferred to segments that are the successors in interest of the contracts of Segment A, an immediate period adjustment is not required if Contractor N and the cognizant Federal official negotiate an amortization schedule pursuant to 9904.413–50(c)(12)(vii).

(14) Contractor O does not renew its government contract and decides to not seek additional government contracts for the affected segment. The contractor reduces the work force of the segment that had been dedicated to the government contract and converts the segment's operations to purely commercial work. In accordance with 9904.413–30(a)(20)(iii), the segment has closed. Immediately prior to the end of the contract the market value of the segment's assets was $20 million and the actuarial accrued liability determined under the actuarial cost method in use was $22 million. An actuarial accrued liability of $16 million is determined using the accrued benefit cost method as required by 9904.413–50(c)(12)(i). The segment closing adjustment is $4 million ($20 million—$16 million).

(15) Contractor P terminated its underfunded defined-benefit pension plan for hourly employees. The market value of the assets for the pension plan is $100 million. Although the actuarial accrued liability exceeds the $100 million of assets, the termination liability for benefits guaranteed by the Pension Benefit Guarantee Corporation (PBGC) is only $85 million. Therefore, the $15 million of assets in excess of the liability for guaranteed benefits are allocated to plan participants in accordance with PBGC regulations. The PBGC does not impose an assessment for unfunded guaranteed benefits against the contractor. The adjustment amount determined under 9904.413–50(c)(12) is zero.

(16) Assume the same facts as 9904.413–60(c)(17), except that the termination liability for benefits guaranteed by the Pension Benefit Guarantee Corporation (PBGC) is $120 million. The PBGC imposes a $20 million ($120 million—$100 Million) assessment against Contractor P for the unfunded guaranteed benefits. The contractor then determines the Government's share of the pension plan termination adjustment charge of $20 million in accordance with 9904.413–50(c)(12)(vi). In accordance with 9904.413–50(c)(12)(vii), the cognizant Federal official may negotiate an amortization schedule based on the contractor's schedule of payments to the PBGC.

(17) Assume the same facts as in 9904.413–60(c)(16), except that pursuant to 9904.412–50(a)(2) Contractor P has an unassignable portion of unfunded actuarial liability for prior unfunded pension costs which equals $8 million. The $8 million represents the value of assets that would have been available had all assignable costs been funded and, therefore, must be added to the assets used to determine the pension plan termination adjustment in accordance with 9904.413–50(c)(12)(ii). In this case, the adjustment charge is determined to be $12 million ($20 million − $8 million).

(18) Contractor Q terminates its qualified defined-benefit pension plan without establishing a replacement plan. At termination, the market value

of assets are $85 million. All obligations for benefits are irrevocably transferred to an insurance company by the purchase of annuity contracts at a cost of $55 million, which thereby determines the actuarial liability in accordance with 9904.413–50(c)(12)(i). The contractor receives a reversion of $30 million ($85 million − $55 million). The adjustment is equal to the reversion amount, which is the excess of the market value of assets over the actuarial liability. However, ERISA imposes a 50% excise tax of $15 million (50% of $30 million) on the reversion amount. In accordance with 9904.413–50(c)(12)(vi), the $30 million adjustment amount is reduced by the $15 million excise tax. Pursuant to 9904.413–50(c)(12)(vi), a share of the $15 million net adjustment ($30 million—$15 million) shall be allocated, without limitation, as a credit to CAS-covered contracts.

(19) Assume that, in addition to the facts of 9904.413–60(c)(18), Contractor Q has an accumulated value of prepayment credits of $10 million. Contractor Q has $3 million of unfunded actuarial liability separately identified and maintained pursuant to 9904.412–50(a)(2). The assets used to determine the adjustment amount equal $78 million. This amount is determined as the market value of assets ($85 million) minus the accumulated value of prepayment credits ($10 million) plus the portion of unfunded actuarial liability maintained pursuant to 9904.412–50(a)(2) ($3 million). Therefore, the difference between the assets and the actuarial liability is $23 million ($78 million − $55 million). In accordance with 9904.413–50(c)(12)(vi), the $23 million adjustment is reduced by the $15 million excise tax to equal $8 million. The contracting officer determines that the pension cost data of the most recent eight years reasonably reflects the government's participation in the pension plan. The sum of costs allocated to fixed-price and cost-type contracts subject to this Standard over the eight-year period is $21 million. The sum of costs assigned to cost accounting periods during the last eight years equals $42 million. Therefore, the government's share of the net adjustment is 50% ($21 million divided by $42 million) of the $8 million and equals $4 million.

(20) Contractor R maintains a qualified defined-benefit pension plan. Contractor R amends the pension plan to eliminate the earning of any future benefits; however the participants do continue to earn vesting service. Pursuant to 9904.413–30(a)(7), a curtailment of benefits has occurred. An actuarial accrued liability of $78 million is determined under the accrued benefit cost method using the interest assumption used for the last four actuarial valuations. The market value of assets, determined in accordance with 9904.413–50(c)(12)(ii), is $90 million. Contractor R shall determine the Government's share of the adjustment in accordance with 9904.413–50(c)(12)(vi). The contractor then shall allocate that share of the $12 million adjustment ($90 million − $78 million) determined under 9904.413–50(c)(12) to CAS-covered contracts. The full amount of adjustment shall be made without limitation in the current cost accounting period unless arrangements to amortize the adjustment are permitted and negotiated pursuant to 9904.413–50(c)(12)(vii).

(21) Contractor S amends its qualified defined-benefit pension plan to ''freeze'' all accrued benefits at their current level. Although not required by law, the amendment also provides that all accrued benefits are fully vested. Contractor S must determine the adjustment for the curtailment of benefits. Fifteen months prior to the date of the plan amendment freezing benefits, Contractor S voluntarily amended the plan to increase benefits. This voluntary amendment resulted in an overall increase of over 10%. All actuarial accrued liabilities are computed using the accrued benefit cost method. The actuarial accrued liability for all accrued benefits is $1.8 million. The actuarial accrued liability for vested benefits immediately prior to the current plan amendment is $1.6 million. The actuarial accrued liability determined for vested benefits based on the plan provisions before the voluntary amendment is $1.4 million. The $1.4 million actuarial liability is based on benefit provisions that have been in effect for six years and is fully recognized. However, the $200,000 increase in liability due to the voluntary benefit improvement adopted 15 months ago must be phased-in on a prorata basis over 60 months. Therefore, only 25% (15 months divided by 60 months) of the $200,000 increase, or $50,000, can be included in the curtailment liability. The current amendment voluntarily increasing vesting was just adopted and, therefore, none of the associated increase in actuarial accrued liability can be included. Accordingly, in accordance with 9904.413–50(c)(12)(iv), Contractor S determines the adjustment for the curtailment of benefits using an actuarial accrued liability of $1.45 million ($1.4 million plus $50,000).

(22) Contractor T has maintained separate qualified defined-benefit plans for Segments A and B and has separately computed pension costs for each segment. Both segments perform work under contracts subject to this Standard. On the first day of the current cost accounting period, Contractor T merges the two pension plans so that segments A and B are now covered by a single pension plan. Because the ratio of assets to liabilities for each plan is materially different from that of the merged plan, the contractor continues the separate computation of pension costs for each segment pursuant to 9904.413–50(c)(3). After considering the assignable cost limitations for each segment, Contractor T determines the potentially assignable pension cost is $12,000 for Segment A and $24,000 for Segment B. The maximum tax-deductible amount for the merged plan is $30,000, which is $6,000 less than the sum of the otherwise assignable costs for the segments ($36,000). To determine the portion of the total maximum tax-deductible amount applicable to each segment on a reasonable basis, the contractor prorates the $30,000 by the pension cost determined for each segment after considering the assignable cost limitations for each segment. Therefore, in accordance with 9904.413–50(c)(1)(i), the assignable pension cost is $10,000 for Segment A ($30,000 times $12,000 divided by $36,000) and $20,000 for Segment B ($30,000 times $24,000 divided by $36,000). Contractor T funds the full $30,000 and allocates the assignable pension cost for each segment to final cost objectives.

(23) Assume the same facts as in 9904.413–60(c)(22), except that the tax-deductible maximum is $40,000 and the ERISA minimum funding requirement is $18,000. Since funding of the accrued pension cost is not constrained by tax-deductibility, Contractor T determines the assignable pension cost to be $12,000 for Segment A and $24,000 for Segment B. If the contractor funds $36,000, the full assigned pension cost of each segment can be allocated to final cost objectives. However, because the contractor funds only the ERISA minimum of $18,000, the contractor must apportion the $18,000 contribution to each segment on a basis that reflects the assignable pension cost of each segment in accordance with 9904.413–50(c)(1)(ii). To measure the funding level of each segment, Contractor T uses an ERISA minimum funding requirement separately determined for each segment, as if the segment were a separate plan. On this basis, the allocable pension cost is determined to be $8,000 for Segment A and $10,000 for

Segment B. In accordance with 9904.412–50(a)(2), Contractor T must separately identify, and eliminate from future cost computations, $4,000 ($12,000 − $8,000) for Segment A and $14,000 ($24,000 − $10,000) for Segment B.

(24) Assume the same facts as in 9904.413–60(c)(23), except that Segment B performs only commercial work. As permitted by 9904.413–50(c)(1)(ii), the contractor first applies $12,000 of the contribution amount to Segment A, which is performing work under Government contracts, for purposes of 9904.412–50(d)(i). The remaining $6,000 is applied to Segment B. The full assigned pension cost of $12,000 for Segment A is funded and such amount is allocable to CAS-covered contracts. Pursuant to 9904.412–50(a)(2), the contractor separately identifies, and eliminates from future pension costs, the $18,000 ($24,000 − $6,000) of unfunded assigned cost for Segment B.

(25) Contractor U has a qualified defined-benefit pension plan covering employees at two segments that perform work on contracts subject to this Standard. The ratio of the actuarial value of assets to actuarial accrued liabilities is significantly different between the two segments. Therefore, Contractor U is required to compute pension cost separately for each segment. The actuarial value of assets allocated to Segment A exceeds the actuarial accrued liability by $50,000. Segment B has an unfunded actuarial liability of $20,000. Thus, the pension plan as a whole has an actuarial surplus of $30,000. Pension cost of $5,000 is computed for Segment B and is less than Segment B's assignable cost limitation of $9,000. The tax-deductible maximum is $0 for the plan as whole and, therefore, $0 for each segment. Contractor U will deem all existing amortization bases maintained for Segment A to be fully amortized in accordance with 9904.412–50(c)(2)(ii). For Segment B, the amortization of existing portions of unfunded actuarial liability continues unabated. Furthermore, pursuant to 9904.412–50(c)(2)(iii), the contractor establishes an additional amortization base for Segment B for the assignable cost deficit of $5,000.

13. Subsection 9904.413–63 is revised to read as follows:

9904.413–63 Effective date.

(a) This Standard is effective as of March 30, 1995.

(b) This Standard shall be followed by each contractor on or after the start of its next cost accounting period beginning after the receipt of a contract or subcontract to which this Standard is applicable.

(c) Contractors with prior CAS-covered contracts with full coverage shall continue to follow Standard 9904.413 in effect prior to March 30, 1995, until this Standard, effective March 30, 1995, becomes applicable following receipt of a contract or subcontract to which this revised Standard applies.

14. A new subsection 9904.413–64 is added to read as follows:

9904.413–64 Transition method.

(a) To be acceptable, any method of transition from compliance with Standard 9904.413 in effect prior to March 30, 1995, to compliance with Standard 9904.413 in effect as of March 30, 1995, must follow the equitable principle that costs, which have been previously provided for, shall not be redundantly provided for under revised methods. Conversely, costs that have not previously been provided for must be provided for under the revised method. This transition subsection is not intended to qualify for purposes of assignment or allocation, pension costs which have previously been disallowed for reasons other than ERISA funding limitations.

(b) The sum of all portions of unfunded actuarial liability identified pursuant to Standard 9904.413, effective March 30, 1995, including such portions of unfunded actuarial liability determined for transition purposes, is subject to the requirements for assignment of 9904.412–40(c).

(c) Furthermore, this Standard, effective March 30, 1995, clarifies, but is not intended to create, rights of the contracting parties, and specifies techniques for determining adjustments pursuant to 9904.413–50(c)(12). These rights and techniques should be used to resolve outstanding issues that will affect pension costs of contracts subject to this Standard.

(d) The method, or methods, employed to achieve an equitable transition shall be consistent with the provisions of this Standard and shall be approved by the contracting officer.

(e) All adjustments shall be prospective only. However, costs/prices of prior and existing contracts not subject to price adjustment may be considered in determining the appropriate transition method or adjustment amount for the computation of costs/prices of contracts subject to this Standard.

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state or imply Governmental endorsement of a product, service or position which the contractor represents.

1403.570–3 Contract clause.

CO's shall include the clause at 48 CFR 1452.203–70, Restriction on Endorsements, in all solicitations, contracts and agreements which are not executed in accordance with SAT procedures.

3. Part 1425 is amended by removing Sections 1425.202 and 1425.204.

4. Part 1452 is amended by adding new Section 1452.203–70 to read as follows:

PART 1452—SOLICITATION PROVISIONS AND CONTRACT CLAUSES

1452.203–70 Restriction on endorsements.

As prescribed in 48 CFR 1403.570–3, insert the following clause in all solicitations, contracts and agreements which are expected to exceed the simplified acquisition threshold.

Restriction on Endorsements—Department of the Interior (Nov 1995)

The contractor shall not refer to contracts awarded by the Department of the Interior in commercial advertising, as defined in FAR 31.205–1, in a manner which states or implies that the product or service provided is approved or endorsed by the Government, or is considered by the Government to be superior to other products or services. This restriction is intended to avoid the appearance of preference by the Government toward any product or service. The contractor may request a determination as to the propriety of promotional material from the CO.

(End of Clause)

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OFFICE OF MANAGEMENT AND BUDGET

Office of Federal Procurement Policy

48 CFR Part 9904

Cost Accounting Standards Board; Treatment of Gains or Losses Subsequent to Mergers or Business Combinations by Government Contractors; Increase in Minimum Acquisition Cost Criterion for Capitalization of Tangible Capital Assets

AGENCY: Cost Accounting Standards Board, Office of Federal Procurement Policy, OMB.

ACTION: Final rule.

SUMMARY: The Office of Federal Procurement Policy, Cost Accounting Standards Board (CASB), hereby amends the Cost Accounting Standards (CAS) relating to the treatment of gains or losses attributable to tangible capital assets subsequent to mergers or business combinations by government contractors, and relating to the minimum acquisition cost criterion for capitalization of tangible capital assets by raising the prescribed criterion from $1,500 to $5,000.

To resolve the problems that have been identified in this area, the Board hereby amends CAS 9904.404, ''Capitalization of Tangible Assets'' and CAS 9904.409, ''Depreciation of Tangible Capital Assets''. These amendments are based on an approach involving a ''no step-up, no step-down'' of asset bases and no recognition of gain or loss on a transfer of assets following a business combination by contractors subject to CAS.

Section 26(g)(1) of the Office of Federal Procurement Policy Act requires that the Board, prior to the promulgation of any new or revised Cost Accounting Standard, publish a final rule. This final rule addresses the Board's proposal to amend CAS 9904.404 and CAS 9904.409 to deal with the issue of gains and losses subsequent to a merger or business combination.

EFFECTIVE DATE: This rule is effective April 15, 1996.

FOR FURTHER INFORMATION CONTACT: Dr. Rein Abel, Director of Research, Cost Accounting Standards Board (telephone 202–395–3254).

SUPPLEMENTARY INFORMATION:

A. Regulatory Process

The Cost Accounting Standards Board's rules and regulations are codified at 48 CFR Chapter 99. Section 26(g)(1) of the Office of Federal Procurement Policy Act, 41 U.S.C. § 422(g)(1), requires that the Board, prior to the establishment of any new or revised Cost Accounting Standard, complete a prescribed rulemaking process. This process consists of the following four steps:

1. Consult with interested persons concerning the advantages, disadvantages and improvements anticipated in the pricing and administration of government contracts as a result of a proposed Standard.
2. Promulgate an Advance Notice of Proposed Rulemaking.
3. Promulgate a Notice of Proposed Rulemaking.
4. Promulgate a final rule.

This final rule is step four in the four step process.

B. Background

Prior Promulgations

The issues addressed in this proposal were first identified by commenters in response to the Board's request for agenda topics in November 1990. Subsequently, two Staff Discussion Papers (SDPs) were issued.

The first SDP, dated August 26, 1991 and titled ''Recognition and Pricing of Changing Capital Asset Values Resulting from Mergers and Business Combination by Government Contractors,'' (56 FR 42079) raised broad issues such as the scope of the proposed project, the basis for any Government claim to gains or losses resulting from a business combination and the likely economic consequences of a policy that would prohibit revaluation of assets following a merger.

The responses to this SDP were used by the Board as the basis for discussing the basic issues involved in this case. As a result of this discussion, the Board decided to issue a second SDP dealing with a series of questions concerning the specific procedures needed to deal effectively with the recognition, allocation and recovery of the gain or loss subsequent to a merger or business combination. The second SDP, entitled ''Treatment of Gains or Losses Subsequent to Mergers or Business Combinations by Government Contractors,'' was issued on November 4, 1993 (58 FR 58882). On the basis of comments received in response to that SDP, an Advance Notice of Proposed Rulemaking (ANPRM) was developed and published in the Federal Register on May 24, 1994 (59 FR 26774). The responses to the ANPRM were of significant assistance to the Board in developing a Notice of Proposed Rulemaking (NPRM). The NPRM was published in the Federal Register on March 8, 1995 (60 FR 12725).

Public Comments

Ten sets of public comments were received in response to the NPRM from government contractors, professional and industrial associations, law firms and Federal agencies.

The views expressed by the various parties were, in essence, consistent with the views expressed by the same parties earlier when the ANPRM was published. The basic no step-up, no step-down approach was supported by the Government commenters and it was generally opposed by other commenters although some of these other commenters did not explicitly express their views on this basic issue.

Besides expressing their views on the proposed approach outlined in the NPRM and the Board's arguments supporting this chosen approach, many commenters offered editorial as well as more substantive detailed comments on the various specific provisions of the document.

These comments are discussed below in greater detail, under Section E., Public Comments. The Board and the CASB staff express their appreciation for the generally constructive and thoughtful responses provided by the commenters.

Benefits

After consideration of all the comments received in response to the NPRM, the Board continues to believe that amendments to CAS 9904.404, ''Capitalization of Tangible Assets,'' and CAS 9904.409, ''Depreciation of Tangible Capital Assets,'' as set forth in the ANPRM and essentially restated in the NPRM, and this final rule, will significantly improve and clarify the implementation of CAS and related procurement regulations in accounting for tangible capital assets after completion of a merger or business combination. In particular, the Board continues to believe that the proposal embodied in this final rule will clarify the current ambiguities in this area and thus should lead to reductions in negotiations and litigation. This point is of particular significance in the current economic and budgetary environment where the need to realize economies in the defense budget can be expected to lead to mergers, business combinations and restructurings among contractors. It is also anticipated that increasing the capitalization criterion for tangible capital assets in CAS 9904.404 from $1,500 to $5,000, will significantly reduce record keeping burden in many instances. The Board believes that the potential benefit to the audit, negotiation, and general contract administration processes accruing from the added clarity and uniformity in the measurement of the cost of depreciation and cost of money subsequent to a business combination will be substantial and will greatly outweigh any added costs.

Summary of Proposed Amendments

A brief description of the proposed amendments follows:

a. The capitalization criterion for tangible capital assets in subsection 9904.404–40(b)(1) is increased from $1,500 to $5,000.

b. The current subsection 9904.404–50(d) is deleted and is replaced by an amended section that prescribes:

(1) That for contract costing purposes, tangible capital assets following a business combination shall retain their net book value recognized during the most recent cost accounting period prior to the business combination provided that the assets generated either depreciation expense or cost of money charges that were allocated during the period either as direct or indirect costs to Federal government contracts and subcontracts negotiated on the basis of cost.

(2) That the cost of tangible capital assets shall be restated after the business combination at a figure not to exceed the fair value at the date of the acquisition pursuant to a business combination where the assets during the most recent cost accounting period prior to the business combination did not generate either depreciation expense or cost of money charges that were allocated either as direct or indirect costs to Federal government contracts negotiated on the basis of cost.

c. A new subparagraph 9904.409–50(j)(5), is added to current subsection 9904.409–50(j). The purpose of this new subparagraph is to make it clear that the CAS 9904.409 provisions dealing with the recapture of gains and losses on disposition of tangible capital assets should not apply when assets are transferred subsequent to a business combination.

C. Paperwork Reduction Act

The Paperwork Reduction Act, Public Law 96–511, does not apply to this rulemaking, because this rule imposes no paperwork burden on offerors, affected contractors and subcontractors, or members of the public which require the approval of OMB under 44 U.S.C. 3501, *et seq.*

D. Executive Order 12866 and the Regulatory Flexibility Act

The economic impact of this rule on contractors and subcontractors is expected to be minor. As a result, the Board has determined that this final rule will not result in the promulgation of a ''major rule'' under the provisions of Executive Order 12866, and that a regulatory impact analysis will not be required. Furthermore, this final rule will not have a significant effect on a substantial number of small entities because small businesses are exempt from the application of the Cost Accounting Standards. Therefore, this final rule does not require a regulatory flexibility analysis under the Regulatory Flexibility Act of 1980.

E. Public Comments

This final rule was developed after consideration of the public comments received in response to the Board's NPRM published on March 8, 1995 (60 FR 12725). The comments have provided valuable input to the Board's rulemaking process. The comments received and the action taken by the Board are summarized in the paragraphs that follow:

Comment: Several commenters indicated that the final rule should make it clear that this revised rule is to be applied on a prospective basis only. One commenter suggested that the language in 9904.404–63 and 9904.409–63 be supplemented to reflect the requirements of paragraph (a)(3) of the contract clause at 9903.201–4(a) which requires the receipt of a new CAS-covered contract for a new CAS requirement to be applicable.

Response: Sections 9904.404–63 and 9904.409–63 have been supplemented to make it clear that these revisions are to be applied prospectively.

Comment: Several commenters stressed once more that they believe there is a conflict between the CAS allocability provisions and the Federal Acquisition Regulation (FAR) allowability provisions in this area. It was suggested again, as in earlier comments, that the OFPP Administrator should address this issue.

Response: The Board is aware that there is an appearance of conflict between the provisions of CAS 9904.404 and FAR 31.205–52. As stated in the proposed rulemakings, the OFPP Administrator will determine whether any changes may be necessary in the FAR cost principles to make them fully compatible with amended CAS 9904.404 and 9904.409.

Comment: One commenter pointed out the apparent inconsistency in the language between sections 9904.404–50(d) (1) and (2) when describing the scope of the two paragraphs. In one paragraph the reference is to costs charged to ''Federal Government contracts'', while in the other, the reference is to ''Federal Government contracts subject to CAS''. In addition, another commenter pointed out that these references did not make clear whether contractors subject to modified CAS coverage are affected by this amendment.

Response: In order to make clear that the amendment applies to those tangible capital assets that were charged to Federal government contracts and subcontracts negotiated on the basis of cost before the business combination, the phrase ''subject to CAS'' has been eliminated. This should make it clear that this revised rule applies to tangible capital assets that generated costs allocated to Federal government contracts and subcontracts negotiated on the basis of cost, where such costs were allocated to contracts and subcontracts by the seller during the most recent cost accounting period prior to the business combination.

Comment: Several suggestions were received dealing with different aspects of materiality in applying this revision. First, several contractors and industry associations suggested that specific materiality criteria be introduced, such as total dollar value of assets acquired or the percentage of commercial or competitively awarded fixed-priced contracts in relation to total sales. One Government commenter suggested that the coverage of the amendment should be extended also to those tangible capital assets that generated relevant costs chargeable to CAS-covered contracts ''anytime during the three accounting periods prior to the business combination''.

Response: The Board does not believe that the introduction of additional materiality criteria is advisable at this time. By its very nature, under full CAS coverage, the amended Standard's requirements apply to major contractors that perform significant amounts of CAS-covered work.

CAS 9904.404–50(d) has been revised to clearly state that the costs of tangible capital assets acquired from a seller (whether CAS-covered or non-CAS covered) which generated depreciation expense or cost of money charges that were allocated to Federal government contracts or subcontracts shall not be written up by the buyer. The primary issue is whether or not a material amount of asset costs have been charged to Federal government contracts and subcontracts that were negotiated on the basis of cost, where such costs were allocated to contracts and subcontracts during the most recent cost accounting period prior to the acquisition date, not the amount of CAS-covered effort performed by the seller.

Comment: One commenter suggested that the acquisition cost criterion in section 9904.404 be raised from $1,500 to $5,000.

Response: The Board accepts this suggestion and therefore section 9904.404–40(b)(1) is modified to increase the minimum acquisition cost criterion from $1,500 to $5,000.

Comment: One Government commenter expressed the view that the provisions of the amendment should also be extended to non-CAS-covered contractors: ''The proposed rule does not provide uniformity or consistency since it provides for different treatment for acquired assets of CAS-covered from non-CAS-covered contractors''.

Response: CAS 9904.404–50(d) has been revised to clearly establish that the acquired tangible capital asset valuations shall be determined in a consistent manner. As revised, application of the prescribed techniques in 9904.404–50(d)(1) and 9904.404–50(d)(2) is dependant upon whether or not the acquired assets were previously utilized in the performance of either CAS-covered and/or non-CAS covered Federal contracts that were negotiated on the basis of cost.

Comment: Several commenters expressed their disagreement with the abandonment of GAAP principles in this revision to CAS 9904.404. The view was expressed that the CASB should deviate from GAAP only in exceptional cases and, in the view of these commenters, such an approach is not warranted in the present case.

Response: The Board has pointed out in its Statement of Objectives, Policies and Concepts that it will make every reasonable effort to avoid conflict or disagreement with other bodies having similar responsibilities. However, it also pointed out that the nature of the Board's authority and its mission is such that it must retain and exercise full responsibility for meeting its objectives.

As stated in previous discussions, the Board adopted the ''no step-up, no step-down'' approach after extensive consideration of the possible alternative approaches. In particular, the issues associated with the recognition, allocation and recovery of the gain or loss subsequent to a merger or business combination were extensively explored in a Staff Discussion Paper (SDP) entitled ''Treatment of Gains or Losses Subsequent to Mergers or Business Combinations by Government Contractors.'' It was only after careful consideration of the responses to the SDP that the Board decided to proceed with the ''no step-up, no step-down'' approach thereby establishing a cost accounting practice that diverges from the corresponding practice recognized for GAAP purposes.

Comment: Several commenters pointed out that since this issue has been under review by the CAS Board, there have been significant changes in the statutes and regulations covering mergers and business combinations by Government contractors. The Government, in order to encourage contractors to consolidate, has recognized ''external restructuring'' which allows, in certain circumstances, contractors' restructuring costs to be charged to Government contracts to the extent that the restructuring results in savings that exceed the costs. The commenters argued that the same rationale should be applied to increased deprecation associated with the revaluation of a purchased company's assets if the business combination is regarded as an ''external restructuring'', and, that it would be inequitable for the Government to benefit from all of the savings resulting from restructuring, while it is unwilling to recognize all of the costs needed to implement such restructuring.

Response: In issuing this revision, the Board does not intend to encourage or discourage contractors to consolidate or restructure their operations. Rather, the Board's intent, in accordance with its stated objectives, in promulgating this revision, is to increase the degree of uniformity and consistency in like circumstances in the cost accounting practices that are used by Government contractors to record tangible capital asset values subsequent to mergers or business combinations. The Board believes that this action will result in cost allocations that are fair and equitable.

Comment: Several commenters offered editorial comments to the proposed revisions.

Response: All of these comments were considered and, as a result, the essence of several of these comments were incorporated in the final rule.

List of Subjects in 48 CFR Part 9904

Cost accounting standards, Government procurement.

Richard C. Loeb,

Executive Secretary, Cost Accounting Standards Board.

For the reasons set forth in this preamble, chapter 99 of title 48 of the Code of Federal Regulations is amended as set forth below:

1. The authority citation for part 9904 continues to read as follows:

Authority: Public Law 100–679, 102 Stat. 4056, 41 U.S.C. 422.

PART 9904—COST ACCOUNTING STANDARDS

9904.404 Capitalization of tangible assets.

2. Section 9904.404–40 is amended by revising paragraph (b)(1) to read as follows:

9904.404–40 Fundamental requirement.

* * * * *

(b) * * *

(1) The contractor's policy shall designate a minimum service life criterion, which shall not exceed 2 years, but which may be a shorter

period. The policy shall also designate a minimum acquisition cost criterion which shall not exceed $5,000, but which may be a smaller amount.

* * * * *

3. Section 9904.404–50 is amended by revising paragraph (d) to read as follows:

9904.404–50 Techniques for application.

* * * * *

(d) The capitalized values of tangible capital assets acquired in a business combination, accounted for under the ''purchase method'' of accounting, shall be assigned to these assets as follows:

(1) All the tangible capital assets of the acquired company that during the most recent cost accounting period prior to a business combination generated either depreciation expense or cost of money charges that were allocated to Federal government contracts or subcontracts negotiated on the basis of cost, shall be capitalized by the buyer at the net book value(s) of the asset(s) as reported by the seller at the time of the transaction.

(2) All the tangible capital asset(s) of the acquired company that during the most recent cost accounting period prior to a business combination did not generate either depreciation expense or cost of money charges that were allocated to Federal government contracts or subcontracts negotiated on the basis of cost, shall be assigned a portion of the cost of the acquired company not to exceed their fair value(s) at the date of acquisition. When the fair value of identifiable acquired assets less liabilities assumed exceeds the purchase price of the acquired company in an acquisition under the ''purchase method,'' the value otherwise assignable to tangible capital assets shall be reduced by a proportionate part of the excess.

* * * * *

4. Section 9904.404–63 is revised to read as follows:

9904.404–63 Effective date.

(a) This Standard is effective April 15, 1996.

(b) This Standard shall be applied beginning with the contractor's next full cost accounting period beginning after the receipt of a contract or subcontract to which this Standard is applicable.

(c) Contractors with prior CAS-covered contracts with full coverage shall continue to follow Standard 9904.404 in effect prior to April 15, 1996, until this Standard, effective April 15, 1996, becomes applicable after the receipt of a contract or subcontract to which this revised Standard applies.

5. Section 9904.409–50 is amended by adding a new paragraph (j)(5) to read as follows:

9904.409–50 Techniques for application.

* * * * *

(j) * * *

(5) The provisions of this subsection 9904.409–50(j) do not apply to business combinations. The carrying values of tangible capital assets acquired subsequent to a business combination shall be established in accordance with the provisions of subsection 9904.404–50(d).

* * * * *

6. Section 9904.409–63 is revised to read as follows:

9904.409–63 Effective date.

(a) This Standard is effective April 15, 1996.

(b) This Standard shall be applied beginning with the contractor's next full cost accounting period beginning after the receipt of a contract or subcontract to which this Standard is applicable.

(c) Contractors with prior CAS-covered contracts with full coverage shall continue to follow Standard 9904.409 in effect prior to April 15, 1996, until this Standard, effective April 15, 1996, becomes applicable after the receipt of a contract or subcontract to which this revised Standard applies.

[FR Doc. 96–3061 Filed 2–12–96; 8:45 am]

BILLING CODE 3110–01–P

OFFICE OF MANAGEMENT AND BUDGET

Office of Federal Procurement Policy

48 CFR Part 9903

Cost Accounting Standards Board; Revisions to the Cost Accounting Standards Board Disclosure Statement Form (CASB DS–1)

AGENCY: Cost Accounting Standards Board, Office of Federal Procurement Policy, OMB.

ACTION: Final rule.

SUMMARY: The Office of Federal Procurement Policy, Cost Accounting Standards Board (CASB), is revising its Disclosure Statement Form (CASB DS–1). Section 26(g)(1) of the Office of Federal Procurement Policy Act, 41 U.S.C. 422(g)(1), requires that the Board, when promulgating any new or revised Cost Accounting Standard, publish a final rule. This final rule incorporates an updated and revised CASB Disclosure Statement developed by the Board.

EFFECTIVE DATE: February 28, 1996.

FOR FURTHER INFORMATION CONTACT: Rein Abel, Director of Research, Cost Accounting Standards Board (telephone: 202–395–3254).

SUPPLEMENTARY INFORMATION:

A. Regulatory Process

The CASB's rules, regulations and Standards are codified at 48 CFR Chapter 99. Section 26(g)(1) of the Office of Federal Procurement Policy Act, 41 U.S.C. 422(g)(1), requires that the Board, prior to the establishment of any new or revised CAS, complete a prescribed rulemaking process. The process generally consists of the following four steps:

1. Consult with interested persons concerning the advantages, disadvantages and improvements anticipated in the pricing and administration of Government contracts as a result of the adoption of a proposed Standard.
2. Promulgate an Advance Notice of Proposed Rulemaking (ANPRM).
3. Promulgate a Notice of Proposed Rulemaking (NPRM).
4. Promulgate a final rule.

This promulgation completes the four step process.

B. Background

Prior Promulgations

The original Disclosure Statement Form (CASB DS–1) was developed and promulgated in the early 1970s. No revisions to the document were made until the Board was reestablished in 1990. In 1992, some minor revisions were made. 57 FR 14148, 14159 (April 17, 1992). Subsequently, a project was initiated to revise and update the Disclosure Statement (CASB DS–1).

On April 2, 1993, a Staff Discussion Paper incorporating a revised Disclosure Statement was distributed to certain interested parties who generally possessed actual field experience in submitting and auditing these Statements. On the basis of the comments received in response to this Staff Discussion Paper, an Advance Notice of Proposed Rulemaking (ANPRM) was developed and published in the Federal Register on April 4, 1994 (59 FR 15695).

The majority of the comments received in response to the ANPRM were generally supportive of the proposed approach, but at the same time, numerous revisions were suggested that were intended to improve and streamline the document. Many of these suggested revisions were incorporated in the Notice of Proposed Rulemaking (NPRM) that was published in the Federal Register on November 29, 1994 (59 FR 60948).

Public Comments

Nine sets of public comments were received in response to the NPRM from government contractors, industry associations and Federal agencies.

Most commenters acknowledged that the NPRM version of the DS–1 was a significant improvement as compared with the earlier versions of the Disclosure Statement. Nevertheless, numerous additional revisions were suggested by commenters in order to further simplify and streamline the DS–1. Of particular concern to several commenters was the amount and type of information needed to respond adequately to questions in Part VII of the Statement.

In general, the Board has tried to be responsive to the suggestions made by commenters. In particular, a careful reevaluation of Part VII has been undertaken. In reevaluating this Part, the instructions have been clarified to make clear that only relevant cost accounting practices and applicable identifying data need be disclosed. Therefore, numeric data representing accounting estimates is not required to be submitted. Also, in most sections of Part VII, the substantive questions have been limited to items that cover only 80-percent of the relevant cost groupings.

The commenters overall concerns and suggestions are addressed in greater detail under Section E., Public Comments.

The Board and the CASB staff express their appreciation for the constructive suggestions and criticisms provided by the commenters with regard to the content of the revised Disclosure Statement. Many of the commenters' suggested improvements have been incorporated into the final rule being promulgated today.

Benefits

After consideration of the public comments received, the Board believes that the revised Disclosure Statement, as set forth in this final rule, will improve the cost accounting practices followed by contractors when estimating, accumulating and reporting costs deemed allocable to Federal contracts. Adequate disclosure of cost accounting practices is essential in order to ensure consistency in cost measurement as costs are first estimated and then accumulated and reported. A Disclosure Statement that has not been updated for some two decades clearly cannot adequately reflect currently prevailing cost accounting practices and cost elements. Therefore, in order to ensure that the policies and Standards promulgated by the Board are implemented in an economical and effective manner, a revised and updated Disclosure Statement becomes essential. In addition, the Board has previously expressed the view that an updated Disclosure Statement should facilitate interaction between contractors and Government representatives when dealing with contract costing matters.

The introduction of the revised statement should not impose any new burden on contractors as it merely replaces an existing form which requires periodic updating of disclosed practices.

To further reduce the possibility of increased costs, the extended dates for submission of the new Disclosure Statement are designed to provide an opportunity to delay submission until such time as contractors would most likely have to file an updated disclosure form regardless of whether a new Disclosure Statement is introduced or not.

Summary of Amendments

The primary purpose of this revision of the Disclosure Statement is to bring it up to date and to improve it in light of two decades of field experience that the government procurement community has had with this document. The basic characteristics of the Disclosure Statement have not been changed. However, a multitude of specific changes are incorporated in the revised Statement. It would be impractical to list here all the specific changes. However, most of these changes can be summarized as follows:

1. The current Disclosure Statement specifies that Parts I through VII be prepared at the segment or business unit level, while Part VIII should be prepared at the corporate or group headquarters level. This revised Statement provides that although Parts V, VI and VII still have to be submitted by segments, they may be completed either at the segment or headquarters level depending on where the applicable practices or procedures are established or where the cost is actually incurred.

2. In general, various legal references have been updated.

3. As the original Disclosure Statement was in essence prepared before any Cost Accounting Standards were issued, the revised format includes references to subsequently issued Standards where appropriate. In this context, some cost accounting practices described in the original Disclosure Statement may not be in compliance with the relevant provisions of a Cost Accounting Standard. The purpose of the Disclosure Statement is not to elicit noncompliant answers, and therefore, any references to potentially non-compliant practices have been eliminated.

4. Requests for certain statistical data have been eliminated as this information is no longer used.

5. Certain new topical areas have been added to the Disclosure Statement. These cover items that have become important from a cost measurement perspective over the last two decades. The topical areas include cost-of-money, post-retirement health benefits and employee stock ownership plans. Most of these new topical areas are incorporated in a significantly revised Part VII.

C. Paperwork Reduction Act

The information collection aspects of this rule have been approved by the Office of Management and Budget, and assigned Control Number 0348–0051.

D. Executive Order 12866 and the Regulatory Flexibility Act

The economic impact of this final rule on contractors and subcontractors is expected to be minor. As a result, the Board has determined that this final rule does not result in the promulgation of a ''major rule'' under the provisions of Executive Order 12866, and that a regulatory impact analysis will not be required. Furthermore, this final rule does not have a significant effect on a substantial number of small entities because small businesses are exempt from the application of the Cost Accounting Standards. Therefore, this rule does not require a regulatory flexibility analysis under the Regulatory Flexibility Act of 1980.

E. Public Comments

This final rule is based upon the NPRM published in the Federal Register on November 29, 1994 (59 FR 60948), wherein public comments were invited. Nine sets of comments were received from government contractors, industry associations and Federal agencies. The more significant comments received, and the Board's actions taken in response thereto, are summarized below. Many other comments that were more of an editorial nature have been incorporated in the document where appropriate.

Comment: Two commenters suggested that compliant as well as non-compliant cost accounting practices should be described in the Disclosure Statement.

Response: The Board agrees that the actual cost accounting practices being followed must be described. However, where the Disclosure Statement provides a list of alternative practices, only compliant alternatives will be listed. If the contractor's practice is not one of the listed alternatives, the actual practice must be described on a continuation sheet. This will not be tantamount to conceding that the practice is non-compliant since such a determination can only be made after appropriate analysis and review.

Comment: Several commenters indicated that although the NPRM has been significantly improved and streamlined, the draft still contains too many questions of a detailed nature that may, in the future, increase rather than decrease the opportunities for disputes.

Response: The Board has, once more, consulted with the respondents to the NPRM and all the concerns have been subjected to additional review. As a result, some changes have been made to the version incorporated in the NPRM that should contribute to further streamlining and clarification of the final document. This comment applies in particular to Part VII of the Disclosure Statement.

Comment: At least two commenters indicated that, in their opinion the revised document still contains too many pages.

Response: In the final format there is no substantial difference in the length of the original and the final Disclosure Statement.

Comment: One commenter stressed that whenever possible, existing CAS wording or definitions should be used.

Response: The Board agrees with this suggestion and, wherever appropriate, the Disclosure Statement has accordingly been changed.

Comment: Several contractors indicated that throughout the document the term ''CAS-covered contracts'' rather than ''Federal contracts'' should be used.

Response: The Disclosure Statement deals with the cost accounting practices of an entity such as a segment or home office and it is presumed that cost accounting practices are applied consistently to all the applicable final cost objectives. Although the dollar amount of CAS-covered contracts received is crucial in determining whether a Disclosure Statement has to be filed, once the requirement to file has been met, the disclosure will cover all of the entity's policies and practices as they affect cost measurement and allocation to all contracts. Therefore, a broader term, such as ''Federal contracts'', seems preferable to a narrower term such as ''CAS-covered contracts''.

Comment: Two commenters suggested a shorter implementation period than the one proposed in the NPRM.

Response: While the Board encourages early adoption of the new form, it does not believe that it can adequately envision all the circumstances that might arise necessitating a delay in the introduction of the new form. It believes that any deadline imposed for the introduction of the new form should make ample provision for any unexpected difficulties that may arise at the implementation stage. Therefore, the final filing date for existing contractors has not been changed, although the Board hopes that an earlier adoption is possible in most cases.

Comment: Several commenters expressed some criticism of the procedure outlined in *General Instructions* that allows parts of contractors' accounting manuals to be incorporated by reference in the Disclosure Statement.

Response: The wording in the Instructions has been changed to make it clear that the procedure in question is an optional one—particularly from the perspective of the contractor.

Comment: Several commenters suggested that the language be clarified to indicate the appropriate circumstances in which home offices may be able to complete Parts V, VI, or VII to be filed by segments reporting to the home office.

Response: The language in the *General Instructions* has been clarified. In particular, it has been made clear that where the home office establishes the applicable cost accounting policies and procedures, it may also complete the relevant Parts of the Disclosure Statement to be submitted by its subordinate segments.

Comment: Several commenters offered suggestions for clarifying the layout and terminology used on the *Cover Sheet.*

Response: Certain changes have been made to the *Cover Sheet,* in particular to item 0.2, Reporting Unit Classification, in order to introduce standard CAS terminology and definitions whenever appropriate.

Comment: Several commenters pointed out that in Part I, General Information, the wording of several items could be improved in order to ensure that the questions are more clearly focused and take into account current practices.

Response: Some changes have been made to Part I to reflect the suggestions made by several commenters. In particular, the question dealing with unallowable costs has been reformatted so as to reflect the basic structure of CAS 9904.405, Accounting for Unallowable Costs.

Comment: A number of comments were received concerning the formulation of questions in Part II, Direct Costs, dealing with direct material, direct labor and other direct costs. Some commenters suggested that the questions included in this part might be more appropriate elsewhere, such as in Part III, Direct vs. Indirect Costs, of the Disclosure Statement.

Response: The basic characteristic of Part II, as a section dealing with direct material, direct labor and other direct costs has been retained. The purpose here is to obtain information on how certain elements of cost are treated once it has been determined that they represent direct costs for government contract costing purposes. Therefore, items such as the question dealing with employee travel expenses that are directly charged to contracts have been retained.

On the other hand, as suggested by several commenters, the question dealing with interorganizational transfers has been eliminated primarily because it requested information about the cost accounting practices of the transferor and not of the transferee who is preparing the Disclosure Statement. It cannot be assumed that such information is always readily available to the transferee. The transferee's practices in this area are covered in Part IV, Indirect Costs.

Comment: A few commenters suggested that Part III should be drastically recast—including a suggestion that instead of long lists of functions, elements of cost and transactions, the equivalent information should be described on a continuation sheet.

Response: The existing format has been retained as it seems to be the most effective way to obtain the relevant information on whether an item of cost is being treated as a direct cost, as an indirect cost or as a sometimes direct/sometimes indirect cost. The lists of functions, elements of cost and transactions have been somewhat modified on the basis of comments received.

Comment: In Part IV, several commenters pointed out that the subtitles used to describe various methods of allocating General and Administrative (G&A) expense did not properly reflect the requirements of CAS 9904.410, Allocation of Business Unit General and Administrative Expenses to Final Cost Objectives.

Response: The subtitles in question have been modified to conform more closely to the requirements of CAS 9904.410.

Comment: A number of commenters were concerned about the amount of detail required in Part IV dealing with modified allocations from indirect cost pools using a modified allocation base or a rate that is either more or less than the normal ''full rate''. Some commenters indicated that too much detail was requested regarding those modified allocations whereas others expressed the view that more information should be made available.

Response: Certain parts of Part IV, in particular the question dealing with the application of overhead and G&A rates to specified transactions or costs, have been restated in an attempt to present a more effective and balanced data gathering instrument. It should, once more, be remembered that the aim has been to provide a vehicle for a contractor to disclose its CAS compliant cost accounting practices. Therefore, the Disclosure Statement should not be regarded as a substitute for an audit check list. It is for this reason that non-compliant practices have been expressly excluded from the Disclosure Statement.

Comment: Several commenters suggested changes in the format in which questions regarding Independent Research and Development (IR&D) and Bid and Proposal (B&P) costs were presented in Part IV.

Response: The two questions that previously dealt separately with IR&D and B&P respectively have been combined to provide a more compact approach to the topic. In particular, the new approach, unlike the one in the NPRM, does not presuppose that every contractor who incurs B&P expense also has incurred IR&D expense—a supposition that does not necessarily hold for civilian agencies.

Comment: One commenter suggested that the headings in the question in Part VI, Other Costs and Credits, dealing with charging and crediting vacation, holiday and sick pay be rearranged.

Response: The column headings have been changed to reflect the fact that salaried exempt and non-exempt employees (as defined by the Fair Labor Standards Act) are generally treated differently in this area.

Comment: Regarding Part VII, Deferred Compensation and Insurance Costs, most commenters representing contractors expressed the view that too much detailed and possibly superfluous and ambiguous information was required with respect to the various pension, post-retirement health, deferred compensation and insurance plans. One commenter had actually tested the proposed NPRM requirements by using actual plan data in completing selected parts of the various sections in Part VII. The estimated time to complete these various sections were clearly significant and possibly burdensome when extrapolated to cover the whole of Part VII. Even though the data submitted was not verified on an overall basis, it did provide valuable insight into the relative amount of time required to complete the various individual questions. The data also distinguished between time required on a ''recurring'' basis to keep the Disclosure Statement current, as contrasted with the initial effort of ''non-recurring'' time required to prepare the original submission. The general comments regarding time required to complete Part VII were frequently supplemented by specific suggestions regarding individual sections or questions.

Response: The Board is grateful to those commenters who spent significant amounts of time to prepare constructive comments on this part of the Disclosure Statement. In particular, the Board would like to express its gratitude to the commenter who actually completed sections of Part VII and made the relevant data available to the Board.

As a result of the input received from commenters, Part VII has been substantially redesigned in order to make it more ''user friendly''. When dealing with pension plans, post-retirement health benefits, employee group insurance, deferred compensation, and worker's compensation and property insurance, the amount of detailed information related to various aspects of cost measurement has been substantially reduced. The detailed data is required only for those plans or policies that account for 80-percent of the relevant category of costs—provided data on at least three plans is disclosed. Only a limited amount of general plan information is sought for all the other plans. By excluding the less significant plans from the more detailed disclosure requirements, it is anticipated that the paperwork burden will be significantly eased.

Some commenters also inferred that in certain instances actual numeric data was requested that would have to be updated annually. It has been made clear in the final document that when dealing with such items as actuarial assumptions, only the basis used to determine numeric values need be disclosed and not the actual values themselves. This clarification should ensure that no regular annual updates of the Disclosure Statement are prepared and submitted merely to reflect changes in the relevant numeric values.

Other, more specific changes to the various sections of Part VII are summarized below:

Pension Plans. The number of General Plan Information questions has been reduced from nine in the NPRM to six in the final document.

In the NPRM, the information requested for Defined Contribution Plans applied to all plans of this type. In the final version, if there are more than three plans, this information has to be supplied only for plans that account for 80-percent of the defined contribution plan costs.

Defined Benefit Plans. The number of questions asked in this area has not been changed. However, the topics covered and the manner of presentation have been somewhat changed. In particular, it has been made clear that regarding actuarial assumptions, no disclosure of actual numeric values is required. Only the basis for determining these numeric values need be described.

Post-Retirement Benefits (PRBs). This section has been rearranged to conform with the pattern established for pension plans in the previous section. In the NPRM, the questions posed were applicable to all PRB plans. In the final rule, questions dealing with general plan information have been separated from questions dealing with more specific aspects of PRB cost determination. The latter group consists of five questions and they have to be completed only for those plans that, in the aggregate, account for at least 80-percent of the total PRB costs. However, if there are three plans or less, then data on all the plans must be disclosed.

Employee Group Insurance Programs. Responses to this section of Part VII of the NPRM indicated that it was the most time consuming section to complete. Therefore, some significant changes have been made to the amount of information to be disclosed. First, if there are more than three policies or self-insurance plans, the applicable information should be provided only for those policies and self-insurance plans that, in the aggregate, account for at least 80-percent of the costs of the program for each category of insured risk. Second, the information previously requested under three separate questions has been recast as a single question in a tabular form. Third, a number of specific questions dealing with treatment of dividends, earned refunds, and employee contributions have been dropped as these items are largely covered by the provision of CAS 9904.416, Accounting for Insurance Costs. It is anticipated that the time needed to complete this section of Part VII will be significantly reduced as a result of the changes listed above.

Deferred Compensation Plans. This section has been recast to conform to the format used in the sections dealing with pension plans and PRBs. Therefore, the first five questions dealing with general plan information are applicable to all the plans. Two other questions, of a more substantive nature, should be completed for all the plans if there are no more than three plans. If there are more than three plans, the information should be provided for those plans that in the aggregate account for at least 80-percent of these deferred compensation costs.

Employee Stock Ownership Plans (ESOPs). Questions in this section have been reformulated, and, as a result, the total number of these general plan information questions has been increased by two as compared with the NPRM. These questions must be completed for all ESOPs.

Worker's Compensation Liability and Property Insurance. This section has been rearranged to conform to the format used in dealing with employee group insurance plans. In addition, the term ''line of insurance'' has been introduced in an attempt to clarify the nature of the aggregation of costs for which the relevant cost data has to be disclosed. In this context, for the purpose of guidance, ''line of insurance'' has the meaning attributed to it in Generally Accepted Auditing Standards (GAAS) literature (see *AICPA Audit and Accounting Guide, Audits of Property and Liability Insurance Companies*) and includes groupings such as fire and similar perils, general liability, marine perils, automobile liability and property damage, worker's compensation, theft, etc. If there are more than three policies or self-insurance plans, the applicable information should be provided only for those policies and plans that in the aggregate account for at least 80-percent of the applicable costs for a line of insurance. Also, two separate questions have been combined into a single question in a tabular form.

Comment: Several comments relating to Part VIII, Corporate or Group Expenses, dealt with the requirement in the NPRM to ''list all active segments and groups that are material in size reporting to the home . . . office''. Suggestions received included deletion of the words ''all'', ''active'', and ''that are material in size'' in the above quote from the first question in this part. At least one commenter suggested that if the term ''material'' is used, criteria for materiality should be developed.

Response: The suggestions regarding deletions have been accepted by the Board. The restated sentence reads: ''list segments and other intermediate level home offices reporting to this home office.''

The Board believes that this is an area where the individuals implementing the Standards and other regulations necessarily must exercise their own judgment in carrying out their tasks. The objective of this provision in the Disclosure Statement is to obtain a listing of segments and other entities to which home office expenses may be allocated. This allocation is part of the cost determination process for government contract costing purposes. Furthermore, this cost determination process, which includes all the relevant pronouncements of the Board, is subject to the materiality provisions of 9903.305. Specific reiteration of the materiality provision in each instance is not needed. Therefore, the requirement in the present instance is to list all the segments or other entities reporting to the home office that may have other than immaterial impact on the cost allocation process from the home office to its subordinate entities.

Comment: Several suggestions were received to improve and streamline the main section of Part VIII that deals with the pooling and allocation of home office expenses.

Response: Several of the suggestions received have been adopted. An addition has been made to the list of allocation base codes used and one question in the NPRM has been eliminated and its substance combined with another question.

List of Subjects in 48 CFR Part 9903

Cost accounting standards, Government procurement.

Richard C. Loeb,

Executive Secretary, Cost Accounting Standards Board.

For the reasons set forth in this preamble, chapter 99 of title 48 of the Code of Federal Regulations is amended as set forth below:

1. The authority citation for Part 9903 continues to read as follows:

Authority: Public Law 100–679, 102 Stat. 4056, 41 U.S.C. 422.

PART 9903—CONTRACT COVERAGE

Subpart 9903.2—CAS Program Requirements

2. Section 9903.202 is amended by deleting the illustrated CASB DS–1 and inserting a revised CASB DS–1.

BILLING CODE 3110–01–P

FORM APPROVED OMB NUMBER
0348-0051

COST ACCOUNTING STANDARDS BOARD DISCLOSURE STATEMENT REQUIRED BY PUBLIC LAW 100-679	INDEX

COST ACCOUNTING STANDARDS BOARD DISCLOSURE STATEMENT REQUIRED BY PUBLIC LAW 100-679	GENERAL INSTRUCTIONS

1. This Disclosure Statement has been designed to meet the requirements of Public Law 100-679, and persons completing it are to describe the contractor and its contract cost accounting practices. For complete regulations, instructions and timing requirements concerning submission of the Disclosure Statement, refer to Section 9903.202 of Chapter 99 Of Title 48 CFR (48 CFR 9903.202).

2. Part I of the Statement provides general information concerning each reporting unit (e.g., segment, Corporate or other intermediate level home office, or a business unit). Parts II through VII pertain to the types of costs generally incurred by the segment or business unit directly performing Federal contracts or similar cost objectives. Part VIII pertains to the types of costs that are generally incurred by a Home office and are allocated to one or more segments performing Federal contracts. For a definition of the term "home office", see 48 CFR 9904.403.

3. Each segment or business unit required to disclose its cost accounting practices should complete the Cover Sheet, the Certification, and Parts I through VII.

4. Each home office required to disclose its cost accounting practices for measuring, assigning and allocating its costs to segments performing Federal contracts or similar cost objectives shall complete the Cover Sheet, the Certification, Part I and Part VIII of the Disclosure Statement. Where a home office either establishes practices or procedures for the types of costs covered by Parts V, VI and VII,or incurs and then allocates these types of cost to its segments, the home office may complete Parts V, VI and VII to be included in the Disclosure Statement submitted by its segments. While a home office may have more than one segment submitting Disclosure Statements, only one Statement needs to be submitted to cover the home office operations.

5. The Statement must be signed by an authorized signatory of the reporting unit.

6. The Disclosure Statement should be answered by marking the appropriate line or inserting the applicable letter code which describes the segment's (reporting unit's) cost accounting practices.

7. A number of questions in this Statement may need narrative answers requiring more space than is provided. In such instances, the reporting unit should use the attached continuation sheet provided. The continuation sheet may be reproduced locally as needed. The number of the question involved should be indicated and the same coding required to answer the questions in the Statement should be used in presenting the answer on the continuation sheet. Continuation sheets should be inserted at the end of the pertinent Part of the Statement. On each continuation sheet, the reporting unit should enter the next sequential page number for that Part and, on the last continuation sheet used, the words "End of Part" should be inserted after the last entry.

8. Where the cost accounting practice being disclosed is clearly set forth in the contractor's existing written accounting policies and procedures, such documents may be cited on a continuation sheet and incorporated by reference at the option of the contractor. In such cases, the contractor should provide the date of issuance and effective date for each accounting policy and/or procedures document cited. Alternatively, copies of the relevant parts of such documents may be attached as appendices to the pertinent Disclosure Statement Part. Such continuation sheets and appendices should be labeled and cross-referenced with the applicable Disclosure Statement number and follow the page number specified in paragraph 7. Any supplementary comments needed to adequately describe the cost accounting practice being disclosed should also be provided.

9. Disclosure Statements must be amended when cost accounting practices are changed to comply with a new CAS or when practices are changed with or without knowledge of the Government (Also see 48 CFR 9903.202-3).

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10. Amendments shall be submitted to the same offices to which submission would have been made were an original Disclosure Statement filed.

11. Each amendment, or set of amendments should be accompanied by an amended cover sheet (indicating revision number and effective date of the change) and a signed certification. For all resubmissions, on each page, insert "Revision Number ____" and "Effective Date _____" in the Item Description block; and, insert a revision mark (e.g., "R") in the right hand margin of any line that is revised. Completely resubmitted Disclosure Statements must be accompanied by similar notations identifying the items which have been changed.

12. Use of this Disclosure Statement, amended February 1996, shall be phased in as follows:

A. New Contractors. This form shall be used by new contractors when they are initially required to disclose their cost accounting practices pursuant to 9903.202-1.

B. Existing Contractors. If a contractor has disclosed its cost accounting practices on a prior edition of the Disclosure Statement (CASB DS-1), such disclosure shall remain in effect until the contractor amends or revises a significant portion of the Disclosure Statement in accordance with CAS 9903.202-3. Minor amendments to an existing DS-1 may continue to be made using the prior form. However, when a substantive change is made, a complete Disclosure Statement must be filed using this form. In any event, all contractors and subcontractors must submit a new Disclosure Statement (this version of the CASB DS-1) not later than the beginning of the contractor's next full fiscal year after December 31, 1998.

ATTACHMENT - Blank Continuation Sheet

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COST ACCOUNTING STANDARDS BOARD DISCLOSURE STATEMENT REQUIRED BY PUBLIC LAW 100-679	CONTINUATION SHEET NAME OF REPORTING UNIT

Item No.	Item description

FORM CASB DS-1 (REV 2/96)

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COST ACCOUNTING STANDARDS BOARD DISCLOSURE STATEMENT REQUIRED BY PUBLIC LAW 100-679	COVER SHEET AND CERTIFICATION

0.1 Company or Reporting Unit.

Name

Street Address

City, State, & Zip Code

Division or Subsidiary of (if applicable)

0.2 Reporting Unit: (Mark one.)

A. ____ Business Unit comprising an entire business organization which is not divided into segments.
B.1. ____ Corporate Home Office
2. ____ Intermediate Level Home Office
3. ____ Segment or business unit reporting directly to a home office.

0.3 Official to Contact Concerning this Statement.

Name and Title

Phone number (including area code and extension)

0.4 Statement Type and Effective Date:

A. (Mark type of submission.. If a revision, enter number)
(a)____ Original Statement
(b)____ Revised Statement; Revision No.____

B. Effective Date of this Statement/Revision:_____

0.5 Statement Submitted To (Provide office name, location and telephone number, include area code and extension):

(a) Cognizant Federal Agency: ______________________________
(b) Cognizant Federal Auditor: ______________________________

CERTIFICATION

I certify that to the best of my knowledge and belief this Statement, as amended in the case of a revision, is the complete and accurate disclosure as of the above date by the above-named organization of its cost accounting practices, as required by the Disclosure Regulation (48 CFR 9903.202) of the Cost Accounting Standards Board under P.L. 100-679.

____
(Name)

____
(Title)

THE PENALTY FOR MAKING A FALSE STATEMENT IN THIS DISCLOSURE IS PRESCRIBED IN 18 U.S.C. § 1001

COST ACCOUNTING STANDARDS BOARD DISCLOSURE STATEMENT REQUIRED BY PUBLIC LAW 100-679	PART I - GENERAL INFORMATION NAME OF REPORTING UNIT

Item No.	Item description

Part I Instructions

Sales data for this part should cover the most recently completed fiscal year of the reporting unit. "Government CAS Covered Sales" includes sales under both prime contracts and subcontracts. "Annual CAS Covered Sales" includes intracorporate transactions.

1.1.0 Type of Business Entity of Which the Reporting Unit is a Part. (Mark one.)

A. _____ Corporation
B. _____ Partnership
C. _____ Proprietorship
D. _____ Not-for-profit organization
E. _____ Joint Venture
F. _____ Federally Funded Research and Development Center (FFRDC)
Y. _____ Other (Specify) ____________________

1.2.0 Predominant Type of Government Sales. (Mark one.) 1/

A. _____ Manufacturing
B. _____ Research and Development
C. _____ Construction
D. _____ Services
Y. _____ Other (Specify)____________________

1.3.0 Annual CAS Covered Government Sales as Percentage of Total Sales (Government and Commercial). (Mark one. An estimate is permitted for this section.) 1/

A. _____ Less than 10%
B. _____ 10%-50%
C. _____ 51%-80%
D. _____ 81% - 95%
E. _____ Over 95%

1.4.0 Description of Your Cost Accounting System for Government Contracts and Subcontracts. (Mark the appropriate line(s) and if more than one is marked, explain on a continuation sheet.) 1/

A. _____ Standard costs - Job order
B. _____ Standard costs - Process
C. _____ Actual costs - Job order
D. _____ Actual costs - Process
Y. _____ Other(s) 2/

1/ Do not complete when Part I is filed in conjunction with Part VIII.
2/ Describe on a Continuation Sheet.

COST ACCOUNTING STANDARDS BOARD DISCLOSURE STATEMENT REQUIRED BY PUBLIC LAW 100-679	PART I - GENERAL INFORMATION NAME OF REPORTING UNIT

Item No.	Item description
1.5.0	Identification of Differences Between Contract Cost Accounting and Financial Accounting Records. List on a continuation sheet, the types of costs charged to Federal contracts that are supported by memorandum records and identify the method used to reconcile with the entity's financial accounting records.
1.6.0	Unallowable Costs. Costs that are not reimbursable as allowable costs under the terms and conditions of Federal awards are identified as follows: (Mark all that apply and if more than one is marked, describe on a continuation sheet the major cost groupings, organizations, or other criteria for using each marked technique.)
1.6.1	Incurred costs. A. ____ Specifically identified and recorded separately in the formal financial accounting records. B. ____ Identified in separately maintained accounting records or workpapers. C. ____ Identifiable through use of less formal accounting techniques that permit audit verification. D. ____ Determinable by other means. 1/
1.6.2	Estimated costs. A. ______ By designation and description (in backup data, workpapers, etc) which have specifically been identified and recognized in making estimates. B. ______ By description of any other estimating technique employed to provide appropriate recognition of any unallowable amounts pertinent to the estimates. C. ______ Other. 1/
1.7.0	Fiscal Year: ________________ (Specify twelve month period used for financial accounting and reporting purposes, e.g., 1/1 to 12/31.)
1.7.1	Cost Accounting Period: ______________ (Specify period. If the cost accounting period used for the accumulation and reporting of costs under Federal contracts is other than the fiscal year identified in Item 1.7.0, explain circumstances on a continuation sheet.) 1/ Describe on a Continuation Sheet.

COST ACCOUNTING STANDARDS BOARD DISCLOSURE STATEMENT REQUIRED BY PUBLIC LAW 100-679	PART II - DIRECT COSTS NAME OF REPORTING UNIT

Item No.	Item description

Part II Instructions

This part covers the three major categories of direct costs, i.e., Direct Material, Direct Labor, and Other Direct Costs.

It is not the intent here to spell out or define the three elements of direct costs. Rather, each contractor should disclose practices based on its own definitions of what costs are, or will be, charged directly to Federal contracts or similar cost objectives as Direct Material, Direct Labor, or Other Direct Costs. For example, a contractor may charge or classify purchased labor of a direct nature as "Direct Material" for purposes of pricing proposals, requests for progress payments, claims for cost reimbursement, etc.; some other contractor may classify the same cost as "Direct Labor," and still another as "Other Direct Costs." In these circumstances, it is expected that each contractor will disclose practices consistent with its own classifications of Direct Material, Direct Labor, and Other Direct Costs.

2.1.0 Description of Direct Material. Direct material as used here is not limited to those items of material actually incorporated into the end product; they also include material, consumable supplies, and other costs when charged to Federal contracts or similar cost objectives as Direct Material. (Describe on a continuation sheet the principal classes or types of material and services which are charged as direct material; group the material and service costs by those which are incorporated in an end product and those which are not.)

2.2.0 Method of Charging Direct Material.

2.2.1 Direct Charge Not Through an Inventory Account at: (Mark the appropriate line(s) and if more than one is marked, explain on a continuation sheet.)

A. _____ Standard costs (Describe the type of standards used.) 1/
B. _____ Actual Costs
Y. _____ Other(s) 1/
Z. _____ Not applicable

2.2.2 Charged Direct from a Contractor-owned Inventory Account at: (Mark the appropriate line(s) and if more than one is marked, explain on a continuation sheet.)

A. _____ Standard costs 1/
B. _____ Average Costs 1/
C. _____ First in, first out
D. _____ Last in, first out
Y. _____ Other(s) 1/
Z. _____ Not applicable

1/ Describe on a Continuation Sheet.

COST ACCOUNTING STANDARDS BOARD DISCLOSURE STATEMENT REQUIRED BY PUBLIC LAW 100-679	PART II - DIRECT COSTS NAME OF REPORTING UNIT

Item No.	Item description
2.3.0	<u>Timing of Charging Direct Material.</u> (Mark the appropriate line(s) to indicate the point in time at which direct material are charged to Federal contracts or similar cost objectives, and if more than one line is marked, explain on a continuation sheet.) A. _____ When orders are placed B. _____ When both the material and invoice are received C. _____ When material is issued or released to a process, batch, or similar intermediate cost objective D. _____ When material is issued or released to a final cost objective E. _____ When invoices are paid Y. _____ Other(s) 1/ Z. _____ Not applicable
2.4.0	<u>Variances from Standard Costs for Direct Material.</u> (Do not complete this item unless you use a standard cost method, i.e., you have marked Line A of Item 2.2.1, or 2.2.2. Mark the appropriate line(s) in Items 2.4.1, 2.4.2, and 2.4.4, and if more than one line is marked, explain on a continuation sheet.)
2.4.1	<u>Type of Variance.</u> A. _____ Price B. _____ Usage C. _____ Combined (A and B) Y. _____ Other(s) 1/
2.4.2	<u>Level of Production Unit used to Accumulate Variance.</u> Indicate which level of production unit is used as a basis for accumulating material variances. A. _____ Plant-wide Basis B. _____ By Department C. _____ By Product or Product Line Y. _____ Other(s) 1/
2.4.3	<u>Method of Disposing of Variance.</u> Describe on a continuation sheet the basis for, and the frequency of, the disposition of the variance.
2.4.4	<u>Revisions.</u> Standard costs for direct materials are revised: A. _____ Semiannually B. _____ Annually C. _____ Revised as needed, but at least once annually Y. _____ Other(s) 1/
	1/ Describe on a Continuation Sheet.

COST ACCOUNTING STANDARDS BOARD DISCLOSURE STATEMENT REQUIRED BY PUBLIC LAW 100-679	PART II - DIRECT COSTS NAME OF REPORTING UNIT

Item No.	Item description
2.5.0	Method of Charging Direct Labor: (Mark the appropriate line(s) for each Direct Labor Category to show how such labor is charged to Federal contracts or similar cost objectives, and if more than one line is marked, explain on a continuation sheet. Also describe on a continuation sheet the principal classes of labor rates that are, or will be applied to Manufacturing Labor, Engineering Labor, and Other Direct Labor, in order to develop direct labor costs.

	Direct Labor Category		
	Manufacturing	Engineering	Other Direct
A. Individual/actual rates	____	____	____
B. Average rates – uncompensated overtime hours included in computation 1/	____	____	____
C. Average rates – uncompensated overtime hours excluded from computation	____	____	____
D. Standard costs/rates 1/	____	____	____
Y. Other(s) 1/	____	____	____
Z. Labor category is not applicable	____	____	____

Item No.	Item description
2.6.0	Variances from Standard Costs for Direct Labor. (Do not complete this item unless you use a standard costs/rate method, i.e., you have marked Line D of Item 2.5.0 for any direct labor category. Mark the appropriate line(s) in each column of Items 2.6.1, 2.6.2, and 2.6.4. If more than one is marked, explain on a continuation sheet.)
2.6.1	Type of Variance.

	Direct Labor Category		
	Manufacturing	Engineering	Other Direct
A. Rate	____	____	____
B. Efficiency	____	____	____
C. Combined (A and B)	____	____	____
Y. Other(s) 1/	____	____	____
Z. Labor category is not applicable	____	____	____

1/ Describe on a Continuation Sheet.

COST ACCOUNTING STANDARDS BOARD DISCLOSURE STATEMENT REQUIRED BY PUBLIC LAW 100-679	PART II - DIRECT COSTS
	NAME OF REPORTING UNIT

Item No.	Item description

2.6.2 Level of Production Unit used to Accumulate Variance. Indicate which level of production unit is used as a basis for accumulating the labor variances.

	Direct Labor Category		
	Manufacturing	Engineering	Other Direct
A. Plant-wide basis	____	____	____
B. By department	____	____	____
C. By product or product line	____	____	____
Y. Other(s) 1/	____	____	____
Z. Labor category is not applicable	____	____	____

2.6.3 Method of Disposing of Variance. Describe on a continuation sheet the basis for, and the frequency of, the disposition of the variance.

2.6.4 Revisions. Standard costs for direct labor are revised:

A. ____ Semiannually
B. ____ Annually
C. ____ Revised as needed, but at least once annually
Y. ____ Other(s) 1/

2.7.0 Description of Other Direct Costs. Other significant items of cost directly identified with Federal contracts or other final cost objectives. Describe on a continuation sheet the principal classes of other costs that are always charged directly, that is, identified specifically with final cost objectives, e.g., fringe benefits, travel costs, services, subcontracts, etc.

2.7.1 When Employee Travel Expenses for lodging and subsistence are charged direct to Federal contracts or similar cost objectives the charge is based on:

A. ____ Actual Costs
B. ____ Per Diem Rates
C. ____ Lodging at actual costs and subsistence at per diem
Y. ____ Other Method 1/
Z. ____ Not Applicable

2.8.0 Credits to Contract Costs. When Federal contracts or similar cost objectives are credited for the following circumstances, are the rates of direct labor, direct materials, other direct costs and applicable indirect costs always the same as those for the original charges? (Mark one line for each circumstance, and for each "No" answer, explain on a continuation sheet how the credit differs from the original charge.)

Circumstance	A. Yes	B. No	Z. Not Applicable
(a) Transfers to other jobs/contracts	____	____	____
(b) Unused or excess materials remaining upon completion of contract	____	____	____

1/ Describe on a Continuation Sheet.

COST ACCOUNTING STANDARDS BOARD DISCLOSURE STATEMENT REQUIRED BY PUBLIC LAW 100-679	PART III - DIRECT VS. INDIRECT COSTS NAME OF REPORTING UNIT

Item No.	Item description

3.1.0 **Criteria for Determining How Costs are Charged to Federal Contracts Or Similar Cost Objectives.** Describe on a continuation sheet your criteria for determining when costs incurred for the same purpose, in like circumstances, are treated either as direct costs only or as indirect costs only with respect to final cost objectives.

3.2.0 **Treatment of Costs of Specified Functions, Elements of Cost, or Transactions.** (For each of the functions, elements of cost or transactions listed in Items 3.2.1, 3.2.2, and 3.2.3, enter one of the Codes A through F, or Y, to indicate how the item is treated. Enter Code Z in those lines that are not applicable to you. Also, specify the name(s) of the indirect pool(s) (as listed in 4.1.0, 4.2.0 and 4.3.0) for each function, element of cost, or transaction coded E or F. If Code E, Sometimes direct/Sometimes indirect, is used, explain on a continuation sheet the circumstances under which both direct and indirect allocations are made.)

Treatment Code

A. Direct material
B. Direct labor
C. Direct material and labor
D. Other direct costs
E. Sometimes direct/Sometimes indirect
F. Indirect only
Y. Other(s) 1/
Z. Not applicable

3.2.1

Functions, Elements of Cost, or Transactions Related to Direct Material	Treatment Code	Name of Pool(s)
(a) Cash Discounts on Purchases	____	____________
(b) Freight in	____	____________
(c) Income from Sale of Scrap	____	____________
(d) Income from Sale of Salvage	____	____________
(e) Incoming Material Inspection (receiving)	____	____________
(f) Inventory adjustment	____	____________
(g) Purchasing	____	____________
(h) Trade Discounts, Refunds, Rebates, and Allowances on Purchases	____	____________

1/ Describe on a Continuation Sheet.

COST ACCOUNTING STANDARDS BOARD DISCLOSURE STATEMENT REQUIRED BY PUBLIC LAW 100-679	PART III - DIRECT VS. INDIRECT COSTS NAME OF REPORTING UNIT

Item No.	Item description			
3.2.2	Functions, Elements of Cost, or Transactions Related to Direct Labor		Treatment Code	Name of Pool(s)
	(a)	Incentive Compensation	____	____________
	(b)	Holiday Differential (Priemium Pay)	____	____________
	(c)	Vacation Pay	____	____________
	(d)	Overtime Premium Pay	____	____________
	(e)	Shift Premium Pay	____	____________
	(f)	Pension Costs	____	____________
	(g)	Post Retirement Benefits Other Than Pensions	____	____________
	(h)	Health Insurance	____	____________
	(i)	Life Insurance	____	____________
	(j)	Other Deferred Compensation 1/	____	____________
	(k)	Training	____	____________
	(l)	Sick Leave	____	____________

1/ Describe on a Continuation Sheet.

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Item No.	Item description			
3.2.3	Functions, Elements of Cost, or Transactions - Miscellaneous		Treatment Code	Name of Pool(s)
	(a)	Design Engineering (in-house)	____	____________
	(b)	Drafting (in-house)	____	____________
	(c)	Computer Operations (in-house)	____	____________
	(d)	Contract Administration	____	____________
	(e)	Subcontract Administration Costs	____	____________
	(f)	Freight Out (finished product)	____	____________
	(g)	Line (or production) Inspection	____	____________
	(h)	Packaging and Preservation	____	____________
	(i)	Preproduction Costs and Start-up Costs	____	____________
	(j)	Departmental Supervision	____	____________
	(k)	Professional Services (consultant fees)	____	____________
	(l)	Purchased Labor of Direct Nature (on premises)	____	____________
	(m)	Purchased Labor of Direct Nature (off premises)	____	____________
	(n)	Rearrangement Costs	____	____________
	(o)	Rework Costs	____	____________
	(p)	Royalties	____	____________
	(q)	Scrap Work	____	____________
	(r)	Special Test Equipment	____	____________
	(s)	Special Tooling	____	____________
	(t)	Warranty Costs	____	____________
	(u)	Rental Costs	____	____________
	(v)	Travel and Subsistence	____	____________
	(w)	Employee Severance Pay	____	____________
	(x)	Security Guards	____	____________

COST ACCOUNTING STANDARDS BOARD DISCLOSURE STATEMENT REQUIRED BY PUBLIC LAW 100-679	PART IV - INDIRECT COSTS NAME OF REPORTING UNIT

Item No.	Item description

Part IV Instructions

For the purpose of this part, indirect costs have been divided into three categories: (i) manufacturing, engineering, and comparable indirect costs, (ii) general and administrative (G&A) expenses, and (iii) service center and expense pool costs, as defined in Item 4.3.0. The term "overhead," as used in this part, refers only to the first category of indirect costs.

The following Allocation Base Codes are provided for use in connection with Items 4.1.0, 4.2.0 and 4.3.0.

- A. Sales
- B. Cost of sales
- C. Total Cost input (direct material, direct labor, other direct costs and applicable overhead)
- D. Value-added cost input (total cost input less direct material and subcontract costs)
- E. Total cost incurred (total cost input plus G&A expenses)
- F. Prime cost (direct material, direct labor and other direct cost)
- G. Processing or conversion cost (direct labor and applicable overhead)
- H. Direct labor dollars
- I. Direct labor hours
- J. Machine hours
- K. Usage
- L. Unit of production
- M. Direct material cost
- N. Total payroll dollars (direct and indirect employees)
- O. Headcount or number of employees (direct and indirect employees)
- P. Square feet
- Y. Other(s), or more than one basis (Describe on a continuation sheet.)
- Z. Pool not applicable

4.1.0 Overhead Pools. List all the overhead pools, i.e., pools of indirect costs, other than general and administrative (G&A) expenses, that are allocated to final cost objectives without any intermediate allocations. A segment or business unit may have only a single pool encompassing all of its overhead costs or alternatively it may have several pools such as manufacturing overhead, engineering overhead, material handling overhead, etc. For each pool listed indicate the base used for allocating such pooled expenses to Federal contracts or similar cost objectives. Also, for each of the pools indicate (a) the major functions, activities, and elements of cost included, and (b) the make up of the allocation base. Use a continuation sheet if additional space is required.

Allocation Base Code

1. ______________________

   (a) Major functions, activities, and elements of cost included:

   ____

   ____

   (b) Description/Make up of the allocation base:

   ____

   ____

COST ACCOUNTING STANDARDS BOARD DISCLOSURE STATEMENT REQUIRED BY PUBLIC LAW 100-679	PART IV - INDIRECT COSTS NAME OF REPORTING UNIT

Item No.	Item description
4.1.0	Continued. Allocation Base Code 2. ____________ ____ (a) Major functions, activities, and elements of cost included: ____________ ____________ (b) Description/Make up of the allocation base: ____________ ____________
4.2.0	General and Administrative (G&A) Expense Pool(s). Select among the three categories of pools below that describe(s) the manner in which G&A expenses are allocated. For each category of pool(s) selected indicate the base(s) used for allocating such pooled expenses to Federal contracts or similar cost objectives. Also, for each category of pool(s) selected, indicate (a) the major functions, activities, and elements of cost included, and (b) the make up of the allocation base(s). For example, if direct labor dollars are used, are fringe benefits included? If a total cost input base is used, is the imputed cost of capital included? Use a continuation sheet if additional space is required. Single Pool Containing G&A Expenses Only — Allocation Base Code ____________ ____ (a) Major functions, activities, and elements of cost included: ____________ ____________ (b) Description/Make up of the allocation base: ____________ ____________

COST ACCOUNTING STANDARDS BOARD DISCLOSURE STATEMENT REQUIRED BY PUBLIC LAW 100-679	PART IV - INDIRECT COSTS NAME OF REPORTING UNIT

Item No.	Item description
4.2.0	Continued.

Single Pool Containing Both G&A and Non-G&A Expenses — Allocation Base Code

______________________ ____

(a) Major functions, activities, and elements of cost included:

____

____

(b) Description/Make up of the allocation base:

____

____

Special Allocations — Allocation Base Code

1. ______________________ ____

(a) Major functions, activities, and elements of cost included:

____

____

(b) Description/Make up of the allocation base:

____

____

2. ______________________ ____

(a) Major functions, activities, and elements of cost included:

____

____

(b) Description/Make up of the allocation base:

____

____

COST ACCOUNTING STANDARDS BOARD DISCLOSURE STATEMENT REQUIRED BY PUBLIC LAW 100-679	PART IV - INDIRECT COSTS NAME OF REPORTING UNIT

Item No.	Item description
4.3.0	Service Center and Expense Pool Allocation Bases.

Service centers are departments or other functional units which perform specific technical and/or administrative services primarily for the benefit of other units within a reporting unit. Expense pools are pools of indirect costs that are allocated primarily to other units within a reporting unit. Examples of service centers are data processing centers, reproduction services and communications services. Examples of expense pools are use and occupancy pools and fringe benefit pools.

Category Code

Generally, costs incurred by such centers or pools are, or can be, charged or allocated (i) partially to specific final cost objectives as direct costs and partially to other indirect cost pools (such as a manufacturing overhead pool) for subsequent reallocation to several final cost objectives, referred to herein as Category "A", and (ii) only to several other indirect cost pools (such as a manufacturing overhead pool, engineering overhead pool and G&A expense pool) for subsequent reallocation to several final cost objectives, referred to herein as Category "B".

Rate Code

Some service centers or expense pools may use predetermined billing or costing rates to charge or allocate the costs (Rate Code A) while others may charge or allocate on an actual basis (Rate Code B).

List all the service centers and expense pools and enter in column (1) Code A or B to indicate the category of pool. Enter in Column (2) one of the Allocation Base Codes A through P, or Y, listed on Page ___, to indicate the base used for charging or allocating service center or expense pool costs. Enter in Column (3) Rate Code A or B to describe the costing method used. Also, for each of the centers and pools indicate (a) the major functions, activities, and elements of cost included, and (b) the make up of the allocation base. Use a continuation sheet if additional space is required.

	Service Center or Expense Pool	Category Code (1)	Allocation Base Code (2)	Rate Code (3)
1.	____________	___	___	___

(a) Major functions, activities, and elements of cost included:

____

____

(b) Description/Make up of the allocation base:

____

____

2.	____________	___	___	___

(a) Major functions, activities, and elements of cost included:

____

____

(b) Description/Make up of the allocation base:

____

____

COST ACCOUNTING STANDARDS BOARD DISCLOSURE STATEMENT REQUIRED BY PUBLIC LAW 100-679	PART IV - INDIRECT COSTS NAME OF REPORTING UNIT

Item No. — **Item description**

4.4.0 **Treatment of Variances from Actual Cost (Underabsorption or Overabsorption).** Where predetermined billing or costing rates are used to charge costs of service centers and expense pools to Federal contracts or other indirect cost pools (Rate Code A in Column (3) of Item 4.3.0), variances from actual costs are: (Mark the appropriate line(s) and if more than one is marked, explain on a continuation sheet.)

A. ____ Prorated to users on the basis of charges made, at least once annually
B. ____ All charged or credited to indirect cost pool(s) at least once annually
Y. ____ Other(s) 1/
Z. ____ Service center is not applicable to reporting unit

4.5.0 **Application of Overhead and G&A Rates to Specified Transactions or Costs.**

This item is directed to ascertaining your practice in special situations where, in lieu of establishing a separate indirect cost pool, allocation is made from an established overhead or G&A pool at a rate other than the normal full rate for that pool. In the case of such a special allocation, the terms "less than full rate" or "more than full rate" should be used to describe the practice. The terms do not apply to situations where, as in some cases of off-site activities, etc., a separate indirect cost pool and base are used and the rate for such activities is lower than the "in-house" rate.

For each of the transactions or costs listed below, enter one of the following codes to indicate your indirect cost allocation practice with respect to that transaction or cost. If Code A, full rate, is entered, identify on a continuation sheet the pool(s) reported under items 4.1.0, 4.2.0, and 4.3.0, which are applicable. If Codes B or C, less than or more than the full rate, is entered, describe on a continuation sheet the major types of expenses that are covered by such a rate.

Rate Code

A. Full rate
B. Special allocation at less than full rate
C. Special allocation at more than full rate
D. No overhead or G&A is applied
Z. Transaction or cost is not applicable to reporting unit

Transaction or Cost to Which Indirect Costs May be Allocated		Rate Code
(a)	Subcontract costs	____
(b)	Purchased Labor	____
(c)	Government-furnished materials	____
(d)	Self-constructed depreciable assets	____
(e)	Labor on installation of assets	____
(f)	Off-site work	____
(g)	Interorganizational transfers out	____
(h)	Interorganizational transfers in (Also indicate on a continuation sheet the basis used by you as transferee to charge the cost or price of interorganizational transfers to Federal contracts or similar cost objectives. If the charge is based on cost, indicate whether the transferor's G&A expenses are included.)	____
(i)	Other transactions or costs (Enter Code B or C on this line if there are other transactions or costs to which either less than full rate or more than full rate is applied. List such transactions or costs on a continuation sheet, and for each describe the major types of expenses covered by such a rate. If there are no other such transactions or costs, enter code Z.)	____

1/ Describe on a Continuation Sheet.

COST ACCOUNTING STANDARDS BOARD DISCLOSURE STATEMENT REQUIRED BY PUBLIC LAW 100-679	PART IV - INDIRECT COSTS NAME OF REPORTING UNIT

Item No.	Item description
4.6.0	Independent Research and Development (IR&D) and Bid and Proposal (B&P) Costs. Definitions of and requirements for the allocation of IR&D and B&P costs are contained in 48 CFR 9904.420. The full rate of all allocable manufacturing, engineering, and/or other overhead is applied to IR&D and B&P costs as if IR&D and B&P projects were under contract, and the "burdened" IR&D and B&P costs are: (Mark appropriate line(s).) A. ____ Allocated to Federal contracts or similar cost objectives by means of a composite pool with G&A expenses. B. ____ Allocated to Federal contracts or similar cost objectives by means of a separate pool. C. ____ Transferred to the corporate or home office level for reallocation to the benefiting segments. Y. ____ Other 1/ Z. ____ Not applicable
4.7.0	Cost of Capital Committed to Facilities. In accordance with instructions for Form CASB-CMF, undistributed facilities capital items are allocated to overhead and G&A expense pools: (Mark one.) A. ____ On a basis identical to that used to absorb the actual depreciation or amortization from these facilities; land is assigned in the same manner as the facilities to which it relates. B. ____ On a basis not identical to that used to absorb the actual depreciation or amortization from these facilities. (Describe on a continuation sheet the difference for each step of the allocation process.) C. ____ By the "alternative allocation process" described in instructions for Form CASB-CMF. Z. ____ Not applicable. 1/ Describe on a Continuation Sheet.

COST ACCOUNTING STANDARDS BOARD DISCLOSURE STATEMENT REQUIRED BY PUBLIC LAW 100-679	PART V - DEPRECIATION AND CAPITALIZATION PRACTICES NAME OF REPORTING UNIT

Item No.	Item description

Part V Instructions

Where a home office either establishes practices or procedures for the types of costs covered in this Part or incurs and then allocates these costs to its segments, the home office may complete this Part to be included in the submission by the segment as indicated on page (i) 4., General Instructions.

5.1.0 Depreciating Tangible Assets for Government Contract Costing. (For each of the asset categories listed on Page ___, enter a code from A through H in Column (1) describing the method of depreciation (Code F for assets that are expensed); a code from A through C in Column (2) describing the basis for determining useful life; a code from A through C in Column (3) describing how depreciation methods or use charges are applied to property units; and a Code A, B or C in Column (4) indicating whether or not residual value is deducted from the total cost of depreciable assets. Enter Code Y in each column of an asset category where another or more than one method applies. Enter Code Z in Column (1) only, if an asset category is not applicable.)

Column (1)–Depreciation Method Code

A. Straight Line
B. Declining balance
C. Sum-of-the years digits
D. Machine hours
E. Unit of production
F. Expensed at acquisition
G. Use charge
H. Method of depreciation used under the applicable Internal Revenue Procedures
Y. Other or more than one method 1/
Z. Asset category is not applicable

Column (2)–Useful Life Code

A. Replacement experience adjusted by expected changes in periods of usefulness
B. Term of Lease
C. Estimated on the basis of Asset Guidelines under Internal Revenue Procedures
Y. Other, or more than one method 1/

Column (3)–Property Units Code

A. Individual units are accounted for separately
B. Applied to groups of assets with similar service lives
C. Applied to groups of assets with varying service lives
Y. Other or more than one method 1/

Column (4)–Residual Value Code

A. Residual value is estimated and deducted
B. Residual value is covered by the depreciation method (e.g., declining balance)
C. Residual value is estimated but not deducted in accordance with the provisions of 48 CFR 9904.409 1/
Y. Other or more than one method 1/

1/ Describe on a Continuation Sheet.

COST ACCOUNTING STANDARDS BOARD DISCLOSURE STATEMENT REQUIRED BY PUBLIC LAW 100-679	PART V - DEPRECIATION AND CAPITALIZATION PRACTICES NAME OF REPORTING UNIT

Item No.	Item description

5.1.0 Continued.

Asset Category	Depreciation Method Code (1)	Useful Life Code (2)	Property Units Code (3)	Residual Value Code (4)
(a) Land improvements	___	___	___	___
(b) Building	___	___	___	___
(c) Building improvements	___	___	___	___
(d) Leasehold improvements	___	___	___	___
(e) Machinery and equipment	___	___	___	___
(f) Furniture and fixtures	___	___	___	___
(g) Automobiles and trucks	___	___	___	___
(h) Data processing equipment	___	___	___	___
(i) Programming/reprogramming costs	___	___	___	___
(j) Patterns and dies	___	___	___	___
(k) Tools	___	___	___	___
(l) Other depreciable asset categories (Enter Code Y on this line if other asset categories are used and enumerate on a continuation sheet each such asset category and the applicable codes. Otherwise enter Code Z.)	___	___	___	___

5.2.0 Depreciation Practices for Costing, Financial Accounting, and Income Tax. Are depreciation practices the same for costing Federal contracts as for financial accounting and income tax? (Mark either (A) or (B) on each line under Financial Accounting and Income Tax. Not-for-profit organizations need not complete this item.)

Financial Accounting	A. Yes	B. No
(a) Methods	___	___
(b) Useful lives	___	___
(c) Property units	___	___
(d) Residual values	___	___

Income Tax	A. Yes	B. No
(e) Methods	___	___
(f) Useful lives	___	___
(g) Property units	___	___
(h) Residual values	___	___

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COST ACCOUNTING STANDARDS BOARD DISCLOSURE STATEMENT REQUIRED BY PUBLIC LAW 100-679	PART V - DEPRECIATION AND CAPITALIZATION PRACTICES NAME OF REPORTING UNIT

Item No.	Item description

5.3.0 Fully Depreciated Assets. Is a usage charge for fully depreciated assets charged to Federal contracts? (Mark one.)

A. ____ Yes 1/
B. ____ No
Z. ____ Not applicable

5.4.0 Treatment of Gains and Losses on Disposition of Depreciable Property. Gains and losses are: (Mark the appropriate line(s) and if more than one is marked, explain on a continuation sheet.)

A. ____ Credited or charged currently to the same overhead or G&A pools to which the depreciation of the assets was charged

B. ____ Taken into consideration in the depreciation cost basis of the new items, where trade-in is involved

C. ____ Not accounted for separately, but reflected in the depreciation reserve account

Y. ____ Other(s) 1/

Z. ____ Not applicable

5.5.0 Capitalization or Expensing of Specified Costs. (Mark one line on each item to indicate your practices regarding capitalization or expensing of specified costs incurred in connection with capital assets. If the same specified cost is sometimes expensed and sometimes capitalized, mark both lines and describe on a continuation sheet the circumstances when each method is used.)

	Cost	A. Expensed	B. Capitalized
(a)	Freight-in	____	____
(b)	Sales taxes	____	____
(c)	Excise taxes	____	____
(d)	Architect-engineer fees	____	____
(e)	Overhauls (extraordinary repairs)	____	____

1/ Describe on a Continuation Sheet.

COST ACCOUNTING STANDARDS BOARD DISCLOSURE STATEMENT REQUIRED BY PUBLIC LAW 100-679	PART V - DEPRECIATION AND CAPITALIZATION PRACTICES NAME OF REPORTING UNIT

Item No.	Item description
5.6.0	Criteria for Capitalization. Enter (a) the minimum dollar amount of acquisition cost or expenditures for addition, alteration and improvement of depreciable assets capitalized, and (b) the minimum number of expected life years of capitalized assets. If more than one dollar amount or number applies, show the information for the majority of your depreciable assets, and enumerate on a continuation sheet the dollar amounts and/or number of years for each category or subcategory of assets involved which differ from those for the majority of assets. (a) Minimum dollar amount capitalized ________ (b) Minimum service life years ________
5.7.0	Group or Mass Purchase. Are group or mass purchases (original complement) of low cost equipment, which individually are less than the capitalization amount indicated above, capitalized? (Mark one. If Yes is marked, provide the minimum aggregate dollar amount capitalized.) A. ___ Yes __________ Minimum aggregate dollar amount capitalized B. ___ No

COST ACCOUNTING STANDARDS BOARD DISCLOSURE STATEMENT REQUIRED BY PUBLIC LAW 100-679	PART VI - OTHER COSTS AND CREDITS NAME OF REPORTING UNIT

Item No. | **Item description**

Part VI Instructions

Where a home office either establishes practices or procedures for the types of costs covered in this Part or incurs and then allocates these costs to its segments, the home office may complete this Part to be included in the submission by the segment as indicated on page (ii) 4., General Instructions.

6.1.0 Method of Charging and Crediting Vacation, Holiday, and Sick Pay. (Mark the appropriate line(s) in each column of Items 6.1.1, 6.1.2, 6.1.3 and 6.1.4 to indicate the method used to charge, or credit any unused or unpaid vacation, holiday, or sick pay. If more than one method is marked, explain on a continuation sheet.)

Item No.	Item description	Hourly (1)	Salaried: Non-exempt 1/ (2)	Salaried: Exempt 1/ (3)
6.1.1	Charges for Vacation Pay			
	A. When Accrued (earned)	___	___	___
	B. When Taken	___	___	___
	Y. Other(s) 2/	___	___	___
6.1.2	Charges for Holiday Pay			
	A. When Accrued (earned)	___	___	___
	B. When Taken	___	___	___
	Y. Other(s) 2/	___	___	___
6.1.3	Charges for Sick Pay			
	A. When Accrued (earned)	___	___	___
	B. When Taken	___	___	___
	Y. Other(s) 2/	___	___	___
6.1.4	Credits for Unused or Unpaid Vacation, Holiday, or Sick Pay			
	A. Credited to Accounts Originally charged at Least Once Annually	___	___	___
	B. Credited to Indirect Cost Pools at Least Once Annually	___	___	___
	C. Carried Over to Future Cost Accounting Periods 2/	___	___	___
	Y. Other(s) 2/	___	___	___
	Z. Not Applicable	___	___	___

1/ For the definition of Non-exempt and Exempt salaries, see the Fair Labor Standards Act, 29 U.S.C. 206.

2/ Describe on a Continuation Sheet.

COST ACCOUNTING STANDARDS BOARD DISCLOSURE STATEMENT REQUIRED BY PUBLIC LAW 100-679	PART VI - OTHER COSTS AND CREDITS NAME OF REPORTING UNIT

Item No.	Item description
6.2.0	Supplemental Unemployment (Extended Layoff) Benefit Plans. Costs of such plans are charged to Federal contracts: (Mark the appropriate line(s) and if more than one is marked, explain on a continuation sheet.) A. ____ When actual payments are made directly to employees B. ____ When accrued (book accrual or funds set aside but no trust fund involved) C. ____ When contributions are made to a nonforfeitable trust fund D. ____ Not charged Y. ____ Other(s) 1/ Z. ____ Not applicable
6.3.0	Severance Pay and Early Retirement. Costs of normal turnover severance pay and early retirement incentive plans, as defined in FAR 31.2 or other pertinent procurement regulations, which are charged directly or indirectly to Federal contracts, are based on: (Mark the appropriate line(s) and if more than one is marked, explain on a continuation sheet.) A. ____ Actual payments made B. ____ Accrued amounts on the basis of past experience C. ____ Not charged Y. ____ Other(s) 1/ Z. ____ Not applicable
6.4.0	Incidental Receipts. (Mark the appropriate line(s) to indicate the method used to account for incidental or miscellaneous receipts, such as revenues from renting real and personal property or selling services, when related costs have been allocated to Federal contracts. If more than one is marked, explain on a continuation sheet.) A. ____ The entire amount of the receipt is credited to the same indirect cost pools to which related costs have been charged B. ____ Where the amount of the receipt includes an allowance for profit, the cost-related part of the receipt is credited to the same indirect cost pools to which related costs have been charged; the profits are credited to Other (Miscellaneous) Income C. ____ The entire amount of the receipt is credited directly to Other (Miscellaneous) Income Y. ____ Other(s) 1/ Z. ____ Not applicable 1/ Describe on a Continuation Sheet.

COST ACCOUNTING STANDARDS BOARD DISCLOSURE STATEMENT REQUIRED BY PUBLIC LAW 100-679	PART VI - OTHER COSTS AND CREDITS NAME OF REPORTING UNIT

Item No.	Item description
6.5.0	<u>Proceeds from Employee Welfare Activities.</u> Employee welfare activities include all of those activities set forth in FAR 31.2 . (Mark the appropriate line(s) to indicate the practice followed in accounting for the proceeds from such activities. If more than one is marked, explain on a continuation sheet.) A. ___ Proceeds are turned over to an employee-welfare organization or fund; such proceeds are reduced by all applicable costs such as depreciation, heat, light and power B. ___ Same as above, except the proceeds are not reduced by all applicable costs C. ___ Proceeds are credited at least once annually to the appropriate cost pools to which costs have been charged D. ___ Proceeds are credited to Other (Miscellaneous) Income Y. ___ Other(s) 1/ Z. ___ Not applicable 1/ Describe on a Continuation Sheet.

COST ACCOUNTING STANDARDS BOARD DISCLOSURE STATEMENT REQUIRED BY PUBLIC LAW 100-679	PART VII - DEFERRED COMPENSATION AND INSURANCE COST NAME OF REPORTING UNIT

Item No.	Item description

Part VII Instructions

This part covers the measurement and assignment of costs for employee pensions, post retirement benefits other than pensions (including post retirement health benefits), certain other types of deferred compensation, and insurance. Some organizations may incur all of these costs at the corporate or home office level, while others may incur them at subordinate organizational levels. Still others may incur a portion of these costs at the corporate level and the balance at subordinate organizational levels.

Where the segment (reporting unit) does not directly incur such costs, the segment should, on a continuation sheet, identify the organizational entity that incurs and records such costs, and should require that entity to complete the applicable portions of this Part VII. Each such entity is to fully disclose the methods and techniques used to measure, assign, and allocate such costs to the segment(s) performing Federal contracts or similar cost objectives. Necessary explanations required to achieve that objective should be provided by the entity on a continuation sheet.

Where a home office either establishes practices or procedures for the types of costs covered in this Part VII or incurs and then allocates those costs to its segments, the home office may complete this Part to be included in the submission by the segment as indicated on page (i) 4., General Instructions.

7.1.0 Pension Plans with Costs Charged to Federal Contracts. Identify the types and number of pension plans whose costs are charged to Federal contracts or similar cost objectives: (Mark applicable line(s) and enter number of plans.)

Type of Pension Plan	Number of Plans
A. Defined-Contribution Plan (Other than ESOPs (see 7.5.0))	
1. Non-Qualified	____
2. Qualified	____
B. Defined-Benefit Plan	
1. Non-Qualified	
a. Costs are measured and assigned on accrual basis	____
b. Costs are measured and assigned on cash (pay-as-you-go) basis	____
2. Qualified	
a. Trusteed (Subject to ERISA's minimum funding requirements)	____
b. Fully-insured plan (Exempt from ERISA's minimum funding requirements) treated as a defined-contribution plan	____
c. Collectively bargained plan treated as a defined-contribution plan	____
Y. ____ Other 1/	____
Z. ____ Not Applicable (Proceed to Item 7.2.0)	

1/ Describe on a Continuation Sheet.

COST ACCOUNTING STANDARDS BOARD DISCLOSURE STATEMENT REQUIRED BY PUBLIC LAW 100-679	PART VII - DEFERRED COMPENSATION AND INSURANCE COST NAME OF REPORTING UNIT

Item No.	Item description
7.1.1	General Plan Information. On a continuation sheet for each plan identified in Item 7.1.0, provide the following information: A. The plan name B. The Employer Identification Number (EIN) of the plan sponsor as reported on IRS Form 5500, if any C. The plan number as reported on IRS Form 5500, if any D. Is there a funding agency established for the plan? E. Indicate where costs are accumulated: (1) Home Office (2) Segment F. If the plan provides supplemental benefits to any other plan, identify the other plan(s).
7.1.2	Defined-Contribution Plan(s) and Certain Defined-Benefit Plans treated as Defined-Contribution Plans. Where numerous plans are listed under 7.1.0.A., 7.1.0.B.2.b., or 7.1.0.B.2.c., for those plans which represent the largest dollar amounts of costs charged to Federal contracts, or similar cost objectives, describe on a continuation sheet the basis for the contribution (including treatment of dividends, credits, and forfeitures) required for each fiscal year. (If there are not more than three plans, provide information for all the plans. If there are more than three plans, information should be provided for those plans that in the aggregate account for at least 80 percent of those defined-contribution plan costs allocable to this segment or business unit.) Z. ____ Not applicable. (Proceed to Item 7.1.3)
7.1.3	Defined-Benefit Plan(s). Where numerous plans are listed under 7.1.0.B. (excluding certain defined-benefit plans treated as defined-contribution plans reported under 7.1.0.B.2.b. and 7.1.0.B.2.c.), for those plans which represent the largest dollar amounts of costs charged to Federal contracts, provide the information requested below on a continuation sheet. (If there are not more than three plans, provide information for all the plans. If there are more than three plans, information should be provided for those plans that in the aggregate account for at least 80 percent of those defined-benefit plan costs allocable to this segment or business unit.): A. <u>Actuarial Cost Method.</u> Identify the actuarial cost method used, including the cost method(s) used to value ancillary benefits, for each plan. Include the method used to determine the actuarial value of assets. Also, if applicable, include whether normal cost is developed as a level dollar amount or as a level percent of salary. For plans listed under 7.1.0.B.1.b., enter "pay-as-you-go". B. <u>Actuarial Assumptions.</u> Describe the events or conditions for which significant actuarial assumptions are made for each plan. Do not include the current numeric values of the assumptions, but provide a description of the basis used for determining these numeric values. Also, describe the criteria used to evaluate the validity of an actuarial assumption. For plans listed under 7.1.0.B.1.b., enter "not applicable". C. <u>Market Value of Funding Agency Assets.</u> Indicate if all assets of the funding agency are valued on the basis of a readily determinable market price. If yes, indicate the basis for the market value. If no, describe how the market values are determined for those assets that do not have a readily determinable market price. For plans listed under 7.1.0.B.1.b., enter "not applicable". D. <u>Basis for Cost Computation.</u> Indicate whether the cost for the segment is determined as: 1. An allocated portion of the total pension plan cost. 2. A separately computed pension cost for one or more segments. If so, identify these segments. Z. ____ Not applicable, proceed to Item 7.2.0.

COST ACCOUNTING STANDARDS BOARD DISCLOSURE STATEMENT REQUIRED BY PUBLIC LAW 100-679	PART VII - DEFERRED COMPENSATION AND INSURANCE COST NAME OF REPORTING UNIT

Item No.	Item description
7.2.0	Post-retirement Benefits (PRBs) Other than Pensions (including post-retirement health care benefits) Charged to Federal Contracts. Identify the accounting method used to determine the costs and the number of PRB plans whose costs are charged to Federal contracts or similar cost objectives. Where retiree benefits are provided as an integral part of an employee group insurance plan that covers active employees, report that plan under 7.3.0. (Mark applicable line(s) and enter number of plans.)

	Method Used to Determine Costs	Number of Plans
A.	Accrual Accounting	_____
B.	Cash (pay-as-you-go) Accounting	_____
C.	Purchased Insurance from unrelated Insurer	_____
D.	Purchased Insurance from Captive Insurer	_____
E.	Self-insurance (including insurance obtained through Captive Insurer)	_____
F.	Terminal Funding	_____
Y.	Other 1/	_____
Z.	_____ Not Applicable (Proceed to Item 7.3.0)	

7.2.1 General PRB Plan Information. On a continuation sheet for each plan identified in item 7.2.0, provide the following information grouped by method used to determine costs:

A. The plan name

B. The Employer Identification Number (EIN) of the plan sponsor as reported on IRS Form 5500, if any

C. The plan number as reported on IRS Form 5500, if any

D. Is there a funding agency or funded reserve established for the plan?

E. Indicate where costs are accumulated:
(1) Home Office
(2) Segment

F. Are benefits provided pursuant to a written plan or an established practice? If established practice, briefly describe.

G. If this PRB plan is listed under 7.2.0.C., 7.2.0.D., or 7.2.0.E., indicate whether the plan is operated as an employee group insurance program. If this PRB plan is listed under 7.2.0.Y., indicate whether the plan is operated as a group insurance program. If the plan is operated as an employee group insurance program, report this plan under 7.3.0. and 7.3.1., as appropriate. If no, report the plan under 7.2.2.

1/ Describe on a Continuation Sheet.

COST ACCOUNTING STANDARDS BOARD DISCLOSURE STATEMENT REQUIRED BY PUBLIC LAW 100-679	PART VII - DEFERRED COMPENSATION AND INSURANCE COST NAME OF REPORTING UNIT

Item No.	Item description
7.2.2	PRB Plan(s). Where numerous plans are listed under 7.2.0, for those plans which represent the largest dollar amounts of costs charged to Federal contracts, or other similar cost objectives, provide the information below on a continuation sheet. (If there are not more than three plans, provide information for all the plans. If there are more than three plans, information should be provided for those plans that in the aggregate account for at least 80 percent of those PRB costs allocable to this segment or business unit.)

A. Actuarial Cost Method. Identify the actuarial cost method used for each plan or each benefit, as appropriate. Include the method used to determine the actuarial value of assets. Identify the amortization methods and periods used, if any. For plans listed under 7.2.0.B., enter "cash accounting". For plans listed under 7.2.0.F., enter "terminal funding" and identify the amortization methods and periods used, if any.

B. Actuarial Assumptions. Describe the events or conditions for which significant actuarial assumptions are made for each plan. Do not include the current numeric values of the assumptions, but provide a description of the basis used for determining these numeric values. Also, describe the criteria used to evaluate the validity of an actuarial assumption. For plans under 7.2.0.B. or 7.2.0.F., enter "not applicable".

C. Funding. Provide the following information on the funding practice for the costs of the plan: (For plans under 7.2.0.B. or 7.2.0.F., enter "not applicable".)

1. Describe the criteria for or practice of funding the measured and assigned cost; e.g., full funding of the accrual, funding is made pursuant to VEBA or 401(h) rules.
2. Briefly describe the funding arrangement.
3. Are all assets valued on the basis of a readily determinable market price? If yes, indicate the basis used for the market value. If no, describe how the market value is determined for those assets that are not valued on the basis of a readily determinable market price.

D. Basis for Cost Computation. Indicate whether the cost for the segment is determined as:

1. An allocated portion of the total PRB plan cost
2. A separately computed PRB cost for one or more segments. If so, identify those segments.

E. Forfeitability. Does each participant have a non-forfeitable contractual right to their benefit or account balance? If no, explain.

Z. _____ Not applicable, proceed to item 7.3.0.

COST ACCOUNTING STANDARDS BOARD DISCLOSURE STATEMENT REQUIRED BY PUBLIC LAW 100-679	PART VII - DEFERRED COMPENSATION AND INSURANCE COST NAME OF REPORTING UNIT

Item No.	Item description

7.3.0 Employee Group Insurance Charged to Federal Contracts or Similar Cost Objectives. Does your organization provide group insurance coverage to its employees? (Includes coverage for life, hospital, surgical, medical, disability, accident, and similar plans for both active and retired employees, even if the coverage was previously described in 7.2.0.)

A. _____ Yes (Complete Item 7.3.1)

B. _____ No (Proceed to Item 7.4.0)

7.3.1 Employee Group Insurance Programs. For each program that covers a category of insured risk (e.g., life, hospital, surgical, medical, disability, accident, and similar programs for both active and retired employees), provide the information below on a continuation sheet, using the codes described below: (If there are not more than three policies or self-insurance plans that comprise the program, provide information for all the policies and self-insurance plans. If there are more that three policies or self-insurance plans, information should be provided for those policies and self-insurance plans that in the aggregate account for at least 80 percent of the costs allocable to this segment or business unit for the program that covers each category of insured risk identified.)

Description of Employee Group Insurance Program: _______________

					Self-Insurance	
Policy or Self-Insurance Plan	Cost Accumulation (1)	Cost Basis (2)	Includes Retirees (3)	Purchased Insurance Rating Basis (4)	Projected Average Loss (5)	Insurance Administrative Expenses (6)

Column (1) – Cost Accumulation

Enter Code A, B, or Y, as appropriate.

A. Costs are accumulated at the Home Office.
B. Costs are accumulated at Segment
Y. Other 1/

Column (2) – Cost Basis

Enter code A, B, C, or Y, as appropriate.

A. Purchased Insurance from unrelated third party
B. Self-insurance
C. Purchased Insurance from a captive insurer
Y. Other 1/

1/ Describe on a Continuation Sheet.

COST ACCOUNTING STANDARDS BOARD DISCLOSURE STATEMENT REQUIRED BY PUBLIC LAW 100-679	PART VII - DEFERRED COMPENSATION AND INSURANCE COST NAME OF REPORTING UNIT

Item No.	Item description
7.3.1	Continued.

Column (3) – Includes Retirees

Enter code A, B, C, or Y, as appropriate.

A. No, does not include benefits for retirees.
B. Yes, PRB benefits for retirees that are a part of a policy or coverage for both active employees and retirees are reported here instead of 7.2.0.
C. Yes, PRB benefits for retirees are a part of a PRB plan previously reported under 7.2.0.
Y. Other 1/

Column (4) – Purchased Insurance Rating Basis

For each plan listed enter code A, B, C, Y, or Z, as appropriate.

A. Retrospective Rating (also called experience rating plan or retention plan).
B. Manually Rated
C. Community Rated
Y. Other, or more than one type 1/
Z. Not applicable

Column (5) – Projected Average Loss

For each self-insured group plan, or the self-insured portion of purchased insurance, enter code A, B, C, Y, or Z, as appropriate.

A. Self-insurance costs represent the projected average loss for the period estimated on the basis of the cost of comparable purchased insurance.
B. Self-insurance costs are based on the contractor's experience, relevant industry experience, and anticipated conditions in accordance with accepted actuarial principles.
C. Actual payments are considered to represent the projected average loss for the period.
Y. Other, or more than one method 1/
Z. Not applicable

Column (6) – Insurance Administration Expenses

For each self-insured group plan, or the self-insured portion of purchased insurance, enter code A, B, C, D, Y, or Z, as appropriate, to indicate how administrative costs are treated.

A. Separately identified and accumulated in indirect cost pool(s).
B. Separately identified, accumulated, and allocated to cost objectives either at the segment and/or home office level (Describe allocation method on a Continuation Sheet).
C. Not separately identified, but included in indirect cost pool(s). (Describe pool(s) on a Continuation Sheet)
D. Incurred by an insurance carrier or third party (Describe accumulation and allocation process on a Continuation Sheet).
Y. Other 1/
Z. Not applicable

1/ Describe on a Continuation Sheet.

COST ACCOUNTING STANDARDS BOARD DISCLOSURE STATEMENT REQUIRED BY PUBLIC LAW 100-679	PART VII - DEFERRED COMPENSATION AND INSURANCE COST NAME OF REPORTING UNIT

Item No.	Item description

7.4.0 Deferred Compensation, as defined in CAS 9904.415. Does your organization award deferred compensation, other than ESOPs, which is charged to Federal contracts or similar cost objectives? (Mark one.)

A. ____ Yes (Complete Item 7.4.1.)

B. ____ No (Proceed to Item 7.5.0.)

7.4.1 General Plan Information. On a continuation sheet for all deferred compensation plans, as defined by CAS 9904.415, provide the following information:

A. The plan name

B. The Employer Identification Number (EIN) of the plan sponsor as reported on IRS Form 5500, if any

C. The plan number as reported on IRS Form 5500, if any

D. Indicate where costs are accumulated:

(1) Home office
(2) Segment

E. Are benefits provided pursuant to a written plan or an established practice? If established practice, briefly describe .

7.4.2 Deferred Compensation Plans. Where numerous plans are listed under 7.4.1, for those plans which represent the largest dollar amounts of costs charged to Federal contracts, or other similar cost objectives, provide the information below on a continuation sheet. (If there are not more than three plans, provide information for all the plans. If there are more than three plans, information should be provided for those plans that in the aggregate account for at least 80% of these deferred compensation costs allocable to this segment or business unit):

A. Description of Plan.

1. Stock Options
2. Stock Appreciation Rights
3. Cash Incentive
4. Other (explain)

B. Method of Charging Costs to Federal Contracts or Similar Cost Objectives.

1. Costs charged when accrued and the accrual is fully funded
2. Costs charged when accrued and the accrual is partially funded or not funded
3. Costs charged when paid to employee (pay-as-you-go)
4. Other (explain)

COST ACCOUNTING STANDARDS BOARD DISCLOSURE STATEMENT REQUIRED BY PUBLIC LAW 100-679	PART VII - DEFERRED COMPENSATION AND INSURANCE COST NAME OF REPORTING UNIT

Item No.	Item description
7.5.0	<u>Employee Stock Ownership Plans (ESOPs).</u> Does your organization make contributions to fund ESOPs that are charged directly or indirectly to Federal contracts or similar cost objectives? (Mark one) A. _____ Yes (Proceed to Item 7.5.1) B. _____ No (Proceed to Item 7.6.0)
7.5.1	General Plan Information. On a continuation sheet, for all ESOPs provide the following information: A. The plan name B. The Employer Identification Number (EIN) of the plan sponsor as reported on IRS Form 5500, if any C. The plan number as reported on IRS Form 5500, if any D. Indicate where costs are accumulated: (1) Home office (2) Segment E. Are benefits provided pursuant to a written plan or an established practice? If established practice, briefly describe. F. Indicate whether the ESOP plan is a defined-contribution plan subject to CAS 9904.412. (Answer Yes or No). G. Indicate whether the ESOP is leveraged or nonleveraged. H. <u>Valuation of Stock or Non-Cash Assets.</u> Are the plan assets valued on the basis of a readily determinable market price? If yes, indicate the basis for the market value. If no, indicate how the market value is determined for those assets that do not have a readily determinable market price. I. <u>Forfeitures and Dividends.</u> Describe the accounting treatment for forfeitures and dividends, on both allocated and unallocated shares, in the measurement of ESOP costs charged directly or indirectly to Federal contracts or similar cost objectives for each plan identified. J. <u>Administrative Costs.</u> Describe how the costs of administration of each plan listed are identified, grouped, and accumulated.

COST ACCOUNTING STANDARDS BOARD DISCLOSURE STATEMENT REQUIRED BY PUBLIC LAW 100-679	PART VII - DEFERRED COMPENSATION AND INSURANCE COST NAME OF REPORTING UNIT

Item No.	Item description

7.6.0 <u>Worker's Compensation, Liability, and Property Insurance.</u> Does your organization have insurance coverage regarding worker's compensation, liability and property insurance?

A. _____ Yes (Complete Item 7.6.1.)

B. _____ No (Proceed to Part VIII)

7.6.1 Worker's Compensation, Liability and Property Insurance Coverage.

For each line of insurance that covers a category of insured risk (e.g., worker's compensation, fire and similar perils, automobile liability and property damage, general liability), provide the information below on a continuation sheet using the codes described below: (If there are not more than three policies or self-insurance plans that are applicable to the line of insurance, provide information for all the policies and self-insurance plans. If there are more than three policies or insurance plans, information should be provided for those policies and self-insurance plans that in the aggregate account for at least 80 percent of the costs allocable to this segment or business unit for each line of insurance identified.)

Description of Line of Insurance Coverage: _______________

				Self-Insurance	
Policy or Self-Insurance Plan	Cost Accumulation (1)	Cost Basis (2)	Crediting of Dividends and Earned Refunds (3)	Projected Average Loss (4)	Insurance Administrative Expenses (5)

Column (1) -- <u>Cost Accumulation</u>

Enter code A, B, or Y, as appropriate.

A. Costs are accumulated at the Home Office.
B. Costs are accumulated at Segment
Y. Other 1/

Column (2) -- <u>Cost Basis</u>

Enter code A, B, C, or Y, as appropriate.

A. Purchased insurance from unrelated third party
B. Self-insurance
C. Purchased insurance from a captive insurer
Y. Other 1/

1/ Describe on a Continuation Sheet.

COST ACCOUNTING STANDARDS BOARD DISCLOSURE STATEMENT REQUIRED BY PUBLIC LAW 100-679	PART VII - DEFERRED COMPENSATION AND INSURANCE COST NAME OF REPORTING UNIT

Item No. | **Item description**

7.6.1 **Continued.**

Column (3) – Crediting of Dividends and Earned Refunds

For each line of coverage listed, enter code A, B, C, D, E, Y, or Z, as appropriate.

A. Credited directly or indirectly to Federal contracts or similar cost objectives in the year earned
B. Credited directly or indirectly to Federal contracts or similar cost objectives in the year received, not necessarily in the year earned
C. Accrued each year, as applicable, to currently reflect the net annual cost of the insurance
D. Not credited or refunded to the contractor but retained by the carriers as reserves in accordance with 48 CFR 9904.416-50(a)(1)(iv)
E. Manually Rated - not applicable
Y. Other, or more than one 1/
Z. Not applicable

Column (4) – Projected Average Loss

For each self-insured group plan, or the self-insured portion of purchased insurance, enter code A, B, C, Y, or Z, as appropriate.

A. Costs that represent the projected average loss for the period estimated on the basis of the cost of comparable purchased insurance.
B. Costs that are based on the contractor's experience, relevant industry experience, and anticipated conditions in accordance with generally accepted actuarial principles and practices.
C. The actual amount of losses are considered to represent the projected average loss for the period.
Y. Other, or more than one method. 1/
Z. Not applicable

Column (5) – Insurance Administration Expenses

For each self-insured group plan, or the self-insured portion of purchased insurance, enter code A, B, C, D, Y, or Z, as appropriate, to indicate how administrative costs are treated.

A. Separately identified and accumulated in indirect cost pool(s).
B. Separately identified, accumulated, and allocated to cost objectives either at the segment and/or home office level (Describe allocation method on a Continuation Sheet).
C. Not separately identified, but included in indirect cost pool(s). (Describe pool(s) on a Continuation Sheet).
D. Incurred by an insurance carrier or third party. (Describe accumulation and [illegible]on process on a Continuation Sheet).
Y. Other 1/
Z. Not applicable

1/ Describe on a Continuation Sheet.

COST ACCOUNTING STANDARDS BOARD DISCLOSURE STATEMENT REQUIRED BY PUBLIC LAW 100-679	PART VIII - HOME OFFICE EXPENSES NAME OF REPORTING UNIT

Item No.	Item description

Part VIII Instructions

FOR HOME OFFICE, AS APPLICABLE (Includes home office type operations of subsidiaries, joint ventures, partnerships, etc.). 1/

This part should be completed only by the office of a corporation or other business entity where such an office is responsible for administering two or more segments, where it allocates its costs to such segments and where at least one of the segments is required to file Parts I through VII of the Disclosure Statement.

Data for this part should cover the reporting unit's (corporate or other intermediate level home office's) most recently completed fiscal year. For a corporate (home) office, such data should cover the entire corporation. For a intermediate level home office, they should cover the subordinate organizations administered by that group office.

8.1.0 Organizational Structure.

On a continuation sheet, provide the following information:

1. In column (1) list segments and other intermediate level home offices reporting to this home office,
2. In column (2) insert "yes" or "no" to indicate if reporting units have recorded any CAS-covered Government Sales, and
3. In column (3) provide the percentage of annual CAS-covered Government Sales as a Percentage of Total Sales (Government and Commercial), if applicable, as follows:

A. Less than 10%
B. 10%-50%
C. 51%-80%
D. 81%-95%
E. Over 95%

Segment or Other Intermediary Home Office (1)	CAS Covered Government Sales (2)	Government Sales as a Percentage of Total Sales (3)

8.2.0 Other Applicable Disclosure Statement Parts. (Refer to page (i) 4., General Instructions, and Parts V, VI and VII of the Disclosure Statement. Indicate below the parts that the reporting unit has completed concurrently with Parts I and VIII.)

A. ____ Part V - Depreciation and Capitalization Practices
B. ____ Part VI - Other Costs and Credits
C. ____ Part VII - Deferred Compensation and Insurance Costs
Z. ____ Not Applicable

1/ For definition of home office see 48 CFR 9904.403.

COST ACCOUNTING STANDARDS BOARD DISCLOSURE STATEMENT REQUIRED BY PUBLIC LAW 100-679	PART VIII - HOME OFFICE EXPENSES NAME OF REPORTING UNIT

Item No.	Item description
8.3.0	Expenses or Pools of Expenses and Methods of Allocation.

For classification purposes, three methods of allocation, defined as follows, are to be used:

(i) Directly Allocated—those expenses that are charged to specific corporate segments or other intermediate level home offices based on a specific identification of costs incurred, as described in 9904.403;

(ii) Homogeneous Expense Pools—those individual or groups of expenses which are allocated using a base which reflects beneficial or causal relationships, as described in 9904.403; and

(iii) Residual Expense—the remaining expenses which are allocated to all segments by means of a base representative of the total activity of such segments.

Allocation Base Codes

A. Sales
B. Cost of Sales
C. Total Cost Input (Direct Material, Direct Labor, Other Direct Costs, and Applicable Overhead)
D. Total Cost Incurred (Total Cost Input Plus G&A Expenses)
E. Prime Cost (Direct Material, Direct Labor, and Other Direct Costs
F. Three factor formula (CAS 9904.403-50(c))
G. Processing or Conversion Cost (Direct Labor and Applicable Overhead)
H. Direct Labor Dollars
I. Direct Labor Hours
J. Machine Hours
K. Usage
L. Unit of Production
M. Direct Material Cost
N. Total Payroll Dollars (Direct and Indirect Employees)
O. Headcount or Number of employees (Direct and Indirect Employees)
P. Square Feet
Q. Value Added
Y. Other, or More than One Basis 1/

(On a continuation sheet, under each of the headings 8.3.1, 8.3.2, and 8.3.3 enter the type of expenses or the name of the expense pool(s). For each of the types of expense or expense pools listed, also indicate as item (a) the major functions, activities, and elements of cost included. In addition, for items listed under 8.3.2 and 8.3.3 enter one of the Allocation Base Codes A through Q, or Y, to indicate the basis of allocation and describe as item (b) the make up of the base(s). For example, if direct labor dollars are used, are ovetime premiums, fringe benefits, etc. included? For items listed under 8.3.2 and 8.3.3, if a pool is not allocated to all reporting units listed under 8.1.0, then list those reporting units either receiving or not receiving an allocation. Also identify special allocations of residual expenses and/or fixed mangement charges (see 9904.403-40(c)(3)).

1/ Describe on a Continuation Sheet.

COST ACCOUNTING STANDARDS BOARD DISCLOSURE STATEMENT REQUIRED BY PUBLIC LAW 100-679	PART VIII - HOME OFFICE EXPENSES NAME OF REPORTING UNIT

Item No.	Item description
	Type of Expenses or Name of Pool of Expenses
8.3.1	Directly Allocated
	1. ____________
	(a) Major functions, activities, and elements of cost include: ____________ ____________
	2. ____________
	(a) Major functions, activities, and elements of cost include: ____________ ____________
8.3.2	Homogeneous Expense Pools — Allocation Base Code
	1. ____________ ____
	(a) Major functions, activities, and elements of cost include: ____________ ____________
	(b) Description/Make up of the allocation base: ____________ ____________
	2. ____________ ____
	(a) Major functions, activities, and elements of cost include: ____________ ____________
	(b) Description/Make up of the allocation base: ____________ ____________

COST ACCOUNTING STANDARDS BOARD DISCLOSURE STATEMENT REQUIRED BY PUBLIC LAW 100-679	PART VIII - HOME OFFICE EXPENSES NAME OF REPORTING UNIT

Item No.	Item description
8.3.3	Residual Expenses ______________ Allocation Base Code ____ (a) Major functions, activities, and elements of cost include: ______________ ______________ (b) Description/Make up of the allocation base: ______________ ______________
8.4.0	Transfer of Expenses. If there are normally transfers of expenses from reporting units to this home office, identify on a continuation sheet the classification of the expense and the name of the reporting unit incurring the expense.

[FR Doc. 96–4472 Filed 2–27–96; 8:45 am]
BILLING CODE 3110–01–C

effective date of the *Interim BOC Out-of-Region Order* to July 29, 1996.

EFFECTIVE DATE: The interim rule published on July 9, 1996 at 61 FR 35964 will be effective July 29, 1996.

FOR FURTHER INFORMATION CONTACT: Michael Pryor (202) 418–0495 or Melissa Waksman (202) 418–0913, Common Carrier Bureau, Policy and Program Planning Division.

SUPPLEMENTARY INFORMATION:

1. On our own motion, pursuant to Section 1.108 of our rules, 47 CFR § 1.108, we reconsider the effective date of the *Interim BOC Out-of-Region Order,* 61 FR 35964, July 9, 1996. In that decision, we established interim rules governing Bell Operating company (BOC) provision of domestic, interstate, interexchange services originating outside of their in-region states. We sought to facilitate the efficient and rapid provision of such services by the BOCs, as contemplated by the Telecommunications Act of 1996, (1996 Act), Public Law No. 104–104, 110 Stat. 56 (1996) *codified at* 47 U.S.C. §§ 151 *et seq.* The *Interim BOC Out-of-Region Order* removes dominant carrier regulation for BOCs that provide such services through an affiliate in compliance with certain safeguards. The requirements established in the Order are interim measures that remain in place until we complete our more comprehensive review of the rules that are applicable to both independent local exchange carriers and BOCs in the provision of out-of-region, interstate, interexchange services.

2. We originally established an effective date for the *Interim BOC Out-of-Region Order* of thirty days following publication in the Federal Register. That Order was published in the Federal Register on July 9, 1996, and the scheduled effective date of the Order is August 8, 1996. Under 5 U.S.C. § 553(d)(1), however, a substantive rule which relieves a restriction may become effective prior to thirty days following Federal Register publication. Because the *Interim BOC Out-of-Region Order* lifts dominant carrier regulation for the out-of-region services of BOC affiliates complying with certain minimum safeguards, we find that the Order falls within the exception to the 30-day rule set forth in 5 U.S.C. § 553(d)(1). Accelerating the effective date of that Order will further the goals of the 1996 Act, which provided that upon enactment the BOCs could provide out-of-region, interstate, interexchange services. We find that the effective date of the *Interim BOC Out-of-Region Order* shall be the date of the publication of this Order on Reconsideration in the Federal Register.

3. Accordingly, *It is ordered* that, pursuant to Sections 4(i), 4(j), 303 and 405 of the Communications Act of 1934, as amended, 47 U.S.C. §§ 154(i), 154(j), 303 and 405, and section 1.108 of the Commission's rules, 47 CFR § 1.108, the ORDER ON RECONSIDERATION is hereby ADOPTED and shall become effective on the date of publication in the Federal Register. *It is further ordered* that the effective date of the *Interim BOC Out-of-Region Order,* FCC 96–288 (rel. July 1, 1996), 61 FR 35964 (July 9, 1996), shall be July 29, 1996.

Federal Communications Commission.

William F. Caton,

Acting Secretary.

[FR Doc. 96–19240 Filed 7–26–96; 8:45 am]

BILLING CODE 6712–01–P

OFFICE OF MANAGEMENT AND BUDGET

Office of Federal Procurement Policy

48 CFR Part 9903

Cost Accounting Standards Board; Applicability of Cost Accounting Standards Coverage

AGENCY: Cost Accounting Standards Board, Office of Federal Procurement Policy, OMB.

ACTION: Interim rule with request for comment.

SUMMARY: The Cost Accounting Standards (CAS) Board is revising the applicability criteria for application of CAS to negotiated Federal contracts. This rulemaking is authorized pursuant to Section 26 of the Office of Federal Procurement Policy Act, 41 U.S.C. 422. The Board is taking action on this topic to adjust CAS applicability requirements in accordance with Section 4205 of Pub. L. 104–106, the ''Federal Acquisition Reform Act of 1996.''

EFFECTIVE DATES: This rule is effective July 29, 1996. Comments upon this interim rule must be in writing and must be received by September 27, 1996.

ADDRESSES: Comments should be addressed to Richard C. Loeb, Executive Secretary, Cost Accounting Standards Board, Office of Federal Procurement Policy, 725 17th Street, NW., Room 9001, Washington, DC 20503. Attn: CASB Docket No. 96–01.

FOR FURTHER INFORMATION CONTACT: Richard C. Loeb, Executive Secretary, Cost Accounting Standards Board (telephone: 202–395–3254).

SUPPLEMENTARY INFORMATION:

A. Background

Section 4205 of Pub. L. 104–106, the ''Federal Acquisition Reform Act of 1996,'' amends 41 U.S.C. § 422(f)(2)(B) to revise clause (i) and delete clause (iii). The phrase ''contracts or subcontracts where the price negotiated is based on established catalog or market prices of commercial items sold in substantial quantities to the general public'' has been substituted with the phrase ''contracts or subcontracts for the acquisition of commercial items.'' The CAS Board is today amending its applicability regulations, solicitation provision and contract clauses in recognition of this change. As amended, firm fixed-price contracts and subcontracts for the acquisition of commercial items (see 48 CFR, Chap. 1, part 12) will be exempt from CAS requirements. Consequently, the Board's December 18, 1995 ''Memorandum for Agency Senior Procurement Executives'' authorizing CAS waivers for individual firm fixed-price contracts for the acquisition of commercial items when cost or pricing data is not obtained is hereby rescinded.

To accomplish these changes, the Board is amending Section 9903.201–1(b)(6) of its rules. Additionally, the solicitation provision found at 9903.201–3, the contract clauses at 9903.201–4, and the definition found at 9903.301 are amended to reflect this change.

The conference report to Pub. L. 104–106 directs the CAS Board, in consultation with the Director of the Defense Contract Audit Agency, to issue guidance, consistent with commercial accounting systems and practices, to ensure that contractors appropriately assign costs to commercial item contracts, other than firm fixed-price commercial item contracts. At the present time, however, commercial item contracts are limited by regulation to the fixed-price variety. Accordingly, after consideration and review of this issue, the Board has concluded that development of the requested guidance should appropriately await the time when other than fixed-price commercial item contracts are authorized, or until another need for such guidance arises. At the time that a need arises for guidance to address the allocation of costs to other than firm fixed-price commercial item contracts, the Board will, of course, pursue the development of guidance to address the issue.

B. Paperwork Reduction Act

The Paperwork Reduction Act, Public Law 96–511, does not apply to this rulemaking, because this rule imposes no paperwork burden on offerors, affected contractors and subcontractors, or members of the public which require the approval of OMB under 44 U.S.C. 3501, *et seq.*

C. Executive Order 12866 and the Regulatory Flexibility Act

The economic impact of this rule on contractors and subcontractors is expected to be minor. As a result, the Board has determined that this final rule will not result in the promulgation of a ''major rule'' under the provisions of Executive Order 12866, and that a regulatory impact analysis will not be required. Furthermore, this rule will not have a significant impact on a substantial number of small businesses because small businesses are exempt from the application of the Cost Accounting Standards. Therefore, this rule does not require a regulatory flexibility analysis under the Regulatory Flexibility Act of 1980.

D. Public Comments

Interested persons are invited to participate by submitting data, views or arguments with respect to this interim rule. All comments must be in writing and submitted to the address indicated in the **ADDRESSES** section.

List of Subjects in 48 CFR Part 9903

Cost accounting standards, Government procurement.

Richard C. Loeb,

Executive Secretary, Cost Accounting Standards Board.

For the reasons set forth in this preamble, chapter 99 of title 48 of the Code of Federal Regulations is amended as set forth below:

PART 9903—CONTRACT COVERAGE

Subpart 9903.2—CAS Program Requirements

1. The authority citation for part 9903 of chapter 99 of title 48 continues to read as follows:

Authority: Pub. L. 100–679, 102 Stat 4056, 41 U.S.C. § 422.

2. Section 9903.201–1 is amended by revising paragraph (b)(6) to read as follows:

9903.201–1 CAS applicability.

* * * * *

(b) * * *

(6) Firm fixed-price contracts and subcontracts for the acquisition of commercial items.

* * * * *

3. Section 9903.201–3 is amended by revising the clause heading and Part I (a) of the clause to read as follows:

9903.201–3 Solicitation provisions.

* * * * *

COST ACCOUNTING STANDARDS NOTICES AND CERTIFICATIONS (JULY 1996)

* * * * *

I. Disclosure Statement—Cost Accounting Practices and Certifications

(a) Any contract in excess of $500,000 resulting from this solicitation, except for those contracts which are exempt as specified in 9903.201–1

* * * * *

4. Section 9903.201–4 is amended by revising the clause headings and paragraphs (d) of the clause entitled Cost Accounting Standards; (d)(2) of the clause entitled Disclosure and Consistency of Cost Accounting Practices; and by revising paragraph (d)(2) and adding paragraph (d)(3) to the clause entitled Cost Accounting Standards—Educational Institutions, to read as follows:

9903.201–4 Contract clauses.

* * * * *

COST ACCOUNTING STANDARDS (JULY 1996)

* * * * *

(d) The Contractor shall include in all negotiated subcontracts which the Contractor enters into, the substance of this clause, except paragraph (b), and shall require such inclusion in all other subcontracts, of any tier, including the obligation to comply with all CAS in effect on the subcontractor's award date or if the subcontractor has submitted cost or pricing data, on the date of final agreement on price as shown on the subcontractor's signed Certificate of Current Cost or Pricing Data. This requirement shall apply only to negotiated subcontracts in excess of $500,000, except that the requirement shall not apply to negotiated subcontracts otherwise exempt from the requirement to include a CAS clause as specified in 9903.201–1.

(End of clause)

* * * * *

DISCLOSURE AND CONSISTENCY OF COST ACCOUNTING PRACTICES (JULY 1996)

* * * * *

(d) * * *

(2) This requirement shall apply only to negotiated subcontracts in excess of $500,000.

* * * * *

COST ACCOUNTING STANDARDS—EDUCATIONAL INSTITUTIONS (JULY 1996)

* * * * *

(d) * * *

(2) This requirement shall apply only to negotiated subcontracts in excess of $500,000.

(3) The requirement shall not apply to negotiated subcontracts otherwise exempt from the requirement to include a CAS clause as specified in 9903.201–1.

(End of clause)

Subpart 9903.3—CAS Rules and Regulations

§ 9903.301 Definitions.

5. Section 9903.301 is amended by deleting the definition for *Established catalog or market price of commercial items sold in substantial quantities to the general public.*

[FR Doc. 96–19067 Filed 7–26–96; 8:45 am]

BILLING CODE 3110–01–P

DEPARTMENT OF COMMERCE

National Oceanic and Atmospheric Administration

50 CFR Part 285

[I.D. 072396B]

Atlantic Tuna Fisheries; Fishery Closure and Reallocation

AGENCY: National Marine Fisheries Service (NMFS), National Oceanic and Atmospheric Administration (NOAA), Commerce.

ACTION: Closure and reallocation.

SUMMARY: NMFS has determined that the Atlantic bluefin tuna (ABT) Harpoon category annual quota and the June/July period General category quota for 1996 will be attained by July 24, 1996. Therefore, the 1996 Harpoon category fishery will be closed effective at 11:30 p.m. on July 24, 1996, and the General category fishery for June/July will be closed effective at 11:30 p.m. on July 24, 1996. This action is being taken to prevent overharvest of these categories. NMFS also announces a transfer of 10 mt of ABT from the longline-south Incidental subcategory to the longline-north Incidental subcategory. NMFS has determined that the fisheries landing ABT under the longline-south Incidental subcategory are not likely to achieve the full 1996 allocation. This reallocation is being taken to extend the season for the longline-north Incidental subcategory, ensure additional collection of biological assessment and monitoring data, and prevent waste of ABT that might otherwise be discarded dead.

EFFECTIVE DATES: The General category closure for the June/July period is effective 11:30 p.m. local time on July

OFFICE OF MANAGEMENT AND BUDGET

Office of Federal Procurement Policy

48 CFR Part 9904

Cost Accounting Standards Board; Allocation of Contractor Restructuring Costs

AGENCY: Cost Accounting Standards Board, Office of Federal Procurement Policy, OMB.

ACTION: Final rule; interpretation.

SUMMARY: The Cost Accounting Standards (CAS) Board is issuing an interpretation designed to address period cost assignment and allocability criteria for restructuring costs incurred under certain national defense contracts.

DATES: *Effective Date:* August 15, 1994.

FOR FURTHER INFORMATION CONTACT: Richard C. Loeb, Executive Secretary, Cost Accounting Standards Board (telephone: 202–395–3254).

SUPPLEMENTARY INFORMATION:

A. Background

Section 818 of the National Defense Authorization Act for Fiscal Year 1995, Pub. L. 103–337, restricts the Department of Defense from reimbursing a contractor or subcontractor that decides to avail itself of incurring restructuring costs associated with a business combination unless certain ''net savings'' provisions are met. Questions have arisen as to the methods to be used in measuring, assigning and allocating such restructuring costs. This interpretation is designed to address these questions, as well as the cost of restructuring activities, in general.

This interpretation is based upon the interim interpretation (with request for comment) issued by the CAS Board on March 8, 1995, 60 *FR* 12711. Ten sets of public comments were received in response to the interim interpretation. None of the commenters identified any substantive issues, although several requested more specificity with respect to the relationship of the interim interpretation to the provisions of CAS 9904.406—Cost Accounting Period. Accordingly, the interim interpretation is being revised to clarify that it serves principally as an interpretation of the provisions of CAS 9904.406 as related to restructuring costs.

B. Authority To Issue an Interpretation

Authority for issuance of this interpretation is provided by 41 U.S.C. 422(f)(1) and 48 CFR 9901.302(b).

Richard C. Loeb,

Executive Secretary, Cost Accounting Standards Board.

List of Subjects in 48 CFR part 9904

Accounting, Government procurement.

Accordingly, 48 CFR part 9904 is amended as follows:

Part 9904—COST ACCOUNTING STANDARDS

Subpart 9904.406—Cost Accounting Standard—Cost Accounting Period

1. The authority citation for part 9904 of chapter 99 of title 48 continues to read as follows:

Authority: Pub. L. 100–679, 102 Stat. 4056, 41 U.S.C. 422.

2. Section 9904.406–61 is amended by adding text to read as follows:

§ 9904.406–61 Interpretation.

(a) Questions have arisen as to the allocation and period cost assignment of certain contract costs (primarily under defense contracts and subcontracts). This section deals primarily with the assignment of restructuring costs to cost accounting periods. In essence, it clarifies whether restructuring costs are to be treated as an expense of the current period or as a deferred charge that is subsequently amortized over future periods.

(b) ''Restructuring costs'' as used in this Interpretation means costs that are incurred after an entity decides to make a significant nonrecurring change in its business operations or structure in order to reduce overall cost levels in future periods through work force reductions, the elimination of selected operations, functions or activities, and/or the combination of ongoing operations, including plant relocations. Restructuring activities do not include ongoing routine changes an entity makes in its business operations or organizational structure. Restructuring costs are comprised both of direct and indirect costs associated with contractor restructuring activities taken after a business combination is effected or after a decision is made to execute a significant restructuring event not related to a business combination. Typical categories of costs that have been included in the past and may be considered in the future as restructuring charges include severance pay, early retirement incentives, retraining, employee relocation, lease cancellation, asset disposition and write-offs, and relocation and rearrangement of plant and equipment. Restructuring costs do not include the cost of such activities when they do not relate either to business combinations or to other significant nonrecurring restructuring decisions.

(c) The costs of betterments or improvements of capital assets that result from restructuring activities shall be capitalized and depreciated in accordance with the provisions of 9904.404 and 9904.409.

(d) When a procuring agency imposes a net savings requirement for the payment of restructuring costs, the contractor shall submit data specifying

(1) the estimated restructuring costs by period,

(2) the estimated restructuring savings by period (if applicable), and

(3) the cost accounting practices by which such costs shall be allocated to cost objectives.

(e) Contractor restructuring costs defined pursuant to this section may be accumulated as deferred cost, and subsequently amortized, over a period during which the benefits of restructuring are expected to accrue. However, a contractor proposal to expense restructuring costs for a specific event in a current period is also acceptable when the Contracting Officer agrees that such treatment will result in a more equitable assignment of costs in the circumstances.

(f) If a contractor incurs restructuring costs but does not have an established or disclosed cost accounting practice covering such costs, the deferral of such restructuring costs may be treated as the initial adoption of a cost accounting practice (see 9903.302–2(a)). If a contractor incurs restructuring costs but does have an existing established or disclosed cost accounting practice that does not provide for deferring such costs, any resulting change in cost accounting practice to defer such costs may be presumed to be desirable and not detrimental to the interests of the Government (see 9903.201–6). Changes in cost accounting practices for restructuring costs shall be subject to disclosure statement revision requirements (see 9903.202–3), if applicable.

(g) Business changes giving rise to restructuring costs may result in changes in cost accounting practice (see 9903.302). If a contract price or cost allowance is affected by such changes in cost accounting practice, adjustments shall be made in accordance with subparagraph (a)(4) of the CAS clause (see 9903.201–4(a)(2), 9903.201–4(c)(2) and 9903.201–4(e)(2)).

(h) The amortization period for deferred restructuring costs shall not exceed five years. The straight-line method of amortization should normally be used, unless another method results in a more appropriate matching of cost to expected benefits.

(i) Restructuring costs that are deferred shall not be included in the computation to determine facilities capital cost of money (see 9904.414). Specifically, deferred charges are not tangible or intangible capital assets and therefore are excluded from the facilities capital values for the computation of facilities capital cost of money.

(j) Restructuring costs incurred at a home office level shall be treated in accordance with the provisions of 9904.403. Restructuring costs incurred at the segment level that benefit more than one segment should be allocated to the home office and treated as home office expense pursuant to 9904.403. Restructuring costs incurred at the segment level that benefit only that segment shall be treated in accordance with the provisions of 9904.418. If one or more indirect cost pools do not comply with the homogeneity requirements of 9904.418 due to the inclusion of the costs of restructuring activities, then the restructuring costs shall be accumulated in indirect cost pools that are distinct from the contractor's ongoing indirect cost pools.

(k) This section is applicable to contractor ''restructuring costs'' paid or approved on or after August 15, 1994.

[FR Doc. 97–14773 Filed 6–5–97; 8:45 am]

BILLING CODE 3110–01–P

OFFICE OF MANAGEMENT AND BUDGET

Office of Federal Procurement Policy

48 CFR Part 9903

Cost Accounting Standards Board; Applicability of Cost Accounting Standards Coverage

AGENCY: Cost Accounting Standards Board, Office of Federal Procurement Policy, OMB.

ACTION: Final rule.

SUMMARY: The Cost Accounting Standards (CAS) Board is revising the applicability criteria for application of CAS to negotiated Federal contracts. This rulemaking is authorized pursuant to Section 26 of the Office of Federal Procurement Policy Act, 41 U.S.C. § 422. The Board is taking action on this topic to adjust CAS applicability requirements in accordance with Section 4205 of Pub. L. 104–106, the ''Federal Acquisition Reform Act of 1996.''

EFFECTIVE DATE: This rule is effective June 6, 1997.

FOR FURTHER INFORMATION CONTACT: Richard C. Loeb, Executive Secretary, Cost Accounting Standards Board (telephone: 202–395–3254).

SUPPLEMENTARY INFORMATION:

A. Background

On July 29, 1996, the Cost Accounting Standards Board (CASB) issued an interim rule with request for comment, 61 FR 39360, implementing Section 4205 of Pub. L. 104–106, the ''Federal Acquisition Reform Act of 1996'' (FARA), also known as the ''Clinger-Cohen Act''. This law amends 41 U.S.C. § 422(f)(2)(B) to revise clause (i) and delete clause (iii). The phase ''contracts or subcontracts where the price negotiated is based on established catalog or market prices of commercial items sold in substantial quantities to the general public'' has been replaced with the phase ''contracts or subcontracts for the acquisition of commercial items.'' The CAS Board is today finalizing it interim applicability regulations, solicitation provision and contract clauses in recognition of this change. As amended, firm fixed-price contracts and subcontracts as well as fixed-price contracts and subcontracts with economic price adjustment (provided that adjustments are not based on actual costs incurred), for the acquisition of commercial items (see 48 CFR, Chap. 1, Part 12) will be exempt from CAS requirements. This exemption (b)(6) supersedes all other exemptions for the acquisition of commercial items under 9903.201–2.

To accomplish these changes, the Board is finalizing the interim amendments to Section 9903.201–1(b)(6) of its rules. Additionally, the interim solicitation provision found at 9903.201–3, the contract clauses at 9903.201–4, and the definition found at 9903.301 are finalized to reflect this change.

The Conference Report to Pub. L. 104–106 directs the CAS Board, in consultation with the Director of the Defense Contract Audit Agency, to issue guidance, consistent with commercial accounting systems and practices, to ensure that contractors appropriately assign costs to commercial item contracts, other than firm fixed-price commercial item contracts. At the present time, however, commercial item contracts are limited by regulation to the firm fixed-price and fixed-price with economic price adjustment (FPEA) variety. The Board recognizes that one of the three varieties of FPEA contracts authorized for use provides for adjustment of price based upon actual incurred costs for labor and material. Consequently, in order to reconcile the Conference Report language with the expansion of this CAS exemption to cover FPEA contracts, the Board's exemption for FPEA contracts does not include those contracts where adjustment is based on actual costs incurred (see FAR 16.203–1(b)).

The Board's inquiry of a number of Federal procuring agencies, including the Department of Defense, has indicated that FPEA contracts with adjustments based on actual costs incurred are rarely, if ever, used (DOD could not identify any contract awards of this type that had been made in the last year). Accordingly, after further consideration and review of this issue, the Board has concluded that development of the requested guidance should appropriately await the time when other than firm fixed-price or fixed-price with economic price adjustment commercial item contracts are authorized, or until another need for such guidance arises. At the time that a need arises for guidance to address the allocation of costs to other than firm fixed-price or fixed-price with economic price adjustment commercial item contracts as exempted by this rule, the Board will, of course, pursue the development of guidance to address the issue.

B. Paperwork Reduction Act

The Paperwork Reduction Act, Public Law 96–511, does not apply to this rulemaking, because this rule imposes no paperwork burden on offerors, affected contractors and subcontractors, or members of the public which require the approval of OMB under 44 U.S.C. 3501, *et seq.*

C. Executive Order 12866 and the Regulatory Flexibility Act

The economic impact of this rule on contractors and subcontractors is expected to be minor. As a result, the Board has determined that this final rule will not result in the promulgation of a ''major rule'' under the provisions of Executive Order 12866, and that a regulatory impact analysis will not be required. Furthermore, this rule will not have a significant impact on a substantial number of small businesses because small businesses are exempt from the application of the Cost Accounting Standards. Therefore, this rule does not require a regulatory flexibility analysis under the Regulatory Flexibility Act of 1980.

D. Public Comments

This final rule is based upon the Board's interim rule that was issued on July 29, 1996, 61 FR 39360. Six public comments were received, including five timely comments, and one late comment. The comments received and the Board's actions taken in response thereto are summarized below:

Comment: Four commenters, representing industry associations, the private bar and Government, supported the issuance of the interim rule.

Response: The Board thanks the commenters for their supportive comments.

Comment: Two commenters opposed the rule. They stated that there was no cost accounting basis for the rule. These commenters argued that whether a contract was subject to DAS should be dependent on the size of the contract (dollar amount) and whether contractor cost information had been submitted to assist or support contract negotiations or contract pricing, and not the product description or nomenclature used to describe the Government's intended purchase; i.e., a ''commercial item''.

Response: The Board believes that the commenters raise valid conceptual accounting concerns. However, inasmuch as Congress has given the Board what it believes to be direction to create this new CAS exemption, the Board believes it would be remiss if it were not to implement the Congressional initiative. In addition, the Board believes that the absence of any agency audit clause from ''commercial item'' contracts renders an enforceability and compliance scheme for CAS, as applied to this contract type, a moot issue.

Comment: Three commenters, including the private bar, objected to or questioned the Board's procedural process for issuing an interim rule. Two of the three commenters believe that the Board must use its statutory ''four-step'' rulemaking process in issuing the new exemption. Another commenter requested a more specific explanation of the authority for issuance of the interim rule.

Response: The Board agrees that it would normally have processed a new regulatory exemption to CAS coverage in accordance with the ''four-step'' rulemaking process normally appertaining to CAS rules. However, in this specific instance, the Board believes that it was following Congressional direction, as embodied in new statutory language contained in FARA, increasing the subject CAS exemption. In this instance, in which a statutory authorization has changed, the Board believes that it is merely implementing a Congressional initiative with respect to CAS. As such, the Board regards the new statutory language as representing a specific circumstance that creates an exception to the Board's regular ''four-step'' rulemaking process.

Comment: Two commenters, representing industry associations, recommended that the Board authorize contracting officers to waive all CAS requirements, for all commercial item contracts, entered into since October 13, 1994, the date of enactment of the Federal Acquisition Streamlining Act (FASA), Pub. L. 103–355.

Response: The Board believes that the present CAS exemption for commercial item contracts, as well as the agency CAS waiver authority that was previously in effect prior to the promulgation of the interim rule, were sufficient to address CAS commercial item contracting issues under both FASA and FARA. In this regard, the Board notes that the effective date of the interim rule was some five months prior to the effective date of the commercial item contracting changes made in the FAR as a result of the enactment of FARA. In addition, the Board is unaware of any contracts in which CAS has served as an impediment with respect to the acquisition of commercial items since the effective date of the FASA commercial item contracting rule on October 1, 1995.

Comment: Two commenters, representing Government and the private bar, recommended that the CAS commercial item exemption be expanded to include both firm fixed-price contracts and fixed-price contracts with economic price adjustment (FPEA). These commenters pointed out that only these two contract types are authorized for the acquisition of commercial items.

Response: The Board agrees with the commenters. However, the Board again notes that the Conference Report to Pub. L. 104–106 directs the CAS Board, in consultation with the Director of the Defense Contract Audit Agency, to issue guidance, consistent with commercial accounting systems and practices, to ensure that contractors appropriately assign costs to commercial item contracts, other than firm fixed-price commercial item contracts. In promulgating the interim rule, the Board chose not to issue this guidance, at the present time, on the basis that it is unnecessary, provided that the CAS commercial item exemption is limited to firm fixed-price commercial item contracts.

However, the Board is also persuaded that failure to include FPEA contracts within the CAS commercial item exemption might tend to contract rather than expand the intent of the Board's previous ''catalog or market price'' exemption for commercial items that was in effect prior to the passage of FARA. Moreover, the Board recognizes that one of the three varieties of FPEA contracts authorized for use, provides for adjustment of price based upon actual incurred costs for labor and material. In order to reconcile the Conference Report language with the expansion of this CAS exemption to cover FPEA contracts, the Board is expanding the exemption provided in the interim rule to include a CAS exemption for FPEA contracts, provided that price adjustments are not based on actual costs incurred (see FAR 16.203–1(b)). The Board believes that this approach to FPEA contracts comports with both the intent of the statute and the Conference Report by expanding the CAS commercial item exemption to FPEA contracts in a manner that will avoid the allocation of costs to cost objectives based on actual contractor incurred costs.

List of Subjects in 48 CFR Part 9903

Costs accounting standards, Government procurement.

Richard C. Loeb

Executive Secretary, Cost Accounting Standards Board.

Accordingly, the interim rule amending 48 CFR Part 9903 which was published at 61 FR 39360 on July 29, 1996, is adopted as a final rule with the following changes:

PART 9903—CONTRACT COVERAGE

Subpart 9903.2—CAS Program Requirements

1. The authority citation for part 9903 of chapter 99 of title 48 continues to read as follows:

Authority: Pub. L. 100–679, 102 Stat 4056, 41 U.S.C. § 422.

2. Section 9903.201–1 is amended by revising paragraph (b)(6) to read as follows:

§ 9903.201–1 CAS applicability.

* * * * *

(b) * * *

(6) Firm fixed-priced and fixed-price with economic price adjustment (provided that price adjustment is not based on actual costs incurred) contracts and subcontracts for the acquisition of commercial items.

* * * * *

3. Section 9903.201–4 is amended by revising the clause heading and paragraph (d) of the clause entitled Cost Accounting Standards; and by revising paragraph (d)(1) of the clause entitled Disclosure and Consistency of Cost Accounting Practices, to read as follows:

§ 9903.201–4 Contract clauses.

* * * * *

Cost Accounting Standards

(May 1997)

* * * * *

(d) The contractor shall include in all negotiated subcontracts which the Contractor enters into, the substance of this clause, except paragraph (b), and shall require such inclusion in all other subcontracts, of any tier, including the obligation to comply with all CAS in effect on the subcontractor's award date or if the subcontractor has submitted cost or pricing data, on the date of final agreement on price as shown on the subcontractor's signed Certificate of Current Cost or Pricing Data. If the subcontract is awarded to a business unit which pursuant to 9903.201–2 is subject to other types of CAS coverage, the substance of the applicable clause set forth in 9903.201–4 shall be inserted. This requirement shall apply only to negotiated subcontracts in excess of $500,000, except that the requirement shall not apply to negotiated subcontracts otherwise exempt from the requirement to include a CAS clause as specified in 9903.201–1.

(End of clause)

* * * * *

Disclosure and Consistency of Cost Accounting Practices

(May 1997)

* * * * *

(d) * * *

(1) If the subcontract is awarded to a business unit which pursuant to 9903.201–2

is subject to other types of CAS coverage, the substance of the applicable clause set forth in 9903.201–4 shall be inserted.

* * * * *

[FR Doc. 97–14775 Filed 6–5–97; 8:45 am]

BILLING CODE 3110–01–M

2136 Federal Register / Vol. 66, No. 7 / Wednesday, January 10, 2001 / Rules and Regulations

52.246–17 Warranty of Supplies of a Noncomplex Nature.

As prescribed in 46.710(a)(1), insert a clause substantially as follows:

WARRANTY OF SUPPLIES OF A NONCOMPLEX NATURE (MAR 2001)

(a) *Definitions.* As used in this clause—

Acceptance means the act of an authorized representative of the Government by which the Government assumes for itself, or as an agent of another, ownership of existing supplies, or approves specific services as partial or complete performance of the contract.

Supplies means the end items furnished by the Contractor and related services required under this contract. The word does not include ''data.''

* * * * *

134. Amend section 52.246–18 by revising the introductory paragraph, the date of the clause, and paragraph (a) of the clause to read as follows:

52.246–18 Warranty of Supplies of a Complex Nature.

As prescribed in 46.710(b)(1), insert a clause substantially as follows:

WARRANTY OF SUPPLIES OF A COMPLEX NATURE (MAR 2001)

(a) *Definitions.* As used in this clause—

Acceptance means the act of an authorized representative of the Government by which the Government assumes for itself, or as an agent of another, ownership of existing and identified supplies, or approves specific services rendered, as partial or complete performance of the contract.

Supplies means the end items furnished by the Contractor and related services required under this contract. The word does not include ''data.''

* * * * *

135. Amend section 52.246–19 by revising the introductory paragraph, the date of the clause, and paragraph (a) of the clause to read as follows:

52.246–19 Warranty of Systems and Equipment under Performance Specifications or Design Criteria.

As prescribed in 46.710(c)(1), the contracting officer may insert a clause substantially as follows:

WARRANTY OF SYSTEMS AND EQUIPMENT UNDER PERFORMANCE SPECIFICATIONS OR DESIGN CRITERIA (MAR 2001)

(a) *Definitions.* As used in this clause—

Acceptance means the act of an authorized representative of the Government by which the Government assumes for itself, or as an agent of another, ownership of existing and identified supplies, or approves specific services rendered, as partial or complete performance of the contract.

Defect means any condition or characteristic in any supplies or services furnished by the Contractor under the contract that is not in compliance with the requirements of the contract.

Supplies means the end items furnished by the Contractor and related services required under this contract. Except when this contract includes the clause entitled Warranty of Data, supplies also mean ''data.''

* * * * *

136. Amend section 52.246–20 by revising the introductory paragraph and the date of the clause; and in paragraph (a) of the clause by removing the paragraph heading ''Definitions'' and adding ''Definition'' in its place; and by removing the definition ''Correction''. The revised text reads as follows:

52.246–20 Warranty of Services.

As prescribed in 46.710(d), insert a clause substantially as follows:

WARRANTY OF SERVICES (MAR 2001)

* * * * *

[FR Doc. 01–11 Filed 1–9–01; 8:45 am]

BILLING CODE 6820–EP–P

DEPARTMENT OF DEFENSE

GENERAL SERVICES ADMINISTRATION

NATIONAL AERONAUTICS AND SPACE ADMINISTRATION

48 CFR Parts 30 and 52

[FAC 97–22; FAR Case 2000–301; Item II]

RIN 9000–AI79

Federal Acquisition Regulation; Applicability, Thresholds and Waiver of Cost Accounting Standards Coverage

AGENCIES: Department of Defense (DoD), General Services Administration (GSA), and National Aeronautics and Space Administration (NASA).

ACTION: Final rule.

SUMMARY: The Civilian Agency Acquisition Council and the Defense Acquisition Regulations Council (Councils) have agreed on a final rule amending the Federal Acquisition Regulation (FAR) to implement Section 802 of the National Defense Authorization Act for Fiscal Year 2000 and the Cost Accounting Standards (CAS) Board's final rule, Applicability, Thresholds and Waiver of Cost Accounting Standards Coverage. The FAR rule revises CAS applicability requirements, dollar thresholds, and waiver requirements.

DATES: *Effective Date:* January 10, 2001.

FOR FURTHER INFORMATION CONTACT: The FAR Secretariat, Room 4035, GS Building, Washington, DC, 20405, (202) 501–4755, for information pertaining to status or publication schedules. For clarification of content, contact Ms. Linda Nelson, Procurement Analyst, at (202) 501–1900. Please cite FAC 97–22, FAR case 2000–301.

SUPPLEMENTARY INFORMATION:

A. Background

Section 802 of the National Defense Authorization Act for Fiscal Year 2000 (Pub. L. 106–65)—

- Revised, at 41 U.S.C. 422(f)(2)(B), the categories of contracts and subcontracts that are exempt from all CAS requirements;
- Required the Administrator for Federal Procurement Policy to revise the rules and procedures issued under 41 U.S.C. 422(f) to increase the dollar threshold for full CAS coverage from $25 million to $50 million; and
- Revised 41 U.S.C. 422(f) to permit the head of an executive agency to waive the applicability of CAS under certain conditions.

In response to Public Law 106–65, the CAS Board in the Office of Federal Procurement Policy published an interim rule in the **Federal Register** on February 7, 2000 (65 FR 5990). The CAS Board rule, Applicability, Thresholds and Waiver of Cost Accounting Standards Coverage, amended the regulations at 48 CFR part 9903 to implement Section 802. After analysis of public comments, the CAS Board converted its interim rule to a final rule, with no change, and published the final rule in the **Federal Register** on June 9, 2000 (65 FR 36768).

DoD, GSA, and NASA published an interim rule in the **Federal Register** at 65 FR 36028, June 6, 2000. One respondent submitted public comments on the interim rule. The Councils considered all comments before agreeing to convert the interim rule to a final rule without change.

This FAR rule—

- Amends the provision at FAR 52.230–1, Cost Accounting Standards Notices and Certification, to remove the requirement that a contractor or subcontractor must have received at least one CAS-covered contract exceeding $1 million (''trigger contract'') to be subject to ''full CAS coverage,'' since the CAS Board removed this ''trigger contract'' amount from its corresponding solicitation provision, Cost Accounting Standards Notices and Certification, at 48 CFR 9903.201–3. The CAS Board added a new ''trigger contract'' dollar amount of $7.5 million at paragraph (b)(7) of 48 CFR 9903.201–1, CAS applicability, which is already referenced at FAR 30.201–1;
- Revises FAR 30.201–4(b)(1), Disclosure and consistency of cost accounting practices, and amends the provision at FAR 52.230–1 to reflect changes made by the CAS Board to

increase the dollar threshold for full CAS coverage from $25 million to $50 million; and

- Revises the CAS waiver procedures and conditions at FAR 30.201–5, as required by Section 802 of Pub. L. 106–65.

This is not a significant regulatory action, and therefore, was not subject to review under Section 6(b) of Executive Order 12866, Regulatory Planning and Review, dated September 30, 1993. This rule is not a major rule under 5 U.S.C. 804.

B. Regulatory Flexibility Act

The Department of Defense, the General Services Administration, and the National Aeronautics and Space Administration certify that this final rule will not have a significant economic impact on a substantial number of small entities within the meaning of the Regulatory Flexibility Act, 5 U.S.C. 601, *et seq.*, because contracts and subcontracts with small businesses are exempt from all CAS requirements in accordance with 48 CFR 9903.201–1(b)(3).

C. Paperwork Reduction Act

The Paperwork Reduction Act does not apply because the changes to the FAR do not impose information collection requirements that require the approval of the Office of Management and Budget under 44 U.S.C. 3501, *et seq.*

List of Subjects in 48 CFR Parts 30 and 52

Government procurement.

Dated: December 22, 2000.

Al Matera,

Acting Director, Federal Acquisition Policy Division

Interim Rule Adopted as Final Without Change

Accordingly, DoD, GSA, and NASA adopt the interim rule amending 48 CFR parts 30 and 52, which was published in the **Federal Register** at 65 FR 36028, June 6, 2000, as a final rule without change.

Authority: 40 U.S.C. 486(c); 10 U.S.C. chapter 137; and 42 U.S.C. 2473(c).

[FR Doc. 01–12 Filed 1–9–01; 8:45 am]

BILLING CODE 6820–EP–P

DEPARTMENT OF DEFENSE

GENERAL SERVICES ADMINISTRATION

NATIONAL AERONAUTICS AND SPACE ADMINISTRATION

48 CFR Parts 32 and 52

[FAC 97–22; FAR Case 1999–016; Item III]

RIN 9000–AI74

Federal Acquisition Regulation; Advance Payments for Non-Commercial Items

AGENCIES: Department of Defense (DoD), General Services Administration (GSA), and National Aeronautics and Space Administration (NASA).

ACTION: Final rule.

SUMMARY: The Civilian Agency Acquisition Council and the Defense Acquisition Regulations Council (Councils) have agreed on a final rule amending the Federal Acquisition Regulation (FAR) to permit federally insured credit unions to participate in the maintenance of special accounts for advance payments.

DATE: Effective Date: March 12, 2001.

FOR FURTHER INFORMATION CONTACT: The FAR Secretariat, Room 4035, GS Building, Washington, DC, 20405, (202) 501–4755, for information pertaining to status or publication schedules. For clarification of content, contact Mr. Jeremy Olson, at (202) 501–4755. Please cite FAC 97–22, FAR case 1999–016.

SUPPLEMENTARY INFORMATION:

A. Background

Prior to publication of this final FAR rule, FAR Subpart 32.4, Advance Payments for Non-Commercial Items, required, unless exempted by FAR 32.409–3(e) or (f), that contractors deposit advance payments in special accounts separate from their general or other funds. FAR 32.411 and other FAR text excluded credit unions from participating in the maintenance of these special accounts by requiring that contractors establish these special accounts only at banks that are members of the Federal Reserve System (FRS) or insured by the Federal Deposit Insurance Corporation (FDIC). However, many credit unions are federally insured through the National Credit Union Administration (NCUA). Therefore, these credit unions also are able to provide the Government a measure of security for Federal funds advanced to contractors.

This final rule amends FAR Subpart 32.4 and FAR 52.232–12 to change certain terminology (*e.g.,* change the word ‘‘bank’’ to ‘‘financial institution’’) to provide contractors an additional option of depositing advance payments in special accounts maintained by credit unions that are federally insured by NCUA. This revision will foster competition among financial institutions that are in the business of providing special accounts for advance payment funds, without increasing the risk to the Government.

DoD, GSA, and NASA published a proposed rule in the **Federal Register** at 65 FR 25614, May 2, 2000. Two respondents submitted public comments on the proposed rule. The Councils considered all comments before agreeing to convert the proposed rule to a final rule without change.

This is not a significant regulatory action, and therefore, was not subject to review under Section 6(b) of Executive Order 12866, Regulatory Planning and Review, dated September 30, 1993. This rule is not a major rule under 5 U.S.C. 804.

B. Regulatory Flexibility Act

The Department of Defense, the General Services Administration, and the National Aeronautics and Space Administration certify that this final rule will not have a significant economic impact on a substantial number of small entities within the meaning of the Regulatory Flexibility Act, 5 U.S.C. 601, *et seq.*, because the rule only applies to the very limited number of contractors that receive advance payments and deposit these payments in special accounts.

C. Paperwork Reduction Act

The Paperwork Reduction Act does not apply because the changes to the FAR do not impose information collection requirements that require the approval of the Office of Management and Budget under 44 U.S.C. 3501, *et seq.*

List of Subjects in 48 CFR Parts 32 and 52

Government procurement.

Dated: December 22, 2000.

Al Matera,

Acting Director, Federal Acquisition Policy Division.

Therefore, DoD, GSA, and NASA amend 48 CFR parts 32 and 52 as set forth below:

1. The authority citation for 48 CFR parts 32 and 52 continues to read as follows:

Authority: 40 U.S.C. 486(c); 10 U.S.C. chapter 137; and 42 U.S.C. 2473(c).

5990 Federal Register / Vol. 65, No. 25 / Monday, February 7, 2000 / Rules and Regulations

OFFICE OF MANAGEMENT AND BUDGET

OFFICE OF FEDERAL PROCUREMENT POLICY

48 CFR Part 9903

Cost Accounting Standards Board; Applicability, Thresholds and Waiver of Cost Accounting Standards Coverage

AGENCY: Cost Accounting Standards Board, Office of Federal Procurement Policy, OMB.

ACTION: Interim Rule.

SUMMARY: The Office of Federal Procurement Policy, Cost Accounting Standards Board, is revising applicability, thresholds and procedures for the application of the Cost Accounting Standards (CAS) to negotiated government contracts. This rulemaking is authorized pursuant to Section 26 of the Office of Federal Procurement Policy Act, 41 U.S.C. 422. The Board is taking action on this topic in order to adjust CAS applicability requirements and dollar thresholds in accordance with the provisions of the National Defense Authorization Act for Fiscal Year 2000, Pub. L. 106–65.

DATES: The effective date of this interim rule is April 2, 2000. Comments on the rule must be submitted in writing, by letter, and must be received by April 7, 2000.

ADDRESSES: Comments should be addressed to Richard C. Loeb, Executive Secretary, Cost Accounting Standards Board, Office of Federal Procurement Policy, 725 17th Street, NW, Room 9013, Washington, DC 20503. Attn: CASB Docket 00–01. The submission of public comments via the Internet by ''E-mail'' will not satisfy the specified requirement that public comments must be submitted in writing, by letter, as receipt of a readable data file cannot be assured.

FOR FURTHER INFORMATION CONTACT: Richard C. Loeb, Executive Secretary, Cost Accounting Standards Board (telephone: 202–395–3254).

SUPPLEMENTARY INFORMATION

A. Regulatory Process

The CAS Board's rules, regulations and Standards are codified at 48 CFR Chapter 99. Normally, the CAS Board follows a statutorily prescribed ''four-step'' rulemaking process prior to the issuance of a final rule (see 41 U.S.C. § 422(g)). However, the Board is proceeding to issue this interim rule in light of recent statutory changes to its enabling statute. The Board welcomes public comment on these changes, and will consider any comments received prior to promulgation of a final rule.

B. Background

On October 5, 1999, the President signed into law the National Defense Authorization Act for Fiscal Year 2000, Pub. L. 106–65. Sec. 802 of that Act, entitled ''Streamlined Applicability of Cost Accounting Standards,'' makes certain changes in the applicability requirements for CAS coverage. This interim rule is designed to reflect these changes in the CAS Board's rules.

Summary of Amendments

''Trigger contract'': 48 CFR 9903.201–1(b) is amended by adding a new subparagraph (7) that exempts contracts and subcontracts from CAS coverage, provided that the business unit of the contractor or subcontractor has not received a single CAS-covered contract or subcontract of $7.5 million or more.

''Firm-fixed price contract exemption'': The Board is implementing this statutory exemption by amending 48 CFR 9903.201–1(b) to revise subparagraph (15) to exempt from CAS coverage, firm-fixed-price contracts and subcontracts awarded on the basis of adequate price competition without submission of cost or pricing data. The Board is using the term ''cost or pricing data'' rather than ''certified'' cost or pricing data in order to conform to the statutory requirements of 10 U.S.C. § 2306(h)(1) and 41 U.S.C. § 254(b), which defines ''Cost or pricing data'' as data that requires certification.

''Types of CAS coverage'': 48 CFR 9903.201–2(a) is amended by revising the dollar threshold for ''full CAS coverage'' from $25 million to $50 million, and deleting the requirement that to be subject to ''full CAS coverage'', that a contractor or subcontractor have received at least one contract or subcontract that exceeded $1 million (the previous ''trigger contract'' amount for initiation of ''full CAS coverage''). 48 CFR 9903.201–2(b) is amended by revising the definition of ''modified CAS coverage'' to indicate that such coverage applies to covered contracts and subcontracts where the total value of CAS-covered contracts and subcontracts received by a business unit is less than $50 million. Conforming amendments have also been made to the solicitation provisions and contract clauses appearing at 9903.201–3 and 9903.201–4, respectively.

''Waiver'': 48 CFR 9903.201–5 is amended by revising this section to provide for agency CAS waiver authority under certain circumstances.

''Disclosure requirements'': 48 CFR 9903.202–1(b) is amended by revising the dollar amount for disclosure from $25 million to $50 million, and deleting the requirement that a contractor or subcontractor have received at least one contract in excess of $1 million.

C. Paperwork Reduction Act

The Paperwork Reduction Act, Public Law 96–511, does not apply to this rule, because this rule imposes no paperwork burden on offerors, affected contractors and subcontractors, or members of the public which requires the approval of OMB under 44 U.S.C. § 3501, *et seq.* The purpose of this rule is to implement Pub. L. 105–65.

D. Executive Order 12866 and the Regulatory Flexibility Act

This rule serves to eliminate certain administrative requirements associated with the administration of the Cost Accounting Standards by covered government contractors and subcontractors. The economic impact on contractors and subcontractors is therefore expected to be minor. As a result, the Board has determined that this is not a ''major rule'' under the provisions of Executive Order 12866, and that a regulatory impact analysis is not required. Furthermore, this rule will not have a significant effect on a substantial number of small entities because small businesses are exempt from the application of the Cost Accounting Standards. Therefore, this rule does not require a regulatory flexibility analysis under the Regulatory Flexibility Act of 1980.

E. Public Comments

Interested persons are invited to participate by submitting data, views or arguments with respect to the amendments contained in this interim rule. All comments must be in writing and submitted timely to the address indicated in the **ADDRESSES** section of this document.

List of Subjects in 48 CFR Part 9903

Cost Accounting Standards, Government Procurement.

Nelson F. Gibbs,

Executive Director, Cost Accounting Standards Board.

For the reasons set forth in this preamble, chapter 99 of title 48 of the Code of Federal Regulations is amended as set forth below:

1. The authority citation for part 9903 of chapter 99 of title 48 continues to read as follows:

Authority: Pub. L. 100–679, 102 Stat 4056, 41 U.S.C. 422.

PART 9903—CONTRACT COVERAGE

Subpart 9903.2—CAS Program Requirements

9903.201 Contract requirements.

2. Section 9903.201–1 is amended by adding paragraph (b)(7) and revising paragraph (b)(15) to read as follows:

9903.201–1 CAS applicability.

* * * * *

(b) * * *

* * * * *

(7) Contracts or subcontracts of less than $7.5 million, provided that, at the time of award, the business unit of the contractor or subcontractor is not currently performing any CAS-covered contracts or subcontracts valued at $7.5 million or greater.

* * * * *

(15) Firm-fixed-price contracts or subcontracts awarded on the basis of adequate price competition without submission of cost or pricing data.

3. Section 9903.201–2 is amended by revising paragraphs (a)(1) and (2) and (b)(1) and (2) to read as follows:

9903.201–2 Types of CAS coverage.

(a) * * *

(1) Receive a single CAS-covered contract award of $50 million or more; or

(2) Received $50 million or more in net CAS-covered awards during its preceding cost accounting period.

(b) *Modified coverage.* (1) Modified CAS coverage requires only that the contractor comply with Standard 9904.401, Consistency in Estimating, Accumulating, and Reporting Costs, Standard 9904.402, Consistency in Allocating Costs Incurred for the Same Purpose, Standard 9904.405, Accounting for Unallowable Costs and Standard 9904.406, Cost Accounting Standard—Cost Accounting Period. Modified, rather, than full, CAS coverage may be applied to a covered contract of less than $50 million awarded to a business unit that received less than $50 million in net CAS-covered awards in the immediately preceding cost accounting period.

(2) If any one contract is awarded with modified CAS coverage, all CAS-covered contracts awarded to that business unit during that cost accounting period must also have modified coverage with the following exception: if the business unit receives a single CAS-covered contract award of $50 million or more, that contract must be subject to full CAS coverage. Thereafter, any covered contract awarded in the same cost accounting period must also be subject to full CAS coverage.

* * * * *

4. Section 9903.201–3 is amended by revising the clause heading; by revising paragraph (c)(3) in Part I of the clause; by revising the CAUTION paragraph following paragraph (c)(4) in Part I; and by revising Part II of the clause, to read as follows:

9903.201–3 Solicitation provisions.

* * * * *

Cost Accounting Standards Notices and Certification (April 2000)

* * * * *

I. DISCLOSURE STATEMENT—COST ACCOUNTING PRACTICES AND CERTIFICATION

* * * * *

(c) * * *

(3) Certificate of Monetary Exemption.

The offeror hereby certifies that the offeror, together with all divisions, subsidiaries, and affiliates under common control, did not receive net awards of negotiated prime contracts and subcontracts subject to CAS totaling $50 million or more in the cost accounting period immediately preceding the period in which this proposal was submitted. The offeror further certifies that if such status changes before an award resulting from this proposal, the offeror will advise the Contracting Officer immediately.

(4) * * *

CAUTION: Offerors currently required to disclose because they were awarded a CAS-covered prime contract or subcontract of $50 million or more in the current cost accounting period may not claim this exemption (4). Further, the exemption applies only in connection with proposals submitted before expiration of the 90-day period following the cost accounting period in which the monetary exemption was exceeded.

II. COST ACCOUNTING STANDARDS—ELIGIBILITY FOR MODIFIED CONTRACT COVERAGE

If the offeror is eligible to use the modified provisions of 9903.201–2(b) and elects to do so, the offeror shall indicate by checking the box below. Checking the box below shall mean that the resultant contract is subject to the Disclosure and Consistency of Cost Accounting Practices clause in lieu of the Cost Accounting Standards clause.

The offeror hereby claims an exemption from the Cost Accounting Standards clause under the provisions of 9903.201–2(b) and certifies that the offeror is eligible for use of the Disclosure and Consistency of Cost Accounting Practices clause because during the cost accounting period immediately preceding the period in which this proposal was submitted, the offeror received less than $50 million in awards of CAS-covered prime contracts and subcontracts. The offeror further certifies that if such status changes before an award resulting from this proposal, the offeror will advise the Contracting Officer immediately.

CAUTION: An offeror may not claim the above eligibility for modified contract coverage if this proposal is expected to result in the award of a CAS-covered contract of $50 million or more or if, during its current cost accounting period, the offeror has been awarded a single CAS-covered prime contract or subcontract of $50 million or more.

* * * * *

5. Section 9903.201–4 is amended by revising paragraph (c)(1) to read as follows:

9903.201–4 Contract clauses.

* * * * *

(c) *Disclosure and Consistency of Cost Accounting Practices.* (1) The contracting officer shall insert the clause set forth below, Disclosure and Consistency of Cost Accounting Practices, in negotiated contracts when the contract amount is over $500,000 but less than $50 million, and the offeror certifies it is eligible for and elects to use modified CAS coverage (see 9903.201–2, unless the clause prescribed in paragraph (d) of this subsection is used).

* * * * *

6. Section 9903.201–5 is revised to read as follows:

9903.201–5 Waiver

(a) The head of an executive agency may waive the applicability of the Cost Accounting Standards for a contract or subcontract with a value of less than $15 million, if that official determines, in writing, that the business unit of the contractor or subcontractor that will perform the work—

(1) Is primarily engaged in the sale of commercial items; and

(2) Would not otherwise be subject to the Cost Accounting Standards under this chapter.

(b) The head of an executive agency may waive the applicability of the Cost Accounting Standards for a contract or subcontract under exceptional circumstances when necessary to meet the needs of the agency. A determination to waive the applicability of the Cost Accounting Standards by the agency head shall be set forth in writing, and shall include a statement of the circumstances justifying the waiver.

(c) The head of an executive agency may not delegate the authority under paragraphs (a) and (b) of this section, to any official below the senior policymaking level in the agency.

(d) The head of each executive agency shall report the waivers granted under paragraphs (a) and (b) of this section, for that agency, to the Cost Accounting Standards Board, on an annual basis, not later than 90 days after the close of the Government's fiscal year.

(e) Upon request of an agency head or his designee, the Cost Accounting Standards Board may waive all or any part of the requirements of 9903.201–4(a), Cost Accounting Standards, or 9903.201–4(c), Disclosure and Consistency of Cost Accounting Practices, with respect to a contract subject to the Cost Accounting Standards. Any request for a waiver shall describe the proposed contract or subcontract for which the waiver is sought and shall contain—

(1) An unequivocal statement that the proposed contractor or subcontractor refuses to accept a contract containing all or a specified part of a CAS clause and the specific reason for that refusal;

(2) A statement as to whether the proposed contractor or subcontractor has accepted any prime contract or subcontract containing a CAS clause;

(3) The amount of the proposed award and the sum of all awards by the agency requesting the waiver to the proposed contractor or subcontractor in each of the preceding 3 years;

(4) A statement that no other source is available to satisfy the agency's needs on a timely basis;

(5) A statement of alternative methods considered for fulfilling the need and the agency's reasons for rejecting them;

(6) A statement of steps being taken by the agency to establish other sources of supply for future contracts for the products or services for which a waiver is being requested; and

(7) Any other information that may be useful in evaluating the request.

(f) Except as provided by the Cost Accounting Standards Board, the authority in paragraph (e) of this section shall not be delegated.

7. Section 9903.202–1 is amended by revising paragraphs (b) (1) and (2) to read as follows:

9903.202–1 General requirements.

* * * * *

(b) * * *

(1) Any business unit that is selected to receive a CAS-covered contract or subcontract of $50 million or more shall submit a Disclosure Statement before award.

(2) Any company which, together with its segments, received net awards of negotiated prime contracts and subcontracts subject to CAS totaling $50 million or more in its most recent cost accounting period, must submit a Disclosure Statement before award of its first CAS-covered contract in the immediately following cost accounting period. However, if the first CAS-covered contract is received within 90 days of the start of the cost accounting period, the contractor is not required to file until the end of 90 days.

* * * * *

[FR Doc. 00–2621 Filed 2–4–00; 8:45 am]

BILLING CODE 3110–01–U

meaning of the Regulatory Flexibility Act, 5 U.S.C. 601, *et seq.*, because it only applies to acquisition of items from Serbia or Afghanistan.

C. Paperwork Reduction Act

The Paperwork Reduction Act does not apply because the changes to the FAR do not impose information collection requirements that require the approval of the Office of Management and Budget under 44 U.S.C. 3501, *et seq.*

List of Subjects in 48 CFR Parts 25 and 52

Government procurement.

Dated: May 26, 2000.

Edward C. Loeb,

Director, Federal Acquisition Policy Division.

Therefore, DoD, GSA, and NASA amend 48 CFR parts 25 and 52 as set forth below:

1. The authority citation for 48 CFR parts 25 and 52 continues to read as follows:

Authority: 40 U.S.C. 486(c); 10 U.S.C. chapter 137; and 42 U.S.C. 2473(c).

PART 25—FOREIGN ACQUISITION

2. Amend section 25.701 by revising paragraph (a) to read as follows:

25.701 Restrictions.

(a)(1) The Government generally does not acquire supplies or services that cannot be imported lawfully into the United States. Therefore, except as provided in paragraph (a)(2) of this section, even for overseas use, agencies and their contractors and subcontractors must not acquire any supplies or services originating from sources within, or that were located in or transported from or through

(i) Cuba (31 CFR part 515);
(ii) Iran (31 CFR part 560);
(iii) Iraq (31 CFR part 575);
(iv) Libya (31 CFR part 550);
(v) North Korea (31 CFR part 500);
(vi) Sudan (31 CFR part 538);
(vii) Territory of Afghanistan controlled by the Taliban (Executive Order 13129 of July 4, 1999, Blocking Property and Prohibiting Transactions With the Taliban); or
(viii) Serbia, excluding the territory of Kosovo (Executive Order 13121 of April 30, 1999, Blocking Property of the Governments of the Federal Republic of Yugoslavia (Serbia and Montenegro), the Republic of Serbia, and the Republic of Montenegro, and Prohibiting Trade Transactions Involving the Federal Republic of Yugoslavia (Serbia and Montenegro) in Response to the Situation in Kosovo).

(2)(i) Unless agency procedures require a higher level of approval, the contracting officer may, in unusual circumstances, acquire for use outside the United States supplies and services restricted in paragraph (a)(1) of this section. Examples of unusual circumstances are an emergency or when the supplies or services are not otherwise available and a substitute is not acceptable.

(ii) The contracting officer must provide documentation in the contract file whenever this exception is used.

* * * * *

3. Revise section 25.702 to read as follows:

25.702 Source of further information.

Refer questions concerning the restrictions in 25.701 to the Department of the Treasury, Office of Foreign Assets Control, Washington, D.C. 20220 (Telephone (202) 622–2520).

4. Amend section 25.1103 by revising paragraph (a) to read as follows:

25.1103 Other provisions and clauses.

(a) *Restrictions on certain foreign purchases.* Insert the clause at 52.225–13, Restrictions on Certain Foreign Purchases, in solicitations and contracts with a value exceeding $2,500, unless an exception applies (see 25.701(a)(2)).

PART 52—SOLICITATION PROVISIONS AND CONTRACT CLAUSES

5. Amend section 52.212–5 by—

a. Revising the date of the clause and paragraph (a);

b. In the first sentence of the introductory text of paragraphs (b), (c), and (d), by removing ''agrees to'' and adding ''shall'' in their place; and

c. Removing paragraph (b)(21) and redesignating paragraphs (b)(19) and (b)(20) as (b)(20) and (b)(21), respectively; and adding a new paragraph (b)(19) to read as follows:

52.212–5 Contract Terms and Conditions Required to Implement Statutes or Executive Orders—Commercial Items.

* * * * *

Contract Terms and Conditions Required to Implement Statutes or Executive Orders—Commercial Items (July 2000)

(a) The Contractor shall comply with the following FAR clauses, which are incorporated in this contract by reference, to implement provisions of law or executive orders applicable to acquisitions of commercial items:

(1) 52.222–3, Convict Labor (E.O. 11755).

(2) 52.233–3, Protest after Award (31 U.S.C. 3553).

(b) * * *

; (19) 52.225–13, Restriction on Certain Foreign Purchases (E.O. 12722, 12724, 13059, 13067, 13121, and 13129).

* * * * *

6. Amend section 52.213–4 by revising the date of the clause and paragraph (a)(1)(ii) to read as follows:

52.213–4 Terms and Conditions—Simplified Acquisitions (Other Than Commercial Items).

* * * * *

Terms and Conditions—Simplified Acquisitions (Other Than Commercial Items) (July 2000)

(a) * * *
(1) * * *

* * * * *

(ii) 52.225–13, Restrictions on Certain Foreign Purchases (July 2000) (E.O.'s 12722, 12724, 13059, 13067, 13121, and 13129).

* * * * *

7. Amend section 52.225–13 by revising the date of the clause and the last sentence of paragraph (a) to read as follows:

52.225–13 Restrictions on Certain Foreign Purchases.

* * * * *

Restrictions on Certain Foreign Purchases (July 2000)

(a) * * * Those countries are Cuba, Iran, Iraq, Libya, North Korea, Sudan, the territory of Afghanistan controlled by the Taliban, and Serbia (excluding the territory of Kosovo).

* * * * *

[FR Doc. 00–13823 Filed 6–1–00; 4:01 pm]

BILLING CODE 6820–EP–P

DEPARTMENT OF DEFENSE

GENERAL SERVICES ADMINISTRATION

NATIONAL AERONAUTICS AND SPACE ADMINISTRATION

48 CFR Parts 30 and 52

[FAC 97–18; FAR Case 2000–301; Item VIII]

RIN 9000–AI79

Federal Acquisition Regulation; Applicability, Thresholds and Waiver of Cost Accounting Standards Coverage

AGENCIES: Department of Defense (DoD), General Services Administration (GSA), and National Aeronautics and Space Administration (NASA).

ACTION: Interim rule with request for comments.

SUMMARY: The Civilian Agency Acquisition Council and the Defense Acquisition Regulations Council (Councils) have agreed on an interim rule amending the Federal Acquisition Regulation (FAR) to implement Section 802 of the National Defense

Authorization Act for Fiscal Year 2000 and the Cost Accounting Standards (CAS) Board's interim rule, Applicability, Thresholds and Waiver of Cost Accounting Standards Coverage. The FAR rule revises CAS applicability requirements, dollar thresholds, and waiver requirements.

DATES: Effective Date: June 6, 2000.

Applicability Date: The FAR, as amended by this rule, is applicable to solicitations issued on or after June 6, 2000.

Comment Date: Interested parties should submit comments to the FAR Secretariat at the address shown below on or before August 7, 2000 to be considered in the formulation of a final rule.

ADDRESSES: Submit written comments to: General Services Administration, FAR Secretariat (MVR), 1800 F Street, NW, Room 4035, Attn: Ms. Laurie Duarte, Washington, DC, 20405.

Submit electronic comments via the Internet to: farcase.2000–301@gsa.gov

Please submit comments only and cite FAC 97–18, FAR case 2000–301 in all correspondence related to this case.

FOR FURTHER INFORMATION CONTACT: The FAR Secretariat, Room 4035, GS Building, Washington, DC 20405, (202) 501–4755, for information pertaining to status or publication schedules. For clarification of content, contact Ms. Linda Nelson, Procurement Analyst, at (202) 501–1900. Please cite FAC 97–18, FAR case 2000–301.

SUPPLEMENTARY INFORMATION:

A. Background

Section 802 of the National Defense Authorization Act for Fiscal Year 2000 (Pub. L. 106–65)—

- Revised, at 41 U.S.C. 422(f)(2)(B), the categories of contracts and subcontracts that are exempt from all CAS requirements;
- Required the Administrator for Federal Procurement Policy to revise the rules and procedures issued under 41 U.S.C. 422(f) to increase the dollar threshold for full CAS coverage from $25 million to $50 million; and
- Revised 41 U.S.C. 422(f) to permit the head of an executive agency to waive the applicability of CAS under certain conditions.

In response to Pub. L. 106–65, the CAS Board in the Office of Federal Procurement Policy published an interim rule in the **Federal Register** on February 7, 2000 (65 FR 5990). The CAS Board rule, Applicability, Thresholds and Waiver of Cost Accounting Standards Coverage, amended the regulations at 48 CFR part 9903 to implement Section 802.

This interim FAR rule—

- Amends the provision at FAR 52.230–1, Cost Accounting Standards Notices and Certification, to remove the requirement that a contractor or subcontractor must have received at least one CAS-covered contract exceeding $1 million (''trigger contract'') to be subject to ''full CAS coverage,'' since the CAS Board removed this ''trigger contract'' amount from its corresponding solicitation provision, Cost Accounting Standards Notices and Certification, at 48 CFR 9903.201–3. The CAS Board added a new ''trigger contract'' dollar amount of $7.5 million at paragraph (b)(7) of 48 CFR 9903.201–1, CAS applicability, which is already referenced at FAR 30.201–1;
- Revises FAR 30.201–4(b), Disclosure and consistency of cost accounting practices, and amends the provision at FAR 52.230–1 to reflect changes made by the CAS Board to increase the dollar threshold for full CAS coverage from $25 million to $50 million; and
- Revises the CAS waiver procedures and conditions at FAR 30.201–5, as required by Section 802 of Pub. L. 106–65.

This rule was not subject to Office of Management and Budget review under Section 6(b) of Executive Order 12866, Regulatory Planning and Review, dated September 30, 1993. This rule is not a major rule under 5 U.S.C. 804.

B. Regulatory Flexibility Act

The interim rule is not expected to have a significant economic impact on a substantial number of small entities within the meaning of the Regulatory Flexibility Act, 5 U.S.C. 601, *et seq.*, because contracts and subcontracts with small businesses are exempt from all CAS requirements in accordance with 48 CFR 9903.201–1(b)(3). Therefore, an Initial Regulatory Flexibility Analysis has not been performed. The Councils will consider comments from small entities concerning the affected FAR subparts in accordance with 5 U.S.C. 610. Interested parties must submit such comments separately and should cite 5 U.S.C 601, *et seq.* (FAC 97–18, FAR case 2000–301), in correspondence.

C. Paperwork Reduction Act

The Paperwork Reduction Act does not apply because the changes to the FAR do not impose information collection requirements that require the approval of the Office of Management and Budget under 44 U.S.C. 3501, *et seq.*

D. Determination To Issue an Interim Rule

A determination has been made under the authority of the Secretary of Defense (DoD), the Administrator of General Services (GSA), and the Administrator of the National Aeronautics and Space Administration (NASA) that urgent and compelling reasons exist to promulgate this interim rule without prior opportunity for public comment. This action is necessary because this rule implements Section 802 of the National Defense Authorization Act for Fiscal Year 2000 (Pub. L. 106–65) and the Cost Accounting Standards (CAS) Board's interim rule, Applicability, Thresholds and Waiver of Cost Accounting Standards Coverage. Section 802 became effective 180 days after the date of enactment of Public Law 106–65 (October 5, 1999). The CAS Board's interim rule that implements Section 802 became effective on April 2, 2000. It is necessary that the Councils publish an interim FAR rule to amend FAR Parts 30 and 52 to implement Section 802 and the CAS Board's interim rule. However, pursuant to Public Law 98–577 and FAR 1.501, the Councils will consider public comments received in response to this interim rule in the formation of the final rule.

List of Subjects in 48 CFR Parts 30 and 52

Government procurement.

Dated: May 26, 2000.

Edward C. Loeb,

Director, Federal Acquisition Policy Division.

Therefore, DoD, GSA, and NASA amend 48 CFR parts 30 and 52 as set forth below:

1. The authority citation for 48 CFR parts 30 and 52 continues to read as follows:

Authority: 40 U.S.C. 486(c); 10 U.S.C. chapter 137; and 42 U.S.C. 2473(c).

PART 30—COST ACCOUNTING STANDARDS ADMINISTRATION

2. Amend section 30.201–4 by revising paragraph (b)(1) to read as follows:

30.201–4 Contract clauses.

* * * * *

(b) *Disclosure and consistency of cost accounting practices.* (1) Insert the clause at FAR 52.230–3, Disclosure and Consistency of Cost Accounting Practices, in negotiated contracts when the contract amount is over $500,000, but less than $50 million, and the offeror certifies it is eligible for and elects to use modified CAS coverage (see 48 CFR 9903.201–2 (FAR

Appendix)), unless the clause prescribed in paragraph (c) of this subsection is used.

* * * * *

3. Revise section 30.201–5 to read as follows:

30.201–5 Waiver.

(a) The head of the agency—

(1) May waive the applicability of CAS for a particular contract or subcontract under the conditions listed in paragraph (b) of this subsection; and

(2) Must not delegate this waiver authority to any official in the agency below the senior contract policymaking level.

(b) The head of the agency may grant a waiver when one of the following conditions exists:

(1) The contract or subcontract value is less than $15,000,000, and the head of the agency determines, in writing, that the segment of the contractor or subcontractor that will perform the contract or subcontract—

(i) Is primarily engaged in the sale of commercial items; and

(ii) Has no contracts or subcontracts that are subject to CAS.

(2) The head of the agency determines that exceptional circumstances exist whereby a waiver of CAS is necessary to meet the needs of the agency. Exceptional circumstances exist only when the benefits to be derived from waiving the CAS outweigh the risk associated with the waiver. The determination that exceptional circumstances exist must—

(i) Be set forth in writing; and

(ii) Include a statement of the specific circumstances that justify granting the waiver.

(c) When one of the conditions in paragraph (b) of this subsection exists, the request for waiver should include the following:

(1) The amount of the proposed award.

(2) A description of the contract or subcontract type (*e.g.,* firm-fixed-price, cost-reimbursement).

(3) Whether the segment(s) that will perform the contract or subcontract has CAS-covered contracts or subcontracts.

(4) A description of the item(s) being procured.

(5) When the contractor or subcontractor will not accept the contract or subcontract if CAS applies, a statement to that effect.

(6) Whether cost or pricing data will be obtained, and if so, a discussion of how the data will be used in negotiating the contract or subcontract price.

(7) The benefits to the Government of waiving CAS.

(8) The potential risk to the Government of waiving CAS.

(9) The date by which the waiver is needed.

(10) Any other information that may be useful in evaluating the request.

(d) When neither of the conditions in paragraph (b) of this subsection exists, the waiver request must be prepared in accordance with 48 CFR 9903.201–5(e) (FAR Appendix) and submitted to the CAS Board.

(e) Each agency must report any waivers granted under paragraph (a) of this subsection to the CAS Board, on a fiscal year basis, not later than 90 days after the close of the Government's fiscal year.

PART 52—SOLICITATION PROVISIONS AND CONTRACT CLAUSES

4. Amend section 52.230–1 by—

a. Revising the date of the provision;

b. In the first sentence of paragraph (c)(3) by removing the phrase ''more than $25 million (of which at least one award exceeded $1 million)'' and adding ''$50 million or more'' in its place;

c. In paragraph (c)(4)—

(i) In the ''Caution'' paragraph, by removing ''$25 million'' and adding ''$50 million'' in its place;

(ii) At ''II. Cost Accounting Standards—Eligibility for Modified Contract Coverage,'' in the second paragraph, by revising the first sentence; and

(iii) In the ''Caution'' paragraph following paragraph II by removing ''$25 million'' each time it is used (twice) and adding ''$50 million'' in their places. The revised text reads as follows:

52.230–1 Cost Accounting Standards Notices and Certification.

* * * * *

COST ACCOUNTING STANDARDS NOTICES AND CERTIFICATION (JUNE 2000)

* * * * *

(c) * * *

(4) * * *

II. Cost Accounting Standards—Eligibility for Modified Contract Coverage

* * * * *

☐ The offeror hereby claims an exemption from the Cost Accounting Standards clause under the provisions of 48 CFR 9903.201–2(b) and certifies that the offeror is eligible for use of the Disclosure and Consistency of Cost Accounting Practices clause because during the cost accounting period immediately preceding the period in which this proposal was submitted, the offeror received less than $50 million in awards of CAS-covered prime contracts and subcontracts.

* * * * *

[FR Doc. 00–13824 Filed 6–1–00; 4:02 pm]

BILLING CODE 6820–EP–P

DEPARTMENT OF DEFENSE

GENERAL SERVICES ADMINISTRATION

NATIONAL AERONAUTICS AND SPACE ADMINISTRATION

48 CFR Parts 3, 5, 47, and 49

[FAC 97–18; Item IX]

Federal Acquisition Regulation; Technical Amendments

AGENCIES: Department of Defense (DoD), General Services Administration (GSA), and National Aeronautics and Space Administration (NASA).

ACTION: Technical amendments.

SUMMARY: This document makes amendments to the Federal Acquisition Regulation in order to update references and make editorial changes.

EFFECTIVE DATE: June 6, 2000.

FOR FURTHER INFORMATION CONTACT: The FAR Secretariat, Room 4035, GS Building, Washington, DC 20405, (202) 501–4755.

List of Subjects in 48 CFR parts 3, 5, 47, and 49

Government procurement.

Dated: May 26, 2000.

Edward C. Loeb,

Director, Federal Acquisition Policy Division.

Therefore, DoD, GSA, and NASA amend 48 CFR parts 3, 47, and 49 as set forth below:

1. The authority citation for 48 CFR parts 3, 47, and 49 continues to read as follows:

Authority: 40 U.S.C. 486(c); 10 U.S.C. chapter 137; and 42 U.S.C. 2473(c).

PART 3—IMPROPER BUSINESS PRACTICES AND PERSONAL CONFLICTS OF INTEREST

3.303 [Amended]

2. Amend section 3.303 in the first sentence of paragraph (a) by removing ''41 U.S.C. 253(B)(e) and 10 U.S.C. 2305(b)(5)'' and adding ''41 U.S.C. 253b(i) and 10 U.S.C. 2305(b)(9)'' in its place.

PART 5—PUBLICIZING CONTRACT ACTIONS

3. Revise the last sentence of section 5.204 to read as follows:

36768 Federal Register / Vol. 65, No. 112 / Friday, June 9, 2000 / Rules and Regulations

OFFICE OF MANAGEMENT AND BUDGET

Office of Federal Procurement Policy

48 CFR Part 9903

Cost Accounting Standards Board; Applicability, Thresholds and Waiver of Cost Accounting Standards Coverage

AGENCY: Cost Accounting Standards Board, Office of Federal Procurement Policy, OMB.

ACTION: Final rule.

SUMMARY: The Office of Federal Procurement Policy, Cost Accounting Standards Board, is revising applicability, thresholds and procedures for the application of the Cost Accounting Standards (CAS) to negotiated government contracts. This rulemaking is authorized pursuant to Section 26 of the Office of Federal Procurement Policy Act. The Board is taking final action on this topic in order to adjust CAS applicability requirements and dollar thresholds in accordance with the provisions of the National Defense Authorization Act for Fiscal Year 2000.

DATES: This final rule is effective June 9, 2000.

FOR FURTHER INFORMATION CONTACT: Richard C. Loeb, Executive Secretary, Cost Accounting Standards Board (telephone: 202–395–3254).

SUPPLEMENTARY INFORMATION

A. Background

On February 7, 2000, the Cost Accounting Standards Board issued an interim rule with request for comment, 65 FR 5990. That rule, implemented Sec. 802 of the National Defense Authorization Act for Fiscal Year 2000, Pub. L. 106–65, ''Streamlined Applicability of Cost Accounting Standards.'' This final rule implements the provisions of Sec. 802 and provides responses to public comments received on the interim CAS Board rule. Many of the public comments received by the Board addressed issues that were beyond the scope of Sec. 802. The Board is limiting its revisions in this final rule to the items specified in Sec. 802.

B. Summary of Amendments

''Trigger contract'': 48 CFR 9903.201–1(b) is amended by adding a new subparagraph (7) that exempts contracts and subcontracts from CAS coverage, provided that the business unit of the contractor or subcontractor is currently performing one or more CAS-covered contracts or subcontracts of $7.5 million or more.

''Firm-fixed price contract exemption'': The Board is implementing this statutory exemption by amending 48 CFR 9903.201–1(b) to revise subparagraph (15) to exempt from CAS coverage, firm-fixed-price contracts and subcontracts awarded on the basis of adequate price competition without submission of cost or pricing data. The Board is using the term ''cost or pricing data'' rather than ''certified'' cost or pricing data in order to conform to the statutory requirements of 10 U.S.C. § 2306(h)(1) and 41 U.S.C. § 254(b), which defines ''Cost or pricing data'' as data that requires certification.

''Types of CAS coverage'': 48 CFR 9903.201–2(a) is amended by revising the dollar threshold for ''full CAS coverage'' from $25 million to $50 million, and deleting the requirement that to be subject to ''full CAS coverage'', that a contractor or subcontractor have received at least one contract or subcontract that exceeded $1 million (the previous ''trigger contract'' amount for initiation of ''full CAS coverage''). 48 CFR 9903.201–2(b) is amended by revising the definition of ''modified CAS coverage'' to indicate that such coverage applies to covered contracts and subcontracts where the total value of CAS-covered contracts and subcontracts received by a business unit is less than $50 million. Conforming amendments have also been made to the solicitation provisions and contract clauses appearing at 9903.201–3 and 9903.201–4, respectively.

''Waiver'': 48 CFR 9903.201–5 is amended by revising this section to provide for agency CAS waiver authority under certain circumstances. ''Disclosure requirements'': 48 CFR 9903.202–1(b) is amended by revising the dollar amount for disclosure from $25 million to $50 million, and deleting the requirement that a contractor or subcontractor have received at least one contract in excess of $1 million.

C. Paperwork Reduction Act

The Paperwork Reduction Act, Public Law 96–511, does not apply to this rule, because this rule imposes no paperwork burden on offerors, affected contractors and subcontractors, or members of the public which requires the approval of OMB under 44 U.S.C. §3501, *et seq.* The purpose of this rule is to implement Pub. L. 106–65.

D. Executive Order 12866 and the Regulatory Flexibility Act

This rule serves to eliminate certain administrative requirements associated with the application and administration of the Cost Accounting Standards by covered government contractors and subcontractors. The economic impact on contractors and subcontractors is therefore expected to be minor. As a result, the Board has determined that this is not a ''major rule'' under the provisions of Executive Order 12866, and that a regulatory impact analysis is not required. Furthermore, this rule will not have a significant effect on a substantial number of small entities because small businesses are exempt from the application of the Cost Accounting Standards. Therefore, this rule does not require a regulatory flexibility analysis under the Regulatory Flexibility Act of 1980.

E. Public Comments

This final rule is based upon the Board's interim rule that was issued on February 7, 2000, 65 FR 5990. Thirteen public comments were received, including eleven timely comments and two late comments. The major comments received and the Board's actions taken in response thereto are summarized below:

Comment: Eight commenters generally supported the interim rule.

Response: The Board noted these supportive comments.

Comment: Four commenters opposed the rule, stating their belief that it provides too many opportunities for contractors to avoid CAS coverage, leaving the Government exposed to undue risk, primarily by permitting the use of inconsistent or inappropriate accounting conventions.

Response: The Board noted the commenters concerns. However, this rule is designed to implement the requirements of Sec. 802 of the National Defense Authorization Act for Fiscal Year 2000, Pub. L. 106–65. In this respect, the Board believes that it is faithfully implementing the requirements of that law.

Comment: Seven commenters recommended that the Board retain the language of the previous CAS exemption found at 48 CFR 9903.201–1(b)(15), while adding the revised language found in the interim rule at 9903.201–1(b)(15), to constitute a new CAS exemption. These commenters believe that CAS should not apply regardless of whether a TINA waiver or exemption was granted.

Conversely, four commenters stated that they believed that the revised language at 9903.201–1(b)(15) represented a compromise, inasmuch as the statutory language at Sec. 802 appears to be designed to avoid encouraging contractors to seek TINA waivers merely in order to be exempted from CAS requirements.

Response: Based on the legal, legislative and administrative history of this issue (including agency CAS waiver reporting requirements), the Board believes that it is adhering to the statutory intent of Sec. 802. As such, the language contained in the interim rule with respect to 9903.201–1(b)(15) is being adopted in this final rule.

Comment: Seven commenters recommended revisions to the language at 9903.201–1(b)(7) to define the term ''currently performing''. Four of the seven commenters recommended a definition(s) that would have the effect of exempting more contracts from CAS coverage; while three commenters recommended definition(s) that would have the effect of including more contracts within the scope of CAS coverage.

Response: The Board believes that the term ''currently performing'' is more than adequately defined in the Board's rules at 48 CFR 9903.301. ''Currently performing'', as used in the Board's rules, means that a contractor has been awarded a CAS-covered contract, but has not yet received notification of final acceptance of all supplies, services and data deliverable under the contract (including options). The Board would draw the commenters attention to the existence of this long-standing definition.

Comment: The Board also received a number of comments regarding additional CAS exemptions, waivers, dollar threshold and applicability changes, and other regulatory matters that would have the general effect of further reducing CAS applicability to contracts and subcontracts. In addition, one commenter opposed the delegation of any CAS waiver authority to the procuring agencies.

Response: While the Board has considered all the comments it has received, it is specifically limiting the scope of this rulemaking to those items required to be addressed by Sec. 802 of Pub. L. 106–65.

List of Subjects in 48 CFR Part 9903

Cost accounting standards, Government procurement.

Nelson F. Gibbs,
Executive Director, Cost Accounting Standards Board.

For the reasons set forth in this preamble, chapter 99 of title 48 of the Code of Federal Regulations is amended as set forth below:

1. The authority citation for part 9903 of chapter 99 of title 48 continues to read as follows:

Authority: Pub. L. 100–679, 102 Stat 4056, 41 U.S.C. 422.

9903.201 [Amended]

2. Section 9903.201–1 is amended by revising paragraph (b)(7) and revising paragraph (b)(15) to read as follows:

9903.201–1 CAS applicability.

* * * * *

(b) * * *

(7) Contracts or subcontracts of less than $7.5 million, provided that, at the time of award, the business unit of the contractor or subcontractor is not currently performing any CAS-covered contracts or subcontracts valued at $7.5 million or greater.

* * * * *

(15) Firm-fixed-price contracts or subcontracts awarded on the basis of adequate price competition without submission of cost or pricing data.

3. Section 9903.201–2 is amended by revising paragraphs (a)(1) and (2) and (b)(1) and (2) to read as follows:

9903.201–2 Types of CAS coverage.

(a) * * *

(1) Receive a single CAS-covered contract award of $50 million or more; or

(2) Received $50 million or more in net CAS-covered awards during its preceding cost accounting period.

(b) *Modified coverage.* (1) Modified CAS coverage requires only that the contractor comply with Standard 9904.401, Consistency in Estimating, Accumulating, and Reporting Costs, Standard 9904.402, Consistency in Allocating Costs Incurred for the Same Purpose, Standard 9904.405, Accounting for Unallowable Costs and Standard 9904.406, Cost Accounting Standard—Cost Accounting Period. Modified, rather, than full, CAS coverage may be applied to a covered contract of less than $50 million awarded to a business unit that received less than $50 million in net CAS-covered awards in the immediately preceding cost accounting period.

(2) If any one contract is awarded with modified CAS coverage, all CAS-covered contracts awarded to that business unit during that cost accounting period must also have modified coverage with the following exception: if the business unit receives a single CAS-covered contract award of $50 million or more, that contract must be subject to full CAS coverage. Thereafter, any covered contract awarded in the same cost accounting period must also be subject to full CAS coverage.

* * * * *

4. Section 9903.201–3 is amended by revising the clause heading; by revising paragraph (c)(3) in Part I of the clause, by revising the CAUTION paragraph following paragraph (c)(4) in Part I of the clause; and by revising Part II of the clause, to read as follows:

9903.201–3 Solicitation provisions.

* * * * *

Cost Accounting Standards Notices and Certification (April 2000)

* * * * *

I. Disclosure Statement—Cost Accounting Practices and Certification

* * * * *

(c) * * *

■(3) Certificate of Monetary Exemption.

The offeror hereby certifies that the offeror, together with all divisions, subsidiaries, and affiliates under common control, did not receive net awards of negotiated prime contracts and subcontracts subject to CAS totaling $50 million or more in the cost accounting period immediately preceding the period in which this proposal was submitted.

The offeror further certifies that if such status changes before an award resulting from this proposal, the offeror will advise the Contracting Officer immediately.

(4) * * *

Caution: Offerors currently required to disclose because they were awarded a CAS-covered prime contract or subcontract of $50 million or more in the current cost accounting period may not claim this exemption (4). Further, the exemption applies only in connection with proposals submitted before expiration of the 90-day period following the cost accounting period in which the monetary exemption was exceeded.

II. Cost Accounting Standards—Eligibility for Modified Contact Coverage

If the offeror is eligible to use the modified provisions of 9903.201–2(b) and elects to do so, the offeror shall indicate by checking the box below. Checking the box below shall mean that the resultant contract is subject to the Disclosure and Consistency of Cost Accounting Practices clause in lieu of the Cost Accounting Standards clause.

■The offeror hereby claims an exemption from the Cost Accounting Standards clause under the provisions of 9903.201–2(b) and certifies that the offeror is eligible for use of the Disclosure and Consistency of Cost Accounting Practices clause because during the cost accounting period immediately preceding the period in which this proposal was submitted, the offeror received less than $50 million in awards of CAS-covered prime contracts and subcontracts. The offeror further certifies that if such status changes before an award resulting from this proposal, the offeror will advise the Contracting Officer immediately.

Caution: An offeror may not claim the above eligibility for modified contract coverage if this proposal is expected to result in the award of a CAS-covered contract of $50 million or more or if, during its current cost accounting period, the offeror has been awarded a single CAS-covered prime contract or subcontract of $50 million or more.

* * * * *

5. Section 9903.201–4 is amended by revising paragraph (c)(1) to read as follows:

9903.201–4 Contract clauses.

* * * * *

(c) *Disclosure and Consistency of Cost Accounting Practices.* (1) The contracting officer shall insert the clause set forth below, Disclosure and Consistency of Cost Accounting Practices, in negotiated contracts when the contract amount is over $500,000 but less than $50 million, and the offeror certifies it is eligible for and elects to use modified CAS coverage (*see* 9903.201–2, unless the clause prescribed in paragraph (d) of this subsection is used).

* * * * *

6. Section 9903.201–5 is revised to read as follows:

9903.201–5 Waiver

(a) The head of an executive agency may waive the applicability of the Cost Accounting Standards for a contract or subcontract with a value of less than $15 million, if that official determines, in writing, that the business unit of the contractor or subcontractor that will perform the work—

(1) Is primarily engaged in the sale of commercial items; and

(2) Would not otherwise be subject to the Cost Accounting Standards under this Chapter.

(b) The head of an executive agency may waive the applicability of the Cost Accounting Standards for a contract or subcontract under exceptional circumstances when necessary to meet the needs of the agency. A determination to waive the applicability of the Cost Accounting Standards by the agency head shall be set forth in writing, and shall include a statement of the circumstances justifying the waiver.

(c) The head of an executive agency may not delegate the authority under paragraphs (a) and (b) of this section, to any official below the senior policymaking level in the agency.

(d) The head of each executive agency shall report the waivers granted under paragraphs (a) and (b) of this section, for that agency, to the Cost Accounting Standards Board, on an annual basis, not later than 90 days after the close of the Government's fiscal year.

(e) Upon request of an agency head or his designee, the Cost Accounting Standards Board may waive all or any part of the requirements of 9903.201–4(a), Cost Accounting Standards, or 9903.201–4(c), Disclosure and Consistency of Cost Accounting Practices, with respect to a contract subject to the Cost Accounting Standards. Any request for a waiver shall describe the proposed contract or subcontract for which the waiver is sought and shall contain—

(1) An unequivocal statement that the proposed contractor or subcontractor refuses to accept a contract containing all or a specified part of a CAS clause and the specific reason for that refusal;

(2) A statement as to whether the proposed contractor or subcontractor has accepted any prime contract or subcontract containing a CAS clause;

(3) The amount of the proposed award and the sum of all awards by the agency requesting the waiver to the proposed contractor or subcontractor in each of the preceding 3 years;

(4) A statement that no other source is available to satisfy the agency's needs on a timely basis;

(5) A statement of alternative methods considered for fulfilling the need and the agency's reasons for rejecting them;

(6) A statement of steps being taken by the agency to establish other sources of supply for future contracts for the products or services for which a waiver is being requested; and

(7) Any other information that may be useful in evaluating the request.

(f) Except as provided by the Cost Accounting Standards Board, the authority in paragraph (e) of this section shall not be delegated.

9903.202 Disclosure requirements.

7. Section 9903.202–1 is amended by revising paragraphs (b)(1) and (2) to read as follows:

9903.202–1 General requirements.

* * * * *

(b) * * *

(1) Any business unit that is selected to receive a CAS-covered contract or subcontract of $50 million or more shall submit a Disclosure Statement before award.

(2) Any company which, together with its segments, received net awards of negotiated prime contracts and subcontracts subject to CAS totaling $50 million or more in its most recent cost accounting period, must submit a Disclosure Statement before award of its first CAS-covered contract in the immediately following cost accounting period. However, if the first CAS-covered contract is received within 90 days of the start of the cost accounting period, the contractor is not required to file until the end of 90 days.

* * * * *

[FR Doc. 00–14242 Filed 6–8–00; 8:45 am]

BILLING CODE 3170–01–P

OFFICE OF MANAGEMENT AND BUDGET

Office of Federal Procurement Policy

48 CFR Part 9903

Cost Accounting Standards Board; Changes In Cost Accounting Practices.

AGENCY: Cost Accounting Standards Board, Office of Federal Procurement Policy, OMB.

ACTION: Final rule.

SUMMARY: The Office of Federal Procurement Policy, Cost Accounting Standards Board (CASB), is amending the Board's regulations pertaining to actions the cognizant Federal agency official can take when a contractor makes a compliant change to an established cost accounting practice that is used to estimate, accumulate and report the costs of covered negotiated government contracts or does not comply with applicable Cost Accounting Standards (CAS). The amendments provide that accounting changes directly associated with external restructuring activities that are subject to and meet certain statutory requirements are not subject to the CASB's contract price and cost adjustment requirements, and establishes new coverage for processing compliant cost accounting practice changes and noncompliant cost accounting practice conditions in accordance with CAS contract clause requirements. The existing CAS contract clause interest rate citation is also amended to make explicit the specific interest rate to be applied when increased costs paid are recovered by the Government. This rulemaking is authorized pursuant to Section 26 of the Office of Federal Procurement Policy Act.

The Board is taking these actions after having given careful consideration to the comments it received regarding the Supplemental Notice of Proposed Rulemaking issued August 20, 1999 on this topic (SNPRM-II).

DATES: The effective date of this final rule is June 14, 2000.

FOR FURTHER INFORMATION CONTACT: Rudolph J. Schuhbauer, Project Director, Cost Accounting Standards Board (telephone: 202–395–1052).

SUPPLEMENTARY INFORMATION:

A. Regulatory Process

The CASB's rules, regulations and Cost Accounting Standards (CAS) are codified at 48 CFR Chapter 99. Section 26(g)(1) of the Office of Federal Procurement Policy Act, 41 U.S.C. § 422(g), requires that the Board, prior to the establishment of any new or revised Standard, complete a prescribed rulemaking process. The process generally consists of the following four steps:

(1) Consult with interested persons concerning the advantages, disadvantages and improvements anticipated in the pricing and administration of Government contracts as a result of the adoption of a proposed Standard (e.g., promulgation of a Staff Discussion Paper (SDP)).

(2) Issue an Advance Notice of Proposed Rulemaking (ANPRM).

(3) Issue a Notice of Proposed Rulemaking (NPRM).

(4) Promulgate a Final Rule.

This Notice is step four of the four-step process.

B. Background

Prior Promulgations.

Many commenters identified the Board's regulatory coverage on ''changes in cost accounting practice'' as a matter requiring clarification and/or further coverage. The CASB requested public comments from interested parties on this topic in an SDP published in the **Federal Register** on April 9, 1993 (58 FR 18428), in an ANPRM published on April 25, 1995 (60 FR 20252) and in an NPRM published on September 18, 1996 (61 FR 49196). The CASB requested additional comments in two Supplemental NPRM's that were published on July 14, 1997 (62 FR 37654) and August 20, 1999 (64 FR 45700).

The various Notices proposed to amend the Board's current coverage governing what constitutes a change to a cost accounting practice. The previously proposed revisions included amendments to conform the language contained in the contract clauses for ''Full'' and ''Modified'' coverage, to address certain Federal agency responsibilities, to expand the criteria for desirable change determinations and to exempt certain changes in a contractor's cost accounting practices from the Board's contract price and cost adjustment requirements. A new subpart was also proposed to delineate the actions to be taken by the contracting parties when a contractor makes a compliant change to a cost accounting practice or follows a noncompliant practice.

Public Comments

Fifty-three sets of public comments were received in response to the SNPRM-II. The public comments were received from contractors, educational institutions, professional associations, Federal agencies, accounting organizations, and individuals. An open public meeting was held on December 6, 1999, regarding the Board's SNPRM-II. On January 7, 2000, the Department of Defense replaced its initial comments submitted on November 22, 1999, with an alternative proposal for the Board's consideration. Twelve public commenters from the contractor community subsequently withdrew their formally submitted comments and advised the Board that they preferred the alternate proposal submitted by the Department of Defense. On February 29, 2000, the Department of Defense submitted a revised alternative proposal. The two alternative proposals were developed in an open forum hosted by the National Contract Management Association. The February 29, 2000, proposal contained alternative language for what constitutes a change to a cost accounting practice, for exempting certain accounting changes from the cost impact process and for determining when a change to an accounting practice may be determined to be a ''desirable'' change. Three of the twelve commenters referred to above, further expressed their preference for the February 29, 2000, proposal.

On February 7, 2000, the CASB published an interim rule in the **Federal Register** (65 FR 5990), to adjust CAS applicability requirements and dollar thresholds in accordance with the provisions of the National Defense Authorization Act for Fiscal Year 2000, Pub. L. 106–65. This action is expected to reduce the number of CAS-covered contracts and the number of contractor business units performing CAS-covered contracts.

On April 18, 2000, the Civilian Agency Acquisition Council and the Defense Acquisition Regulations Council (Councils) proposed to amend the Federal Acquisition Regulation (FAR) to delineate the process for determining and resolving the cost impact on contracts and subcontracts when a contractor makes a compliant change to a cost accounting practice or follows a noncompliant practice. The FAR proposal was in response to an initiative by the Administrator, Office of Federal Procurement Policy. The proposed FAR coverage addresses many aspects of the fundamental CAS administration process that the Board's above referenced proposals also addressed. The Board encourages the Councils to finalize the proposed rulemaking.

In view of the circumstances that now prevail, a projected decline in CAS-covered contracts and the expected issuance of more explicit FAR guidance regarding the CAS cost impact process, the Board believes that issuance of any amendments to its regulations, in addition to those included in this final rule, is not presently warranted.

Summary of Amendments

In subpart 9903.2, CAS Program Requirements, of Part 9903, Contract Coverage, subsection 9903.201–4 is amended to clarify, in certain prescribed CAS contract clauses, that the applicable interest rate cited for use when recovering increased cost paid due to a contractor's failure to comply with an applicable CAS or to follow any cost accounting practice consistently is the underpayment rate established under section 6621(a)(2) of the Internal Revenue Code of 1986 (26 U.S.C. 6621(a)(2)).

Subsection 9903.201–6 is amended to provide guidance for determining:

— For a required change, that a change to an established cost accounting practice is required to comply with applicable CAS;
— For a unilateral practice change that a contractor makes, that the contemplated contract price and cost adjustments will protect the United States from payment of increased costs, in the aggregate; and that the net effect of the adjustments being made does not result in the recovery of more than the estimated amount of such increased costs;
— When a compliant change in cost accounting practice may be determined to be desirable and not detrimental to the Government's interests; and,
— For a noncompliant cost accounting practice, that the contemplated contract price and cost adjustments will protect the United States from payment of increased costs, in the aggregate; and that the net effect of the adjustments being made does not result in the recovery of more than the estimated amount of such increased costs.

Subsection 9903.201–8 is added to establish that the CASB's contract price and cost adjustment requirements are not applicable to compliant cost accounting practice changes directly associated with external restructuring activities that are subject to and meet the requirements of 10 U.S.C. § 2325.

C. Paperwork Reduction Act

The Paperwork Reduction Act, Public Law 96–511, does not apply to this rule, because this rule imposes no paperwork burden on offerors, affected contractors and subcontractors, or members of the public which requires the approval of OMB under 44 U.S.C. 3501, *et seq.*

D. Executive Order 12866 and the Regulatory Flexibility Act

The economic impact of this rule on contractors and subcontractors is expected to be minor. As a result, the Board has determined that this is not a "major rule" under the provisions of Executive Order 12866, and that a regulatory impact analysis is not required. Furthermore, this rule will not have a significant effect on a substantial number of small entities because small businesses are exempt from the application of the Cost Accounting Standards. Therefore, this rule does not require a regulatory flexibility analysis under the Regulatory Flexibility Act of 1980.

List of Subjects in 48 CFR Part 9903

Cost accounting standards, government procurement.

Nelson F. Gibbs,
Executive Director, Cost Accounting Standards Board.

For the reasons set forth in this preamble, chapter 99 of title 48 of the Code of Federal Regulations is amended as set forth below:

1. The authority citation for part 9903 continues to read as follows:

Authority: Pub. L. 100–679, 102 Stat. 4056, 41 U.S.C. 422.

2. Section 9903.201–4 is amended as follows:

a. The contract clause heading immediately following paragraph (a) is revised, and in that contract clause the second sentence of paragraph (a)(5) is revised;

b. The contract clause heading immediately following paragraph (c) is revised, and in that contract clause the first sentence of paragraph (a)(3)(ii) and the second sentence of paragraph (a)(4) are revised;

c. The contract clause heading immediately following paragraph (e) is revsied, and in that contract clause the second sentence of paragraph (a)(5) is revised.

The revisions read as follows:

9903.201–4 Contract clauses.

(a) * * *

* * * * *

Cost Accounting Standards (June 2000)

(a) * * *

(5) * * * Such adjustment shall provide for recovery of the increased costs to the United States, together with interest thereon computed at the annual rate established under section 6621(a)(2) of the Internal Revenue Code of 1986 (26 U.S.C. 6621(a)(2)) for such period, from the time the payment by the United States was made to the time the adjustment is effected. * * *

* * * * *

(c) * * *

* * * * *

Disclosure and Consistency of Cost Accounting Practices (June 2000)

(a) * * *

(3)(i) * * *

(ii) The Contractor shall, when the parties agree to a change to a cost accounting practice and the Contracting Officer has made the finding required in 9903.201–6(c) that the change is desirable and not detrimental to the interests of the Government, negotiate an equitable adjustment as provided in the Changes clause of this contract. * * *

(4) * * * Such adjustment shall provide for recovery of the increased costs to the United States, together with interest thereon computed at the annual rate established under section 6621(a)(2) of the Internal Revenue Code of 1986 (26 U.S.C. 6621(a)(2)) for such period, from the time the payment by the United States was made to the time the adjustment is effected. * * *

* * * * *

(e) * * *

* * * * *

Cost Accounting Standards— Educational Institutions (June 2000)

(a) * * *

(5) * * * Such adjustment shall provide for recovery of the increased costs to the United States, together with interest thereon computed at the annual rate established under section 6621(a)(2) of the Internal Revenue Code of 1986 (26 U.S.C. 6621(a)(2)) for such period, from the time the payment by the United States was made to the time the adjustment is effected. * * *

* * * * *

3. Section 9903.201–6 is revised to read as follows:

9903.201–6 Findings.

(a) Required change. (1) *Finding.* Prior to making any equitable adjustment under the provisions of paragraph (a)(4)(i) of the contract clause set forth in 9903.201–4(a) or 9903.201–4(e), or paragraph (a)(3)(i) of the contract clause set forth in 9903.201–4(c), the Contracting Officer shall make a finding that the practice change was required to comply with a CAS, modification or interpretation thereof, that subsequently became applicable to the contract; or, for planned changes being made in order to remain CAS compliant, that the former practice was in compliance with applicable CAS and the planned change is necessary for the contractor to remain in compliance.

(2) *Required change* means a change in cost accounting practice that a contractor is required to make in order to comply with applicable Standards, modifications, or interpretations thereto, that subsequently become applicable to an existing CAS-covered contract due to the receipt of another CAS-covered contract or subcontract. It also includes a prospective change to a disclosed or established cost accounting practice when the cognizant Federal agency official determines that the former practice was in compliance with applicable CAS and the change is necessary for the contractor to remain in compliance.

(b) Unilateral change. (1) *Findings.* Prior to making any contract price or cost adjustment(s) under the change provisions of paragraph (a)(4)(ii) of the contract clause set forth in 9903.201–4(a) or 9903.201–4(e), or paragraph (a)(3)(ii) of the contract clause set forth in 9903.201–4(c), the Contracting Officer shall make a finding that the contemplated contract price and cost adjustments will protect the United States from payment of increased costs, in the aggregate; and that the net effect of the adjustments being made does not result in the recovery of more than the estimated amount of such increased costs.

(2) *Unilateral change by a contractor* means a change in cost accounting practice from one compliant practice to another compliant practice that a contractor with a CAS-covered contract(s) elects to make that has not been deemed desirable by the cognizant Federal agency official and for which the Government will pay no aggregate increased costs.

(3) *Action to preclude the payment of aggregate increased costs by the Government.* In the absence of a finding pursuant to paragraph (c) of this subsection that a compliant change is desirable, no agreement may be made with regard to a change to a cost accounting practice that will result in the payment of aggregate increased costs by the United States. For these changes, the cognizant Federal agency official shall limit upward contract price adjustments to affected contracts to the amount of downward contract price adjustments of other affected contracts, i.e., no net upward contract price adjustment shall be permitted.

(c) Desirable change. (1) *Finding.* Prior to making any equitable adjustment under the provisions of paragraph (a)(4)(iii) of the contract clause set forth in 9903.201–4(a) or 9903.201–4(e), or paragraph (a)(3)(ii) of the contract clause set forth in 9903.201–4(c), the cognizant Federal agency official shall make a finding that the change to a cost accounting practice is desirable and not detrimental to the interests of the Government.

(2) *Desirable change* means a compliant change to a contractor's established or disclosed cost accounting practices that the cognizant Federal agency official finds is desirable and not detrimental to the Government and is therefore not subject to the no increased cost prohibition provisions of CAS-covered contracts affected by the change. The cognizant Federal agency official's finding need not be based solely on the cost impact that a proposed practice change will have on a contractor's or subcontractor's current CAS-covered contracts. The change to a cost accounting practice may be determined to be desirable even though existing contract prices and/or cost allowances may increase. The determination that the change to a cost accounting practice is desirable, should be made on a case-by-case basis.

(3) Once a determination has been made that a compliant change to a cost accounting practice is a desirable change, associated management actions that also have an impact on contract costs should be considered when negotiating contract price or cost adjustments that may be needed to equitably resolve the overall cost impact of the aggregated actions.

(4) Until the cognizant Federal agency official has determined that a change to a cost accounting practice is deemed to be a desirable change, the change shall be considered to be a change for which the Government will not pay increased costs, in the aggregate.

(d) *Noncompliant cost accounting practices.* (1) *Findings.* Prior to making any contract price or cost adjustment(s) under the provisions of paragraph (a)(5) of the contract clause set forth in 9903.201–4(a) or 9903.201–4(e), or paragraph (a)(4) of the contract clause set forth in 9903.201–4(c), the Contracting Officer shall make a finding that the contemplated contract price and cost adjustments will protect the United States from payment of increased costs, in the aggregate; and that the net effect of the adjustments being made does not result in the recovery of more than the estimated amount of such increased costs. While individual contract prices, including cost ceilings or target costs, as applicable, may be increased as well as decreased to resolve an estimating noncompliance, the aggregate value of all contracts affected by the estimating noncompliance shall not be increased.

4. Section 9903.201–8 is added to read as follows:

9903.201–8 Compliant accounting changes due to external restructuring activities

The contract price and cost adjustment requirements of this part 9903 are not applicable to compliant cost accounting practice changes directly associated with external restructuring activities that are subject to and meet the requirements of 10 U.S.C. 2325.

[FR Doc. 00–14243 Filed 6–13–00; 8:45 am]

BILLING CODE 3110–01–P

A. Background

On June 16, 2004, the Assistant Administrator for Procurement approved a deviation to NFS 1802.101 to designate the Associate Administrator for Exploration Systems as head of the contracting activity in lieu of the Center Director(s) for all contracts that directly support the Exploration Systems Mission Directorate (ESMD). This deviation was approved in support of the Headquarters transformation and the realignment of program management responsibilities between NASA Headquarters and the field centers. This final rule implements that deviation.

B. Regulatory Flexibility Act

This final rule does not constitute a significant revision within the meaning of FAR 1.501 and Public Law 98–577, and publication for public comment is not required. However, NASA will consider comments from small entities concerning the affected NFS Part 1802 in accordance with 5 U.S.C. 610.

C. Paperwork Reduction Act

The Paperwork Reduction Act does not apply because the changes do not impose recordkeeping or information collection requirements which require the approval of the Office of Management and Budget under 44 U.S.C. 3501, *et seq.*

List of Subjects in 48 CFR Part 1802

Government procurement.

Tom Luedtke,
Assistant Administrator for Procurement.

PART 1802—DEFINITIONS OF WORDS AND TERMS

■ Accordingly, 48 CFR part 1802 is amended as follows:

■ 1. The authority citation for 48 CFR part 1802 continues to read as follows:

Authority: 42 U.S.C. 2473(c)(1)

■ 2. Amend section 1802.101 by revising the definition of ''head of the contracting activity (HCA)'' to read as follows:

1802.101 Definitions.

* * * * *

Head of the contracting activity (HCA) means, for field installations, the Director or other head and, for NASA Headquarters, the Assistant Administrator for Management Systems. For International Space Station (ISS) and Space Shuttle Program contracts, the HCA is the Headquarters Deputy Associate Administrator for ISS and Shuttle Programs in lieu of the field Center Director(s). For Exploration Systems Mission Directorate (ESMD) contracts, the HCA is the Associate Administrator for ESMD in lieu of the field Center Director(s).

* * * * *

[FR Doc. 05–9953 Filed 5–20–05; 8:45 am]

BILLING CODE 7510–01–P

OFFICE OF MANAGEMENT AND BUDGET

Office of Federal Procurement Policy

48 CFR Part 9903

Cost Accounting Standards Board; Applicability of Cost Accounting Standards Coverage

AGENCY: Cost Accounting Standards Board, Office of Federal Procurement Policy, OMB.

ACTION: Interim rule with request for comment.

SUMMARY: The Cost Accounting Standards (CAS) Board is revising the criteria applicable to United Kingdom (UK) contractors for filing a Disclosure Statement, Form No. CASB DS–1. This rulemaking is authorized pursuant to section 26 of the Office of Federal Procurement Policy Act. The Board is promulgating this interim rule in order to comply with a specific request by the UK Ministry of Defence to simplify the compliance process with CAS Board disclosure requirements for UK contractors.

DATES: *Effective Date:* This rule is effective May 23, 2005.

Comment Date: Comments upon this interim rule must be in writing and must be received by July 22, 2005.

ADDRESSES: Comments should be addressed to Dr. Rein Abel, Director of Research, Cost Accounting Standards Board, Office of Federal Procurement Policy, 725 17th Street, NW., Room 9013, Washington, DC 20503. Comments should be faxed to Rein Abel, at 202–395–5105.

FOR FURTHER INFORMATION CONTACT: Rein Abel, Director of Research, Cost Accounting Standards Board (telephone: 202–395–3254).

SUPPLEMENTARY INFORMATION:

A. Background

Unlike certain other foreign contractors (*e.g.*, German and Canadian), UK contractors currently have to file a regular CAS Board Disclosure Statement (DS–1) in accordance with CAS regulations. The UK Ministry of Defence initially approached the Board with a request to use the corresponding UK form ''Questionnaire on Method of Allocation of Costs'' (QMAC), in lieu of the DS–1. After a review of the content of the QMAC, the UK and U.S. representatives agreed that it did not have the same scope as the DS–1. Therefore, it was agreed that to cover the gap in the coverage a ''Supplemental QMAC'' was needed.

The CAS Board has approved a Supplemental QMAC that is acceptable to the UK Ministry of Defence, and the CAS Board has received a request from the UK Ministry of Defence to allow UK contractors to submit their basic QMAC, together with the Supplemental QMAC, in lieu of the DS–1. At its meeting on February 23, 2005, the Board agreed to this change in the CAS requirements so that UK contractors with CAS-covered contracts will be allowed to file the UK QMAC together with its Supplement in lieu of the DS–1 required of U.S. contractors.

The Board believes that an interim rule with request for comment is an appropriate mode for the promulgation of this rule. It is based on a request by the UK Ministry of Defense for a specific action regarding the CAS disclosure statement to be used by the UK defense contractors. The Board believes that its response to this request as incorporated in this rule is straight forward and, in essence, non controversial. Therefore, the Board believes that in this instance the Board's usual ''four step'' promulgation process is not necessary or appropriate.

To effect this change, the interim rule includes the following revisions:

(1) The deletion of 9903.201–1(b)(12) (all foreign contractors, including UK contractors, are subject to the requirements at 9903.201–1(b)(4));

(2) The deletion of 9903.201–4(d); and

(3) An amendment to 9903.202–1(e) to add the U.K. to the list of the countries whose contractors may file a disclosure form adopted by an agency of their own Government in lieu of the DS–1.

B. Paperwork Reduction Act

The Paperwork Reduction Act, Public Law 96–511, does not apply to this rulemaking, because this rule imposes no paperwork burden on offerors, affected contractors and subcontractors, or members of the public which require the approval of OMB under 44 U.S.C. 3501, *et seq.*

C. Executive Order 12866 and the Regulatory Flexibility Act

The economic impact of this rule on contractors and subcontractors is expected to be minor. As a result, the Board has determined that this interim rule will not result in the promulgation of a ''major rule'' under the provisions of Executive Order 12866, and that a regulatory impact analysis will not be required. Furthermore, this rule will not have a significant impact on a substantial number of small businesses because small businesses are exempt from the application of the Cost Accounting Standards. Therefore, this rule does not require a regulatory flexibility analysis under the Regulatory Flexibility Act of 1980.

D. Public Comments

Interested persons are invited to participate by submitting data, views or arguments with respect to this interim rule. All comments must be in writing and submitted to the address indicated in the **ADDRESSES** section.

List of Subjects in 48 CFR Part 9903

Accounting, Government procurement.

David H. Safavian,

Chair, Cost Accounting Standards Board.

■ For the reasons set forth in this preamble, chapter 99 of title 48 of the Code of Federal Regulations is amended as set forth below:

PART 9903—CONTRACT COVERAGE

Subpart 9903.2—CAS Program Requirements

9903.201–1 [Amended]

■ 1. Section 9903.201–1 is amended by removing and reserving paragraph (b)(12).

9903.201–4 [Amended]

■ 2. Section 9903.201–4 is amended by removing and reserving paragraph (d).

■ 3. Section 9903.202–1 is amended by revising paragraph (e) to read as follows:

9903.202–1 General requirements.

* * * * *

(e) Foreign contractors and subcontractors who are required to submit a Disclosure Statement may, in lieu of filing a Form No CASB–DS–1, make disclosure by using a disclosure form prescribed by an agency of its Government, provided that the Cost Accounting Standards Board determines that the information disclosed by that means will satisfy the objectives of Public Law 100–679. The use of alternative forms has been approved for the contractors of the following countries:

(1) Canada.

(2) Federal Republic of Germany.

(3) United Kingdom.

* * * * *

[FR Doc. 05–9847 Filed 5–20–05; 8:45 am]

BILLING CODE 3110–01–P

DEPARTMENT OF THE INTERIOR

Fish and Wildlife Service

50 CFR Part 17

RIN 1018–AT65

Endangered and Threatened Wildlife and Plants; Establishment of an Additional Manatee Protection Area in Lee County, FL

AGENCY: Fish and Wildlife Service, Interior.

ACTION: Final rule; correction.

SUMMARY: We, the Fish and Wildlife Service (Service), are correcting a typographical error in the final rule promulgated on April 7, 2005, to establish an additional manatee protection area in Lee County, Florida (Pine Island—Estero Bay Manatee Refuge). This correction is not substantive.

DATES: Effective April 4, 2005.

ADDRESSES: The complete file for this rule is available for inspection, by appointment, during normal business hours from 8 a.m. to 4:30 p.m. at the South Florida Field Office, U.S. Fish and Wildlife Service, 1339 20th Street, Vero Beach, Florida 32960.

FOR FURTHER INFORMATION CONTACT: Jay Slack or Kalani Cairns (see **ADDRESSES** section), telephone 772/562–3909; or visit our Web site at *http://verobeach.fws.gov*.

SUPPLEMENTARY INFORMATION: On April 7, 2005, we, the Service, promulgated a final rule (70 FR 17864) to establish the Pine Island—Estero Bay Manatee Refuge in Lee County, Florida. Because we made a typographical error in the regulatory text of the rule, we introduced an incorrect coordinate into the description of the Pine Island—Estero Bay Manatee Refuge. We correct this error now. This change is not substantive.

List of Subjects in 50 CFR Part 17

Endangered and threatened species, Exports, Imports, Reporting and recordkeeping requirements, Transportation.

Regulation Correction

■ For reasons set forth in the preamble, we correct 50 CFR part 17 by making the following correcting amendment:

PART 17—[CORRECTED]

■ 1. The authority citation for part 17 continues to read as follows:

Authority: 16 U.S.C. 1361–1407; 16 U.S.C. 1531–1544; 16 U.S.C. 4201–4245; Pub. L. 99–625, 100 Stat. 3500; unless otherwise noted.

§ 17.108 [Corrected]

■ 2. In § 17.108, amend paragraph (c)(13)(B) by removing ''81°05′09″ West'' and adding in its place 82°05′09″ West''.

Dated: May 17, 2005.

Sara Prigan,

Fish and Wildlife Service Federal Register Liaison.

[FR Doc. 05–10176 Filed 5–20–05; 8:45 am]

BILLING CODE 4310–55–P

DEPARTMENT OF COMMERCE

National Oceanic and Atmospheric Administration

50 CFR Part 679

[Docket No. 041126332–5039–02; I.D. 051705F]

Fisheries of the Exclusive Economic Zone Off Alaska; Yellowfin Sole in the Bering Sea and Aleutian Islands Management Area

AGENCY: National Marine Fisheries Service (NMFS), National Oceanic and Atmospheric Administration (NOAA), Commerce.

ACTION: Closure.

SUMMARY: NMFS is prohibiting directed fishing for yellowfin sole in the Bering Sea and Aleutian Islands management area (BSAI). This action is necessary to prevent exceeding the 2005 yellowfin sole total allowable catch (TAC) in the BSAI.

DATES: Effective 1200 hrs, Alaska local time (A.l.t.), May 19, 2005, through 2400 hrs, A.l.t., December 31, 2005.

FOR FURTHER INFORMATION CONTACT: Josh Keaton, 907–586–7228.

SUPPLEMENTARY INFORMATION: NMFS manages the groundfish fishery in the BSAI according to the Fishery Management Plan for Groundfish of the Bering Sea and Aleutian Islands Management Area (FMP) prepared by the North Pacific Fishery Management Council under authority of the Magnuson-Stevens Fishery Conservation and Management Act. Regulations governing fishing by U.S. vessels in accordance with the FMP appear at subpart H of 50 CFR part 600 and 50 CFR part 679.

The 2005 yellowfin sole TAC in the BSAI is 77,083 metric tons (mt) as established by the 2005 and 2006 final harvest specifications for groundfish in the BSAI (70 FR 8979, February 24, 2005).

In accordance with § 679.20(d)(1)(i), the Administrator, Alaska Region, NMFS (Regional Administrator), has determined that the 2005 yellowfin sole

Federal Register / Vol. 70, No. 237 / Monday, December 12, 2005 / Proposed Rules 73423

''(Date)''; and removing from the last sentence of paragraph (d) of the clause ''$500,000'' and adding ''$550,000'' in its place.

52.230–3 [Amended]

84. Amend section 52.230–3 by revising the date of the clause to read ''(Date)''; and removing from paragraph (d)(2) ''$500,000'' and adding ''$550,000'' in its place.

52.230–5 [Amended]

85. Amend section 52.230–5 by revising the date of the clause to read ''(Date)''; and removing from paragraph (d)(2) of the clause ''$500,000'' and adding ''$550,000'' in its place.

86. Amend section 52.236–1 by revising the introductory paragraph to read as follows:

52.236–1 Performance of Work by the Contractor.

As prescribed in 36.501(b), insert the following clause. Complete the clause by inserting the appropriate percentage consistent with the complexity and magnitude of the work and customary or necessary specialty subcontracting (see 36.501(a)):

* * * * *

87. Amend section 52.243–7 by revising the introductory paragraph to read as follows:

52.243–7 Notification of Changes.

As prescribed in 43.107, insert the following clause:

* * * * *

52.244–6 [Amended]

88. Amend section 52.244–6 by revising the date of the clause to read ''(Date)''; removing from paragraph (c)(1)(i) of the clause ''$500,000'' and adding ''$550,000'' in its place, and removing from paragraph (c)(1)(iii) of the clause ''(Dec 2001)'' and adding ''(Date)'' in its place.

52.248–3 [Amended]

89. Amend section 52.248–3 by revising the date of the clause to read ''(Date)''; and removing from the first sentence of paragraph (h) of the clause ''$50,000'' and adding ''$55,000'' in its place.

90. Amend section 52.249–1 by revising the introductory paragraph to read as follows:

52.249–1 Termination for Convenience of the Government (Fixed-Price) (Short Form).

As prescribed in 49.502(a)(1), insert the following clause:

* * * * *

PART 53—FORMS

53.219 [Amended]

91. Amend section 53.219 by removing from paragraphs (a) and (b) ''(Rev. 10/01)'' and adding ''(Date)'' in its place.

53.301–294 [Amended]

92. Amend section 53.301–294 at the bottom of page 1 of the form by revising the date of the form to read ''(Date)''; and on page 2 of the form, by removing from the first sentence of paragraph 3, under General Instructions, ''$500,000'' and adding ''$550,000'' in its place.

53.301–295 [Amended]

93. Amend section 53.301–295 at the bottom of page 1 of the form by revising the date of the form to read ''(Date)''; and on page 2 of the form, by removing from the first sentences of paragraphs 2 and 5, under General Instructions, ''$500,000'' and adding ''$550,000'' in their place.

[FR Doc. 05–16971 Filed 12–9–05; 8:45 am]

BILLING CODE 6820–EP–S

OFFICE OF MANAGEMENT AND BUDGET

Office of Federal Procurement Policy

48 CFR Parts 9901 and 9903

Cost Accounting Standards Board (CAS) Changes to Acquisition Thresholds

AGENCY: Cost Accounting Standards Board, Office of Federal Procurement Policy, OMB.

ACTION: Proposed rule with request for comment.

SUMMARY: The Cost Accounting Standards (CAS) Board is proposing to adjust the CAS application and full coverage thresholds for inflation in accordance with section 807 of the Ronald W. Reagan National Defense Authorization Act for Fiscal Year 2005 (Pub. L. 108–375).

DATES: Comments upon this proposed rule must be in writing and must be received by February 10, 2006.

ADDRESSES: Due to delays in OMB's receipt and processing of mail, respondents are strongly encouraged to submit comments electronically to ensure timely receipt. Electronic comments may be submitted to *casb2@omb.eop.gov.* Please put the full body of your comments in the text of the electronic message and also as an attachment readable in either MS Word or Corel WordPerfect. Please include your name, title, organization, postal address, telephone number, and e-mail address in the text of the message. Comments may also be submitted via facsimile to (202) 395–5105.

FOR FURTHER INFORMATION CONTACT: David J. Capitano, Cost Accounting Standards Board (telephone: 703–847–7486).

SUPPLEMENTARY INFORMATION:

A. Background

Analysis of Statutory Acquisition-Related Thresholds

Section 807 provides for adjustment every 5 years of acquisition-related thresholds, except for thresholds set by the Davis-Bacon Act, Service Contract Act, and trade agreements. The statute requires that the adjustment be based on inflation, using the Consumer Price Index (CPI) for all-urban consumers. Acquisition-related thresholds in statutes that were in effect on October 1, 2000, are subject to 5 years of inflation. For purposes of this proposed rule, the calculation of escalation is based on the CPI from December 1999 to December 2004 (the most recent available data), which currently computes at 1.1307, as determined by the Federal Acquisition Regulatory (FAR) Council.

Once the escalation factor is applied to the acquisition-related threshold, the law requires rounding of the calculated threshold as follows:

< $10,000	Nearest $500
$10,000–<$100,000	Nearest $5,000
$100,000–<$1,000,000	Nearest $50,000
$1,000,000 or more	Nearest $500,000

Applying the 1.1307 factor and the rounding criteria described above, the CAS thresholds have been revised as follows:

(a) For contract applicability, from $500,000 to $550,000;

(b) For applicability to a business unit, from $7.5 million to $8.5 million;

(c) For waiver authority, from $15 million to $17 million;

(d) For full coverage, from $50 million to $56.5 million;

(e) For disclosure statement submissions by a company (other than educational institutions), from $50 million to $56.5 million;

(f) For disclosure statement submissions by a segment of a company, from $10 million to $11.5 million; and

(g) For disclosure statement submissions by an educational institutions, from $25 million to $28.3 million.

B. Paperwork Reduction Act

The Paperwork Reduction Act, Public Law 96–511, does not apply to this rulemaking, because this rule imposes no paperwork burden on offerors, affected contractors and subcontractors, or members of the public which requires the approval of OMB under 44 U.S.C. 3501, *et seq.*

C. Executive Order 12866 and the Regulatory Flexibility Act

The economic impact of this rule on contractors and subcontractors is expected to be minor. As a result, the Board has determined that this rule is not significant under the provisions of Executive Order 12866, and that a regulatory impact analysis will not be required. Furthermore, this rule will not have a significant impact on a substantial number of small businesses because small businesses are exempt from the application of the Cost Accounting Standards. Therefore, this rule does not require a regulatory flexibility analysis under the Regulatory Flexibility Act of 1980.

D. Public Comments

Interested persons are invited to participate by submitting data, views or arguments with respect to this proposed rule. All comments must be in writing and submitted to the address indicated in the ADDRESSES section.

List of Subjects in 48 CFR Part 9903

Accounting, Government procurement.

Joshua B. Bolten,

Director.

For the reasons set forth in this preamble, chapter 99 of title 48 of the Code of Federal Regulations is proposed to be amended as set forth below:

PART 9901—RULES AND PROCEDURES

1. The authority citation for part 9901 is revised to read as follows:

Authority: 41 U.S.C. 422(f).

2. Revise section 9901.306 to read as follows:

§ 9901.306 Standards applicability.

Cost Accounting Standards promulgated by the Board shall be mandatory for use by all executive agencies and by contractors and subcontractors in estimating, accumulating, and reporting costs in connection with pricing and administration of, and settlement of disputes concerning, all negotiated prime contract and subcontract procurements with the United States Government in excess of $550,000, other than contracts or subcontracts that have been exempted by the Board's regulations.

PART 9903—CONTRACT COVERAGE

3. The authority citation for part 9903 continues to read as follows:

Authority: 41 U.S.C. 422(f).

Subpart 9903.2—CAS Program Requirements

4. Section 9903.201–1 is amended by revising paragraphs (b)(2) and (b)(7) to read as follows:

§ 9903.201–1 CAS applicability.

* * * * *

(b) * * *

(2) Negotiated contracts and subcontracts not in excess of $550,000. For purposes of this paragraph (b)(2) an order issued by one segment to another segment shall be treated as a subcontract.

* * * * *

(7) Contracts or subcontracts of less than $8.5 million, provided that, at the time of award, the business unit of the contractor or subcontractor is not currently performing any CAS-covered contracts or subcontracts valued at $8.5 million or greater.

* * * * *

5. Section 9903–201–2 is amended by revising paragraphs (a)(1) and (2), (b)(1) and (2), and (c)(3) and (5) to read as follows:

§ 9903.201–2 Types of CAS coverage.

(a) * * *

(1) Receive a single CAS-covered contract award of $56.5 million or more;

(2) Receive $56.5 million or more in net CAS-covered awards during its preceding accounting period.

(b) *Modified coverage.* (1) Modified CAS coverage requires only that the contractor comply with Standard 9904.401, Consistency in Estimating, Accumulating, and Reporting Costs, Standard 9904.402, Consistency in Allocating Costs Incurred for the Same Purpose, Standard 9904.405, Accounting for Unallowable Costs and Standard 9904.406, Cost Accounting Standard—Cost Accounting Period. Modified, rather than full, CAS coverage may be applied to a covered contract if less than $56.5 million awarded to a business unit that received less than $56.5 million in net CAS-covered awards in the immediately preceding cost accounting period.

(2) If any one contract is awarded with modified CAS coverage, all CAS-covered contracts awarded to that business unit during that cost accounting period must also have modified coverage with the following exceptions: if the business unit receives a single CAS-covered contract award of $56.5 million or more, the contract must be subject to full CAS coverage. Thereafter, any covered contract awarded in the same cost accounting period must also be subject to full CAS coverage.

* * * * *

(c) * * *

(3) Applicable Standards. Coverage for educational institutions requires that the business unit comply with all of the CAS specified in part 9905 that are in effect on the date of the contract award and with any CAS that become applicable because of later award of a CAS-covered contract. This coverage applies to business units that receive negotiated contracts in excess of $550,000, except for CAS-covered contracts awarded to FFRDCs operated by an educational institution.

* * * * *

(5) Contract Clauses. The contract clause at 9903.201–4(e) shall be incorporated in each negotiated contract and subcontract awarded to an educational institution when the negotiated contract or subcontract price exceeds $550,000. For CAS-covered contracts awarded to an FFRDC operated by an educational institution, however, the full or modified CAS contract clause specified at 9903.201–4(a) or (c), as applicable, shall be incorporated.

* * * * *

6. Section 9903–201–3 is amended by revising the clause heading; by revising paragraphs (a) and (c)(3) in Part I of the clause, by revising the CAUTION paragraph following paragraph (c)(4) in Part I of the clause; and by revising Part II of the clause, to read as follows:

§ 9903.201–3 Solicitation provisions.

* * * * *

Cost Accounting Standards Notices and Certification (October 2005)

* * * * *

I. Disclosure Statement—Cost Accounting Practices and Certification

(a) Any contract in excess of $550,000 resulting from this solicitation, except for those contracts which are exempt as specified in 9903.201–1.

* * * * *

(c) * * *

(3) Certificate of Monetary Exemption.

The offeror hereby certifies that the offeror, together with all divisions, subsidiaries, and affiliates under common control, did not receive net awards of negotiated prime contracts and subcontracts subject to CAS totaling $56.5 million or more in the cost accounting period immediately preceding the period in which this proposal was submitted. The offeror further certifies that if such status changes before an award resulting from this proposal, the offeror will advise the Contracting Officer immediately.

(4) * * *

Caution: Offerors currently required to disclose because they were awarded a CAS-covered prime contract or subcontract of $56.5 million or more in the current cost accounting period may not claim this exemption (4). Further, the exemption applies only in connection with proposals submitted before expiration of the 90-day period following the cost accounting period in which the monetary exemption was exceeded.

II. Cost Accounting Standards—Eligibility for Modified Contract Coverage

If the offeror is eligible to use the modified provisions of 9903.201–2(b) and elects to do so, the offeror shall indicate by checking the box below. Checking the box below shall mean that the resultant contract is subject to the Disclosure and Consistency of Cost Accounting Practices clause in lieu of the Cost Accounting Standards clause.

The offeror hereby claims an exemption from the Cost Accounting Standards clause under the provisions of 9903.201–2(b) and certifies that the offeror is eligible for use of the Disclosure and Consistency of Cost Accounting Practices clause because during the cost accounting period immediately preceding the period in which this proposal was submitted, the offeror received less than $56.5 million in awards of CAS-covered prime contracts and subcontracts. The offeror further certifies that if such status changes before an award resulting from this proposal, the offeror will advise the Contracting Officer immediately.

Caution: An offeror may not claim the above eligibility for modified contract coverage if this proposal is expected to result in the award of a CAS-covered contract of $56.5 million or more or if, during its current cost accounting period, the offeror has been awarded a single CAS-covered prime contract or subcontract of $56.5 million or more.

* * * * *

7. Section 9903.201–4 is amended by revising:

A. The clause heading in paragraph (a)(2);

B. Paragraph (d) of the clause in paragraph (a);

C. Paragraph (c)(1);

D. The clause heading in paragraph (c)(2);

E. Paragraph (d)(2) of the clause in paragraph (c);

F. The clause heading in paragraph (e)(2); and

G. Paragraph (d) introductory text and (d)(2) of the clause in paragraph (e).

The revisions read as follows:

9903.201–4 Contract clauses.

(a) * * *

(2) * * *

Cost Accounting Standards (October 2005)

* * * * *

(d) The contractor shall include in all negotiated subcontracts which the Contractor enters into, the substance of this clause, except paragraph (b), and shall require such inclusion in all other subcontracts, of any tier, including the obligation to comply with all CAS in effect on the subcontractor's award date or if the subcontractor has submitted cost or pricing data, on the date of final agreement on price as shown on the subcontractor's signed Certificate of Current Cost or Pricing Data. If the subcontract is awarded to a business unit which pursuant to 9903.201–2 is subject to other types of CAS coverage, the substance of the applicable clause set forth in 9903.201–4 shall be inserted. This requirement shall apply only to negotiated subcontracts in excess of $550,000, except that the requirement shall not apply to negotiated subcontracts otherwise exempt from the requirement to include a CAS clause as specified in 9903.201–1.

(End of Clause)

* * * * *

(c) *Disclosure and Consistency of Cost Accounting Practices.* (1) The contracting officer shall insert the clause set forth below, Disclosure and Consistency of Cost Accounting Practices, in negotiated contracts when the contract amount is over $550,000 but less than $56.5 million, and the offeror certifies it is eligible for and elects to use modified CAS coverage (see 9903.201–2, unless the clause prescribed in paragraph (d) of this subsection is used).

(2) * * *

Disclosure and Consistency of Cost Accounting Practices (October 2005)

* * * * *

(d) * * *

(2) This requirement shall apply only to negotiated subcontracts in excess of $550,000.

* * * * *

(e) *Cost Accounting Standards—Educational Institutions.* * * *

(2) * * *

Cost Accounting Standards—Educational Institution (October 2005)

* * * * *

(d) The Contractor shall include in all negotiated subcontracts which the Contractor enters into, the substance of this clause, except paragraph (b), and shall require such inclusion in all other subcontracts, of any tier, including the obligation to comply with all applicable CAS in effect on the subcontractor's award date or if the subcontractor has submitted cost or pricing data, on the date of final agreement on price as shown on the subcontractor's signed Certificate of Current Cost or Pricing Data, except that:

(1) * * *

(2) This requirement shall apply only to negotiated subcontracts in excess of $550,000.

* * * * *

8. Section 9903.201–5 is amended by revising paragraph (a) to read as follows:

9903.201–5 Waiver.

(a) The head of an executive agency may waive the applicability of the Cost Accounting Standards for a contract or subcontract with a value of less than $17 million, if that official determines, in writing, that the business unit of the contractor or subcontractor that will perform the work:

(1) Is primarily engaged in the sale of commercial items; and

(2) Would not otherwise be subject to the Cost Accounting Standards under this Chapter.

* * * * *

9903.202 Disclosure requirements.

9. Section 9903–202–1 is amended by revising (b)(1) and (2); (c); and (f)(2)(i), (ii), and (iii) to read as follows:

9903.202–1 General requirements.

* * * * *

(b) Completed Disclosure Statements are required in the following circumstances:

(1) Any business unit that is selected to receive a CAS-covered contract or subcontract of $56.5 million or more shall submit a Disclosure Statement before award.

(2) Any company which, together with its segments, received net awards of negotiated prime contracts and subcontracts subject to CAS totaling $56.5 million or more in its most recent cost accounting period, must submit a Disclosure Statement before award of its first CAS-covered contract in the immediately following cost accounting period. However, if the first CAS-covered contract is received within 90 days of the start of the cost accounting period, the contractor is not required to file until the end of 90 days.

(c) When a Disclosure Statement is required, a separate Disclosure Statement must be submitted for each segment whose costs included in the total price of any CAS-covered contract or subcontract exceed $550,000, unless:

(1) The contract or subcontract is of the type or value exempted by 9903.201–1 or

(2) In the most recently completed cost accounting period the segment's CAS-covered awards are less than 30 percent of total segment sales for the period and less than $11.5 million.

* * * * *

(f) *Educational institutions-disclosure requirements.*

(1) * * *

(2) * * *

(i) Any business unit of an educational institution that is selected to receive a CAS-covered contract or subcontract in excess of $550,000 and is part of a college or university location listed in Exhibit A of Office of Management and Budget (OMB) Circular A–21 shall submit a Disclosure Statement before award. A Disclosure Statement is not required, however, if the listed entity can demonstrate that the net amount of Federal contract and financial assistance awards received during its immediately preceding cost accounting period was less than $28.5 million.

(ii) Any business unit that is selected to receive a CAS-covered contract or subcontract of $28.5 million or more shall submit a Disclosure Statement before award.

(iii) Any educational institution which, together with its segments, received net awards of negotiated prime contracts and subcontracts subject to CAS totaling $28.5 million or more in its most recent cost accounting period, of which, at least one award exceeded $1 million, must submit a Disclosure Statement before award of its first CAS-covered contract in the immediately following cost accounting period. However, if the first CAS-covered contract is received within 90 days of the start of the cost accounting period, the institution is not required to file until the end of 90 days.

* * * * *

[FR Doc. 05–23647 Filed 12–9–05; 8:45 am]

BILLING CODE 3110–01–P

DEPARTMENT OF COMMERCE

National Oceanic and Atmospheric Administration

50 CFR Part 216

[Docket No. 051110296–5296–01; I.D. 102405A]

RIN 0648–AU02

Protecting Spinner Dolphins in the Main Hawaiian Islands From Human Activities that Cause ''Take,'' as Defined in the Marine Mammal Protection Act and Its Implementing Regulations, or To Otherwise Adversely Affect the Dolphins

AGENCY: National Marine Fisheries Service (NMFS), National Oceanic and Atmospheric Administration (NOAA), Commerce.

ACTION: Advance notice of proposed rulemaking.

SUMMARY: NMFS is considering whether to propose regulations to protect wild spinner dolphins (*Stenella longirostris*) in the main Hawaiian Islands from ''take,'' as defined in the Marine Mammal Protection Act (MMPA) and its implementing regulations, or to otherwise adversely affect the dolphins. The scope of this advance notice of proposed rulemaking (ANPR) encompasses the activities of any person or conveyance that may result in the unauthorized taking of spinner dolphins and/or that may diminish the value to the dolphins of habitat routinely used by them for resting and/or that may cause detrimental individual-level and population-level impacts. The proposed regulation would apply only to the main Hawaiian Islands and only to spinner dolphins. NMFS requests comments on whether—and if so, what type of—conservation measures, regulations, and, if necessary, other measures would be appropriate to protect spinner dolphins in the main Hawaiian Islands from the effects of these activities.

DATES: Comments must be received at the appropriate address (see **ADDRESSES**) no later than January 11, 2006.

ADDRESSES: You may submit comments by any of the following methods:

- E-mail: *0648–AU02.NOA@noaa.gov.* Include in the subject line the following document identifier: 0648–AU02–NOA.
- Federal e-rulemaking Portal: *http://www.regulations.gov.*
- Mail: Marine Mammal Branch Chief, Protected Resources Division, Pacific Islands Regional Office, National Marine Fisheries Service, 1601 Kapiolani Boulevard, Suite 1110, Honolulu, HI 96814.

FOR FURTHER INFORMATION CONTACT: Chris Yates or Jennifer Sepez, Pacific Islands Regional Office, 808–944–2105; or Trevor Spradlin, Office of Protected Resources, 301–713–2322.

SUPPLEMENTARY INFORMATION:

Background

Viewing wild marine mammals in Hawaii is a popular recreational activity for both tourists and residents alike. In the past, most recreational viewing focused on humpback whales (*Megaptera novaeangliae*) during the winter months when the whales migrate from their feeding grounds off the coast of Alaska to Hawaii's warm and protected waters to breed and calve. However, in recent years, recreational activities have increasingly focused on viewing small cetaceans, with a particular emphasis on spinner dolphins (*Stenella longirostris*), which are routinely found close to shore in shallow coves and bays and other areas throughout the main Hawaiian Islands. NMFS is concerned that some of these activities cause unauthorized taking of dolphins, diminish the value to the dolphins of habitat routinely used by them for resting, and cause detrimental individual-level and population-level impacts.

The biology and behavior of Hawaiian spinner dolphins has been well documented in the scientific literature. Hawaiian spinner dolphins are identified as a race of Pacific spinner dolphins found in and around the Hawaiian Islands, including both the main Islands of Hawaii and the Northwestern Hawaiian Islands (Norris *et al.* 1994, page 17). Hawaiian spinner dolphins routinely utilize shallow coves and bays and other areas close to shore during the day to rest, care for their young and avoid predators before traveling to deeper water at night to hunt for food (Würsig *et al.* 1994, Norris 1994). As the dolphins begin or end their resting period, they engage in aerial spinning and leaping behaviors that are noticeable from shore (Würsig *et al.* 1994). However, when they are in a period of deep rest, their behavior consists of synchronous dives and extended periods swimming in quiet formation along the shallow bottom (see: Norris and Dohl 1980, Norris *et al.* 1985, Wells and Norris 1994, Würsig *et al.* 1994).

Scientific research studies have documented human disturbance of Hawaiian spinner dolphins during their resting periods along the west coast of the Big Island of Hawaii, most notably in and around Kealakekua Bay. Norris and Dohl (1980) noted that ''cruise boats'' would seek out and run through groups of spinner dolphins during an initial study of the dolphins in 1970, and in follow up research, Norris *et al.* (1985) found that spinner dolphins were particularly sensitive to disturbance during the early stage of their entry into the bay. Forest (2001) compared sightings records of spinner dolphins in Kealakekua Bay from 1979–1980 and 1993–1994, and found that the dolphins were utilizing the bay and engaging in aerial behaviors less frequently than before, and suggested increasing human disturbance as a cause. Courbis (2004) reported high levels of vessel and swimmer traffic in Kealakekua Bay and neighboring Honaunau Bay and Kauhako Bay, and found that spinner dolphins exhibited decreased aerial activity during their entry and exit into Kealakekua Bay when compared to previous studies, as well as increased aerial activity during mid-day when dolphins typically rest. Spinner dolphins in Kealakekua Bay also appeared to have shifted their preferred resting area in response to vessel and swimmer presence. In Kauhako Bay, dolphins were documented avoiding swimmers and leaving the bay in

PART 602—OMB CONTROL NUMBERS UNDER THE PAPERWORK REDUCTION ACT

■ **Par. 47**. The authority citation for part 602 continues to read as follows:

Authority: 26 U.S.C. 7805.

§ 602.101 [Amended]

■ **Par. 48**.

■ 1. In § 602.101(b), the following entries to the table are removed:

1.302–2T	1545–2019
1.302–4T	1545–2019
1.331–1T	1545–2019
1.332–6T	1545–2019
1.338–10T	1545–2019
1.351–3T	1545–2019
1.355–5T	1545–2019
1.368–3T	1545–2019
1.381(b)–1T	1545–2019
1.382–8T	1545–2019
1.382–11T	1545–2019
1.1081–11T	1545–2019
1.1221–2T	1545–2019
1.1502–13T	1545–2019
1.1502–31T	1545–2019
1.1502–32T	1545–2019
1.1502–33T	1545–2019
1.1502–95T	1545–2019
1.1563–3T	1545–2019
1.6012–2T	1545–2019

■ 2. The following entries are added in numerical order to the table:

1.332–6	1545–2019
1.351–3	1545–2019
1.355–5	1545–2019
1.368–3	1545–2019
1.382–11	1545–2019
1.1081–11	1545–2019

Kevin M. Brown,

Deputy Commissioner for Services and Enforcement.

Approved: June 4, 2007.

Eric Solomon,

Assistant Secretary of the Treasury.

[FR Doc. E7–11148 Filed 6–13–07; 8:45 am]

BILLING CODE 4830–01–P

OFFICE OF MANAGEMENT AND BUDGET

Office of Federal Procurement Policy

48 CFR Parts 9901 and 9903

Cost Accounting Standards Board (CAS) Changes to Acquisition Thresholds

AGENCY: Cost Accounting Standards Board, Office of Federal Procurement Policy, OMB.

ACTION: Final rule.

SUMMARY: The Office of Federal Procurement Policy, Cost Accounting Standards (CAS) Board, is revising the threshold for the application of CAS to negotiated Government contracts. This rulemaking is authorized pursuant to Section 26 of the Office of Federal Procurement Policy Act. The Board is taking final action on this topic in order to adjust the CAS applicability threshold in accordance with Section 822 of the 2006 National Defense Authorization Act (Pub. L. 109–163). Section 822 amended 41 U.S.C. 422(f)(2)(A) to require that the threshold for CAS applicability be the same as the threshold for compliance with the Truth in Negotiations Act (TINA).

DATES: This final rule is effective June 14, 2007.

FOR FURTHER INFORMATION CONTACT: Laura Auletta, Manager, Cost Accounting Standards Board, 725 17th Street, NW., Room 9013, Washington, DC 20503 (telephone: 202–395–3256).

SUPPLEMENTARY INFORMATION:

A. Background

On December 15, 2005, the CAS Board issued a proposed rule with request for comment (70 FR 73423) for the purpose of implementing Sec. 807 of the Ronald W. Reagan National Defense Authorization Act for Fiscal Year 2005, Pub. L. 108–375, ''Inflation Adjustment of Acquisition-Related Dollar Thresholds.'' Section 807 of Pub. L. 108–375 requires the periodic adjustment of acquisition-related thresholds contained in statutes that were in effect on October 1, 2000, with certain exceptions. The Federal Acquisition Regulation (FAR) Council is authorized to adjust these thresholds based on increases in the Consumer Price Index for all-urban consumers (CPI) and as prescribed in the Public Law.

Based on further review, the Board has determined that its thresholds are not subject to the provisions of Section 807 of the Pub. L 108–375 because these thresholds are not ''acquisition related,'' as defined by Section 807. Therefore, this final rule does not adjust the CAS thresholds to reflect the provisions of Section 807.

However, subsequent to the issuance of the CAS Board's proposed rule, Section 822 of the 2006 National Defense Authorization Act (Pub. L. 109–163) amended 41 U.S.C. 422(f)(2)(A) to require that the threshold for CAS applicability be the same as the threshold for compliance with the Truth in Negotiations Act (TINA). The TINA threshold is currently $650,000 (71 FR 57363). Accordingly, the Board is increasing the CAS applicability threshold to $650,000 to comply with Public Law 109–163.

B. Public Comments

The Board received three sets of public comments in response to the proposed rule.

1. PL 108–375 Does Not Require Threshold Adjustments

Comment: Two commenters opined that Section 807 of Public Law 108–375 does not apply to statutory thresholds in the Board's rules, regulations and standards. These commenters asserted that the law applies only to acquisition-related statutory dollar thresholds contained in the FAR. Thus, the Board is not required to adjust its statutory thresholds in response to Pub. L. 108–375.

Response: After further review of this issue, the Board agrees that Section 807 does not apply to the CAS thresholds. Section 807 of Public Law 108–375 requires the Federal Acquisition Regulatory Council to adjust each ''acquisition-related dollar threshold.'' Section 807 defines an acquisition-related dollar threshold as ''a dollar threshold that is specified in law as a factor in defining the scope of the applicability of a policy, procedure, requirement, or restriction provided in that law to the procurement of property or services by an executive agency, as determined by the Federal Acquisition Regulatory Council.'' The scope and applicability of the CAS is within the sole purview of the CAS Board. The Federal Acquisition Regulatory Council does not determine the scope or applicability of the Cost Accounting Standards. Therefore, for purposes of applying Section 807, the thresholds in the CAS do not meet the definition of an ''acquisition threshold.'' Thus, the requirements of Public Law 108–375 do not apply to the CAS thresholds. However, the Board is issuing a final rule to adjust the CAS applicability threshold required by Public Law 109–163.

2. Consistency Between CAS Applicability and TINA Thresholds

Comment: One commenter recommended that the CAS applicability threshold be modified to adopt the Truth in Negotiations Act (TINA) threshold for requiring cost or pricing data (FAR 15.403–4) since it will be very difficult to administer the impact of CAS issues associated with such contracts.

Response: As previously noted, shortly after the publication of the proposed rule, 41 U.S.C. 422(f)(2)(A) was amended to require that the CAS applicability threshold be equal to the TINA threshold. Accordingly, this final rule adjusts the CAS applicability threshold to $650,000, which is the current TINA threshold.

3. Advisability of Adjusting CAS Thresholds

Comment: One commenter asserted that the proposed threshold adjustments represent bad public policy and that previous increases in these thresholds have been ''simply astounding, and far in excess of any inflationary increases, no matter how measured.''

Response: Consistent with the intent of the proposed rule, the final rule includes only those adjustments of the CAS applicability threshold that are statutorily required. As such, the Board does not believe the commenter's assertion regarding the adjustments in the final rule has any merit.

4. Failure To Track CAS Thresholds to Inflation Expands CAS Applicability Beyond Its Original Intent

Comment: One commenter recommended that the Board independently review its thresholds to determine whether ''economic factors have caused more contractors to have become subject to CAS coverage'' and ''consider if there are now contractors covered in 2006 that the Board did not intend to cover in 1992.''

Response: The purpose of the proposed and final rules was to adjust the CAS thresholds to reflect statutory requirements. As such, the Board is confining the adjustment of CAS thresholds in this final rule to those adjustments required by statute. The Board will consider the commenter's recommendation to review the other CAS thresholds when formulating its agenda for future actions.

C. Paperwork Reduction Act

The Paperwork Reduction Act, Public Law 96–511, does not apply to this rulemaking, because this rule imposes no paperwork burden on offerors, affected contractors and subcontractors, or members of the public which requires the approval of OMB under 44 U.S.C. 3501, *et seq.*

D. Executive Order 12866 and the Regulatory Flexibility Act

The Board certifies that this rule will not have a significant effect on a substantial number of small entities within the meaning of the Regulatory Flexibility Act, 5 U.S.C. 601, *et seq.*, because small businesses are exempt from the application of the Cost Accounting Standards.

List of Subjects in 48 CFR Part 9903

Accounting, Government procurement.

Paul A. Denett,

Administrator, Office of Federal Procurement Policy.

■ For the reasons set forth in this preamble, Chapter 99 of Title 48 of the Code of Federal Regulations is amended as set forth below:

PART 9901—RULES AND PROCEDURES

■ 1. The authority citation for part 9901 continues to read as follows:

Authority: Pub. L. 100–679, 102 Stat. 4056, 41 U.S.C. 422.

■ 2. Revise section 9901.306 to read as follows:

9901.306 Standards applicability.

Cost Accounting Standards promulgated by the Board shall be mandatory for use by all executive agencies and by contractors and subcontractors in estimating, accumulating, and reporting costs in connection with pricing and administration of, and settlement of disputes concerning, all negotiated prime contract and subcontract procurements with the United States Government in excess of $650,000, other than contracts or subcontracts that have been exempted by the Board's regulations.

PART 9903—CONTRACT COVERAGE

■ 3. The authority citation for part 9903 continues to read as follows:

Authority: Pub. L. 100–679, 102 Stat. 4056, 41 U.S.C. 422.

Subpart 9903.2—CAS Program Requirements

■ 4. Section 9903.201–1 is amended by revising paragraph (b)(2) to read as follows:

9903.201–1 CAS applicability.

* * * * *

(b) * * *

(2) Negotiated contracts and subcontracts not in excess of $650,000. For purposes of this paragraph (b)(2) an order issued by one segment to another segment shall be treated as a subcontract.

* * * * *

■ 5. Section 9903.201–2 is amended by revising paragraphs (c)(3) and (c)(5) to read as follows:

9903.201–2 Types of CAS coverage.

(c) * * *

(3) *Applicable standards.* Coverage for educational institutions requires that the business unit comply with all of the CAS specified in part 9905 that are in effect on the date of the contract award and with any CAS that become applicable because of later award of a CAS-covered contract. This coverage applies to business units that receive negotiated contracts in excess of $650,000, except for CAS-covered contracts awarded to FFRDCs operated by an educational institution.

* * * * *

(5) *Contract clauses.* The contract clause at 9903.201–4(e) shall be incorporated in each negotiated contract and subcontract awarded to an educational institution when the negotiated contract or subcontract price exceeds $650,000. For CAS-covered contracts awarded to an FFRDC operated by an educational institution, however, the full or modified CAS contract clause specified at 9903.201–4(a) or (c), as applicable, shall be incorporated.

* * * * *

■ 6. Section 9903.201–3 is amended by revising the provision heading and by revising paragraph (a) in Part I of the provision to read as follows:

9903.201–3 Solicitation provisions.

* * * * *

Cost Accounting Standards Notices and Certification (June 2007)

* * * * *

I. *Disclosure Statement—Cost Accounting Practices and Certification*

(a) Any contract in excess of $650,000 resulting from this solicitation, except for those contracts which are exempt as specified in 9903.201–1.

* * * * *

■ 7. Section 9903.201–4 is revised to read as follows:

9903.201–4 Contract clauses.

(a) *Cost Accounting Standards.* (1) The contracting officer shall insert the clause set forth below, Cost Accounting Standards, in negotiated contracts, unless the contract is exempted (see 9903.201–1), the contract is subject to modified coverage (see 9903.201–2), or the clause prescribed in paragraph (e) of this section is used.

(2) The clause below requires the contractor to comply with all CAS specified in part 9904, to disclose actual cost accounting practices (applicable to CAS-covered contracts only), and to follow disclosed and established cost accounting practices consistently.

Cost Accounting Standards (June 2007)

(a) Unless the contract is exempt under 9903.201–1 and 9903.201–2, the provisions of 9903 are incorporated herein by reference and the Contractor in connection with this contract, shall—

(1) (CAS-covered Contracts Only) By submission of a Disclosure Statement, disclosed in writing the Contractor's cost accounting practices as required by 9903.202–1 through 9903.202–5 including methods of distinguishing direct costs from indirect costs and the basis used for allocating indirect costs. The practices disclosed for this contract shall be the same as the practices currently disclosed and applied on all other contracts and subcontracts being performed by the Contractor and which contain a Cost Accounting Standards (CAS) clause. If the Contractor has notified the Contracting Officer that the Disclosure Statement contains trade secrets, and commercial or financial information which is privileged and confidential, the Disclosure Statement shall be protected and shall not be released outside of the Government.

(2) Follow consistently the Contractor's cost accounting practices in accumulating and reporting contract performance cost data concerning this contract. If any change in cost accounting practices is made for the purposes of any contract or subcontract subject to CAS requirements, the change must be applied prospectively to this contract and the Disclosure Statement must be amended accordingly. If the contract price or cost allowance of this contract is affected by such changes, adjustment shall be made in accordance with subparagraph (a)(4) or (a)(5) of this clause, as appropriate.

(3) Comply with all CAS, including any modifications and interpretations indicated thereto contained in part 9904, in effect on the date of award of this contract or, if the Contractor has submitted cost or pricing data, on the date of final agreement on price as shown on the Contractor's signed certificate of current cost or pricing data. The Contractor shall also comply with any CAS (or modifications to CAS) which hereafter become applicable to a contract or subcontract of the Contractor. Such compliance shall be required prospectively from the date of applicability of such contract or subcontract.

(4)(i) Agree to an equitable adjustment as provided in the Changes clause of this contract if the contract cost is affected by a change which, pursuant to subparagraph (a)(3) of this clause, the Contractor is required to make to the Contractor's established cost accounting practices.

(ii) Negotiate with the Contracting Officer to determine the terms and conditions under which a change may be made to a cost accounting practice, other than a change made under other provisions of subparagraph (a)(4) of this clause; provided that no agreement may be made under this provision that will increase costs paid by the United States.

(iii) When the parties agree to a change to a cost accounting practice, other than a change under subdivision (a)(4)(i) of this clause, negotiate an equitable adjustment as provided in the Changes clause of this contract.

(5) Agree to an adjustment of the contract price or cost allowance, as appropriate, if the Contractor or a subcontractor fails to comply with an applicable Cost Accounting Standard, or to follow any cost accounting practice consistently and such failure results in any increased costs paid by the United States. Such adjustment shall provide for recovery of the increased costs to the United States, together with interest thereon computed at the annual rate established under section 6621(a)(2) of the Internal Revenue Code of 1986 (26 U.S.C. 6621(a)(2)) for such period, from the time the payment by the United States was made to the time the adjustment is effected. In no case shall the Government recover costs greater than the increased cost to the Government, in the aggregate, on the relevant contracts subject to the price adjustment, unless the Contractor made a change in its cost accounting practices of which it was aware or should have been aware at the time of price negotiations and which it failed to disclose to the Government.

(b) If the parties fail to agree whether the Contractor or a subcontractor has complied with an applicable CAS in part 9904 or a CAS rule or regulation in part 9903 and as to any cost adjustment demanded by the United States, such failure to agree will constitute a dispute under the Contract Disputes Act (41 U.S.C. 601).

(c) The Contractor shall permit any authorized representatives of the Government to examine and make copies of any documents, papers, or records relating to compliance with the requirements of this clause.

(d) The Contractor shall include in all negotiated subcontracts which the Contractor enters into, the substance of this clause, except paragraph (b), and shall require such inclusion in all other subcontracts, of any tier, including the obligation to comply with all CAS in effect on the subcontractor's award date or if the subcontractor has submitted cost or pricing data, on the date of final agreement on price as shown on the subcontractor's signed Certificate of Current Cost or Pricing Data. If the subcontract is awarded to a business unit which pursuant to 9903.201–2 is subject to other types of CAS coverage, the substance of the applicable clause set forth in 9903.201–4 shall be inserted. This requirement shall apply only to negotiated subcontracts in excess of $650,000, except that the requirement shall not apply to negotiated subcontracts otherwise exempt from the requirement to include a CAS clause as specified in 9903.201–1.

(End of Clause)

(b) [Reserved]

(c) *Disclosure and Consistency of Cost Accounting Practices.* (1) The Contracting Officer shall insert the clause set forth below, Disclosure and Consistency of Cost Accounting Practices, in negotiated contracts when the contract amount is over $650,000 but less than $50 million, and the offeror certifies it is eligible for and elects to use modified CAS coverage (see 9903.201–2, unless the clause prescribed in paragraph (d) of this subsection is used).

(2) The clause below requires the Contractor to comply with CAS 9904.401, 9904.402, 9904.405, and 9904.406, to disclose (if it meets certain requirements) actual cost accounting practices, and to follow consistently disclosed and established cost accounting practices.

Disclosure and Consistency of Cost Accounting Practices (June 2007)

(a) The Contractor, in connection with this contract, shall—

(1) Comply with the requirements of 9904.401, Consistency in Estimating, Accumulating, and Reporting Costs; 9904.402, Consistency in Allocating Costs Incurred for the Same Purpose; 9904.405, Accounting for Unallowable Costs; and 9904.406, Cost Accounting Standard—Cost Accounting Period, in effect on the date of award of this contract, as indicated in part 9904.

(2) (CAS-covered Contracts Only) If it is a business unit of a company required to submit a Disclosure Statement, disclose in writing its cost accounting practices as required by 9903.202–1 through 9903.202–5. If the Contractor has notified the Contracting Officer that the Disclosure Statement contains trade secrets and commercial or financial information which is privileged and confidential, the Disclosure Statement shall be protected and shall not be released outside of the Government.

(3)(i) Follow consistently the Contractor's cost accounting practices. A change to such practices may be proposed, however, by either the Government or the Contractor, and the Contractor agrees to negotiate with the Contracting Officer the terms and conditions under which a change may be made. After the terms and conditions under which the change is to be made have been agreed to, the change must be applied prospectively to this contract, and the Disclosure Statement, if affected, must be amended accordingly.

(ii) The Contractor shall, when the parties agree to a change to a cost accounting practice and the Contracting Officer has made the finding required in 9903.201–6(c) that the change is desirable and not detrimental to the interests of the Government, negotiate an equitable adjustment as provided in the Changes clause of this contract. In the absence of the required finding, no agreement may be made under this contract clause that will increase costs paid by the United States.

(4) Agree to an adjustment of the contract price or cost allowance, as appropriate, if the Contractor or a subcontractor fails to comply with the applicable CAS or to follow any cost accounting practice, and such failure results in any increased costs paid by the United States. Such adjustment shall provide for recovery of the increased costs to the United States, together with interest thereon computed at the annual rate established under section 6621(a)(2) of the Internal Revenue Code of 1986 (26 U.S.C. 6621(a)(2)) for such period, from the time the payment by the United States was made to the time the adjustment is effected.

(b) If the parties fail to agree whether the Contractor has complied with an applicable

CAS rule, or regulation as specified in parts 9903 and 9904 and as to any cost adjustment demanded by the United States, such failure to agree will constitute a dispute under the Contract Disputes Act (41 U.S.C. 601).

(c) The Contractor shall permit any authorized representatives of the Government to examine and make copies of any documents, papers, and records relating to compliance with the requirements of this clause.

(d) The Contractor shall include in all negotiated subcontracts, which the Contractor enters into, the substance of this clause, except paragraph (b), and shall require such inclusion in all other subcontracts of any tier, except that—

(1) If the subcontract is awarded to a business unit which pursuant to 9903.201–2 is subject to other types of CAS coverage, the substance of the applicable clause set forth in 9903.201–4 shall be inserted.

(2) This requirement shall apply only to negotiated subcontracts in excess of $650,000.

(3) The requirement shall not apply to negotiated subcontracts otherwise exempt from the requirement to include a CAS clause as specified in 9903.201–1.

(End of clause)

(d) [Reserved]

(e) *Cost Accounting Standards—Educational Institutions.* (1) The contracting officer shall insert the clause set forth below, Cost Accounting Standards—Educational Institutions, in negotiated contracts awarded to educational institutions, unless the contract is exempted (see 9903.201–1), the contract is to be performed by an FFRDC (see 9903.201–2(c)(5)), or the provision at 9903.201–2(c)(6) applies.

(2) The clause below requires the educational institution to comply with all CAS specified in part 9905, to disclose actual cost accounting practices as required by 9903.202–1(f), and to follow disclosed and established cost accounting practices consistently.

Cost Accounting Standards—Educational Institutions (June 2007)

(a) Unless the contract is exempt under 9903.201–1 and 9903.201–2, the provisions of part 9903 are incorporated herein by reference and the Contractor in connection with this contract, shall—

(1) (CAS-covered Contracts Only) If a business unit of an educational institution required to submit a Disclosure Statement, disclose in writing the Contractor's cost accounting practices as required by 9903.202–1 through 9903.202–5 including methods of distinguishing direct costs from indirect costs and the basis used for accumulating and allocating indirect costs. The practices disclosed for this contract shall be the same as the practices currently disclosed and applied on all other contracts and subcontracts being performed by the Contractor and which contain a Cost Accounting Standards (CAS) clause. If the Contractor has notified the Contracting Officer that the Disclosure Statement contains trade secrets, and commercial or financial information which is privileged and confidential, the Disclosure Statement shall be protected and shall not be released outside of the Government.

(2) Follow consistently the Contractor's cost accounting practices in accumulating and reporting contract performance cost data concerning this contract. If any change in cost accounting practices is made for the purposes of any contract or subcontract subject to CAS requirements, the change must be applied prospectively to this contract and the Disclosure Statement, if required, must be amended accordingly. If an accounting principle change mandated under Office of Management and Budget (OMB) Circular A–21, Cost Principles for Educational Institutions, requires that a change in the Contractor's cost accounting practices be made after the date of this contract award, the change must be applied prospectively to this contract and the Disclosure Statement, if required, must be amended accordingly. If the contract price or cost allowance of this contract is affected by such changes, adjustment shall be made in accordance with subparagraph (a)(4) or (a)(5) of this clause, as appropriate.

(3) Comply with all CAS, including any modifications and interpretations indicated thereto contained in 48 CFR part 9905, in effect on the date of award of this contract or, if the Contractor has submitted cost or pricing data, on the date of final agreement on price as shown on the Contractor's signed certificate of current cost or pricing data. The Contractor shall also comply with any CAS (or modifications to CAS) which hereafter become applicable to a contract or subcontract of the Contractor. Such compliance shall be required prospectively from the date of applicability to such contract or subcontract.

(4)(i) Agree to an equitable adjustment as provided in the Changes clause of this contract if the contract cost is affected by a change which, pursuant to subparagraph (a)(3) of this clause, the Contractor is required to make to the Contractor's established cost accounting practices.

(ii) Negotiate with the Contracting Officer to determine the terms and conditions under which a change may be made to a cost accounting practice, other than a change made under other provisions of subparagraph (a)(4) of this clause; provided that no agreement may be made under this provision that will increase costs paid by the United States.

(iii) When the parties agree to a change to a cost accounting practice, other than a change under subdivision (a)(4)(i) or (a)(4)(iv) of this clause, negotiate an equitable adjustment as provided in the Changes clause of this contract.

(iv) Agree to an equitable adjustment as provided in the Changes clause of this contract, if the contract cost is materially affected by an OMB Circular A–21 accounting principle amendment which, on becoming effective after the date of contract award, requires the Contractor to make a change to the Contractor's established cost accounting practices.

(5) Agree to an adjustment of the contract price or cost allowance, as appropriate, if the Contractor or a subcontractor fails to comply with an applicable Cost Accounting Standard, or to follow any cost accounting practice consistently and such failure results in any increased costs paid by the United States. Such adjustment shall provide for recovery of the increased costs to the United States, together with interest thereon computed at the annual rate established under section 6621(a)(2) of the Internal Revenue Code of 1986 (26 U.S.C. 6621(a)(2)) for such period, from the time the payment by the United States was made to the time the adjustment is effected. In no case shall the Government recover costs greater than the increased cost to the Government, in the aggregate, on the relevant contracts subject to the price adjustment, unless the Contractor made a change in its cost accounting practices of which it was aware or should have been aware at the time of price negotiations and which it failed to disclose to the Government.

(b) If the parties fail to agree whether the Contractor or a subcontractor has complied with an applicable CAS or a CAS rule or regulation in 9903 and as to any cost adjustment demanded by the United States, such failure to agree will constitute a dispute under the Contract Disputes Act (41 U.S.C. 601).

(c) The Contractor shall permit any authorized representatives of the Government to examine and make copies of any documents, papers, or records relating to compliance with the requirements of this clause.

(d) The Contractor shall include in all negotiated subcontracts which the Contractor enters into, the substance of this clause, except paragraph (b), and shall require such inclusion in all other subcontracts, of any tier, including the obligation to comply with all applicable CAS in effect on the subcontractor's award date or if the subcontractor has submitted cost or pricing data, on the date of final agreement on price as shown on the subcontractor's signed Certificate of Current Cost or Pricing Data, except that—

(1) If the subcontract is awarded to a business unit which pursuant to 9903.201–2 is subject to other types of CAS coverage, the substance of the applicable clause set forth in 9903.201–4 shall be inserted; and

(2) This requirement shall apply only to negotiated subcontracts in excess of $650,000.

(3) The requirement shall not apply to negotiated subcontracts otherwise exempt from the requirement to include a CAS clause as specified in 9903.201–1.

(End of clause)

■ 8. Section 9903.202–1 is amended by revising:

■ A. Paragraph (c);

■ B. Paragraph (f)(2)(i); and

■ C. Paragraphs (f)(3)(i), (ii), and (iii)

The revisions read as follows:

9903.202–1 General requirements.

* * * * *

(c) When a Disclosure Statement is required, a separate Disclosure

Statement must be submitted for each segment whose costs included in the total price of any CAS-covered contract or subcontract exceed $650,000, unless * * *

(f) * * *

(2) * * *

(i) Any business unit of an educational institution that is selected to receive a CAS-covered contract or subcontract in excess of $650,000 and is part of a college or university location listed in Exhibit A of Office of Management and Budget (OMB) Circular A–21 shall submit a Disclosure Statement before award.* * *

(3) * * *

(i) For business units that are selected to receive a CAS-covered contract or subcontract in excess of $650,000 and are part of the first 20 college or university locations (i.e., numbers 1 through 20) listed in Exhibit A of OMB Circular A–21, Disclosure Statements shall be submitted within six months after the date of contract award.

(ii) For business units that are selected to receive a CAS-covered contract or subcontract in excess of $650,000 and are part of a college or university location that is listed as one of the institutions numbered 21 through 50, in Exhibit A of OMB Circular A–21, Disclosure Statements shall be submitted during the six month period ending twelve months after the date of contract award.

(iii) For business units that are selected to receive a CAS-covered contract or subcontract in excess of $650,000 and are part of a college or university location that is listed as one of the institutions numbered 51 through 99, in Exhibit A of OMB Circular A–21, Disclosure Statements shall be submitted during the six month period ending eighteen months after the date of contract award.

[FR Doc. E7–11328 Filed 6–13–07; 8:45 am]

BILLING CODE 3110–01–P

DEPARTMENT OF COMMERCE

National Oceanic and Atmospheric Administration

50 CFR Part 648

RIN 0648–AT60

[Docket No. 061020273–7001–03; I.D. 010307A]

Fisheries of the Northeastern United States; Summer Flounder Fishery; Emergency Rule Extension

AGENCY: National Marine Fisheries Service (NMFS), National Oceanic and Atmospheric Administration (NOAA), Commerce.

ACTION: Temporary rule; emergency action extended.

SUMMARY: NMFS is extending the revised summer flounder total allowable landings (TAL) implemented on January 19, 2007, until December 31, 2007, the end of the 2007 fishing year. This emergency rule extension specifies allowed harvest limits for both the commercial and recreational summer flounder fisheries. The TAL contained within this emergency rule extension continues the previous harvest limits for summer flounder that became effective on January 19, 2007, which superceded the harvest limits initially implemented on January 1, 2007. This action continues the prohibition on federally permitted commercial vessels landing summer flounder in Delaware in 2007 due to continued quota repayment of previous year's overages.

This emergency rule extension is necessary to maintain the increased 2007 summer flounder harvest levels previously found to be consistent with the Magnuson-Stevens Fishery Conservation and Management Reauthorization Act of 2006 (Reauthorized Magnuson-Stevens Act) through the end of the 2007 fishing year. Extending this emergency action will ensure continued compliance with regulations implementing the Summer Flounder, Scup, and Black Sea Bass Fishery Management Plan (FMP). In addition, this action will continue to ensure that fishing mortality rates (F) or exploitation rates, as specified in the FMP, are not exceeded.

DATES: Effective from July 18, 2007 through December 31, 2007.

ADDRESSES: Copies of the Supplemental Environmental Assessment are available from Patricia A. Kurkul, Regional Administrator, Northeast Region, National Marine Fisheries Service, One Blackburn Drive, Gloucester, MA 01930–2298. This document is also accessible via the Internet at *http://www.nero.noaa.gov*.

FOR FURTHER INFORMATION CONTACT: Michael P. Ruccio, Fishery Policy Analyst, (978) 281–9104.

SUPPLEMENTARY INFORMATION: Summer flounder is currently under a rebuilding plan. NMFS published a final rule containing the 2007 summer flounder TAL on December 14, 2006 (71 FR 75134). The 12.983–million-lb (5,889–mt) TAL in that rule became effective on January 1, 2007, which was a 45–percent decrease from the TAL specified for 2006.

Following the publication of the 2007 summer flounder TAL in the **Federal Register**, the Reauthorized Magnuson-Stevens Act was signed into law on January 12, 2007. Contained within the Reauthorized Magnuson-Stevens Act is a specific provision under section 120(a) that authorizes the Secretary of Commerce (Secretary) to extend the rebuilding time frame for summer flounder to no later than January 1, 2013, provided that several specific conditions are met. The Secretary must determine that:

1. Overfishing is not occurring in the summer flounder fishery and that a mechanism is in place to ensure overfishing does not occur in the fishery and stock biomass levels are increasing;
2. The biomass rebuilding target previously applicable to the summer flounder stock will be met or exceeded within the new time for rebuilding;
3. The extension period is based on the status and biology of the stock and the rate of rebuilding;
4. Monitoring will ensure rebuilding continues;
5. The extension meets the requirements of National Standard 1 found at section 301(a)(1) of the Magnuson-Stevens Act; and
6. The best scientific information available shows that the extension will allow continued rebuilding.

On behalf of the Secretary, NMFS previously determined that these six criteria had been met and that there is a reasonable basis to extend the summer flounder rebuilding time frame to no later than January 1, 2013. Based on these determinations, NMFS implemented an emergency rule, effective January 19, 2007 (72 FR 2458), to increase the TAL to 17.112 million lb (7,762 mt). The agency's decision to enact emergency rulemaking was consistent with the policy guidelines for the use of emergency rules published in the **Federal Register** on August 21, 1997 (62 FR 44421).

A detailed discussion of the Secretarial determinations made relative to section 120(a) of the revised Magnuson-Stevens Act appears in the initial emergency rule (72 FR 2458, January 19, 2007) and is not repeated here. The emergency rule TAL is based on the revised rebuilding time frame ending no later than January 1, 2013, which supersedes the previous TAL of 12.983 million lb (5,889 mt) that was based on a rebuilding period end date of January 1, 2010. The 17.112–million-lb (7,762–mt) TAL will continue to be allocated 10.27 million lb (4,658 mt) to the commercial sector and 6.84 million lb (3,104 mt) to the recreational sector under this extension. The commercial

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of the United States. EPA will submit a report containing these final rule amendments and other required information to the U.S. Senate, the U.S. House of Representatives, and the Comptroller General of the United States prior to publication of the final rule amendments in the **Federal Register**. A major rule cannot take effect until 60 days after it is published in the **Federal Register**. This action is not a ''major rule'' as defined by 5 U.S.C. 804(2). This final rule will be effective on October 1, 2007.

List of Subjects in 40 CFR Part 63

Environmental protection, Air pollution control, Hazardous substances, Reporting and Recordkeeping requirements.

Dated: June 27, 2007.

Stephen L. Johnson,

Administrator.

■ For the reasons stated in the preamble, title 40, chapter I, part 63 of the Code of Federal Regulations is amended as follows:

PART 63—[AMENDED]

■ 1. The authority citation for part 63 continues to read as follows:

Authority: 42 U.S.C. 7401 *et seq.*

Subpart EEEEEE—[Amended]

■ 2. Section 63.11148 is amended by revising paragraph (a)(2)(ii) to read as follows:

§ 63.11148 What are the standards and compliance requirements for existing sources using batch copper converters?

(a) * * *

(2) * * *

(ii) During periods when no copper ore concentrate feed is charged to the smelting vessel but the smelting vessel remains in operation to temporarily hold molten material in the vessel before resuming copper production, you must exhaust the process off gas from the smelting vessel to an electrostatic precipitator, wet scrubber, or baghouse prior to discharge to the atmosphere.

* * * * *

■ 3. Section 63.11150 is amended as follows:

■ a. By revising paragraph (c) introductory text.

■ b. By redesignating paragraph (c)(4) as paragraph (c)(5).

■ c. By redesignating the second paragraph (c)(3) as paragraph (c)(4).

§ 63.11150 What General Provisions apply to this subpart?

* * * * *

(c) If you own or operate an existing affected source subject to § 63.11148, your notification of compliance status required by § 63.9(h) must include the information specified in paragraphs (c)(1) through (5) of this section.

* * * * *

Subpart FFFFFF—[Amended]

■ 4. Section 63.11153 is amended by revising the last sentence in paragraph (b) to read as follows:

§ 63.11153 Am I subject to this subpart?

* * * * *

(b) * * * Your secondary copper smelter is a new affected source if you commenced constructed or reconstruction of the affected source on or after October 6, 2006.

* * * * *

■ 5. Section 63.11157 is amended by revising paragraph (b)(5) to read as follows:

§ 63.11157 What General Provisions apply to this subpart?

* * * * *

(b) * * *

(5) This certification of compliance, signed by a responsible official, for the work practice standard in § 63.11155(g): ''This facility has an approved monitoring plan in accordance with § 63.11155(g).''

[FR Doc. E7–12847 Filed 7–2–07; 8:45 am]

BILLING CODE 6560–50–P

OFFICE OF MANAGEMENT AND BUDGET

Office of Federal Procurement Policy

48 CFR Part 9903

Cost Accounting Standards Board; Time and Material and Labor Hour (T&M/LH) Contracts for Commercial Items

AGENCY: Cost Accounting Standards Board, Office of Federal Procurement Policy, OMB.

ACTION: Final rule.

SUMMARY: The Office of Federal Procurement Policy, Cost Accounting Standards (CAS) Board, has adopted, without change, a final rule to provide an exemption for T&M/LH contracts for commercial items. This rulemaking is authorized pursuant to Section 26 of the Office of Federal Procurement Policy Act.

DATES: *Effective Date:* July 3, 2007.

FOR FURTHER INFORMATION CONTACT: Laura Auletta, Manager, Cost Accounting Standards Board, 725 17th Street, NW., Room 9013, Washington, DC 20503 (telephone: 202–395–3256).

SUPPLEMENTARY INFORMATION:

A. Background

On January 4, 2006, the Cost Accounting Standards Board published a proposed rule with request for comment (71 FR 313) for the purpose of providing an exemption for T&M/LH contracts for commercial items. The final rule adopts the proposed rule without change, thereby exempting T&M/LH contracts from CAS coverage.

The Board's action is consistent with its previous actions to exempt those types of contracts permitted by Congress for the acquisition of commercial items. For example, on June 6, 1997, 1996, the Board issued a final rule implementing the Federal Acquisition Reform Act (FARA) by providing an exemption from CAS for contracts for the acquisition of commercial items that are firm fixed price and fixed price with economic price adjustment (except when the adjustment is made on the basis of actual costs). At the time the CAS Board implemented this exemption, FAR limited the permissible contract types for the acquisition of commercial items to firm fixed price and fixed price with economic price adjustment. Effective February 12, 2007, FAR was amended to add T&M/LH contracts as an acceptable contract type for acquiring commercial items. This final rule is consistent with that FAR amendment.

B. Public Comments

The Board received six sets of public comments in response to the Proposed Rule.

1. Support Issuance of the Proposed Rule

Comment: Three commenters supported the issuance of the final rule.

Response: The Board thanks the commenters for their comments.

2. The Proposed Exemption Is Not Required by SARA

Comment: One commenter opined that the proposed exemption is not required by SARA and that the CAS Board made an ''erroneous leap of logic to state that a CAS exemption exists when the statute provides that CAS is not mandatory.''

Response: The Board believes an exemption is appropriate at this time in light of the recently promulgated final FAR rule that implements Section 1432 of the National Defense Authorization Act for Fiscal Year 2004 (SARA) (Pub. L. 108–136), which expressly authorized the use of time-and-materials (T&M) and labor-hour (LH) contracts for the acquisition of certain categories of commercial services. Based on the provisions in the final FAR rule, the Board believes there is no significant benefit to the application of CAS to T&M/LH contracts for commercial items. The Board's specific rationale is discussed below.

Under the FAR provisions, a T&M contract is composed of a ''time'' element and a ''materials'' element, while a LH contract is only composed of a ''time'' element. The time element in a T&M/LH contract is a fixed hourly rate by labor category. Under the FAR provisions for T&M/LH contracts for commercial items, these fixed hourly rates are determined based on adequate price competition without the submission of cost or pricing data. These fixed rates apply to both prime and subcontractor labor (except subcontracts for incidental services). These fixed hourly rates are akin to a firm fixed price contract awarded on the basis of adequate competition without submission of cost or pricing data. Such contracts are currently exempt from CAS requirements because there is no discernible benefit from applying CAS. The Board believes the same logic applies to these fixed hourly rates, and thus there is no benefit to applying CAS to the ''time'' element of a T&M/LH contract for commercial items.

In regards to the materials element, the FAR provisions for T&M contracts for commercial items define materials as including indirect costs, direct materials, and other direct costs. Under these FAR provisions, indirect costs are reimbursed at a fixed amount established at the time of contract award, *i.e.*, there is no adjustment for indirect costs based on actual costs occurred. Thus, consistent with the prior discussion regarding the fixed hourly rate, there is no benefit to applying CAS to these fixed amounts.

Conversely, the FAR provisions provide for reimbursement of direct materials and other direct costs based on actual costs. However, the FAR also includes some limitations on such reimbursement. For example, the FAR provides for reimbursement of the actual cost of these materials (less any rebates, refunds, or discounts received by the contractor that are identifiable to the contract) provided the contractor has made payments for the materials in accordance with the terms and conditions of the agreement or invoice, or makes these payments within 30 days of the submission of the Contractor's payment request to the Government. The FAR also requires the contractor to obtain the materials at the most advantageous prices available (with due regard to securing prompt delivery of satisfactory materials) and to give credit to the Government for cash and trade discounts, rebates, scrap, commissions, and other amounts that are identifiable to the contract. Furthermore, the FAR provision limits reimbursement of other direct costs to those cost elements specifically listed in the contract.

Based on the above discussion, the Board believes the existing FAR provisions provide adequate coverage regarding the reimbursement of direct materials and other direct costs. As noted earlier, the remainder of the contract price/cost is based on fixed hourly rates and/or amounts established at the time of award based on adequate competition without the submission of cost or pricing data. Thus, the Board has concluded that it is appropriate to exempt T&M/LH contracts for commercial items from CAS coverage. The Board notes that this position is consistent with the Board's May 1992 Statement of Objectives, Policies and Concepts (''the cost of an accounting application should not exceed its benefit'').

3. T&M/LH Contracts Should Be Considered Cost-Reimbursement Type Contracts

Comment: One commenter asserted that T&M/LH contracts should be considered cost-reimbursement type contracts because the premise that labor rates are fixed under a T&M/LH contract is faulty, and T&M/LH contracts ''can never be subject to adequate price competition'' because there is no price established at the time the contract is awarded. The commenter also opined that the proposed CAS exemption removes the protection against a contractor's double-counting of costs, the inclusion of unallowable costs and the inconsistent application of the accounting period under fixed T&M/LH contacts.

Response: As noted in those comments, there are some elements of a T&M contract for commercial items that are fixed (*e.g.*, fixed hourly rates and fixed indirect costs) and others that are based on actual cost (*e.g.* direct materials and other direct costs). As such, it is necessary to analyze each aspect of the T&M/LH contract to determine if an exemption is appropriate, rather than trying to classify T&M contracts as ''cost reimbursement'' or ''fixed price.'' The Board's rationale in response to Comment 2 provides this necessary analysis.

4. CAS Applicability to Large Dollar Sole Source T&M/LH Contracts

Comment: One commenter opined that the proposed rule should not exempt ''very large dollar value T&M/LH task and delivery orders to be awarded on what is effectively a sole source basis without the protections afforded by CAS.''

Response: The commenter asserts that this exemption may be used to exempt from CAS indefinite delivery/indefinite quantity contracts under which very large dollar value T&M/LH task or delivery orders are awarded on ''effectively a sole source basis.'' The statute and the FAR provisions both require that awards be made on the basis of adequate competition without the submission of cost or pricing data. As such, the Board does not believe the contract could be awarded on a sole source basis and still comply with the statutory and regulatory requirements.

5. T&M/LH Contract Exceeding CAS Applicability Thresholds Should Be Subject to Some Existing Standards

Comment: One commenter suggests that the Board analyze which of its standards should be made applicable to T&M/LH contracts for the acquisition of commercial items or services, and take the necessary steps to ensure that these contracts comply with the selected standards. The commenter suggests that such contracts should be subject, at a minimum, to the provisions of CAS 401, 402, 405, 406, 407 and 411.

Response: The Board disagrees with the commenter since the application of CAS to T&M/LH contracts for commercial items and services would serve no purpose, regardless of the dollar value of a particular contract. As discussed in the response to Comment 2 above, the ''time'' element of T&M/LH contracts is fixed price, not cost reimbursable, and the contracts are awarded based on adequate price competition. In addition, the FAR provides limitations on the reimbursement of direct materials and other direct costs that the Board believes adequately protect the Government's interest. The application of CAS to these T&M/LH contracts would be of no benefit to the Government since it would not affect the contract price (but, see last sentence of response to comment 6).

6. The Board Is Required To Issue Guidance

Comment: One commenter asserted that the Board failed to implement the requirements of the Conference Report on Section 4205 of FARA because it did not issue guidance for the allocation of costs to commercial item contracts when other than firm fixed-price and fixed price economic price adjustment contracts are authorized.

Response: The CAS Board recognizes the discussion in the Conference Report. However, the Board does not believe that guidance is needed at this time in light of the restrictions on the use of T&M and labor-hour contracts in the FAR. First, the Board believes that it was envisioned that reimbursable actual direct material and other direct costs will be incidental to the overall contract price. Second, the restrictions in the FAR provide the appropriate protections at this time. However, should the FAR requirements be revised or should direct material/other direct costs become more than incidental, the CAS Board will re-examine this issue.

7. CAS Applicability to Hybrid Contracts

Comment: One commenter opined that ''CAS should not be applicable to portions of a contract whose price is not based on certified cost or pricing data or whose payment is not based on actual costs incurred'' and urged the Board to place hybrid contracts on their near-term agenda. The commenter also recommended granting contracting officers the authority to determine CAS applicability to selected portions of a contract.

Response: Since the Board has determined that it is appropriate to exempt all T&M/LH contracts for commercial items from CAS coverage, the issue of whether a portion of the contract should be exempt is moot. The Board will consider commenter's recommendation when it formulates its future agenda actions.

8. Other Contract Types for Commercial Items

Comment: Three commenters, while supporting the proposed revision, noted the difference between the permissible contract types specified at FAR 12.207 and the proposed CAS exemption. The commenters recommended that the Board adopt their interpretation of the exemption language contained at Section 4204 of the Clinger-Cohen Act (Pub. L. 104–106)—''contracts or subcontracts for the acquisition of commercial items.''

Response: The Board did not deliberate this recommendation because it was outside the scope of the proposed rule to provide an exemption for T&M/LH contracts. The Board will consider this recommendation when it formulates future agenda items.

C. Paperwork Reduction Act

The Paperwork Reduction Act, Public Law 96–511, does not apply to this rulemaking, because this rule imposes no paperwork burden on offerors, affected contractors and subcontractors, or members of the public which requires the approval of OMB under 44 U.S.C. 3501, *et seq.*

D. Executive Order 12866 and the Regulatory Flexibility Act

The Board certifies that this rule will not have a significant effect on a substantial number of small entities within the meaning of the Regulatory Flexibility Act, 5 U.S.C. 601, *et seq.*, because small businesses are exempt from the application of the Cost Accounting Standards.

List of Subjects in 48 CFR Part 9903

Accounting, Government procurement.

Paul A. Denett,

Administrator, Office of Federal Procurement Policy.

■ For the reasons set forth in this preamble, chapter 99 of title 48 of the Code of Federal Regulations is amended as set forth below:

PART 9903—CONTRACT COVERAGE

■ 1. The authority citation for part 9903 continues to read as follows:

Authority: Pub. L. 100–679, 102 Stat. 4056, 41 U.S.C. 422.

Subpart 9903.2—CAS Program Requirements

■ 2. Section 9903.201–1(b)(6) is revised to read as follows:

9903.201–1 CAS Applicability.

* * * * *

(b) * * *

(6) Firm fixed-priced, fixed-priced with economic price adjustment (provided that price adjustment is not based on actual costs incurred), time-and-materials, and labor-hour contracts and subcontracts for the acquisition of commercial items.

* * * * *

[FR Doc. E7–12888 Filed 7–2–07; 8:45 am]

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final OMB approval, on any information collection requirements set forth in rulemaking.

This rule will not impose any information collection burden or affect information currently collected by OIG.

IV. Inspection of Public Comments

All comments received before the end of the comment period are available for viewing by the public. All comments will be posted on *http://www.regulations.gov* as soon as possible after they have been received. Comments received timely will also be available for public inspection as they are received at Office of Inspector General, Department of Health and Human Services, Cohen Building, 330 Independence Avenue, SW., Washington, DC 20201, Monday through Friday of each week from 8:30 a.m. to 4 p.m. To schedule an appointment to view public comments, phone (202) 619–0089.

List of Subjects in 42 CFR Part 1008

Administrative practice and procedure, Fraud, Grant programs—health, Health facilities, Health professions, Medicaid, Medicare, Penalties.

■ Accordingly, 42 CFR chapter V, subchapter B is mended as set forth below:

PART 1008—[AMENDED]

■ 1. The authority citation for part 1008 continues to read as follows:

Authority: 42 U.S.C. 1320a–7d(b)

■ 2. Section 1008.31 is amended by revising paragraph (b) to read as follows:

§ 1008.31 OIG fees for the cost of advisory opinions.

* * * * *

(b) *Payment Method.* Payment for a request for an advisory opinion must be made to the Treasury of the United States, as directed by OIG.

* * * * *

■ 3. Section 1008.36 is amended by removing paragraph (b)(6) and redesignating paragraphs (b)(7) and (b)(8) as (b)(6) and (b)(7) respectively.

* * * * *

■ 4. Section 1008.43 is amended by revising paragraph (d) to read as follows:

§ 1008.43 Issuance of a formal advisory opinion.

* * * * *

(d) After OIG has notified the requestor of the full amount owed and OIG has determined that the full payment of that amount has been properly paid by the requestor, OIG will issue the advisory opinion and promptly mail it to the requestor by regular first class U.S. mail.

Dated: January 30, 2008.

Daniel R. Levinson,

Inspector General.

Approved: February 28, 2008.

Michael O. Leavitt, Secretary.

[FR Doc. E8–6164 Filed 3–25–08; 8:45 am]

BILLING CODE 4152–01–P

OFFICE OF MANAGEMENT AND BUDGET

Office of Federal Procurement Policy

48 CFR Part 9903

Cost Accounting Standards Board; Contract Clauses

AGENCY: Cost Accounting Standards Board, Office of Federal Procurement Policy, OMB.

ACTION: Final rule.

SUMMARY: The Cost Accounting Standards (CAS) Board has adopted, without change, a final rule to add a clause for inclusion in CAS-covered contracts and subcontracts awarded to foreign concerns. The Board is taking this action to provide a standard clause for use by Government and contractor personnel in applying the CAS requirements to contracts and subcontracts awarded to foreign concerns.

DATES: *Effective Date:* April 25, 2008.

FOR FURTHER INFORMATION CONTACT: Laura Auletta, Manager, Cost Accounting Standards Board, 725 17th Street, NW., Room 9013, Washington, DC 20503 (telephone: 202–395–3256). Reference CAS–2007–01F.

SUPPLEMENTARY INFORMATION:

A. Background

The CAS Board published a proposed rule on June 14, 2007 (72 FR 32829) to provide a clause for use in contracts with foreign concerns. Prior to November 4, 1993, modified CAS coverage required a contractor to comply with only CAS 401 and CAS 402. Similarly, 9903.201–1(b)(4) required that foreign concerns comply with only CAS 401 and 402. Thus, prior to November 4, 1993, the contract clause at 9903.201–4(c) was used for both contracts with modified coverage and contracts with foreign concerns.

However, on November 4, 1993, the Board revised the definition of modified coverage to include CAS 405 and 406, so that modified coverage currently includes CAS 401, 402, 405, and 406 (see 9903.201–2(b)). In conjunction with the revised definition of modified coverage, the Board also amended the clause at 9903.201–4(c) to include CAS 405 and 406. However, the Board did not change the requirement that foreign concerns comply with only CAS 401 and 402. As a result, the contract clause at 9903.201–4(c) could not be used for foreign concerns without modification by the parties.

This final rule provides a clause for use in contracts with foreign concerns that will not require modification. Except that it includes only CAS 401 and 402, this clause is identical to the clause currently applicable to contracts subject to modified coverage. To effect this change, this final rule amends 9903.201–4, Contract Clauses, to include the new clause at (f), Disclosure and Consistency of Cost Accounting Practices—Foreign Concerns.

The Board received no public comments in response to the proposed rule and has adopted the proposed rule as a final rule without change.

B. Paperwork Reduction Act

The Paperwork Reduction Act, Public Law 96–511, does not apply to this rulemaking, because this rule imposes no paperwork burden on offerors, affected contractors and subcontractors, or members of the public which requires the approval of OMB under 44 U.S.C. 3501, *et seq.*

C. Regulatory Flexibility Act, Unfunded Mandates Reform Act, Congressional Review Act, and Executive Orders 12866 and 13132

The Board certifies that this rule will not have a significant effect on a substantial number of small entities within the meaning of the Regulatory Flexibility Act, 5 U.S.C. 601, *et seq.*, because small businesses are exempt from the application of the Cost Accounting Standards. For purposes of the Unfunded Mandates Reform Act of 1995, as well as Executive Orders 12866 and 13132, the final rule will not significantly or uniquely affect small governments, does not have federalism implications, and will not result in increased expenditures by State, local, and tribal governments, or by the private sector, of $100 million or more. In addition, the Board has determined that this rule is not economically significant under the provisions of Executive Order 12866 or otherwise subject to Executive Order 12866 review. Finally, the final rule is not a ‘‘major rule’’ under 5 U.S.C. Chapter 8; the rule will not have any of the effects set forth in 5 U.S.C. 804(2).

List of Subjects in 48 CFR Part 9903

Government procurement, Cost Accounting Standards.

Paul A. Denett,

Administrator, Office of Federal Procurement Policy.

■ For the reasons set forth in this preamble, Chapter 99 of Title 48 of the Code of Federal Regulations is amended as set forth below:

PART 9903—CONTRACT COVERAGE

■ 1. The authority citation for part 9903 continues to read as follows:

Authority: Pub. L. 100–679, 102 Stat. 4056, 41 U.S.C. 422.

Subpart 9903.2—CAS Program Requirements

■ 2. Section 9903.201–4 is revised to read as follows:

9903.201–4 Contract clauses.

(a) *Cost Accounting Standards.* (1) The contracting officer shall insert the clause set forth below, Cost Accounting Standards, in negotiated contracts, unless the contract is exempted (see 9903.201–1), the contract is subject to modified coverage (see 9903.201–2), or the clause prescribed in paragraph (e) of this section is used.

(2) The clause below requires the contractor to comply with all CAS specified in part 9904, to disclose actual cost accounting practices (applicable to CAS-covered contracts only), and to follow disclosed and established cost accounting practices consistently.

COST ACCOUNTING STANDARDS (JUNE 2007)

(a) Unless the contract is exempt under 9903.201–1 and 9903.201–2, the provisions of 9903 are incorporated herein by reference and the Contractor in connection with this contract, shall—

(1) (CAS-covered Contracts Only) By submission of a Disclosure Statement, disclosed in writing the Contractor's cost accounting practices as required by 9903.202–1 through 9903.202–5 including methods of distinguishing direct costs from indirect costs and the basis used for allocating indirect costs. The practices disclosed for this contract shall be the same as the practices currently disclosed and applied on all other contracts and subcontracts being performed by the Contractor and which contain a Cost Accounting Standards (CAS) clause. If the Contractor has notified the Contracting Officer that the Disclosure Statement contains trade secrets, and commercial or financial information which is privileged and confidential, the Disclosure Statement shall be protected and shall not be released outside of the Government.

(2) Follow consistently the Contractor's cost accounting practices in accumulating and reporting contract performance cost data concerning this contract. If any change in cost accounting practices is made for the purposes of any contract or subcontract subject to CAS requirements, the change must be applied prospectively to this contract and the Disclosure Statement must be amended accordingly. If the contract price or cost allowance of this contract is affected by such changes, adjustment shall be made in accordance with subparagraph (a)(4) or (a)(5) of this clause, as appropriate.

(3) Comply with all CAS, including any modifications and interpretations indicated thereto contained in part 9904, in effect on the date of award of this contract or, if the Contractor has submitted cost or pricing data, on the date of final agreement on price as shown on the Contractor's signed certificate of current cost or pricing data. The Contractor shall also comply with any CAS (or modifications to CAS) which hereafter become applicable to a contract or subcontract of the Contractor. Such compliance shall be required prospectively from the date of applicability of such contract or subcontract.

(4)(i) Agree to an equitable adjustment as provided in the Changes clause of this contract if the contract cost is affected by a change which, pursuant to subparagraph (a)(3) of this clause, the Contractor is required to make to the Contractor's established cost accounting practices.

(ii) Negotiate with the Contracting Officer to determine the terms and conditions under which a change may be made to a cost accounting practice, other than a change made under other provisions of subparagraph (a)(4) of this clause; provided that no agreement may be made under this provision that will increase costs paid by the United States.

(iii) When the parties agree to a change to a cost accounting practice, other than a change under subdivision (a)(4)(i) of this clause, negotiate an equitable adjustment as provided in the Changes clause of this contract.

(5) Agree to an adjustment of the contract price or cost allowance, as appropriate, if the Contractor or a subcontractor fails to comply with an applicable Cost Accounting Standard, or to follow any cost accounting practice consistently and such failure results in any increased costs paid by the United States. Such adjustment shall provide for recovery of the increased costs to the United States, together with interest thereon computed at the annual rate established under section 6621(a)(2) of the Internal Revenue Code of 1986 (26 U.S.C. 6621(a)(2)) for such period, from the time the payment by the United States was made to the time the adjustment is effected. In no case shall the Government recover costs greater than the increased cost to the Government, in the aggregate, on the relevant contracts subject to the price adjustment, unless the Contractor made a change in its cost accounting practices of which it was aware or should have been aware at the time of price negotiations and which it failed to disclose to the Government.

(b) If the parties fail to agree whether the Contractor or a subcontractor has complied with an applicable CAS in part 9904 or a CAS rule or regulation in part 9903 and as to any cost adjustment demanded by the United States, such failure to agree will constitute a dispute under the Contract Disputes Act (41 U.S.C. 601).

(c) The Contractor shall permit any authorized representatives of the Government to examine and make copies of any documents, papers, or records relating to compliance with the requirements of this clause.

(d) The contractor shall include in all negotiated subcontracts which the Contractor enters into, the substance of this clause, except paragraph (b), and shall require such inclusion in all other subcontracts, of any tier, including the obligation to comply with all CAS in effect on the subcontractor's award date or if the subcontractor has submitted cost or pricing data, on the date of final agreement on price as shown on the subcontractor's signed Certificate of Current Cost or Pricing Data. If the subcontract is awarded to a business unit which pursuant to 9903.201–2 is subject to other types of CAS coverage, the substance of the applicable clause set forth in 9903.201–4 shall be inserted. This requirement shall apply only to negotiated subcontracts in excess of $650,000, except that the requirement shall not apply to negotiated subcontracts otherwise exempt from the requirement to include a CAS clause as specified in 9903.201–1.

(End of Clause)

(b) [Reserved]

(c) *Disclosure and Consistency of Cost Accounting Practices.* (1) The contracting officer shall insert the clause set forth below, Disclosure and Consistency of Cost Accounting Practices, in negotiated contracts when the contract amount is over $650,000 but less than $50 million, and the offeror certifies it is eligible for and elects to use modified CAS coverage (*see* 9903.201–2, unless the clause prescribed in paragraph (d) of this subsection is used).

(2) The clause below requires the contractor to comply with CAS 9904.401, 9904.402, 9904.405, and 9904.406, to disclose (if it meets certain requirements) actual cost accounting practices, and to follow consistently disclosed and established cost accounting practices.

DISCLOSURE AND CONSISTENCY OF COST ACCOUNTING PRACTICES (JUNE 2007)

(a) The Contractor, in connection with this contract, shall—

(1) Comply with the requirements of 9904.401, Consistency in Estimating, Accumulating, and Reporting Costs; 9904.402, Consistency in Allocating Costs Incurred for the Same Purpose; 9904.405, Accounting for Unallowable Costs; and 9904.406, Cost Accounting Standard—Cost Accounting Period, in effect on the date of

award of this contract, as indicated in part 9904.

(2) (CAS-covered Contracts Only) If it is a business unit of a company required to submit a Disclosure Statement, disclose in writing its cost accounting practices as required by 9903.202–1 through 9903.202–5. If the Contractor has notified the Contracting Officer that the Disclosure Statement contains trade secrets and commercial or financial information which is privileged and confidential, the Disclosure Statement shall be protected and shall not be released outside of the Government.

(3)(i) Follow consistently the Contractor's cost accounting practices. A change to such practices may be proposed, however, by either the Government or the Contractor, and the Contractor agrees to negotiate with the Contracting Officer the terms and conditions under which a change may be made. After the terms and conditions under which the change is to be made have been agreed to, the change must be applied prospectively to this contract, and the Disclosure Statement, if affected, must be amended accordingly.

(ii) The Contractor shall, when the parties agree to a change to a cost accounting practice and the Contracting Officer has made the finding required in 9903.201–6(c) that the change is desirable and not detrimental to the interests of the Government, negotiate an equitable adjustment as provided in the Changes clause of this contract. In the absence of the required finding, no agreement may be made under this contract clause that will increase costs paid by the United States.

(4) Agree to an adjustment of the contract price or cost allowance, as appropriate, if the Contractor or a subcontractor fails to comply with the applicable CAS or to follow any cost accounting practice, and such failure results in any increased costs paid by the United States. Such adjustment shall provide for recovery of the increased costs to the United States, together with interest thereon computed at the annual rate established under section 6621(a)(2) of the Internal Revenue Code of 1986 (26 U.S.C. 6621(a)(2)) for such period, from the time the payment by the United States was made to the time the adjustment is effected.

(b) If the parties fail to agree whether the Contractor has complied with an applicable CAS rule, or regulation as specified in parts 9903 and 9904 and as to any cost adjustment demanded by the United States, such failure to agree will constitute a dispute under the Contract Disputes Act (41 U.S.C. 601).

(c) The Contractor shall permit any authorized representatives of the Government to examine and make copies of any documents, papers, and records relating to compliance with the requirements of this clause.

(d) The Contractor shall include in all negotiated subcontracts, which the Contractor enters into, the substance of this clause, except paragraph (b), and shall require such inclusion in all other subcontracts of any tier, except that—

(1) If the subcontract is awarded to a business unit which pursuant to 9903.201–2 is subject to other types of CAS coverage, the substance of the applicable clause set forth in 9903.201–4 shall be inserted.

(2) This requirement shall apply only to negotiated subcontracts in excess of $650,000.

(3) The requirement shall not apply to negotiated subcontracts otherwise exempt from the requirement to include a CAS clause as specified in 9903.201–1.

(End of clause)

(d) [Reserved]

(e) *Cost Accounting Standards—Educational Institutions.* (1) The contracting officer shall insert the clause set forth below, Cost Accounting Standards—Educational Institution, in negotiated contracts awarded to educational institutions, unless the contract is exempted (see 9903.201–1), the contract is to be performed by an FFRDC (see 9903.201–2(c)(5)), or the provision at 9903.201–2(c)(6) applies.

(2) The clause below requires the educational institution to comply with all CAS specified in part 9905, to disclose actual cost accounting practices as required by 9903.202–1(f), and to follow disclosed and established cost accounting practices consistently.

COST ACCOUNTING STANDARDS—EDUCATIONAL INSTITUTIONS (JUNE 2007)

(a) Unless the contract is exempt under 9903.201–1 and 9903.201–2, the provisions of part 9903 are incorporated herein by reference and the Contractor in connection with this contract, shall—

(1) (CAS-covered Contracts Only) If a business unit of an educational institution required to submit a Disclosure Statement, disclose in writing the Contractor's cost accounting practices as required by 9903.202–1 through 9903.202–5 including methods of distinguishing direct costs from indirect costs and the basis used for accumulating and allocating indirect costs. The practices disclosed for this contract shall be the same as the practices currently disclosed and applied on all other contracts and subcontracts being performed by the Contractor and which contain a Cost Accounting Standards (CAS) clause. If the Contractor has notified the Contracting Officer that the Disclosure Statement contains trade secrets, and commercial or financial information which is privileged and confidential, the Disclosure Statement shall be protected and shall not be released outside of the Government.

(2) Follow consistently the Contractor's cost accounting practices in accumulating and reporting contract performance cost data concerning this contract. If any change in cost accounting practices is made for the purposes of any contract or subcontract subject to CAS requirements, the change must be applied prospectively to this contract and the Disclosure Statement, if required, must be amended accordingly. If an accounting principle change mandated under Office of Management and Budget (OMB) Circular A–21, Cost Principles for Educational Institutions, requires that a change in the Contractor's cost accounting practices be made after the date of this contract award, the change must be applied prospectively to this contract and the Disclosure Statement, if required, must be amended accordingly. If the contract price or cost allowance of this contract is affected by such changes, adjustment shall be made in accordance with subparagraph (a)(4) or (a)(5) of this clause, as appropriate.

(3) Comply with all CAS, including any modifications and interpretations indicated thereto contained in 48 CFR part 9905, in effect on the date of award of this contract or, if the Contractor has submitted cost or pricing data, on the date of final agreement on price as shown on the Contractor's signed certificate of current cost or pricing data. The Contractor shall also comply with any CAS (or modifications to CAS) which hereafter become applicable to a contract or subcontract of the Contractor. Such compliance shall be required prospectively from the date of applicability to such contract or subcontract.

(4)(i) Agree to an equitable adjustment as provided in the Changes clause of this contract if the contract cost is affected by a change which, pursuant to subparagraph (a)(3) of this clause, the Contractor is required to make to the Contractor's established cost accounting practices.

(ii) Negotiate with the Contracting Officer to determine the terms and conditions under which a change may be made to a cost accounting practice, other than a change made under other provisions of subparagraph (a)(4) of this clause; provided that no agreement may be made under this provision that will increase costs paid by the United States.

(iii) When the parties agree to a change to a cost accounting practice, other than a change under subdivision (a)(4)(i) or (a)(4)(iv) of this clause, negotiate an equitable adjustment as provided in the Changes clause of this contract.

(iv) Agree to an equitable adjustment as provided in the Changes clause of this contract, if the contract cost is materially affected by an OMB Circular A–21 accounting principle amendment which, on becoming effective after the date of contract award, requires the Contractor to make a change to the Contractor's established cost accounting practices.

(5) Agree to an adjustment of the contract price or cost allowance, as appropriate, if the Contractor or a subcontractor fails to comply with an applicable Cost Accounting Standard, or to follow any cost accounting practice consistently and such failure results in any increased costs paid by the United States. Such adjustment shall provide for recovery of the increased costs to the United States, together with interest thereon computed at the annual rate established under section 6621(a)(2) of the Internal Revenue Code of 1986 (26 U.S.C. 6621(a)(2)) for such period, from the time the payment by the United States was made to the time the adjustment is effected. In no case shall the Government recover costs greater than the increased cost to the Government, in the aggregate, on the relevant contracts subject to the price adjustment, unless the Contractor made a change in its cost accounting

practices of which it was aware or should have been aware at the time of price negotiations and which it failed to disclose to the Government.

(b) If the parties fail to agree whether the Contractor or a subcontractor has complied with an applicable CAS or a CAS rule or regulation in 9903 and as to any cost adjustment demanded by the United States, such failure to agree will constitute a dispute under the Contract Disputes Act (41 U.S.C. 601).

(c) The Contractor shall permit any authorized representatives of the Government to examine and make copies of any documents, papers, or records relating to compliance with the requirements of this clause.

(d) The Contractor shall include in all negotiated subcontracts which the Contractor enters into, the substance of this clause, except paragraph (b), and shall require such inclusion in all other subcontracts, of any tier, including the obligation to comply with all applicable CAS in effect on the subcontractor's award date or if the subcontractor has submitted cost or pricing data, on the date of final agreement on price as shown on the subcontractor's signed Certificate of Current Cost or Pricing Data, except that—

(1) If the subcontract is awarded to a business unit which pursuant to 9903.201–2 is subject to other types of CAS coverage, the substance of the applicable clause set forth in 9903.201–4 shall be inserted; and

(2) This requirement shall apply only to negotiated subcontracts in excess of $650,000.

(3) The requirement shall not apply to negotiated subcontracts otherwise exempt from the requirement to include a CAS clause as specified in 9903.201–1.

(End of clause)

(f) *Disclosure and Consistency of Cost Accounting Practices—Foreign Concerns.*

(1) The contracting officer shall insert the clause set forth below, Disclosure and Consistency of Cost Accounting Practices—Foreign Concerns, in negotiated contracts when the contract is with a foreign concern and the contract is not otherwise exempt under 9903.201–1 (see 9903.201–2(e)).

(2) The clause below requires the contractor to comply with 9904.401 and 9904.402, to disclose (if it meets certain requirements) actual cost accounting practices, and to follow consistently disclosed and established cost accounting practices.

DISCLOSURE AND CONSISTENCY OF COST ACCOUNTING PRACTICES—FOREIGN CONCERNS (April 25, 2008)

(a) The Contractor, in connection with this contract, shall—

(1) Comply with the requirements of 9904.401, Consistency in Estimating, Accumulating, and Reporting Costs; and 9904.402, Consistency in Allocating Costs Incurred for the Same Purpose, in effect on the date of award of this contract, as indicated in Part 9904.

(2) (CAS-covered Contracts Only) If it is a business unit of a company required to submit a Disclosure Statement, disclose in writing its cost accounting practices as required by 9903.202–1 through 9903.202–5. If the Contractor has notified the Contracting Officer that the Disclosure Statement contains trade secrets and commercial or financial information which is privileged and confidential, the Disclosure Statement shall be protected and shall not be released outside of the Government.

(3)(i) Follow consistently the Contractor's cost accounting practices. A change to such practices may be proposed, however, by either the Government or the Contractor, and the Contractor agrees to negotiate with the Contracting Officer the terms and conditions under which a change may be made. After the terms and conditions under which the change is to be made have been agreed to, the change must be applied prospectively to this contract, and the Disclosure Statement, if affected, must be amended accordingly.

(ii) The Contractor shall, when the parties agree to a change to a cost accounting practice and the Contracting Officer has made the finding required in 9903.201–6(c) that the change is desirable and not detrimental to the interests of the Government, negotiate an equitable adjustment as provided in the Changes clause of this contract. In the absence of the required finding, no agreement may be made under this contract clause that will increase costs paid by the United States.

(4) Agree to an adjustment of the contract price or cost allowance, as appropriate, if the Contractor or a subcontractor fails to comply with the applicable CAS or to follow any cost accounting practice, and such failure results in any increased costs paid by the United States. Such adjustment shall provide for recovery of the increased costs to the United States, together with interest thereon computed at the annual rate established under section 6621(a)(2) of the Internal Revenue Code of 1986 (26 U.S.C. 6621(a)(2)) for such period, from the time the payment by the United States was made to the time the adjustment is effected.

(b) If the parties fail to agree whether the Contractor has complied with an applicable CAS rule, or regulation as specified in Parts 9903 and 9904 and as to any cost adjustment demanded by the United States, such failure to agree will constitute a dispute under the Contract Disputes Act (41 U.S.C. 601).

(c) The Contractor shall permit any authorized representatives of the Government to examine and make copies of any documents, papers, and records relating to compliance with the requirements of this clause.

(d) The Contractor shall include in all negotiated subcontracts, which the Contractor enters into, the substance of this clause, except paragraph (b), and shall require such inclusion in all other subcontracts of any tier, except that—

(1) If the subcontract is awarded to a business unit which pursuant to 9903.201–2 is subject to other types of CAS coverage, the substance of the applicable clause set forth in 9903.201–4 shall be inserted.

(2) This requirement shall apply only to negotiated subcontracts in excess of $650,000.

(3) The requirement shall not apply to negotiated subcontracts otherwise exempt from the requirement to include a CAS clause as specified in 9903.201–1.

(End of Clause)

[FR Doc. E8–5981 Filed 3–24–08; 8:45 am]

BILLING CODE 3110–01–P

DEPARTMENT OF COMMERCE

National Oceanic and Atmospheric Administration

50 CFR Part 679

[Docket No. 071106671–8010–02]

RIN 0648–XG62

Fisheries of the Exclusive Economic Zone Off Alaska; Shallow-Water Species Fishery by Vessels Using Trawl Gear in the Gulf of Alaska

AGENCY: National Marine Fisheries Service (NMFS), National Oceanic and Atmospheric Administration (NOAA), Commerce.

ACTION: Temporary rule; modification of a closure.

SUMMARY: NMFS is opening directed fishing for shallow-water species by vessels using trawl gear in the Gulf of Alaska (GOA). This action is necessary to allow the shallow-water species fishery in the GOA to resume.

DATES: Effective 1200 hrs, Alaska local time (A.l.t.), March 21, 2008, through 1200 hrs, A.l.t., April 1, 2008. Comments must be received at the following address no later than 4:30 p.m., A.l.t., April 7, 2008.

ADDRESSES: Send comments to Sue Salveson, Assistant Regional Administrator, Sustainable Fisheries Division, Alaska Region, NMFS, Attn: Ellen Sebastian. You may submit comments, identified by 0648–XG62, by any one of the following methods:

- Electronic Submissions: Submit all electronic public comments via the Federal eRulemaking Portal website at *http://www.regulations.gov*;
- Mail: P.O. Box 21668, Juneau, AK 99802;
- Fax: (907) 586–7557; or
- Hand delivery to the Federal Building: 709 West 9th Street, Room 420A, Juneau, AK.

Instructions: All comments received are a part of the public record and will generally be posted to *http://www.regulations.gov* without change.

Indian Tribal Governments'' (65 FR 67249, November 6, 2000), requires EPA to develop an accountable process to ensure meaningful and timely input by Tribal officials in the development of regulatory policies that have Tribal implications. This rule does not have tribal implications, as specified in Executive Order 13175. Thus Executive Order 13175 does not apply to this rule.

G. Executive Order 13045: Protection of Children From Environmental Health and Safety Risks

EPA interprets Executive Order 13045 (62 FR 19885, April 23, 1997) as applying only to regulatory actions that concern health or safety risks, such that the analysis required under section 5–501 of the Executive Order had the potential to influence the regulation. This action is not subject to Executive Order 13045 because it does not establish an environmental standard intended to mitigate health or safety risks. This rule simply extends the deadline for EPA to take action on a petition and does not impose any regulatory requirements.

H. Executive Order 13211: Actions That Significantly Affect Energy Supply, Distribution, or Use

This rule is not subject to Executive Order 13211, ''Actions That Significantly Affect Energy Supply, Distribution, or Use'' (66 FR 28355; May 22, 2001) because it is not a significant regulatory action under Executive Order 12866. This action does not establish any new regulatory requirements.

I. National Technology Transfer and Advancement Act

Section 12(d) of the National Technology Transfer and Advancement Act of 1995 (NTTAA), Public Law 104–113, section 12(d) (15 U.S.C. 272 note) directs EPA to use voluntary consensus standards in its regulatory activities unless to do so would be inconsistent with applicable law or otherwise impractical. Voluntary consensus standards are technical standards (e.g., materials specifications, test methods, sampling procedures, and business practices) that are developed or adopted by voluntary consensus standards bodies. NTTAA directs EPA to provide Congress through OMB, explanations when the Agency decides not to use available and applicably voluntary consensus standards.

This action does not involve technical standards. Therefore, EPA did not consider the use of any voluntary consensus standards.

J. Executive Order 12898—Federal Actions to Address Environmental Justice in Minority Populations and Low-Income Populations

Executive Order 12898 (59 FR 7629 (February 16, 1994)) establishes Federal executive policy on environmental justice. Its main provision directs Federal agencies, to the greatest extent practicable and permitted by law, to make environmental justice part of their mission by identifying and addressing, as appropriate, disproportionately high and adverse human health or environmental effects of its programs, policies, and activities on minorities and low-income populations in the United States.

The EPA has determined that this final rule will not have disproportionately high and adverse human health or environmental effects on minority or low-income populations because it does not affect the level of protection provided to human health or the environment. This rule simply extends the deadline for EPA to take action on a petition and does not impose any regulatory requirements.

K. Congressional Review Act

The Congressional Review Act (CRA), 5 U.S.C. 801 *et seq.*, as added by the Small Business Regulatory Enforcement Fairness Act of 1996, generally provides that before a rule may take effect, the agency promulgating the rule must submit a rule report, which includes a copy of the rule, to each House of the Congress and to the Comptroller General of the United States. Section 808 allows the issuing agency to make a rule effective sooner than otherwise provided by the CRA if the agency makes a good cause finding that notice and public procedure is impracticable, unnecessary or contrary to the public interest. This determination must be supported by a brief statement. 5 U.S.C. 808(2). As stated previously, EPA has made such a good cause finding, including the reasons therefore, and established an effective date of April 24, 2008. EPA will submit a report containing this rule and other required information to the U.S. Senate, the U.S. House of Representatives, and the Comptroller General of the United States prior to publication of the rule in the **Federal Register**. This action is not a ''major rule'' as defined by 5 U.S.C. 804(2).

L. Judicial Review

Section 307(b)(1) of the CAA indicates which Federal Courts of Appeal have venue for petitions of review of final actions by EPA. This section provides, in part, that petitions for review must be filed in the Court of Appeals for the District of Columbia Circuit (i) when the agency action consists of ''nationally applicable regulations promulgated, or final actions taken, by the Administrator,'' or (ii) when such action is locally or regionally applicable, if ''such action is based on a determination of nationwide scope or effect and if in taking such action the Administrator finds and publishes that such action is based on such a determination.''

Under CAA section 307(b)(1), a petition to review this action must be filed in the Court of Appeals for the District of Columbia Circuit within 60 days of May 1, 2008.

List of Subjects in 40 CFR Part 52

Environmental protection, Administrative practice and procedure, Air pollution control, Electric utilities, Intergovernmental relations, Nitrogen oxides, Ozone, Particulate matter, Reporting and recordkeeping requirements, Sulfur dioxide.

Dated: April 24, 2008.

Stephen L. Johnson,

Administrator.

[FR Doc. E8–9485 Filed 4–30–08; 8:45 am]

BILLING CODE 6560–50–P

OFFICE OF MANAGEMENT AND BUDGET

Office of Federal Procurement Policy

48 CFR Part 9904

Cost Accounting Standards Board; Accounting for the Costs of Employee Stock Ownership Plans (ESOPs) Sponsored by Government Contractors

AGENCY: Cost Accounting Standards Board, Office of Federal Procurement Policy, OMB.

ACTION: Final rule.

SUMMARY: The Cost Accounting Standards Board (the Board), Office of Federal Procurement Policy, has adopted a final rule to amend Cost Accounting Standard (CAS) 412, ''Cost Accounting Standard for composition and measurement of pension cost,'' and CAS 415, ''Accounting for the cost of deferred compensation.'' These amendments address issues concerning the recognition of the costs of Employee Stock Ownership Plans (ESOPs) under Government cost-based contracts and subcontracts. These amendments provide criteria for measuring the costs of ESOPs and their assignment to cost

accounting periods. The allocation of a contractor's assigned ESOP costs to contracts and subcontracts is addressed in other Standards. The amendments also specify that accounting for the costs of ESOPs will be covered by the provisions of CAS 415, ''Accounting for the cost of deferred compensation,'' and not by any other Standard. This rulemaking is authorized pursuant to Section 26 of the Office of Federal Procurement Policy (OFPP) Act.

DATES: *Effective Date:* June 2, 2008.

FOR FURTHER INFORMATION CONTACT: Laura Auletta, Manager, CAS Board, 725 17th Street, NW., Room 9013, Washington, DC 20503 (telephone: 202–395–3256).

SUPPLEMENTARY INFORMATION:

A. Regulatory Process

The Board's rules, regulations and standards are codified at 48 CFR chapter 99. The OFPP Act, 41 U.S.C. 422(g)(1), requires the Board, prior to the establishment of any new or revised Cost Accounting Standard, to complete a prescribed rulemaking process. The process generally consists of the following four steps:

1. Consult with interested persons concerning the advantages, disadvantages and improvements anticipated in the pricing and administration of government contracts as a result of the adoption of a proposed Standard (*e.g.*, promulgation of a Staff Discussion Paper.)
2. Promulgate an Advance Notice of Proposed Rulemaking (ANPRM).
3. Promulgate a Notice of Proposed Rulemaking (NPRM).
4. Promulgate a Final Rule.

This final rule is issued by the Board in accordance with the requirements of 41 U.S.C. 422(g)(1), and, is step four of the four-step process.

B. Background and Summary

The CAS and Federal Acquisition Regulation (FAR) have dealt with issues associated with ESOPs since ESOPs became popular in the late 1970s as a vehicle for providing incentive compensation to employees, as well as a means for corporations to finance their capital requirements. The popularity of ESOPs was greatly enhanced by their inclusion in the Employee Retirement Income Security Act of 1974 (ERISA) and by several beneficial changes to the Federal Income Tax Code in that same time period.

At first, the issues that arose were regarded as allowability matters that were to be treated in the FAR (or one of its predecessors, the Defense Acquisition Regulation or Armed Services Procurement Regulation). The views of the Board were sought primarily on an advisory basis. However, after issuance of the decision of the Armed Services Board of Contract Appeals (ASBCA) in the ''Parsons case,'' Ralph Parsons Co., ASBCA Nos. 37391, 37946, and 37947, December 20, 1990, 91–1 BCA 23648, reconsideration denied 91–2 BCA 23751, various government commenters suggested to the Board that ESOP cost measurement and period assignment matters warranted placement on the Board's agenda. These suggestions were amplified in light of the decision of the ASBCA in Ball Corp., ASBCA No. 49118, April 3, 2000, 00–1 BCA 30864. This position has been reiterated both by the Department of Defense and by some contractors.

The Board first considered issuing an Interpretation of its existing Standards, but then decided that additional research was needed. Various approaches for dealing with ESOP accounting issues were considered by the Board and other interested parties in the late 1990s. On September 15, 2000, the Board issued a Staff Discussion Paper (SDP) on this topic (65 FR 56008, Sept. 15, 2000). In response to the comments submitted on the SDP, on August 20, 2003 the Board issued an ANPRM (68 FR 50111) for the purpose of amending CAS 412 and 415 to address issues concerning the recognition of the costs of Employee Stock Ownership Plans (ESOPs) under Government cost-based contacts and subcontracts.

After considering the public comments submitted in response to the ANPRM, the Board published an NPRM on July 22, 2005 with request for comment (70 FR 42293). The Board received three sets of public comments in response to the NPRM. This final rule adopts the language in the NPRM, with minor changes to the transition provision. The final rule directs that costs of all ESOPs, regardless of type, be accounted for in accordance with CAS 415, and provides criteria in CAS 415 for measuring the costs of ESOPs and assigning those costs to cost accounting periods.

C. Public Comments

A summary of the comments received in response to the NPRM and the Board response are as follows:

1. Support Issuance of the Proposed Rule

Comment: Two commenters supported the issuance of the final rule. One commenter noted that the changes made to the NPRM in response to its comments on the ANRPM very effectively addressed its concerns. The second commenter noted that the NPRM indicated that the drafters diligently reviewed how ESOPs operated and reviewed carefully why Congress has consistently supported the creation of employer ownership through ESOPs for over thirty years. This commenter provided some recommendations for clarification and requested the Board move forward with the rulemaking process.

Response: The Board thanks the commenters for their responses.

2. Transition Provisions

Comment: One commenter opined that the proposed transition provisions at 9904.415–63 are overridden by 48 CFR 9904.412–20(b) and most existing ESOPs would not be subject to the revised rules.

Response: The Board recognizes the commenter's concern and has amended the transition provision in the final rule to specify that all ESOPs, including those considered to be pension ESOPs, are henceforth subject to CAS 415. When the transition provisions are read in conjunction with 412–20(b), the Board believes that following the receipt of a new CAS covered contract or subcontract all ESOPs shall be covered in CAS 415.

3. ''Awarded'' vs. ''Allocated''

Comment: One commenter opined that the term ''awarded'' has no meaning in the context of a qualified ESOP plan and requires clarification.

Response: As stated previously in the NPRM (70 FR 42293, dated July 22, 2005), the Board's objective in amending CAS 412 and 415 is to provide consistent cost accounting practices for the measurement and assignment of costs of ESOPs, regardless of whether or not a particular ESOP is a qualified plan under ERISA and the IRS. Accordingly, the Board believes it need not limit itself to the terms and concepts embodied in ERISA or IRS rules and regulations in defining the cost accounting practices to be used in the measurement and assignment of costs of ESOPs. For the reasons stated in the NPRM (see responses to the ANPRM, which are contained in the NPRM and annotated as Comment 3, ''Assignment of Costs Based on Award of Shares'' and Comment 5, ''Definition of an ESOP''), the Board continues to believe that it is appropriate to impose separate allocation and award criteria in order for an ESOP contribution to be measured and assigned to a particular cost accounting period. The Board also believes it has adequately distinguished between the concepts of allocation and award in both the techniques for application at 9904.415–50(f) and the illustrations at 9904.415–60, and that no further clarification is required.

4. Interest Included in ESOP Contributions

Comment: One commenter opined that contractors should be required to separately identify the interest component of ESOP costs to promote transparency.

Response: The Board continues to believe that it is not necessary to impose a separate disclosure requirement regarding interest paid by the ESOP trust out of a contractor's ESOP contributions. The Board's reasoning, as provided in the NPRM (70 FR 42293, dated July 22, 2005), also applies here and is summarized, in relevant part, below.

The final rule recognizes the resources used by the contractor to fund the current year's award to employees, whether those shares are purchased by the ESOP in the year of award or made available for allocation by repayment of ESOP debt. In finalizing this rule, the Board believes that it is providing for the measurement of ESOP costs for contract costing purposes in a manner that reflects the CAS objective of consistency in cost accounting practices.

For financial accounting purposes, contractors are required to follow generally accepted accounting principles (GAAP). Under GAAP (specifically American Institute of Certified Public Accountants (AICPA) Statement of Position 93–6, paragraphs 6.24 thru 6.27, ''Employer's Accounting for Employee Stock Ownership Plans''), companies are required to separately identify the interest and principal of the ESOP financing, and thus the transparency noted by the commenter already exists. Therefore, there is no need for the Board to promulgate a duplicate requirement. The Board further notes that whether interest or other cost components associated with financing a leveraged ESOP are allowable costs is determined under FAR Part 31. The final rule does not, in any manner, preclude the FAR Council from drafting rules that explicitly allow or disallow interest or any other cost component associated with an ESOP. Should the FAR Council decide to explicitly disallow interest or any other cost component associated with an ESOP, CAS 405 already requires that such costs be segregated in the contractor's accounting records. In addition, CAS 405 also requires that such costs be identified and excluded from any billing, claim, or proposal applicable to a Government contract. Therefore, the Board does not believe it is necessary to require separate disclosure of any interest paid by the ESOP trust out of a contractor's ESOP contribution.

5. Clarification of Examples

Comment: One commenter opined that the following illustrations should be clarified:

a. The commenter recommended that 9904.415–60(f) should be revised to read as follows:

Contractor F has a non-leveraged ESOP. Under the contractor's plan, employees are awarded 5,000 shares of stock for the year ended December 31, 2007. The market value of the stock as of 12/31/07, as determined on 2/5/08 is $10.00 per share. On February 5, 2008, the 5,000 shares are contributed to the ESOP and allocated to the individual employee accounts.

Response: The Board does not believe a change to the illustration in the NPRM is warranted. The recommended revision would alter the content of the example and render it inconsistent with the language in the revised standard. The illustration in the NPRM is intended to demonstrate that the valuation date of the stock is the date the contribution is made in accordance with CAS 415–50(f)(1), not the date that employees are awarded the stock under the contractor's plan. As stated in the ANPRM, the Board believes that the ''contribution'' approach to ESOP cost accounting is the best measure of a contractor's cost to provide the ESOP benefit awarded to an employee. Therefore, the value of the shares transferred to an ESOP is established as of the contribution date (the date when the title to the shares is transferred to the trust), not the date when the shares are awarded to the employee. As such, the language in the NPRM remains unchanged.

b. The commenter recommended that 9904.415–60(g) should be revised to read as follows:

On February 15, 2008, the contractor contributes $780,000 in cash to the ESOP trust (ESOT) to satisfy the principal and interest payment on the ESOT loan for FY 2007. The contractor's contribution of $780,000 causes 9,000 shares of stock to be allocated in the true ESOP. One thousand (1,000) shares of stock are contributed to a true ESOP on 2/2/05, valued at $60,000 as of 12/31/07.

Response: The Board does not believe a change to the illustration in the NPRM is warranted. The introduction of the term ''true ESOP'' would be inappropriate since it is not defined or used in the standard, and the language of the standard clearly distinguishes between the ESOP and the ESOP trust (ESOT). Furthermore, the illustration makes an important distinction between shares released to the ESOT as a result of the cash payment by the contractor, the additional shares contributed to the ESOT, and the total shares actually allocated to individual employee accounts. Thus, the language in the NPRM remains unchanged.

c. The commenter recommended that 9904.415–60(h)(1) should be revised to read as follows:

Contractor H has a leveraged ESOP. Under the contractor's plan, employees are awarded 8,000 shares of stock for the year ended December 31, 2007. Only 8,000 shares of stock are allocated as of 12/31/07. $100,000 of the total payment of $500,000 made on 1/31/08 was for the FY '08, and 2,000 shares will be allocated as of 12/31/08.

Response: The Board does not believe a change to the illustration in the NPRM is warranted. The commenter's recommendation would revise the example to state that the 2,000 shares remaining in the ESOT and not awarded for 2007 will be awarded in 2008. The Board does not believe this should be added to the example because it may result in the reader incorrectly assuming that the remaining shares will always be awarded in the following year (in this case, 2008). This assumption cannot be made since there will not necessarily be an obligation to award these shares in 2008. Thus, the language in the NPRM remains unchanged.

d. The commenter recommended that 9904.415–60(h)(2) should be revised to read as follows:

At December 31, 2008, the employees are awarded 12,000 shares of stock. On January 31, 2009, Contractor H contributes $500,000 in cash to the ESOT to satisfy the principal and interest payment on the ESOT loan for 2008, resulting in the bank releasing 10,000 shares of stock. On February 10, 2009, 12,000 shares are allocated to individual employee accounts satisfying the deferred compensation obligation for 2008. If the contractor claims the contribution or an allowable cost, or claims a tax deduction, for 2007, then the shares released as a result of the contribution must be allocated for the year in which the contribution is allowed or claimed as a corporate tax deduction. In addition to the $500,000 contribution, which resulted in 10,000 shares being allocated as of 12/31/08, an additional 2,000 shares of stock were contributed to a true ESOP on 2/10/09, and allocated as of 12/31/08.

Response: The Board does not believe a change to the illustration in the NPRM is warranted. As stated in the NPRM (70 FR 42293, dated July 22, 2005), the cost accounting practices specified in CAS 415 are not dependent on tax deductibility of any contribution since two plans with identical contribution requirements should not have different cost accounting treatment solely because of differences in tax deductibility. Therefore, changing the illustration would result in inconsistency with the language in the revised standard, since such a change would base the assignment of ESOP costs for contract costing purposes on ERISA and/or IRS rules that have not been incorporated into the Standard. As such, the language in the NPRM remains unchanged.

e. The commenter recommended that 9904.415–60(i) should be revised to read as follows:

Contractor I has a leveraged ESOP. Under the contractor's plan, employees are awarded 10,000 shares for FY 2007, which ended December 31, 2007. On February 10, 2008, Contractor I contributes $700,000 in cash to satisfy the principal and interest payment for the ESOP loan for FY 2007. This contribution results in the bank releasing 10,000 shares of stock. On March 1, 2008, the ESOP allocates the 10,000 shares to individual employee accounts satisfying the 2007 obligation. The 10,000 shares of stock are allocated as of 12/31/07.

Response: The Board does not believe a change to the illustration in the NPRM is warranted. The recommended revision would eliminate the purpose of this illustration, which is intended to address instances where the shares are awarded on one date (in this example, December 31, 2007) but are not allocated to individual employee accounts until a later date (in this case, March 1, 2008). This example is intended to illustrate the assignment of ESOP contributions in accordance with 9904.415–50(f)(2) and the distinction between award and allocation. As such, the language in the NPRM remains unchanged.

D. Paperwork Reduction Act

The Paperwork Reduction Act, Public Law 96–511, does not apply to this rulemaking, because this rule imposes no paperwork burden on offerors, affected contractors and subcontractors, or members of the public which requires the approval of OMB under 44 U.S.C. 3501, *et seq.*

E. Regulatory Flexibility Act, Unfunded Mandates Reform Act, Congressional Review Act, and Executive Orders 12866 and 13132

The Board certifies that this rule will not have a significant effect on a substantial number of small entities within the meaning of the Regulatory Flexibility Act, 5 U.S.C. 601, *et seq.,* because small businesses are exempt from the application of the Cost Accounting Standards. For purposes of the Unfunded Mandates Reform Act of 1995 (Pub. L. 104–4), as well as Executive Orders 12866 and 13132, the final rule will not significantly or uniquely affect small governments, and will not result in increased expenditures by State, local, and tribal governments, or by the private sector, of $100 million or more. The final rule is not a ''major rule'' under 5 U.S.C. Chapter 8; the rule will not have any of the effects set forth in 5 U.S.C. 804(2). Finally, the rule does not have federalism implications as described in Executive Order 13132.

List of Subjects in 48 CFR Part 9904

Accounting, Government procurement.

Paul A. Denett,

Administrator, Office of Federal Procurement Policy.

■ For the reasons set forth in this preamble, chapter 99 of title 48 of the Code of Federal Regulations is amended as set forth below:

PART 9904—COST ACCOUNTING STANDARDS

■ 1. The authority citation for part 9904 continues to read as follows:

Authority: Pub. L. 100–679, 102 Stat 4056, 41 U.S.C. 422.

■ 2. Section 9904.412–20 is revised to read as follows:

9904.412–20 Purpose.

(a) The purpose of this Standard 9904.412 is to provide guidance for determining and measuring the components of pension cost. The Standard establishes the basis on which pension costs shall be assigned to cost accounting periods. The provisions of this Cost Accounting Standard should enhance uniformity and consistency in accounting for pension costs and thereby increase the probability that those costs are properly allocated to cost objectives.

(b) This Standard does not cover the cost of Employee Stock Ownership Plans (ESOPs) that meet the definition of a pension plan. Such plans are considered a form of deferred compensation and are covered under 9904.415.

■ 3. Section 9904.415–20 is revised to read as follows:

9904.415–20 Purpose.

(a) The purpose of this Standard 9904.415 is to provide criteria for the measurement of the cost of deferred compensation and the assignment of such cost to cost accounting periods. The application of these criteria should increase the probability that the cost of deferred compensation is allocated to cost objectives in a uniform and consistent manner.

(b) This Standard is applicable to the cost of all deferred compensation except the following which are covered in other Cost Accounting Standards:

(1) The cost for compensated personal absence, and

(2) The cost for pension plans that do not meet the definition of an Employee Stock Ownership Plan (ESOP).

■ 4. Section 9904.415–30 is amended by revising paragraph (a), introductory text, adding paragraphs (a)(2) and (3), and revising paragraph (b) to read as follows:

9904.415–30 Definitions.

(a) The following are definitions of terms which are prominent in this Standard 9904.415. Other terms defined elsewhere in this Chapter 99 shall have the meanings ascribed to them in those definitions unless paragraph (b) of this section requires otherwise.

* * * * *

(2) Employee Stock Ownership Plan (ESOP) means:

(i) An employee benefit plan that is described by the Employee Retirement Income Security Act of 1974 (ERISA) and the Internal Revenue Code (IRC) of 1986 as a stock bonus plan, or combination stock bonus and money purchase pension plan, designed to invest primarily in employer stock, and

(ii) Any other deferred compensation plan designed to invest primarily in the stock of the contractor's corporation including, but not limited to, plans covered by ERISA.

(3) Fair value means the amount that a seller would reasonably expect to receive in a current arm's length transaction between a willing buyer and a willing seller, other than a forced or liquidation sale.

(b) The following modifications of terms defined elsewhere in this Chapter 99 are applicable to this Standard:

(1) Market value means the current or prevailing price of a stock or other property as indicated by market quotations.

(2) [Reserved]

■ 5. Section 9904.415–40 is revised to read as follows:

9904.415–40 Fundamental requirement.

(a) The cost of deferred compensation shall be assigned to the cost accounting period in which the contractor incurs an obligation to compensate the employee. In the event no obligation is incurred prior to payment, the cost of deferred compensation shall be the amount paid and shall be assigned to the cost accounting period in which the payment is made.

(b) Measurement of deferred compensation costs.

(1) For deferred compensation other than ESOPs, the deferred compensation cost shall be the present value of the future benefits to be paid by the contractor.

(2) For an ESOP, the deferred compensation cost shall be the amount contributed to the ESOP by the contractor.

(c) The cost of each award of deferred compensation shall be considered separately for purposes of measurement and assignment of such costs to cost accounting periods. However, if the cost of deferred compensation for the employees covered by a deferred compensation plan can be measured and assigned with reasonable accuracy on a group basis, separate computations for each employee are not required.

■ 6. Section 9904.415–50 is amended by revising paragraph (d) introductory text and (e) introductory text and adding paragraph (f) to read as follows:

9904.415–50 Techniques for application.

* * * * *

(d) The following provisions are applicable for plans, other than ESOPs, that meet the conditions of 9904.415–50(a) and the compensation is to be paid in money.

* * * * *

(e) The following provisions are applicable for plans, other than ESOPs, that meet the conditions of 9904.415–50(a) and the compensation is received by the employee in other than money. The measurements set forth in this paragraph constitute the present value of future benefits for awards made in other than money and, therefore, shall be deemed to be a reasonable measure of the amount of the future payment:

* * * * *

(f)(1) For an ESOP, the contractor's cost shall be measured by the contractor's contribution, including interest and dividends if applicable, to the ESOP. The measurement of contributions made in the form of stock of the corporation or property, shall be based on the market value of the stock or property at the time the contributions are made. If the market value is not available, then fair value of the stock or property shall be used.

(2) A contractor's contribution to an ESOP shall be assignable to a cost accounting period only to the extent that the stock, cash, or any combination thereof resulting from the contribution is awarded to employees and allocated to individual employee accounts by the tax filing date for that period, including any permissible extensions thereof. All stock or cash that is allocated to the individual employee accounts between the end of the cost accounting period and the tax filing date for that period must be assigned to the cost accounting period in which the employee is awarded the stock or cash. Any portion of the stock or cash resulting from a contractor's contribution that is not awarded to employees or allocated to individual employee accounts by the tax filing date for that period, including any permissible extensions thereof, shall be assigned to a future cost accounting period or periods when the remaining portion of stock or cash has been awarded to employees and allocated to individual employee accounts. This stock shall retain the value established when it was originally purchased by or otherwise made available to the ESOP.

■ 7. Section 9904.415–60 is amended by adding paragraphs (f), (g), (h) and (i) to read as follows:

9904.415–60 Illustrations.

* * * * *

(f) Contractor F has a non-leveraged ESOP. Under the contractor's plan, employees are awarded 5,000 shares of stock for the year ended December 31, 2007. On February 5, 2008, when the shares have a market value of $10.00 each, the 5,000 shares are contributed to the ESOP and allocated to the individual employee accounts. The total measured and assigned deferred compensation cost for FY 2007 is $50,000 (5,000 × $10 = $50,000). The market value of the contractor's stock when awarded to the employees, whether higher or lower than the $10.00 per share market value when the contractor's contribution was made to the ESOP, is irrelevant to the measurement of the contractor's ESOP costs.

(g) Contractor G has a leveraged ESOP. Under the contractor's plan, employees are awarded 10,000 shares of stock for the year ended December 31, 2007. On February 15, 2008, the contractor contributes $780,000 in cash to the ESOP trust (ESOT) to satisfy the principal and interest payment on the ESOT loan for FY 2007, resulting in the bank releasing 9,000 shares of stock, and 1,000 shares of stock valued at $60,000 to the ESOT, representing the balance of the 10,000 shares. On February 22, 2008, the ESOP allocates 10,000 shares to the individual employee accounts. The total measured and assigned deferred compensation cost for FY 2007 is $840,000—the contractor's total contribution required to satisfy the deferred compensation obligation totaling 10,000 shares.

(h)(1) Contractor H has a leveraged ESOP. Under the contractor's plan, employees are awarded 8,000 shares of stock for the year ended December 31, 2007. On January 31, 2008, the contractor contributes $500,000 in cash to the ESOT to satisfy the principal and interest payment on the ESOT loan for 2007, resulting in the bank releasing 10,000 shares of stock. On February 10, 2008, 8,000 shares are allocated to individual employee accounts, satisfying the deferred compensation obligation for 2007. The total measured deferred compensation cost for 2007 is $500,000—the contractor's contribution for the cost accounting period. However, the total assignable deferred compensation cost for 2007 is $400,000—the portion of the contribution that satisfies the 2007 deferred compensation obligation of 8,000 shares [(8,000 shares / 10,000 shares) × $500,000 = $400,000]. The remaining $100,000 of the contribution made in 2007 is assignable to future periods in which the remaining 2,000 shares of stock are awarded to employees and allocated to individual employee accounts.

(2) At December 31, 2008, the employees are awarded 12,000 shares of stock. On January 31, 2009, Contractor H contributes $500,000 in cash to the ESOT to satisfy the principal and interest payment on the ESOT loan for 2008, resulting in the bank releasing 10,000 shares of stock. On February 10, 2009, 12,000 shares are allocated to individual employee accounts satisfying the deferred compensation obligation for 2008. The total deferred compensation assignable to 2008 is $600,000, the cost of the 12,000 shares awarded to employees and allocated to individual employee accounts for 2008. The cost of the award is comprised of the contractor's contribution for the current cost accounting period (10,000 shares at $500,000) and the 2007 contribution carryover (2,000 shares at $100,000).

(i) Contractor I has a leveraged ESOP. Under the contractor's plan, employees are awarded 10,000 shares for FY 2007, which ended December 31, 2007. On

February 10, 2008, Contractor I contributes $700,000 in cash to satisfy the principal and interest payment for the ESOP loan for FY 2007. This contribution results in the bank releasing 10,000 shares of stock. On March 1, 2008, the ESOP allocates the 10,000 shares to individual employee accounts satisfying the 2007 obligation. The 10,000 shares of stock must be assigned to FY 2007 (these shares cannot be assigned to 2008).

■ 8. Section 9904.415–63 is revised to read as follows:

9904.415–63 Effective date.

(a) This Standard 9904.415 is effective as of June 2, 2008.

(b) This Standard shall be followed by each contractor on or after the start of its next cost accounting period beginning after the receipt of a contract or subcontract to which this Standard is applicable.

(c) Contractors with prior CAS-covered contracts with full coverage shall continue to follow Standard 9904.415 in effect prior to June 2, 2008 until this Standard, effective June 2, 2008, becomes applicable following receipt of a contract or subcontract to which this revised Standard applies.

(d) For contractors and subcontractors that have established advance agreements prior to June 2, 2008 regarding the recognition of the costs of existing ESOPs, the awarding agency and contractor shall comply with the provisions of such advance agreement(s) for these existing ESOPs, regardless of whether the ESOP was previously subject to CAS 412 or 415. These advance agreements may be modified, by mutual agreement, to incorporate the requirements effective on June 2, 2008.

[FR Doc. E8–9376 Filed 4–30–08; 8:45 am]

BILLING CODE 3110–01–P

DEPARTMENT OF THE INTERIOR

Fish and Wildlife Service

50 CFR Part 17

[FWS—R2—ES—2008—0044; 40120—1113—0000–B3]

RIN 1018—AW12

Endangered and Threatened Wildlife and Plants; Listing the Potential Sonoran Desert Bald Eagle Distinct Population Segment as Threatened Under the Endangered Species Act

AGENCY: Fish and Wildlife Service, Interior.

ACTION: Final rule.

SUMMARY: We, the U.S. Fish and Wildlife Service (Service), are issuing a final rule to amend the regulations for the Federal List of Endangered and Threatened Wildlife at 50 CFR 17.11 by designating bald eagles (*Haliaeetus leucocephalus*) in the Sonoran Desert area of central Arizona as threatened under the authority of the Endangered Species Act of 1973, as amended (Act). We are also reinstating and clarifying the former special rule at 50 CFR 17.41 that applied to threatened members of this species. This action revises the CFR to reflect a March 6, 2008, court order.

DATES: This action is effective May 1, 2008. However, the court order had legal effect immediately upon being filed on March 6, 2008.

FOR FURTHER INFORMATION CONTACT: Steve Spangle, Field Supervisor, U.S. Fish and Wildlife Service, Arizona Ecological Services Field Office, 2321 West Royal Palm Road, Suite 103, Phoenix, Arizona 85021; telephone 602–242–0210; facsimile 602–242–2513; *http://www.fws.gov/southwest/es/arizona/.*

SUPPLEMENTARY INFORMATION:

Background

Information about the bald eagle's life history can be found in our July 9, 2007 (72 FR 37346), final delisting rule for bald eagles in the lower 48 States.

Previous Federal Action

Information about previous Federal actions was provided in our July 9, 2007 (72 FR 37346), final delisting rule for bald eagles in the lower 48 States.

On October 6, 2004, we received a petition, dated October 6, 2004, from the Center for Biological Diversity (CBD), the Maricopa Audubon Society, and the Arizona Audubon Council requesting that the ''Southwestern desert nesting bald eagle population'' be classified as a distinct population segment (DPS), that this DPS be reclassified from a threatened species to an endangered species, and that we concurrently designate critical habitat for the DPS under the Act.

On March 27, 2006, the CBD and the Maricopa Audubon Society filed a lawsuit against the U.S. Department of the Interior and the Service for failing to make a timely finding on the petition. The parties reached a settlement and the Service agreed to complete its petition finding by August 2006. We announced our 90-day finding, required under 16 U.S.C. 1533(b)(3)(A), on August 30, 2006 (71 FR 51549), that the petition did not present substantial scientific or commercial information indicating that the petitioned action may be warranted.

On January 5, 2007, the CBD and the Maricopa Audubon Society filed a lawsuit challenging the Service's 90-day finding that the ''Sonoran Desert population'' of the bald eagle did not qualify as a DPS, and further challenging the Service's 90-day finding that the population should not be up-listed to endangered status.

On July 9, 2007 (72 FR 37346), we published the final delisting rule for bald eagles in the lower 48 States. In that final delisting rule, we stated that our findings on the status of the Sonoran Desert population of bald eagles superseded our 90-day petition finding because the final delisting rule constituted a final decision on whether the Sonoran Desert population of bald eagles qualified for listing as a DPS under the Act.

On August 17, 2007, the CBD and the Maricopa Audubon Society filed a motion for summary judgment, requesting the court to make a decision on their January 5, 2007, lawsuit. On March 5, 2008, the U.S. District Court for the District of Arizona ruled in favor of the CBD and the Maricopa Audubon Society. The court order (Center for *Biological Diversity* v. *Kempthorne,* CV 07–0038–PHX–MHM (D. Ariz)), was filed on March 6, 2008.

The court ruled for the plaintiffs and found that the Service:

(1) Finding on the status of the Sonoran Desert population of bald eagles in our July 9, 2007 (72 FR 37346), final delisting rule did not moot the plaintiff's challenge to the August 30, 2006, negative 90-day petition finding;

(2) Applied an inappropriately strict evidentiary burden on the petition at the 90-day review stage and thus arbitrarily and capriciously concluded that the petition did not present substantial information that listing the ''Desert bald eagle population'' may be warranted; and

(3) Arbitrarily and capriciously conducted the 90-day review of the petition by soliciting information and opinions from a limited outside source.

The court provided the following remedies and ordered the Service to:

(1) Conduct a status review of the Desert bald eagle population pursuant to the Act to determine whether listing that population as a DPS is warranted, and if so, whether listing that DPS as threatened or endangered pursuant to the Act is warranted;

(2) Issue a 12-month finding, pursuant to 16 U.S.C. 1533(b)(3)(B), on whether listing the Desert bald eagle population as a DPS is warranted, and if so, whether listing that DPS as threatened or endangered is warranted; and

DISCLOSURE AND CONSISTENCY OF COST ACCOUNTING PRACTICES (OCT 2008)

(a) * * *

(4) * * * Such adjustment shall provide for recovery of the increased costs to the United States together with interest thereon computed at the annual rate established under section 6621(a)(2) of the Internal Revenue Code of 1986 (26 U.S.C. 6621(a)(2)), from the time the payment by the United States was made to the time the adjustment is effected.

* * * * *

52.230–4 [Amended]

■ 6. Amend section 52.230–4 by revising the date of the clause date to read ''(OCT 2008)''; and removing ''6621'' and adding ''6621(a)(2)'' in its place each time it appears.

52.230–5 [Amended]

■ 7. Amend section 52.230–5 by—

■ a. Revising the date of the clause date to read ''(OCT 2008)'';

■ b. Removing from paragraph (a)(5) ''6621'' and adding ''6621(a)(2)'' in its place each time it appears; and

■ c. Removing from paragraph (d)(2) ''$500,000'' and adding ''$650,000'' in its place.

[FR Doc. E8–21367 Filed 9–16–08; 8:45 am]

BILLING CODE 6820–EP–S

DEPARTMENT OF DEFENSE

GENERAL SERVICES ADMINISTRATION

NATIONAL AERONAUTICS AND SPACE ADMINISTRATION

48 CFR Parts 30 and 52

[FAC 2005–27; FAR Case 2006–004; Item XII; Docket 2008–0001; Sequence 14]

RIN 9000–AK58

Federal Acquisition Regulation; FAR Case 2006–004, CAS Administration

AGENCIES: Department of Defense (DoD), General Services Administration (GSA), and National Aeronautics and Space Administration (NASA).

ACTION: Final rule.

SUMMARY: The Civilian Agency Acquisition Council and the Defense Acquisition Regulations Council (Councils) have agreed to adopt a proposed rule, published in the **Federal Register** at 71 FR 58338, October 3, 2006, as a final rule, with minor changes. The rule amends the Federal Acquisition Regulation (FAR) to implement revisions to the regulations related to the administration of the Cost Accounting Standards (CAS) as they pertain to contracts with foreign concerns, including United Kingdom (U.K.) concerns.

DATES: *Effective Date:* October 17, 2008.

FOR FURTHER INFORMATION CONTACT: For clarification of content, contact Mr. Edward Chambers, at (202) 501–3221. For information pertaining to status or publication schedules, contact the Regulatory Secretariat at (202) 501–4755. Please cite FAC 2005–27, FAR case 2006–004.

SUPPLEMENTARY INFORMATION:

A. Background

The Councils published a proposed rule in the **Federal Register** at 71 FR 58338, October 3, 2006, to maintain consistency between CAS and FAR in matters relating to disclosure requirements and the administration of CAS for contracts awarded to foreign concerns, including U.K. concerns.

This proposed rule was issued in response to the Cost Accounting Standards Board's interim rule (70 FR 29457, May 23, 2005) (finalized without change at 72 FR 32546, June 13, 2007), revising the applicability of CAS to U.K. contracts and subcontracts.

The Councils received no comments on the proposed rule and have adopted the proposed rule as a final rule with minor changes. The minor changes to 30.201–4(c) clarify that clause 52.230–4 need not be included in contracts with foreign concerns otherwise exempt from CAS coverage, and that foreign concerns do not include foreign governments, or their agents or instrumentalities.

This is not a significant regulatory action and, therefore, was not subject to review under Section 6(b) of Executive Order 12866, Regulatory Planning and Review, dated September 30, 1993. This rule is not a major rule under 5 U.S.C. 804.

B. Regulatory Flexibility Act

The Department of Defense, the General Services Administration, and the National Aeronautics and Space Administration certify that this final rule will not have a significant economic impact on a substantial number of small entities within the meaning of the Regulatory Flexibility Act, 5 U.S.C. 601, *et seq.*, because all small businesses are exempt from CAS.

C. Paperwork Reduction Act

The Paperwork Reduction Act does not apply because the changes to the FAR do not impose information collection requirements that require the approval of the Office of Management and Budget under 44 U.S.C. 3501, *et seq.*

List of Subjects in 48 CFR Parts 30 and 52

Government procurement.

Dated: September 9, 2008.

Al Matera,

Director, Office of Acquisition Policy.

■ Therefore, DoD, GSA, and NASA amend 48 CFR parts 30 and 52 as set forth below:

■ 1. The authority citation for 48 CFR parts 30 and 52 continues to read as follows:

Authority: 40 U.S.C. 121(c); 10 U.S.C. chapter 137; and 42 U.S.C. 2473(c).

PART 30—COST ACCOUNTING STANDARDS ADMINISTRATION

■ 2. Amend section 30.201–4 by revising paragraph (c) to read as follows:

30.201–4 Contract clauses.

* * * * *

(c) *Disclosure and Consistency of Cost Accounting Practices for Contracts Awarded to Foreign Concerns.* The contracting officer shall insert the clause at FAR 52.230–4, Disclosure and Consistency of Cost Accounting Practices for Contracts Awarded to Foreign Concerns, in negotiated contracts with foreign concerns, unless the contract is otherwise exempt from CAS (see 48 CFR 9903.201–1). Such contracts are subject to CAS 401 and 402 under 48 CFR 9903.201–1(b)(4)(FAR Appendix). Foreign concerns do not include foreign governments or their agents or instrumentalities.

* * * * *

PART 52—SOLICITATION PROVISIONS AND CONTRACT CLAUSES

■ 3. Amend section 52.230–4 by revising the section heading, the clause heading and date, and the first, second, and fourth sentences of the clause to read as follows.

52.230–4 Disclosure and Consistency of Cost Accounting Practices for Contracts Awarded to Foreign Concerns.

* * * * *

DISCLOSURE AND CONSISTENCY OF COST ACCOUNTING PRACTICES FOR CONTRACTS AWARDED TO FOREIGN CONCERNS (OCT 2008).

The Contactor agrees that it will consistently follow the cost accounting practices disclosed on FORM CASB DS–1, or other disclosure form as permitted by 48 CFR 9903.202–1(e), in estimating, accumulating, and reporting costs under this contract, and comply with the requirements of CAS 401, Consistency in Estimating, Accumulating, and Reporting Costs, and CAS 402, Consistency in Allocating Costs Incurred for the Same Purpose. In the event the Contractor fails to follow such practices, or comply consistently with CAS 401 and 402, it agrees that the contract price shall be adjusted, together with interest, if such failure results in increased cost paid by the U.S. Government. * * * The Contractor agrees that the Disclosure Statement or other form permitted, pursuant to 48 CFR 9903.202–1(e) shall be available for inspection and use by authorized representatives of the United States Government.

(End of clause)

[FR Doc. E8–21365 Filed 9–16–08; 8:45 am]

BILLING CODE 6820–EP–S

DEPARTMENT OF DEFENSE

GENERAL SERVICES ADMINISTRATION

NATIONAL AERONAUTICS AND SPACE ADMINISTRATION

48 CFR Parts 37 and 52

[FAC 2005–27; FAR Case 2006–027; Item XIII;Docket 2007–0001; Sequence 5]

RIN 9000–AK54

Federal Acquisition Regulation; FAR Case 2006–027, Accepting and Dispensing of $1 Coin

AGENCIES: Department of Defense (DoD), General Services Administration (GSA), and National Aeronautics and Space Administration (NASA).

ACTION: Final rule.

SUMMARY: The Civilian Agency Acquisition Council and the Defense Acquisition Regulations Council (Councils) have agreed to adopt as final, with change, the interim rule amending the Federal Acquisition Regulation (FAR) to implement Section 104 of the Presidential $1 Coin Act of 2005. Section 104 requires that entities that operate any business on any premises owned or controlled by the United States be capable of accepting and dispensing $1 coins on January 1, 2008. Subsequent to this, Pub. L. 110–147 amended 31 U.S.C. 5112(p)(1)(A), to allow an exception from the $1 coin dispensing capability requirement for vending machines that do not receive currency denominations greater than $1.

DATES: *Effective Date*: September 17, 2008.

Applicability Date: This rule applies to all service contracts that involve business operations conducted in U.S. coins and currency, including vending machines, on any premises owned by the United States or under the control of any agency or instrumentality of the United States. The clause shall be placed in all such solicitations and contracts on and after the effective date of this rule. Those applicable contracts in existence before January 1, 2008, that do not already have the clause shall be modified to include the clause; those contracts that have the August 2007 edition of the clause shall be modified if the contractor requests, to include the newer version contained in this FAC, without requiring consideration from the contractor.

FOR FURTHER INFORMATION CONTACT: Mr. Michael Jackson, Procurement Analyst, at (202) 208–4949 for clarification of content. For information pertaining to status or publication schedules, contact the FAR Secretariat at (202) 501–4755. Please cite FAC 2005–27, FAR case 2006–027.

SUPPLEMENTARY INFORMATION:

A. Background

This final rule amends the FAR to implement the Presidential $1 Coin Act of 2005 (Pub. L. 109–145). The Presidential $1 Coin Act of 2005 requires the Secretary of the Treasury to mint and issue annually four new $1 coins bearing the likenesses of Presidents of the United States in the order of their service and to continue to mint and issue ''Sacagawea-design'' coins for circulation. In order to promote circulation of the coins, Section 104 of the Public Law also requires that Federal agencies take action so that, by January 1, 2008, entities that operate any business, including vending machines, on any premises owned by the United States or under the control of any agency or instrumentality of the United States, are capable of accepting and dispensing $1 coins and that the entities display notices of this capability on the business premises. Subsequent to the passage of the Presidential Coin Act, Pub. L. 110–147 amended 31 U.S.C. 5112(p)(1)(A), to allow an exception from the $1 coin dispensing capability requirement for vending machines that do not receive currency denominations greater than $1. This will require modification of existing covered contracts whose period of performance extends beyond the January 1, 2008 date in order to assure compliance with Section 104 of the Act, as well as compliance with Pub. L. 110–147.

DoD, GSA, and NASA published an interim rule in the **Federal Register** at 72 FR 46361, August 17, 2007. The 60–day comment period for the interim rule ended October 16, 2007. Three respondents provided comments. The comments are discussed below.

Public Comments

Comment 1: One respondent asked why does the FAR matrix show that 52.237–11 is applicable to R&D contracts and to A&E contracts?

R&D contracts and A&E contracts are usually paid by electronic funds transfer. There is usually no cash payment involved in such contracts. Therefore, why would contractors who provide R&D or A&E services have to be capable of accepting dollar coins?

Response: The inclusion of R&D and A&E contracts in the FAR matrix as applicable to 52.237–11 was an inadvertent error.

Comment 2: One respondent stated in order to implement these widespread and extensive changes to vending machines, our members simply need more time. Contrary to the statement contained in the **Federal Register** notice, this interim rule *does* have a significant economic impact. It is not accurate to state that ''receiving and dispensing the new coins as part of business operations should not add to workload or expense'' (72 FR 46361, August 17, 2007). Accordingly, we strongly encourage the Councils to account for both the workload and expense by extending the compliance date to July 1, 2008.

Response: Section 104 of the Presidential $1 Coin Act of 2005 (31 U.S.C. 5112(p)(1)), established the effective date for this provision to be January 1, 2008. The effect of this clause is merely to implement the provision of law. Notwithstanding, the provision of law cannot be modified under these circumstances without further consideration by Congress, who passed the provision of law. Pub. L. 110–147 amended section 5112(p)(1)(A) of title 31, U.S.C., to allow an exception from the $1 coin dispensing capability requirement for vending machines that do not receive currency denominations greater than $1. Thus, the exception of the law provides relief for those vending machines.

Comment 3: One respondent requested an amendment to the interim rule published in the **Federal Register**, August 17, 2007, amending 48 CFR 52 (Solicitation Provisions and Contract Clauses), Section 52.237–11 (Accepting and Dispensing of $1 Coin) to exempt vending machines on Federal property that do not accept currency denominations above $1 from the requirement to dispense dollar coins.

Response: The very intent of the statute is to require those businesses and instrumentalities operating on Federal property to be able to accept and dispense the $1 coin if that business or instrumentality is conducting a business whereby coins or currency is exchanged. However, Pub. L. 110–147 amended section 5112(p)(1)(A) of title

DEPARTMENT OF DEFENSE

GENERAL SERVICES ADMINISTRATION

NATIONAL AERONAUTICS AND SPACE ADMINISTRATION

48 CFR Part 23

[FAC 2005–27; FAR Case 2006–025; Item X; Docket 2007–0001; Sequence 18]

RIN 9000–AK76

Federal Acquisition Regulation; FAR Case 2006–025, Online Representations and Certifications Application Review

AGENCIES: Department of Defense (DoD), General Services Administration (GSA), and National Aeronautics and Space Administration (NASA).

ACTION: Final rule.

SUMMARY: The Civilian Agency Acquisition Council and the Defense Acquisition Regulations Council (Councils) have agreed to adopt as final, without change, an interim rule amending the Federal Acquisition Regulation (FAR) to revise the prescription for use of clauses for the use of Environmental Protection Agency-designated products and toxic chemical release reporting.

DATES: *Effective Date:* September 17, 2008.

FOR FURTHER INFORMATION CONTACT Mr. Ernest Woodson Procurement Analyst, at (202) 501–3775 for clarification of content. For information pertaining to status or publication schedules, contact the FAR Secretariat at (202) 501–4755. Please cite FAC 2005–27, FAR case 2006–025.

SUPPLEMENTARY INFORMATION:

A. Background

DoD, GSA, and NASA published an interim rule in the **Federal Register** at 72 FR 46359 on August 17, 2007, to amend FAR 23.406 and 23.906 to revise the prescriptions for the use of 52.223–9 and 52.223–14 to provide for their use under the same circumstances as the prescription for use of their associated provisions. These revisions ensure compliance with the requirements of 40 CFR part 247 and 42 U.S.C. 11023. The comment period closed October 16, 2007. No public comments were received on the rule. The Councils have determined to adopt the interim rule as final, without change.

This is not a significant regulatory action and, therefore, was not subject to review under Section 6(b) of Executive Order 12866, Regulatory Planning and Review, dated September 30, 1993. This rule is not a major rule under 5 U.S.C. 804.

B. Regulatory Flexibility Act

The Department of Defense, the General Services Administration, and the National Aeronautics and Space Administration certify that this final rule will not have a significant economic impact on a substantial number of small entities within the meaning of the Regulatory Flexibility Act, 5 U.S.C. 601, *et seq.*, because the rule revises language that the Office of Management and Budget (OMB) has already approved for obtaining representations and certifications under OMB Control Numbers 9000–0134 and 9000–0139 for compliance with Section 6002 of the Resource Conservation and Recovery Act and the requirements of Executive Order 12969, Emergency Planning and Community Right-to-Know Act of 1986. No comments were received with regard to an impact on small entities.

C. Paperwork Reduction Act

The Paperwork Reduction Act does apply; however, these changes to the FAR do not impose additional information collection requirements to the paperwork burden previously approved under OMB Control Numbers 9000–0134 and 9000–0139.

List of Subjects in 48 CFR Part 23

Government procurement.

Dated: September 9, 2008.

Al Matera,

Director, Office of Acquisition Policy.

Interim Rule Adopted as Final Without Change

■ Accordingly, under the authority of 40 U.S.C. 121, the interim rule amending 48 CFR part 23 which was published in the **Federal Register** at 72 FR 46359, August 17, 2007, is adopted as a final rule without change.

[FR Doc. E8–21378 Filed 9–16–08; 8:45 am]

BILLING CODE 6820–EP–S

DEPARTMENT OF DEFENSE

GENERAL SERVICES ADMINISTRATION

NATIONAL AERONAUTICS AND SPACE ADMINISTRATION

48 CFR Parts 30 and 52

[FAC 2005–27; FAR Case 2007–002; Item XI; Docket 2008–0001, Sequence 7]

RIN 9000–AL09

Federal Acquisition Regulation; FAR Case 2007–002, Cost Accounting Standards (CAS) Administration and Associated Federal Acquisition Regulation Clauses

AGENCIES: Department of Defense (DoD), General Services Administration (GSA), and National Aeronautics and Space Administration (NASA).

ACTION: Interim rule with request for comments.

SUMMARY: The Civilian Agency Acquisition Council and the Defense Acquisition Regulations Council (Councils) have agreed on an interim rule amending the Federal Acquisition Regulation (FAR) to revise the contract clauses related to the administration of the Cost Accounting Standards (CAS) to maintain consistency between the FAR and CAS.

DATES: *Effective Date:* October 17, 2008.

Comment Date: Interested parties should submit written comments to the FAR Secretariat on or before November 17, 2008 to be considered in the formulation of a final rule.

ADDRESSES: Submit comments identified by FAC 2005–27, FAR case 2007–002, by any of the following methods:

- Regulations.gov: *http://www.regulations.gov*. Submit comments via the Federal eRulemaking portal by inputting ''FAR Case 2007–002'' under the heading ''Comment or Submission''. Select the link ''Send a Comment or Submission'' that corresponds with FAR Case 2007–002. Follow the instructions provided to complete the ''Public Comment and Submission Form''. Please include your name, company name (if any), and ''FAR Case 2007–002'' on your attached document.
- Fax: 202–501–4067.
- Mail: General Services Administration, Regulatory Secretariat (VPR), 1800 F Street, NW., Room 4041, ATTN: Laurieann Duarte, Washington, DC 20405.

Instructions: Please submit comments only and cite FAC 2005–27, FAR case 2007–002, in all correspondence related to this case. All comments received will be posted without change to *http://www.regulations.gov*, including any personal and/or business confidential information provided.

FOR FURTHER INFORMATION CONTACT Mr. Ed Chambers, Procurement Analyst, at (202) 501–3221 for clarification of content. Please cite FAC 2005–27, FAR case 2007–002. For information pertaining to status or publication schedules, contact the FAR Secretariat at (202) 501–4755.

SUPPLEMENTARY INFORMATION:

A. Background

On June 14, 2007, the CAS Board published a final rule (72 FR 32809) revising the contract clauses for CAS administration. The final rule effected the following changes:

- Amended the CAS applicability threshold to be the same as the threshold for compliance with the Truth in Negotiations Act (TINA) as required by section 822 of the 2006 National Defense Authorization Act (Pub. L. 109–163). The TINA threshold is currently $650,000.
- Changed the effective dates of 48 CFR 9903.201–3 and 48 CFR 9903.201–4(a), (c), and (e) from April 2000 and June 2000, respectively, to June 2007.

On June 14, 2000, the CAS Board published a final rule (65 FR 37470) revising the contract clauses for CAS administration. The final rule effected the following changes:

- Specified that the interest rate for overpayments by the Government under 48 CFR 9903.201–4(a), (c), and (e) shall be computed at the annual rate established under section 6621(a)(2) of the Internal Revenue Code of 1986 (26 U.S.C. 6621(a)(2)).

In order to maintain consistency between CAS and FAR in matters relating to the administration of CAS, the Councils are revising the FAR as outlined below:

1. FAR 30.201–4(b)(1), the prescription for use of the FAR clause at 52.230–3, is revised to reflect the amendments promulgated by the CAS Board on June 14, 2007.

2. *FAR 52.230.* The following clauses are revised to reflect the amendments promulgated by the CAS Board on June 14, 2007 and June 14, 2000:

a. FAR 52.230–2, Cost Accounting Standards.

b. FAR 52.230–3, Disclosure and Consistency of Cost Accounting Practices.

c. FAR 52.230–5, Cost Accounting Standards—Educational Institution.

3. FAR 52.230–1, Cost Accounting Standards Notices and Certification, is revised to reflect the amendments promulgated by the CAS Board on June 14, 2007.

4. FAR 52.230–4, Consistency of Cost Accounting Practices, is revised to maintain consistency with all other CAS clauses in specifying the rate to be used to compute interest on overpayments by the Government.

5. FAR 52.230–3(a)(3)(ii) is revised to correctly reference 48 CFR 9903.201–6(c), Desirable change.

This is not a significant regulatory action and, therefore, was not subject to review under Section 6(b) of Executive Order 12866, Regulatory Planning and Review, dated September 30, 1993. This rule is not a major rule under 5 U.S.C. 804.

B. Regulatory Flexibility Act

The interim rule is not expected to have a significant economic impact on a substantial number of small entities within the meaning of the Regulatory Flexibility Act, 5 U.S.C. 601, *et seq.*, because contracts and subcontracts awarded to small businesses are exempt from the Cost Accounting Standards. Therefore, an Initial Regulatory Flexibility Analysis has not been performed. The Councils will consider comments from small entities concerning the affected FAR Parts 30 and 52 in accordance with 5 U.S.C. 610. Interested parties must submit such comments separately and should cite 5 U.S.C 601, *et seq.* (FAC 2005–27, FAR case 2007–002), in correspondence.

C. Paperwork Reduction Act

The Paperwork Reduction Act does not apply because the changes to the FAR do not impose information collection requirements that require the approval of the Office of Management and Budget under 44 U.S.C. 3501, *et seq.*

D. Determination to Issue an Interim Rule

A determination has been made under the authority of the Secretary of Defense (DoD), the Administrator of General Services (GSA), and the Administrator of the National Aeronautics and Space Administration (NASA) that urgent and compelling reasons exist to promulgate this interim rule without prior opportunity for public comment. This action is necessary because Federal Acquisition Regulation Part 30, Cost Accounting Standards, describes policies and procedures for applying the Cost Accounting Standards Board (CASB) rules and regulations (48 CFR Chapter 99 (FAR Appendix). Without this interim rule, FAR Part 30 is inconsistent with the Cost Accounting Standards that it is to describe. However, pursuant to Public Law 98–577 and FAR 1.501, the Councils will consider public comments received in response to this interim rule in the formation of the final rule.

List of Subjects in 48 CFR Parts 30 and 52

Government procurement.

Dated: September 9, 2008.

Al Matera,

Director, Office of Acquisition Policy.

■ Therefore, DoD, GSA, and NASA amend 48 CFR parts 30 and 52 as set forth below:

■ 1. The authority citation for 48 CFR parts 30 and 52 continues to read as follows:

Authority: 40 U.S.C. 121(c); 10 U.S.C. chapter 137; and 42 U.S.C. 2473(c).

PART 30—COST ACCOUNTING STANDARDS ADMINISTRATION

30.201–4 [Amended]

■ 2. Amend section 30.201–4 in paragraph (b)(1) by removing ''$500,000'' and adding ''$650,000'' in its place.

PART 52—SOLICITATION PROVISIONS AND CONTRACT CLAUSES

52.230–1 [Amended]

■ 3. Amend section 52.230–1 by revising the date of the provision to read ''(OCT 2008)'', and by removing from I. Disclosure Statement—Cost Accounting Practices and Certification, in paragraph (a) ''$500,000'' and adding ''$650,000'' in its place.

52.230–2 [Amended]

■ 4. Amend section 52.230–2 by—

■ a. Revising the date of the clause to read ''(OCT 2008)'';

■ b. Removing from paragraph (a)(5) ''6621'' and adding ''6621(a)(2)'' in its place each time it appears; and

■ c. Removing from paragraph (d) ''$500,000'' and adding ''$650,000'' in its place.

■ 5. Amend section 52.230–3 by—

■ a. Revising the date of the clause;

■ b. Removing from paragraph (a)(3)(ii) ''9903.201–6(b)'' and adding ''9903.201–6(c)'' in its place;

■ c. Revising the second sentence of paragraph (a)(4); and

■ d. Removing from paragraph (d)(2) ''$500,000'' and adding ''$650,000'' in its place.

■ The revised text reads as follows:

52.230–3 Disclosure and Consistency of Cost Accounting Practices.

* * * * *

DISCLOSURE AND CONSISTENCY OF COST ACCOUNTING PRACTICES (OCT 2008)

(a) * * *

(4) * * * Such adjustment shall provide for recovery of the increased costs to the United States together with interest thereon computed at the annual rate established under section 6621(a)(2) of the Internal Revenue Code of 1986 (26 U.S.C. 6621(a)(2)), from the time the payment by the United States was made to the time the adjustment is effected.

* * * * *

52.230–4 [Amended]

■ 6. Amend section 52.230–4 by revising the date of the clause date to read ''(OCT 2008)''; and removing ''6621'' and adding ''6621(a)(2)'' in its place each time it appears.

52.230–5 [Amended]

■ 7. Amend section 52.230–5 by—

■ a. Revising the date of the clause date to read ''(OCT 2008)'';

■ b. Removing from paragraph (a)(5) ''6621'' and adding ''6621(a)(2)'' in its place each time it appears; and

■ c. Removing from paragraph (d)(2) ''$500,000'' and adding ''$650,000'' in its place.

[FR Doc. E8–21367 Filed 9–16–08; 8:45 am]

BILLING CODE 6820–EP–S

DEPARTMENT OF DEFENSE

GENERAL SERVICES ADMINISTRATION

NATIONAL AERONAUTICS AND SPACE ADMINISTRATION

48 CFR Parts 30 and 52

[FAC 2005–27; FAR Case 2006–004; Item XII; Docket 2008–0001; Sequence 14]

RIN 9000–AK58

Federal Acquisition Regulation; FAR Case 2006–004, CAS Administration

AGENCIES: Department of Defense (DoD), General Services Administration (GSA), and National Aeronautics and Space Administration (NASA).

ACTION: Final rule.

SUMMARY: The Civilian Agency Acquisition Council and the Defense Acquisition Regulations Council (Councils) have agreed to adopt a proposed rule, published in the **Federal Register** at 71 FR 58338, October 3, 2006, as a final rule, with minor changes. The rule amends the Federal Acquisition Regulation (FAR) to implement revisions to the regulations related to the administration of the Cost Accounting Standards (CAS) as they pertain to contracts with foreign concerns, including United Kingdom (U.K.) concerns.

DATES: *Effective Date:* October 17, 2008.

FOR FURTHER INFORMATION CONTACT: For clarification of content, contact Mr. Edward Chambers, at (202) 501–3221. For information pertaining to status or publication schedules, contact the Regulatory Secretariat at (202) 501–4755. Please cite FAC 2005–27, FAR case 2006–004.

SUPPLEMENTARY INFORMATION:

A. Background

The Councils published a proposed rule in the **Federal Register** at 71 FR 58338, October 3, 2006, to maintain consistency between CAS and FAR in matters relating to disclosure requirements and the administration of CAS for contracts awarded to foreign concerns, including U.K. concerns.

This proposed rule was issued in response to the Cost Accounting Standards Board's interim rule (70 FR 29457, May 23, 2005) (finalized without change at 72 FR 32546, June 13, 2007), revising the applicability of CAS to U.K. contracts and subcontracts.

The Councils received no comments on the proposed rule and have adopted the proposed rule as a final rule with minor changes. The minor changes to 30.201–4(c) clarify that clause 52.230–4 need not be included in contracts with foreign concerns otherwise exempt from CAS coverage, and that foreign concerns do not include foreign governments, or their agents or instrumentalities.

This is not a significant regulatory action and, therefore, was not subject to review under Section 6(b) of Executive Order 12866, Regulatory Planning and Review, dated September 30, 1993. This rule is not a major rule under 5 U.S.C. 804.

B. Regulatory Flexibility Act

The Department of Defense, the General Services Administration, and the National Aeronautics and Space Administration certify that this final rule will not have a significant economic impact on a substantial number of small entities within the meaning of the Regulatory Flexibility Act, 5 U.S.C. 601, *et seq.*, because all small businesses are exempt from CAS.

C. Paperwork Reduction Act

The Paperwork Reduction Act does not apply because the changes to the FAR do not impose information collection requirements that require the approval of the Office of Management and Budget under 44 U.S.C. 3501, *et seq.*

List of Subjects in 48 CFR Parts 30 and 52

Government procurement.

Dated: September 9, 2008.

Al Matera,

Director, Office of Acquisition Policy.

■ Therefore, DoD, GSA, and NASA amend 48 CFR parts 30 and 52 as set forth below:

■ 1. The authority citation for 48 CFR parts 30 and 52 continues to read as follows:

Authority: 40 U.S.C. 121(c); 10 U.S.C. chapter 137; and 42 U.S.C. 2473(c).

PART 30—COST ACCOUNTING STANDARDS ADMINISTRATION

■ 2. Amend section 30.201–4 by revising paragraph (c) to read as follows:

30.201–4 Contract clauses.

* * * * *

(c) *Disclosure and Consistency of Cost Accounting Practices for Contracts Awarded to Foreign Concerns.* The contracting officer shall insert the clause at FAR 52.230–4, Disclosure and Consistency of Cost Accounting Practices for Contracts Awarded to Foreign Concerns, in negotiated contracts with foreign concerns, unless the contract is otherwise exempt from CAS (see 48 CFR 9903.201–1). Such contracts are subject to CAS 401 and 402 under 48 CFR 9903.201–1(b)(4)(FAR Appendix). Foreign concerns do not include foreign governments or their agents or instrumentalities.

* * * * *

PART 52—SOLICITATION PROVISIONS AND CONTRACT CLAUSES

■ 3. Amend section 52.230–4 by revising the section heading, the clause heading and date, and the first, second, and fourth sentences of the clause to read as follows.

52.230–4 Disclosure and Consistency of Cost Accounting Practices for Contracts Awarded to Foreign Concerns.

* * * * *

DISCLOSURE AND CONSISTENCY OF COST ACCOUNTING PRACTICES FOR CONTRACTS AWARDED TO FOREIGN CONCERNS (OCT 2008).

The Contactor agrees that it will consistently follow the cost accounting practices disclosed on FORM CASB DS–1, or other disclosure form as permitted by 48 CFR 9903.202–1(e), in estimating, accumulating, and reporting costs under this contract, and comply with the requirements of CAS 401, Consistency in Estimating, Accumulating, and Reporting Costs, and CAS 402, Consistency in Allocating Costs Incurred for the Same Purpose. In the event the Contractor fails to follow such practices, or comply consistently with CAS 401 and 402, it agrees that the contract price shall be adjusted, together with interest, if such failure results in increased cost paid by the U.S. Government. * * * The Contractor agrees that the Disclosure Statement or other form permitted, pursuant to 48 CFR 9903.202–1(e) shall be available for inspection and use by authorized representatives of the United States Government.

(End of clause)

[FR Doc. E8–21365 Filed 9–16–08; 8:45 am]

BILLING CODE 6820–EP–S

DEPARTMENT OF DEFENSE

GENERAL SERVICES ADMINISTRATION

NATIONAL AERONAUTICS AND SPACE ADMINISTRATION

48 CFR Parts 37 and 52

[FAC 2005–27; FAR Case 2006–027; Item XIII;Docket 2007–0001; Sequence 5]

RIN 9000–AK54

Federal Acquisition Regulation; FAR Case 2006–027, Accepting and Dispensing of $1 Coin

AGENCIES: Department of Defense (DoD), General Services Administration (GSA), and National Aeronautics and Space Administration (NASA).

ACTION: Final rule.

SUMMARY: The Civilian Agency Acquisition Council and the Defense Acquisition Regulations Council (Councils) have agreed to adopt as final, with change, the interim rule amending the Federal Acquisition Regulation (FAR) to implement Section 104 of the Presidential $1 Coin Act of 2005. Section 104 requires that entities that operate any business on any premises owned or controlled by the United States be capable of accepting and dispensing $1 coins on January 1, 2008. Subsequent to this, Pub. L. 110–147 amended 31 U.S.C. 5112(p)(1)(A), to allow an exception from the $1 coin dispensing capability requirement for vending machines that do not receive currency denominations greater than $1.

DATES: *Effective Date*: September 17, 2008.

Applicability Date: This rule applies to all service contracts that involve business operations conducted in U.S. coins and currency, including vending machines, on any premises owned by the United States or under the control of any agency or instrumentality of the United States. The clause shall be placed in all such solicitations and contracts on and after the effective date of this rule. Those applicable contracts in existence before January 1, 2008, that do not already have the clause shall be modified to include the clause; those contracts that have the August 2007 edition of the clause shall be modified if the contractor requests, to include the newer version contained in this FAC, without requiring consideration from the contractor.

FOR FURTHER INFORMATION CONTACT: Mr. Michael Jackson, Procurement Analyst, at (202) 208–4949 for clarification of content. For information pertaining to status or publication schedules, contact the FAR Secretariat at (202) 501–4755. Please cite FAC 2005–27, FAR case 2006–027.

SUPPLEMENTARY INFORMATION:

A. Background

This final rule amends the FAR to implement the Presidential $1 Coin Act of 2005 (Pub. L. 109–145). The Presidential $1 Coin Act of 2005 requires the Secretary of the Treasury to mint and issue annually four new $1 coins bearing the likenesses of Presidents of the United States in the order of their service and to continue to mint and issue ''Sacagawea-design'' coins for circulation. In order to promote circulation of the coins, Section 104 of the Public Law also requires that Federal agencies take action so that, by January 1, 2008, entities that operate any business, including vending machines, on any premises owned by the United States or under the control of any agency or instrumentality of the United States, are capable of accepting and dispensing $1 coins and that the entities display notices of this capability on the business premises. Subsequent to the passage of the Presidential Coin Act, Pub. L. 110–147 amended 31 U.S.C. 5112(p)(1)(A), to allow an exception from the $1 coin dispensing capability requirement for vending machines that do not receive currency denominations greater than $1. This will require modification of existing covered contracts whose period of performance extends beyond the January 1, 2008 date in order to assure compliance with Section 104 of the Act, as well as compliance with Pub. L. 110–147.

DoD, GSA, and NASA published an interim rule in the **Federal Register** at 72 FR 46361, August 17, 2007. The 60-day comment period for the interim rule ended October 16, 2007. Three respondents provided comments. The comments are discussed below.

Public Comments

Comment 1: One respondent asked why does the FAR matrix show that 52.237–11 is applicable to R&D contracts and to A&E contracts?

R&D contracts and A&E contracts are usually paid by electronic funds transfer. There is usually no cash payment involved in such contracts. Therefore, why would contractors who provide R&D or A&E services have to be capable of accepting dollar coins?

Response: The inclusion of R&D and A&E contracts in the FAR matrix as applicable to 52.237–11 was an inadvertent error.

Comment 2: One respondent stated in order to implement these widespread and extensive changes to vending machines, our members simply need more time. Contrary to the statement contained in the **Federal Register** notice, this interim rule *does* have a significant economic impact. It is not accurate to state that ''receiving and dispensing the new coins as part of business operations should not add to workload or expense'' (72 FR 46361, August 17, 2007). Accordingly, we strongly encourage the Councils to account for both the workload and expense by extending the compliance date to July 1, 2008.

Response: Section 104 of the Presidential $1 Coin Act of 2005 (31 U.S.C. 5112(p)(1)), established the effective date for this provision to be January 1, 2008. The effect of this clause is merely to implement the provision of law. Notwithstanding, the provision of law cannot be modified under these circumstances without further consideration by Congress, who passed the provision of law. Pub. L. 110–147 amended section 5112(p)(1)(A) of title 31, U.S.C., to allow an exception from the $1 coin dispensing capability requirement for vending machines that do not receive currency denominations greater than $1. Thus, the exception of the law provides relief for those vending machines.

Comment 3: One respondent requested an amendment to the interim rule published in the **Federal Register**, August 17, 2007, amending 48 CFR 52 (Solicitation Provisions and Contract Clauses), Section 52.237–11 (Accepting and Dispensing of $1 Coin) to exempt vending machines on Federal property that do not accept currency denominations above $1 from the requirement to dispense dollar coins.

Response: The very intent of the statute is to require those businesses and instrumentalities operating on Federal property to be able to accept and dispense the $1 coin if that business or instrumentality is conducting a business whereby coins or currency is exchanged. However, Pub. L. 110–147 amended section 5112(p)(1)(A) of title

(Catalog of Federal Domestic Assistance No. 97.022, ''Flood Insurance.'')

Dated: June 15, 2011

Sandra K. Knight,

Deputy Federal Insurance and Mitigation Administrator, Mitigation, Department of Homeland Security, Federal Emergency Management Agency.

[FR Doc. 2011–17451 Filed 7–11–11; 8:45 am]

BILLING CODE 9110–12–P

FEDERAL COMMUNICATIONS COMMISSION

47 CFR Part 1

[WC Docket No. 07–245, GN Docket No. 09–51; FCC 11–50]

Implementation of Section 224 of the Act; A National Broadband Plan for Our Future

AGENCY: Federal Communications Commission.

ACTION: Final rule; announcement of effective date.

SUMMARY: The Federal Communications Commission published a document in the Federal Register that contained new information collection requirements. The Office of Management and Budget (OMB) gave approval for these information requirements contained in the Commission's Report and Order and Order on Reconsideration, Implementation of Section 224 of the Act; A National Broadband Plan for Our Future.

DATES: The final rules published at 76 FR 26620, May 9, 2011, including 47 CFR 1.1420, 1.1422, and 1.1424, are effective on July 12, 2011.

FOR FURTHER INFORMATION CONTACT: Jonathan Reel, Competition Policy Division, Wireline Competition Bureau, at (202) 418–0637, or via the Internet at *Jonathan.Reel@fcc.gov.*

SUPPLEMENTARY INFORMATION: The Federal Communications Commission has received OMB approval for the rules contained in information collection OMB Control No: 3060–1151, Pole Attachment Access Rules. The information collection was adopted in the Report and Order and Order on Reconsideration, Implementation of Section 224 of the Act; A National Broadband Plan for Our Future in WC Docket No. 07–245, GN Docket No. 09–51, which appears at 76 FR 26620, May 9, 2011. The effective date of the rules adopted in that Order was published as June 8, 2011, except for 47 CFR 1.1420, 1.1422 and 1.1424, which contain information collection requirements that would not be effective until approved by the Office of Management and Budget. Through this document, the Commission announces that it has received this approval (OMB Control No. 3060–1151, *Expiration Date:* December 31, 2011), and that 47 CFR 1.1420, 1.1422, and 1.1424 are effective on July 12, 2011.

Pursuant to the Paperwork Reduction Act of 1995, Public Law 104–13, an agency may not conduct or sponsor a collection of information unless it displays a currently valid control number. Notwithstanding any other provisions of law, no person shall be subject to any penalty for failing to comply with a collection of information subject to the Paperwork Reduction Act (PRA) that does not display a valid control number. Questions concerning the OMB control numbers and expiration dates should be directed to Cathy Williams, Federal Communications Commission, (202) 418–2918, or via the Internet at *Cathy.Williams@fcc.gov.*

Federal Communications Commission.

Bulah P. Wheeler,

Deputy Manager.

[FR Doc. 2011–17369 Filed 7–11–11; 8:45 am]

BILLING CODE 6712–01–P

OFFICE OF MANAGEMENT AND BUDGET

Office of Federal Procurement Policy

48 CFR Parts 9901 and 9903

Cost Accounting Standards: Change to the CAS Applicability Threshold for the Inflation Adjustment to the Truth in Negotiations Act Threshold

AGENCY: Cost Accounting Standards Board, Office of Federal Procurement Policy, Office of Management and Budget (OMB).

ACTION: Interim rule.

SUMMARY: The Office of Federal Procurement Policy (OFPP), Cost Accounting Standards (CAS) Board (Board), invites public comments concerning this interim rule revising the threshold for the application of CAS from ''$650,000'' to ''the Truth in Negotiations Act (TINA) threshold, as adjusted for inflation.'' The change is being made because the CAS applicability threshold is statutorily tied to TINA. The TINA threshold for obtaining cost or pricing data was recently adjusted for inflation to $700,000 in the Federal Acquisition Regulation (FAR), as required by the Ronald W. Reagan National Defense Authorization Act for Fiscal Year 2005. Until this interim change, the CAS applicability threshold was a stated dollar amount ($650,000) in the Code of Federal Regulations. This wording change will effectively revise the CAS threshold to $700,000 and cause future changes to the CAS applicability threshold to self-execute upon any changes to the TINA threshold as they are implemented in the FAR.

DATES: *Effective date:* August 11, 2011.

Comment date: Comments must be in writing and must be received by September 12, 2011.

ADDRESSES: All comments to this interim rule must be in writing. Electronic comments may be submitted in any one of three ways:

1. *Federal eRulemaking Portal:* Comments may be directly sent via *http://www.regulations.gov*—a Federal E-Government Web site that allows the public to find, review, and submit comments on documents that agencies have published in the **Federal Register** and that are open for comment. Simply type ''CAS–TINA Threshold'' (without quotation marks) in the Comment or Submission search box, click Go, and follow the instructions for submitting comments;

2. *E-mail:* Comments may be included in an e-mail message sent to *casb2@omb.eop.gov.* The comments may be submitted in the text of the e-mail message or as an attachment;

3. *Facsimile:* Comments may also be submitted via facsimile to (202) 395–5105; or

4. *Mail:* If you choose to submit your responses via regular mail, please mail them to: Office of Federal Procurement Policy, 725 17th Street, NW., Room 9013, Washington, DC 20503, ATTN: Raymond J. M. Wong. Due to delays caused by the screening and processing of mail, respondents are strongly encouraged to submit responses electronically.

Be sure to include your name, title, organization, postal address, telephone number, and e-mail address in the text of your public comment and reference ''CAS–TINA Threshold'' in the subject line irrespective of how you submit your comments. Comments received by the date specified above will be included as part of the official record. Comments delayed due to use of regular mail may not be considered.

Please note that all public comments received will be available in their entirety at *http://www.whitehouse.gov/omb/casb_index_public_comments/* and *http://www.regulations.gov* after the close of the comment period. Do not include any information whose disclosure you would object to.

FOR FURTHER INFORMATION CONTACT: Raymond J. M. Wong, Director, Cost Accounting Standards Board (telephone: 202–395–6805; e-mail: *Raymond_wong@omb.eop.gov*).

SUPPLEMENTARY INFORMATION:

A. Regulatory Process

Rules, Regulations and Standards issued by the Cost Accounting Standards Board (Board) are codified at 48 CFR chapter 99. The Office of Federal Procurement Policy (OFPP) Act, at 41 U.S.C. 1502(c) [formerly, 41 U.S.C. 422(g)], requires that the Board, prior to the establishment of any new or revised Cost Accounting Standard (CAS or Standard), complete a prescribed rulemaking process. The process generally consists of the following four steps:

1. Consult with interested persons concerning the advantages, disadvantages and improvements anticipated in the pricing and administration of Government contracts as a result of the adoption of a proposed Standard.
2. Promulgate an Advance Notice of Proposed Rulemaking (ANPRM).
3. Promulgate a Notice of Proposed Rulemaking (NPRM).
4. Promulgate a Final Rule.

The Board notes that the CAS applicability threshold in 48 CFR Chapter 99 (at 48 CFR 9901.306; 9903.201–1, .201–2, 201–3, and 201–4; and 9903.202–1) is not subject to the four-step process required by 41 U.S.C. 1502(c) [formerly, 41 U.S.C. 422(g)(1)] because it is not a Cost Accounting Standard. However, the Board elects to follow some of those requirements in the OFPP Act, at 41 U.S.C. 1502(c) [formerly, 41 U.S.C. 422(g)(1)], i.e., to consult with interested persons concerning the advantages, disadvantages, and improvements anticipated in the pricing and administration of Government contracts as a result of the adoption of any new or revised rule on the CAS applicability threshold, prior to its promulgation.

B. Background and Summary

The Office of Federal Procurement Policy (OFPP), Cost Accounting Standards Board (Board), is today releasing this interim rule to revise the Cost Accounting Standards (CAS) applicability threshold in 48 CFR chapter 99 from ''$650,000'' to ''the Truth in Negotiations Act (TINA) threshold, as adjusted for inflation (41 U.S.C. 1908) and (41 U.S.C. 1502(b)(1)(B))'', because of a revision to the Truth in Negotiations Act (TINA) threshold for the submission of cost or pricing data as adjusted for inflation by section 807 of the Ronald W. Reagan National Defense Authorization Act for Fiscal Year 2005 (Pub. L. 108–375) as incorporated into Federal Acquisition Regulation (FAR) 15.403–4(a)(1) by the Civilian Agency Acquisition Council and the Defense Acquisition Regulations Council on August 30, 2010 (at 75 FR 53129). By revising the CAS applicability threshold so that it directly references the FAR TINA threshold for the submission of cost or pricing data (rather than referencing a stated dollar amount), any future changes to the FAR TINA threshold will automatically apply to the CAS applicability threshold (thereby eliminating the need to revise this regulation to specify a different dollar amount).

Statutory Requirement for Inflation Adjustment of TINA Thresholds

Section 807 of the Ronald W. Reagan National Defense Authorization Act for Fiscal Year 2005 (Pub. L. 108–375) requires a periodic adjustment for inflation every five years to the acquisition related thresholds using the Consumer Price Index (CPI) for all urban consumers, except for the Davis-Bacon Act, Service Contract Act, and trade agreement thresholds. The threshold in TINA (10 U.S.C. 2306a(a)(1)(A)(i)) for the submission of cost or pricing data is one of the acquisition related thresholds adjusted for inflation by section 807. The Civilian Agency Acquisition Council and the Defense Acquisition Regulations Council (Councils) published a final rule in the **Federal Register** on August 30, 2010 (75 FR 53129) amending the FAR to implement section 807, including the TINA threshold at FAR 15.403–4, Requiring cost or pricing data (10 U.S.C. 2306a and 41 U.S.C. 3502 [formerly, 41 U.S.C. 254b]). This FAR final rule was effective October 1, 2010, and revised the TINA threshold from $650,000 to $700,000.

Statutory Requirement for Threshold for CAS Applicability

Section 26(f)(2(A) of the OFPP Act (41 U.S.C. 1502(b)(1)(B) [formerly, 41 U.S.C. 422(f)(2)(A)]) addresses the CAS applicability threshold. Section 822 of the 2006 National Defense Authorization Act (Pub. L. 109–163) amended 41 U.S.C. 1502(b)(1)(B) [formerly, 41 U.S.C. 422(f)(2)(A)] to tie the statutory CAS threshold to the threshold for compliance with the TINA requirement to submit cost or pricing data, as set forth in section 2306a(a)(1)(A)(i) of title 10, United States Code. The recent changes to the TINA threshold described above require identical changes to the CAS applicability threshold (i.e., from $650,000 to $700,000). To date, the CAS applicability threshold has been identified in the CAS Board rules as a stated dollar amount. To avoid repeated rulemakings in the future that would update the stated dollar amount, in order to keep the CAS applicability threshold tied to the TINA threshold, the Board is revising the CAS applicability threshold from a stated dollar amount (which has been ''$650,000'') to ''the Truth in Negotiations Act (TINA) threshold, as adjusted for inflation (41 U.S.C. 1908 and 41 U.S.C. 1502(b)(1)(B)).'' This revision makes any future changes to the CAS applicability threshold self-executing upon any changes that the FAR makes to the TINA threshold. Thus, because the FAR's TINA threshold is now $700,000, the CAS applicability threshold under this interim rule will be $700,000.

C. Paperwork Reduction Act

The Paperwork Reduction Act (44 U.S.C. chapter 35, Subtitle I) does not apply to this rulemaking because this rule imposes no additional paperwork burden on offerors, affected contractors and subcontractors, or members of the public which requires the approval of OMB under 44 U.S.C. 3501, *et seq.* The records required by this interim rule are those normally maintained by contractors and subcontractors who claim reimbursement of costs under government contracts.

D. Executive Order 12866, the Congressional Review Act, and the Regulatory Flexibility Act

Because the affected contractors and subcontractors are those who are already subject to CAS but for the increase in the CAS applicability threshold, the economic impact of this interim rule on contractors and subcontractors is expected to be minor. As a result, the Board has determined that this interim rule will not result in the promulgation of an ''economically significant rule'' under the provisions of Executive Order 12866, and that a regulatory impact analysis will not be required. For the same reason, the Administrator of the Office of Information and Regulatory Affairs has determined that this interim rule is not a ''major rule'' under the Congressional Review Act, 5 U.S.C. Chapter 8. Finally, this interim rule does not have a significant effect on a substantial number of small entities because small businesses are exempt from the application of the Cost Accounting Standards. Therefore, this interim rule does not require a regulatory flexibility analysis under the Regulatory Flexibility Act of 1980, 5 U.S.C. chapter 6.

E. Public Comments to This Interim Rulemaking

Interested persons are invited to provide input to this interim rule to revise the CAS applicability threshold from ''$650,000'' to ''the Truth in Negotiations Act (TINA) threshold, as adjusted for inflation (41 U.S.C. 1908 and 41 U.S.C. 1502(b)(1)(B))'' as a result of the periodic statutory adjustment of the TINA threshold for inflation. Respondents are encouraged to identify, comment and provide information on any issues that they believe are important to the subject. All comments must be in writing, and submitted via facsimile, by e-mail, or by any other means as instructed in the **ADDRESSES** section.

List of Subjects in 48 CFR Parts 9901 and 9903

Government procurement, cost accounting standards.

Daniel I. Gordon,

Chair, Cost Accounting Standards Boards.

For the reasons set forth in this preamble, Chapter 99 of Title 48 of the Code of Federal Regulations is amended as set forth below:

PART 9901—RULES AND PROCEDURES

■ 1. The authority citation for Part 9901 continues to read as follows:

Authority: Pub. L. 111–350, 124 Stat. 3677, 41 U.S.C. 1502.

■ 2. Revise section 9901.306 to read as follows:

9901.306 Standards applicability.

Cost Accounting Standards promulgated by the Board shall be mandatory for use by all executive agencies and by contractors and subcontractors in estimating, accumulating, and reporting costs in connection with pricing and administration of, and settlement of disputes concerning, all negotiated prime contract and subcontract procurements with the United States Government in excess of the Truth in Negotiations Act (TINA) threshold, as adjusted for inflation (41 U.S.C. 1908 and 41 U.S.C. 1502(b)(1)(B)), other than contracts or subcontracts that have been exempted by the Board's regulations.

PART 9903—CONTRACT COVERAGE

■ 3. The authority citation for Part 9903 continues to read as follows:

Authority: Pub. L. 111–350, 124 Stat. 3677, 41 U.S.C. 1502.

Subpart 9903.2—CAS Program Requirements

■ 4. Section 9903.201–1 is amended by revising paragraph (b)(2) to read as follows:

9903.201–1 CAS applicability.

* * * * *

(b) * * *

(2) Negotiated contracts and subcontracts not in excess of the Truth in Negotiations Act (TINA) threshold, as adjusted for inflation (41 U.S.C. 1908 and 41 U.S.C. 1502(b)(1)(B)). For purposes of this paragraph (b)(2), an order issued by one segment to another segment shall be treated as a subcontract.

* * * * *

■ 5. Section 9903.201–2 is amended by revising paragraphs (c)(3) and (5) to read as follows:

9903.201–2 Types of CAS coverage.

* * * * *

(c) * * *

(3) *Applicable standards.* Coverage for educational institutions requires that the business unit comply with all of the CAS specified in part 9905 that are in effect on the date of the contract award and with any CAS that become applicable because of later award of a CAS-covered contract. This coverage applies to business units that receive negotiated contracts in excess of the Truth in Negotiations Act (TINA) threshold, as adjusted for inflation (41 U.S.C. 1908 and 41 U.S.C. 1502(b)(1)(B)), except for CAS-covered contracts awarded to FFRDCs operated by an educational institution.

* * * * *

(5) *Contract clauses.* The contract clause at 9903.201–4(e) shall be incorporated in each negotiated contract and subcontract awarded to an educational institution when the negotiated contract or subcontract price exceeds the Truth in Negotiations Act (TINA) threshold, as adjusted for inflation (41 U.S.C. 1908 and 41 U.S.C. 1502(b)(1)(B)). For CAS-covered contracts awarded to an FFRDC operated by an educational institution, however, the full or modified CAS contract clause specified at 9903.201–4(a) or (c), as applicable, shall be incorporated.

* * * * *

■ 6. Section 9903.201–3 is amended in paragraph (a)(2) under the provision heading, ''Cost Accounting Standards Notices and Certification'', by revising the provision date and paragraph (a) of Part I of the provision to read as follows:

9903.201–3 Solicitation provisions.

* * * * *

Cost Accounting Standards Notices and Certification (JUL 2011)

* * * * *

I. Disclosure Statement—Cost Accounting Practices and Certification

(a) Any contract in excess of the Truth in Negotiations Act (TINA) threshold, as adjusted for inflation (41 U.S.C. 1908 and 41 U.S.C. 1502(b)(1)(B)), resulting from this solicitation, except for those contracts which are exempt as specified in 9903.201–1.

* * * * *

■ 7. Section 9903.201–4 is amended:

■ a. In paragraph (a)(2) under the clause heading, ''Cost Accounting Standards'', by revising the clause date and paragraph (d) of the clause.

■ b. By revising paragraph (c)(1); and in paragraph (c)(2) under the clause heading ''Disclosure and Consistency of Cost Accounting Practices'', by revising the clause date and paragraph (d)(2) of the clause.

■ c. In paragraph (e)(2) under the clause heading, ''Cost Accounting Standards—Educational Institutions'', by revising the clause date and paragraph (d)(2) of the clause; and in paragraph (f)(2) under the clause heading, ''Cost Accounting Practices—Foreign Concerns'', by revising the clause date and paragraph (d)(2) of the clause .

9903.201–4 Contract clauses.

(a) * * *

(2) * * *

Cost Accounting Standards (JUL 2011)

* * * * *

(d) The contractor shall include in all negotiated subcontracts which the Contractor enters into, the substance of this clause, except paragraph (b), and shall require such inclusion in all other subcontracts, of any tier, including the obligation to comply with all CAS in effect on the subcontractor's award date or if the subcontractor has submitted cost or pricing data, on the date of final agreement on price as shown on the subcontractor's signed Certificate of Current Cost or Pricing Data. If the subcontract is awarded to a business unit which pursuant to 9903.201–2 is subject to other types of CAS coverage, the substance of the applicable clause set forth in 9903.201–4 shall be inserted. This requirement shall apply only to negotiated subcontracts in excess of the Truth in Negotiations Act (TINA) threshold, as adjusted for inflation (41 U.S.C. 1908 and 41 U.S.C. 1502(b)(1)(B)), except that the requirement shall not apply to negotiated subcontracts otherwise exempt from the requirement to include a CAS clause as specified in 9903.201–1.

(End of clause)

* * * * *

(c) *Disclosure and Consistency of Cost Accounting Practices.* (1) The contracting officer shall insert the clause set forth below, Disclosure and Consistency of Cost Accounting Practices, in negotiated contracts when the contract amount is over the Truth in Negotiations Act (TINA) threshold, as adjusted for inflation (41 U.S.C. 1908 and 41 U.S.C. 1502(b)(1)(B)), but less than $50 million, and the offeror certifies it is eligible for and elects to use modified CAS coverage (*see* 9903.201–2, unless the clause prescribed in paragraph (d) of this subsection is used).

(2) * * *

Disclosure and Consistency of Cost Accounting Practices (JUL 2011)

* * * * *

(d) * * *

(2) This requirement shall apply only to negotiated subcontracts in excess of the Truth in Negotiations Act (TINA) threshold, as adjusted for inflation (41 U.S.C. 1908 and 41 U.S.C. 1502(b)(1)(B)).

* * * * *

(End of clause)

* * * * *

(e) * * *

(2) * * *

Cost Accounting Standards—Education Institutions (JUL 2011)

* * * * *

(d) * * *

(2) This requirement shall apply only to negotiated subcontracts in excess of the Truth in Negotiations Act (TINA) threshold, as adjusted for inflation (41 U.S.C. 1908 and 41 U.S.C 1502(b)(1)B)).

* * * * *

(End of clause)

(f) * * *

(2) * * *

Disclosure and Consistency of Cost Accounting Practices—Foreign Concerns (JUL 2011)

* * * * *

(d) * * *

(2) This requirement shall apply only to negotiated subcontracts in excess of the Truth in Negotiations Act (TINA) threshold, as adjusted for inflation (41 U.S.C. 1908 and 41 U.S.C. 1502(b)(1)(B)).

* * * * *

(End of clause)

* * * * *

■ 8. Section 9903.202–1 is amended by revising paragraphs (c) introductory text, (f)(2)(i), and (f)(3)(i) through (iii) to read as follows:

§ 9903.202–1 General requirements.

* * * * *

(c) When a Disclosure Statement is required, a separate Disclosure Statement must be submitted for each segment whose costs included in the total price of any CAS-covered contract or subcontract exceed the Truth in Negotiations Act (TINA) threshold, as adjusted for inflation (41 U.S.C. 1908 and 41 U.S.C. 1502(b)(1)(B)) unless

* * * * *

(f) * * *

(2) * * *

(i) Any business unit of an educational institution that is selected to receive a CAS-covered contract or subcontract in excess of the Truth in Negotiations Act (TINA) threshold, as adjusted for inflation (41 U.S.C. 1908 and 41 U.S.C. 1502(b)(1)(B)), and is part of a college or university location listed in Exhibit A of Office of Management and Budget (OMB) Circular A–21 shall submit a Disclosure Statement before award. A Disclosure Statement is not required; however, if the listed entity can demonstrate that the net amount of Federal contract and financial assistance awards received during its immediately preceding cost accounting period was less than $25 million.

* * * * *

(3) * * *

(i) For business units that are selected to receive a CAS-covered contract or subcontract in excess of the Truth in Negotiations Act (TINA) threshold, as adjusted for inflation (41 U.S.C. 1908 and 41 U.S.C. 1502(b)(1)(B)), and are part of the first 20 college or university locations (*i.e.,* numbers 1 through 20) listed in Exhibit A of OMB Circular A–21, Disclosure Statements shall be submitted within six months after the date of contract award.

(ii) For business units that are selected to receive a CAS-covered contract or subcontract in excess of the Truth in Negotiations Act (TINA) threshold, as adjusted for inflation (41 U.S.C. 1908 and 41 U.S.C. 1502(b)(1)(B)), and are part of a college or university location that is listed as one of the institutions numbered 21 through 50, in Exhibit A of OMB Circular A–21, Disclosure Statements shall be submitted during the six month period ending twelve months after the date of contract award.

(iii) For business units that are selected to receive a CAS-covered contract or subcontract in excess of the Truth in Negotiations Act (TINA) threshold, as adjusted for inflation (41 U.S.C. 1908 and 41 U.S.C. 1502(b)(1)(B)), and are part of a college or university location that is listed as one of the institutions numbered 51 through 99, in Exhibit A of OMB Circular A–21, Disclosure Statements shall be submitted during the six month period ending eighteen months after the date of contract award.

* * * * *

[FR Doc. 2011–16846 Filed 7–11–11; 8:45 am]

BILLING CODE P

DEPARTMENT OF TRANSPORTATION

Pipeline and Hazardous Materials Safety Administration

49 CFR Part 190

[Docket No. PHMSA–2011–0161]

Pipeline Safety; Enforcement Proceedings Involving an Informal Hearing

AGENCY: Pipeline and Hazardous Materials Safety Administration (PHMSA); DOT.

ACTION: General policy statement; informal hearing process.

SUMMARY: PHMSA is issuing this document to notify operators of natural gas and hazardous liquid pipeline facilities of the creation of a dedicated ''Presiding Official'' for informal pipeline enforcement hearings and the process operators can expect when requesting an informal hearing. Hearings in pipeline safety enforcement cases are conducted by a hearing officer in accordance with certain procedures designed to ensure a fair and impartial decision on the merits. This document explains those procedures and includes a description of the dedicated hearing officer's roles and responsibilities, the process for requesting a hearing, and the manner in which a case will proceed once a hearing has been requested.

FOR FURTHER INFORMATION CONTACT: Sherri Pappas, Deputy Chief Counsel, at 202–366–4400. Information about PHMSA may be found at *http://phmsa.dot.gov.*

SUPPLEMENTARY INFORMATION:

I. Background

The Federal safety statute and regulations for natural gas and hazardous liquid pipeline facilities provide a description of the enforcement authority and sanctions exercised by the Associate Administrator for achieving and maintaining pipeline safety. Pursuant to chapter 601 of Title 49, United States Code, after notice and an opportunity for a hearing, the Associate Administrator may order an operator of a pipeline facility to take necessary corrective action, including revisions to

Federal Register / Vol. 76, No. 154 / Wednesday, August 10, 2011 / Rules and Regulations 49365

List of Subjects in 47 CFR Part 73

Radio, Radio broadcasting.

Federal Communications Commission.

James D. Bradshaw,

Deputy Chief, Audio Division, Media Bureau.

Rule Changes

For the reasons discussed in the preamble, the Federal Communications Commission amends 47 CFR part 73 as follows:

PART 73—RADIO BROADCAST SERVICES

■ 1. The authority citation for part 73 continues to read as follows:

Authority: 47 U.S.C. 154, 303, 334, 336, and 339.

§ 73.202 [Amended]

■ 2. Section 73.202(b), the Table of FM Allotments under Oregon, is amended by adding Gearhart, Channel 227A, by removing Channel *251C1 at Madras, by adding Channel *243C1 at Madras, and by adding Manzanita, Channel 248C3.

[FR Doc. 2011–20340 Filed 8–9–11; 8:45 am]

BILLING CODE 6712–01–P

OFFICE OF MANAGEMENT AND BUDGET

Office of Federal Procurement Policy

48 CFR Part 9903

Cost Accounting Standards: Elimination of the Exemption From Cost Accounting Standards for Contracts and Subcontracts Executed and Performed Entirely Outside the United States, Its Territories, and Possessions

AGENCY: Office of Management and Budget (OMB), Office of Federal Procurement Policy (OFPP), Cost Accounting Standards Board (Board).

ACTION: Final rule.

SUMMARY: The Office of Federal Procurement Policy (OFPP), Cost Accounting Standards (CAS) Board, is publishing a final rule to eliminate the exemption from regulations regarding Cost Accounting Standards for contracts executed and performed entirely outside the United States, its territories, and possessions.

DATES: *Effective Date:* October 11, 2011.

FOR FURTHER INFORMATION CONTACT: Raymond J. M. Wong, Director, Cost Accounting Standards Board (*telephone:* 202–395–6805; *e-mail: Raymond_wong@omb.eop.gov*).

SUPPLEMENTARY INFORMATION:

A. Regulatory Process—Changes to 48 CFR Part 9903

The CAS Board's regulations and Standards are codified at 48 CFR chapter 99. This notice concerns the amendment of a CAS Board regulation other than a Standard, and as such is not subject to the statutorily prescribed rulemaking process for the promulgation of a Standard at 41 U.S.C. 1502(c) [formerly, 41 U.S.C. 422(g)]. The document being published today is a Final Rule.

B. Background and Summary

The Office of Federal Procurement Policy (OFPP), Cost Accounting Standards (CAS) Board, is publishing a final rule to eliminate the exemption at 48 CFR 9903.201–1(b)(14) from the Cost Accounting Standards for contracts executed and performed entirely outside the United States, its territories, and possessions (hereafter referred to as the ''(b)(14) overseas exemption'').

The CAS Board is publishing a final rule which eliminates the (b)(14) overseas exemption from CAS for contracts and subcontracts executed and performed entirely outside the United States, its territories, and possessions.

Statutory Requirement

Section 823(a) of the Duncan Hunter National Defense Authorization Act for Fiscal Year 2009 (NDAA FY 2009) required the CAS Board to: ''(1) Review the inapplicability of the cost accounting standards, in accordance with existing exemptions, to any contract and subcontract that is executed and performed outside the United States when such a contract or subcontract is performed by a contractor that, but for the fact that the contract or subcontract is being executed and performed entirely outside the United States, would be required to comply with such standards; and (2) determine whether the application of the standards to such a contract and subcontract (or any category of such contracts and subcontracts) would benefit the Government.'' Section 823 further required the CAS Board to publish a request for information and to submit to the appropriate committees of Congress a report containing: (1) Any proposed revision to the CAS regulations as a result of the review and a copy of any proposed rulemaking implementing the revision or (2) if no revision and rulemaking are proposed, a detailed justification for such decision.

History of the (b)(14) Overseas Exemption

The (b)(14) overseas exemption was first promulgated in 1973 at Section 3–1204 of the Armed Services Procurement Regulation (ASPR). See Defense Procurement Circular No. 115 (dated September 24, 1973). The reason given for promulgation of the (b)(14) overseas exemption was that the underlying authority for CAS, Section 2168 of the Defense Production Act (DPA), was applicable to the United States, its Territories and possessions, and the District of Columbia (Section 2163 of the DPA). The (b)(14) overseas exemption was intended to eliminate confusion that had existed at that time over the applicability of CAS outside the United States.

In 1980, the CAS Board ceased to exist under the DPA. Congress reestablished the CAS Board in 1988 under Section 22 of the OFPP Act, 41 U.S.C. 1501 [formerly, 41 U.S.C. 422]. Unlike the DPA, under the OFPP Act, CAS is not limited in applicability to the United States. However, in 1991, the CAS Board, after reviewing the rules and regulations applicable to the administration of CAS, opted to retain the (b)(14) overseas exemption.

The CAS Board later sought to reevaluate the (b)(14) overseas exemption. On September 13, 2005, the CAS Board published a notice seeking comment on the Staff Discussion Paper (SDP) discussing the appropriateness of continuing the exemption (70 FR 53977). Only three public comments were received, all of which supported retaining the exemption. The CAS Board took no further action at that time and published a notice discontinuing the review on February 13, 2008 (73 FR 8259).

In response to Section 823(a) of NDAA FY 2009, the CAS Board published on April 23, 2009, another notice requesting information on six general questions regarding the (b)(14) overseas exemption (74 FR 18491). In addition to this notice, the CAS Board requested assessments directly from three Federal agencies with significant volume of contracts performed outside of the United States—the Department of Defense (DOD), the Department of State (DOS) and the United States Agency for International Development (USAID). After reviewing the comments received from the notice and the assessments of the three Federal agencies, the CAS Board published a Notice of Proposed Rule (NPR) on October 20, 2010, proposing to eliminate the (b)(14) overseas exemption (75 FR 64684). A copy of the proposed rule was provided to the appropriate committees of Congress in accordance with Section 823.

Conclusions

The CAS Board has considered the comments received in response to the NPR, which are available to the public on the CAS Board's Web site at *http://www.whitehouse.gov/omb/casb_index_public_comments/* and *http://www.regulations.gov,* and has concluded that the (b)(14) overseas exemption should be eliminated. Although the CAS Board's responses to specific comments received are discussed later in this notice, the principal reasons for eliminating the exemptions are as follows:

(1) The statutory basis originally used to justify the (b)(14) overseas exemption no longer exists. Absent such justification, the CAS Board must give deference to the existing CAS applicability statutes as mandatory for use by all executive agencies and by contractors and subcontractors in estimating, accumulating, and reporting costs in connection with pricing and administration of, and settlement of disputes concerning, all negotiated prime contract and subcontract procurements with the United States (41 U.S.C. 1502(b)(1)(B) [formerly, 41 U.S.C. 422(f)(2)(A)]).

(2) There is not an accounting basis for the (b)(14) overseas exemption. The place of contract execution and performance is not germane to the fundamental requirements and practices set forth in CAS used to measure, assign, and allocate the costs of contract performance.

(3) The CAS Board was not persuaded that the imposition of CAS in situations where the (b)(14) overseas had been applied would create hardships for Federal agencies, prime contractors, and subcontractors, particularly in view of mitigating factors. Foremost among these factors would be that a contractor would still have available the exemption at 48 CFR 9903.201–1(b)(4) which states ''Contracts and subcontracts with foreign governments or their agents or instrumentalities or, insofar as the requirements of CAS other than 9904.401 and 9904.402 are concerned, any contract or subcontract awarded to a foreign concern.'' In the CAS Board's view, the imposition of CAS 401, ''Consistency in Estimating, Accumulating and Reporting Costs,'' and CAS 402, ''Consistency in Allocating Costs Incurred for the Same Purpose,'' are the minimal requirements necessary to meet the requirements of CAS. In the Board's view, these minimal requirements are not substantively different from what is already imposed under the Federal Acquisition Regulation (FAR).

C. Public Comments to the Notice of Proposed Rule

In response to the NPR, the CAS Board received a total of five comments from a Federal agency, consultant, public interest group, and industry and trade associations. The comments, which were all considered by the Board in its deliberations, reflected a difference of views on whether to retain or eliminate the (b)(14) overseas exemption. They are summarized and addressed in this section, grouped by common themes.

1. *Comment:* Two respondents supported the CAS Board's proposed rule to eliminate the (b)(14) overseas exemption.

Response: The CAS Board noted the agreement.

2. *Comment:* One respondent believed that eliminating the (b)(14) overseas exemption will have a very narrow impact in terms of the number of foreign concerns which will become subject to the consistency requirements of CAS 401 and 402, respectively, consistency in estimating, accumulating and reporting costs, and consistency in allocating costs incurred for the same purpose. Contract savvy foreign concerns will attempt to enter into contracts where another CAS exemption is applicable. To the contrary, another respondent opined that there is a misconception that some other CAS exemptions are applicable if the (b)(14) overseas exemption is eliminated. The respondent opined that the other CAS exemptions are of limited applicability, and that even the limited applicability of CAS 401 and 402 would be a deterrent to foreign concerns in accepting subcontracts to satisfy the U.S. contractors' offset requirements. A greater deterrent to foreign concerns are the requirements to submit a CAS Disclosure Statement and notifications of changes in accounting practice with cost impact analyses.

Response: The imposition of CAS 401 and CAS 402 are not likely to be a hardship, since they are already substantively applied by the FAR. The threshold for submitting a CAS Disclosure Statement was significantly increased in 2000 to $50 million in recognition that this requirement should be applied to levels of contracting activity where a more formal disclosure was appropriate.

3. *Comment:* One respondent noted that there is an obvious accounting basis for retaining the (b)(14) overseas exemption, specifically, the differences between the fundamental accounting principles between U.S. GAAP (Generally Accepted Accounting Principles) and IFRS (International Financial Reporting Standards).

Response: The CAS Board does not believe differences between GAAP and IFRS are relevant to the question of extending the (b)(14) overseas exemption.

4. *Comment:* Two respondents noted that the costs of CAS administration would exceed any benefits achieved from requiring CAS. One respondent noted that essentially no aspect of the CAS rulemaking during the past 37 years has received any input from entities otherwise exempt from all CAS requirements. Another respondent noted that foreign concerns will have difficulty understanding and interpreting the CAS Disclosure Statement, which is published only in English. The respondent also noted that not only foreign concerns will have administrative costs in implementing and administering CAS for foreign concerns; the Government, and higher tier subcontractors and prime contractors with foreign concerns as subcontractors will also have administrative costs associated with administering the CAS Disclosure Statement process, as well as the cost impacts for cost accounting changes and CAS non-compliances.

Response: For reasons previously discussed, the CAS Board does not agree that the administrative costs of essentially applying CAS 401 and CAS 402 will exceed the benefits received by the taxpayers. There presently are foreign concerns, unable to take advantage of the (b)(14) overseas exemption, that are able to comply with the applicable requirements of CAS. Moreover, the same requirements are in the FAR.

5. *Comment:* Two respondents raised concerns about an unintended consequence of imposing CAS on foreign concerns: the negative impact on exports which would result. The expressed concern was that the U.S. aerospace export sales would be endangered. The respondents stated that U.S. aerospace export sales have been enabled by the purchase of parts supplied by foreign concern subcontractors who are currently exempted from CAS, presumably by the (b)(14) overseas exemption. The respondents argued that contractors must satisfy offset requirements in order to make the sale to the foreign country. Offset requirements are host country industrial participation requirements imposed by the foreign host country as a condition of the contract. Contractors establish relationships with foreign subcontractors to develop potential offset placements to position themselves

for future contract awards for export sales. Such relationships are established and developed with strategic placement of subcontracts for contracts with the U.S. in anticipation of new export sales opportunities and related offset obligations.

Response: Based on these comments, the CAS Board sought additional guidance on the matter of exports. Aerospace sales to foreign countries are made through either foreign military sales (FMS) contracts with the U.S. Government as the party to the contract with the contractor or contracts executed directly between the foreign host country and the U.S. contractor as a ''commercial sale.'' The CAS requirements are only imposed on sales to the U.S. Government (in this case, to the FMS contracts), and not on a commercial sale made directly with the foreign host country. U.S. Government funded FMS contracts do not have offset requirements, while foreign government funded FMS contracts may have offset requirements. In those instances when there are offset requirements in FMS contracts, the imposition of CAS 401 and CAS 402, if applicable, are not likely to be a hardship, since they are already substantively applied by the FAR for subcontracts. See the responses to Comments 2 and 4.

6. *Comment:* One respondent stated that the other CAS exemptions or applicability requirements are not applicable to foreign concerns, generally. Sealed bidding would not be effective for subcontracting to meet offset requirements where discussions are likely to be necessary. The CAS applicability threshold of $650,000 (soon to be adjusted to $700,000) still leaves many foreign concern subcontractors subject to it. The small business exemption from CAS only applies to U.S. businesses. While contracts and subcontracts with foreign governments or their instrumentalities are exempted from CAS, other foreign concerns are still subject to CAS 401 and 402, which would be a deterrent to foreign concerns accepting subcontracts to satisfy offset for U.S. contractors when they do not have CAS requirements for subcontracts with non-U.S. contractors. The larger deterrent for the larger subcontractors (who exceed the $50 million CAS Disclosure Statement filing threshold) is the Disclosure Statement filing requirement. The CAS exemption applicable when the price is set by law or regulation is irrelevant to foreign concern subcontracts for aerospace products. The CAS exemption for firm-fixed price (FFP) contracts, fixed price contracts with economic price adjustments, and contracts and subcontracts for commercial items has limited applicability. The CAS exemption for the NATO PHM Ship program has limited applicability, and is not germane to foreign concern subcontracts for aerospace products. The limited technical capabilities of the industrial bases of many countries with offset requirements make competition not tenable. Even in the most competitive emerging markets, i.e., India, South Korea, Saudi Arabia, and Turkey, competition in the award of subcontracts will be severely limited by the industrial base, limiting the applicability of the CAS exemption for FFP contracts and subcontracts awarded on the basis of adequate price competition without cost or pricing data.

Response: Whether or not another CAS exemption might apply, aside from the previously discussed exemption at 48 CFR 9903.201–1(b)(4), is not germane to the question of eliminating the (b)(14) overseas exemption. While it is likely that other exemptions might apply in certain situations, it is recognized that some exemptions would never apply. However, finding an alternative exemption that yields the same result as the (b)(14) overseas exemption is not the objective of this assessment. The relevant question is whether, given the absence of conditions which created the exemption in the first place, there are other sufficient reasons for retaining the exemption. As previously stated, the CAS Board has not been persuaded that there are other sufficient reasons for retaining the exemption.

7. *Comment:* A respondent noted that the CAS waiver process is not suitable in the foreign concern subcontracting context. A CAS waiver must be requested by an agency, rather than the contractor, considering the needs of the agency with supporting justification from the perspective of the agency. The waiver process is not conducive to the offset obligations of the contractor as the offset requirement may be contrary to the requirement to establish other sources to avoid a waiver in the future.

Response: The CAS Board agrees that the waiver process may be arduous. However, given that only CAS 401 and CAS 402 would be imposed in the absence of the (b)(14) overseas exemption, the CAS Board believes it is unlikely that a CAS waiver would be requested.

8. *Comment:* A respondent opined that the impact from the elimination of the (b)(14) overseas exemption on foreign concern subcontractors is understated. The respondent stated the impact of eliminating (b)(14) overseas exemption will be most acute on foreign concern subcontractors, and the prime contractors and higher-tier subcontractors who have relied on the that exemption historically. Foreign concern subcontractor usage data is not readily available because there is no requirement to capture it. While everyone believes subcontractors will be affected, the scope of the impact is unknown.

Response: The CAS Board understands that the visibility into subcontracting activities of a prime contractor is limited, particularly foreign concern subcontractors. The CAS Board notes that this condition has also been given as reasoning for eliminating the (b)(14) overseas exemption. As previously discussed, the CAS Board believes there will be mitigating factors that lessen the impact on foreign concern subcontractors. If this proves to be unfounded, then the CAS Board can reconsider the (b)(14) overseas exemption.

9. *Comment:* Two respondents stated that the elimination of the (b)(14) overseas exemption is contrary to U.S. export and foreign economic development policies. There is a long standing belief that export of defense industry products benefit the US, and laws and regulations reflect that. NDAA FYs 1988 and 1989 (respectively, Pub. L. 100–202 and 100–456) made allowable the costs of promoting the export of US defense industry products. The March 11, 2010 Executive Order (EO) on the National Export Initiative established the Administration's goal to double exports over the next five years as a critical component to stimulate economic growth in US. Elimination of exemption would create competitive disadvantages for U.S. firms attempting to grow export sales of defense industry products as exports are linked to offsets. A key element of Government policy in war torn and economically underdeveloped countries is to require prime contractors to subcontract with host foreign country subcontractors. Imposition of CAS ''will likely shrink the local competitive landscape, stymie host country economic development, potentially harm project missions, and stress relations with foreign governments.''

Response: The CAS Board does not accept the notion that eliminating the (b)(14) overseas exemption is contrary to U.S. export and foreign economic development policies. No one within the Legislative or Executive Branches has made that claim at any time during the rulemaking process. The CAS Board has not been persuaded that the burden imposed by CAS 401 and CAS 402, as well as perhaps the CAS Disclosure Statement, will be significant.

10. *Comment:* A respondent observed that the (b)(14) overseas exemption has not been identified as a cause for overseas subcontracting challenges in recent testimonies. On June 29, 2010, Stuart W. Bowen, Jr., Special Inspector General for Iraq Reconstruction, testified before the House Subcommittee on National Security and Foreign Affairs, and identified many subcontracting issues. However, he did not mention the (b)(14) overseas exemption from CAS as a cause for any of the issues, nor did he recommend the imposition of CAS coverage on foreign concern subcontracts as a potential solution. In the July 26, 2010 hearing on war zone subcontracting before the Commission on Wartime Contracting (CWC), none of the witnesses cited the (b)(14) overseas exemption from CAS as contributing to the subcontracting challenges identified during the hearings, nor did any witness recommend the imposition of CAS coverage as a solution to overseas subcontracting problems. None of the CWC commissioners spoke of, or inquired about, subcontractor CAS coverage or CAS compliance during opening statements or witness testimony.

Response: The CAS Board does not accept this reasoning for retaining the (b)(14) overseas exemption.

D. Paperwork Reduction Act

The Paperwork Reduction Act (44 U.S.C. chapter 35, subchapter I) does not apply to this rulemaking, because this rule imposes no additional paperwork burden on offerors, affected contractors and subcontractors, or members of the public which requires the approval of OMB under 44 U.S.C. 3501, *et seq.* The records required by this final rule are those normally maintained by contractors and subcontractors who claim reimbursement of costs under government contracts.

E. Executive Order 12866, the Congressional Review Act, and the Regulatory Flexibility Act

Because the affected contractors and subcontractors are those who are already subject to CAS but for the (b)(14) overseas exemption, and those who are subject to only CAS 401 and 402 under the (b)(4) foreign concern exemption, the economic impact of this final rule on contractors and subcontractors is expected to be minor. As a result, the CAS Board has determined that this final rule will not result in the promulgation of an ''economically significant rule'' under the provisions of Executive Order 12866, and that a regulatory impact analysis is not required. For the same reason, the Administrator of the Office of Information and Regulatory Affairs has determined that this final rule is not a ''major rule'' under the Congressional Review Act, 5 U.S.C. chapter 8. Finally, this rule does not have a significant effect on a substantial number of small entities because small businesses are exempt from the application of the Cost Accounting Standards. Therefore, this final rule does not require a regulatory flexibility analysis under the Regulatory Flexibility Act of 1980, 5 U.S.C. chapter 6.

F. List of Subjects in 48 CFR 9903

Government procurement, Cost accounting standards.

Daniel I. Gordon,
Chair, Cost Accounting Standards Board.

For the reasons set forth in this preamble, Chapter 99 of Title 48 of the Code of Federal Regulations is proposed to be amended as set forth below:

PART 9903—COST ACCOUNTING STANDARDS

■ 1. The authority citation for Part 9903 is amended to read as follows:

Authority: Public Law 111–350, 124 Stat. 3677, 41 U.S.C. 1502.

9903.201–1 [Amended]

■ 2. Section 9903.201–1 is amended by removing and reserving paragraph (b)(14).

[FR Doc. 2011–20212 Filed 8–9–11; 8:45 am]

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DEPARTMENT OF COMMERCE

National Oceanic and Atmospheric Administration

50 CFR Part 635

[Docket No. 110112022–1262–02]

RIN 0648–BA45

Atlantic Highly Migratory Species; Modification of the Retention of Incidentally-Caught Highly Migratory Species in Atlantic Trawl Fisheries

AGENCY: National Marine Fisheries Service (NMFS), National Oceanic and Atmospheric Administration (NOAA), Commerce.

ACTION: Final rule.

SUMMARY: This final rule modifies the permitting requirements and retention limits for Atlantic highly migratory species (HMS) that are incidentally-caught in Atlantic trawl fisheries. This action will reduce regulatory dead discards of incidentally-caught Atlantic swordfish in the *Illex* squid trawl fishery by establishing a new Incidental HMS Squid Trawl permit for all valid *Illex* squid moratorium permit holders. The Incidental HMS Squid Trawl permit will allow up to 15 swordfish per trip to be retained. The final rule also establishes a retention limit for smoothhound sharks in all Atlantic trawl fisheries. These actions are necessary to achieve domestic management objectives under the Magnuson-Stevens Fishery Conservation and Management Act (Magnuson-Stevens Act), and to implement the 2006 Consolidated HMS Fishery Management Plan (Consolidated HMS FMP), including objectives in the FMP to monitor and control all components of fishing mortality, both directed and incidental, so as to ensure the long-term sustainability of HMS stocks, and to provide the data necessary for assessing HMS fish stocks and managing HMS, including addressing inadequacies in current data collection and the ongoing collection of economic and bycatch data in Atlantic HMS fisheries.

DATES: Effective *August 10, 2011*, except for the amendments to § 635.21(e)(3)(i), § 635.24(a)(7), and § 635.71(d)(18), which are delayed indefinitely. NMFS will publish a document in the **Federal Register** announcing the effective dates for this amendments.

ADDRESSES: Highly Migratory Species Management Division, 1315 East-West Highway, Silver Spring, MD 20910. Copies of the supporting documents—including the Environmental Assessment (EA), Regulatory Impact Review (RIR), Final Regulatory Flexibility Analysis (FRFA), small entity compliance guide, and the 2006 Consolidated Atlantic HMSFMP—are available from the HMS Web site at *http://www.nmfs.noaa.gov/sfa/hms/*. Written comments regarding the burden-hour estimates or other aspects of the collection-of-information requirements contained in this final rule may be submitted to the HMS Management Division (see above) and by e-mail to *OIRA_Submission@omb.eop.gov*, or fax to (202) 395–7285.

FOR FURTHER INFORMATION CONTACT: Rick Pearson at (727) 824–5399, Steve Durkee at (202) 670–6637, or Delisse Ortiz at (301) 427–8503.

SUPPLEMENTARY INFORMATION: North Atlantic swordfish and smoothhound shark species are managed under the

81296 Federal Register / Vol. 76, No. 248 / Tuesday, December 27, 2011 / Rules and Regulations

OFFICE OF MANAGEMENT AND BUDGET

Office of Federal Procurement Policy

48 CFR Part 9904

Cost Accounting Standards: Cost Accounting Standards 412 and 413—Cost Accounting Standards Pension Harmonization Rule

AGENCY: Cost Accounting Standards Board, Office of Federal Procurement Policy, Office of Management and Budget.

ACTION: Final rule.

SUMMARY: The Office of Federal Procurement Policy (OFPP), Cost Accounting Standards Board (Board), is publishing this final rule to revise Cost Accounting Standard (CAS) 412, ''Composition and Measurement of Pension Cost,'' and CAS 413, ''Adjustment and Allocation of Pension Cost.'' This revision will harmonize the measurement and period assignment of the pension cost allocable to Government contracts, and the minimum required contribution under the Employee Retirement Income Security Act of 1974 (ERISA), as amended, as required by the Pension Protection Act (PPA) of 2006. The PPA amended the minimum funding requirements for qualified defined benefit pension plans. The Board issues this final rule to revise CAS 412 and CAS 413 to include the recognition of a ''minimum actuarial liability'' and ''minimum normal cost,'' which are measured on a basis consistent with the liability measurement used to determine the PPA minimum required contribution, and accelerate the recognition of actuarial gains and losses. These and other revisions will better align both the measurement and period assignment of pension cost allocable to a contractor's Government contracts and other final cost objectives in accordance with CAS, and the measurement and period assignment requirements for determining the contractor's minimum pension contribution under the PPA.

DATES: *Effective Date:* February 27, 2012.

FOR FURTHER INFORMATION CONTACT: Eric Shipley, Project Director, Cost Accounting Standards Board (telephone: (410) 786–6381).

SUPPLEMENTARY INFORMATION:

A. Regulatory Process

The Rules, Regulations and Standards issued by the Board are codified at 48 CFR chapter 99. The Office of Federal Procurement Policy Act, 41 U.S.C. 1502(c) [formerly, 41 U.S.C. 422(g)], requires that the Board, prior to the establishment of any new or revised Cost Accounting Standard, complete a prescribed rulemaking process. The process consists of the following four steps:

1. Consult with interested persons concerning the advantages, disadvantages and improvements anticipated in the pricing and administration of Government contracts as a result of the adoption of a proposed Standard, and prepare and publish a report on the issues reviewed, which is normally accomplished by publication of a staff discussion paper (SDP).
2. Promulgate an advance notice of proposed rulemaking (ANPRM).
3. Promulgate a notice of proposed rulemaking (NPRM).
4. Promulgate a final rule.

This final rule completes the four-step process.

B. Background and Summary

The Board is releasing a final rule on the revisions to 48 CFR 9904.412 and 9904.413 (respectively, CAS 412 and 413, or 9904.412 and 9904.413) to implement paragraph (d) of section 106 of the Pension Protection Act (PPA) of 2006 (Pub. L. 109–280, 120 Stat. 780).

The PPA amended the minimum funding requirements for, and the tax-deductibility of contributions to, qualified defined benefit pension plans under ERISA. Paragraph (d) of section 106 of the PPA requires the Board to revise CAS 412 and 413 to harmonize the ERISA minimum required contribution and the reimbursable pension cost.

In addition to the revisions to implement harmonization, the Board is making technical corrections to cross references and minor inconsistencies in the current rule. These technical corrections are not intended to change the meaning or provisions of CAS 412 and 413. The technical corrections for CAS 412 are being made to paragraphs 9904.412–30(a)(1), (8) and (9); paragraph 9904.412–50(a)(6); paragraphs 9904.412–50(c)(1), (2) and (5); and paragraph 9904.412–60(c)(13). In CAS 413, the technical corrections are being made to paragraph 9904.413–30(a)(1), subsection 9904.413–40(c), paragraph 9904.413–50(c)(1)(i), and paragraphs 9904.413–60(c)(12) and (18).

Different Roles and Responsibilities

The Board recognizes that heightened interest in pension-related matters may attract attention to this regulatory action by members of the public who are not familiar with CAS and the Board. The Board has a limited role, albeit an indirect one, with respect to pension funding, through its rulemaking regarding reimbursement of Government contractor pension costs. Under ERISA, the authority to implement the statute and promulgate rules and regulations regarding the minimum funding requirements for pension plans, tax deductibility of contributions, and protection of participant's rights has been granted to the Department of Treasury, Department of Labor (DOL) and the Pension Benefit Guaranty Corporation (PBGC). By contrast, the OFPP Act gave the CAS Board the exclusive authority to ''make, promulgate, amend, and rescind cost accounting standards and interpretations thereof designed to achieve uniformity and consistency in the cost accounting standards governing measurement, assignment, and allocation of costs to contracts with the United States.''

In this preamble, references to ERISA serve to identify and distinguish the federal system of funding requirements and restrictions for qualified pension plans from financial disclosure and reporting guidance, which is also known as generally accepted accounting principles (GAAP), and the CAS. References to ERISA may include: ERISA as amended to date; relevant sections of the Internal Revenue Code (IRC) at Title 26 of the U.S.C.; regulations and other pertinent guidance issued by Treasury, DOL and PBGC; and pertinent case law. The Board acknowledges that the tax deductibility of pension contributions is governed by the IRC at Title 26 of the U.S.C. and refers to the IRC when addressing issues related to tax deductibility. The Board acknowledges the pension funding responsibilities of ERISA as being distinct from the Board's responsibilities under the OFPP Act, which are to establish contract cost accounting standards governing the reimbursement of contract costs, including pension costs. Government contractors must continue to comply with ERISA and its implementing regulations that govern the funding of pension plans. This includes the new minimum funding requirements imposed by the PPA as implemented by Treasury. The Board's rules do not change the minimum funding requirements imposed by ERISA or Treasury's implementing regulations. To the contrary, the Board has changed its regulations to harmonize with the PPA and Treasury's implementing regulations by revising the CAS measurement basis for determining the amount of pension cost allocable to

Government contracts, which is reimbursable through contract pricing.

Prior Promulgations

On July 3, 2007, the Board published a SDP (72 FR 36508) to solicit public views with respect to section 106 of the PPA that required the Board to review and revise CAS 412 and 413. Differences between CAS 412 and 413, and the PPA, as well as potential issues associated with addressing those differences, were identified in the SDP.

The ANPRM (73 FR 51261, September 2, 2008) proposed changes to CAS 412 and 413. These proposed changes included the recognition of a ''minimum actuarial liability,'' a ''minimum normal cost,'' special recognition of ''mandatory prepayment credits,'' accelerated gain and loss amortization, and revision of the assignable cost limitation. Other proposed changes addressed the PPA's mandatory cessation of benefit accruals for severely underfunded plans, projection of flat dollar benefits, recognition of accrued contribution values on a discounted basis, interest on prepayment credits, and prior period unfunded pension costs. The Board also proposed a transition period to phase in certain provisions to promote fairness and equity to the contracting parties, as has been done by the Board in other rulemaking. The public was invited to offer comments on these proposed changes and any other related matters. In response to many respondents who asked for additional time for the submission of additional or supplemental public comments, on November 26, 2008, the Board published a notice (73 FR 72086) extending the comment period for the ANPRM.

After considering the comments received on the ANPRM, as well as the results of further analysis and deliberations conducted by the Board, the Board published a NPRM (75 FR 25982) on May 10, 2010, to solicit public views with respect to the proposed revisions to CAS 412 and 413. The NPRM reflected public comments in response to the SDP and ANPRM, as well as research accomplished by the staff for consideration by the Board.

The NPRM proposed changes to CAS 412 and 413 that were considered necessary to harmonize the minimum required contributions under ERISA for Government contractor pension plans and the Government's reimbursable pension plan costs. The primary proposed changes were the recognition of a ''minimum actuarial liability,'' ''minimum normal cost,'' and an accelerated amortization of actuarial gains and losses. The minimum actuarial liability and minimum normal cost are measured on a settlement basis using the expected payout of currently accrued benefits that have been discounted using yield rates on investment grade corporate bonds with matching durations to forecasted pension benefit payments, and that are in the top three quality levels available, *e.g.,* Moody's grade A and above. Other proposed changes addressed the PPA's mandatory cessation of benefit accruals for severely underfunded plans, the projection of flat dollar benefits, recognition of accrued contribution values on a discounted basis, interest on prepayments credits, and prior period unfunded pension costs. The Board continued to propose a transition period to phase in certain provisions to promote fairness and equity to the contracting parties, as has been done by the Board in other rulemaking. The public was invited to offer comments on these proposed changes and any other related matters.

A major feature of the NPRM was the proposal that the minimum actuarial liability and minimum normal cost would only be recognized if three threshold criteria were met. Otherwise, the actuarial accrued liability and normal cost are measured on a going concern basis using the expected payout of projected benefits that have been discounted using an interest assumption equal to the expected future rate of return on investments which reflect long-term trends so as to avoid distortions caused by short-term market fluctuations. (Note that the SDP, ANPRM and NPRM referred to this as the ''long-term'' interest assumption.) These threshold criteria, which have been referred to as ''triggers,'' required that:

(i) The ERISA minimum required contribution exceeds the contract pension costs measured on a going concern basis, referred to as ''trigger 1;''

(ii) The sum of the minimum actuarial liability and minimum normal cost exceeds the sum of the going concern actuarial accrued liability and normal cost, referred to as ''trigger 2;'' and

(iii) The contract pension cost measured using the sum of the minimum actuarial liability and minimum normal cost exceeds the contract pension cost measured using the sum of the actuarial accrued liability and normal cost, referred to as ''trigger 3.''

The Board provided illustrations of these proposed revisions in a new section 9904.412–60.1, Illustrations—CAS Pension Harmonization Rule. The illustrations showed the measurement, assignment and allocation of pension cost under the proposed rule for a contractor that separately accounted for pension costs for one segment and an aggregation of the remaining segments.

The NPRM also added language to clarify that any difference between the expected and actual unfunded actuarial liability caused by a change between recognition of the going concern actuarial accrued liability and the minimum actuarial liability would be treated as part of the actuarial gain or loss for the period. The actuarial gain and loss recognition arising from the change in the liability basis (between using the actuarial accrued liability and the minimum actuarial liability) for computing pension costs was illustrated in the NPRM at 9904.412–60.1(h). The proposed structural format differed from the format for 9904.412–60.

The final rule considered the comments and other concerns expressed by the public in response to the NPRM. The Board's responses to the public comments are discussed in Section C—Public Comments to the NPRM.

Basis for Conclusions

Paragraph (d) of section 106 of the PPA instructs the Board to revise CAS 412 and 413, as follows:

> COST ACCOUNTING STANDARDS PENSION HARMONIZATION RULE—The Cost Accounting Standards Board shall review and revise sections 412 and 413 of the Cost Accounting Standards (48 CFR 9904.412 and 9904.413) to harmonize the minimum required contribution under the Employee Retirement Income Security Act of 1974 of eligible government contractor plans and government reimbursable pension plan costs not later than January 1, 2010. Any final rule adopted by the Cost Accounting Standards Board shall be deemed the Cost Accounting Standards Pension Harmonization Rule.

In deliberating and deciding upon a final rule, the Board adopted the following criteria for harmonizing the minimum required contribution under ERISA:

- Accounting rules must satisfy the Board's Statement of Objectives, Policies and Concepts (57 FR 31036 published July 13, 1992);
- Accounting rules must promote fairness and equity to both contracting parties;
- Measurement of pension costs must be objectively verifiable;
- Accounting rules must keep volatility to a minimum in the pricing of Government contracts; and
- Accounting rules must be understandable, particularly given the complexity of CAS 412.

Throughout the comment process afforded by the SDP, ANPRM, and NPRM, many respondents commented that ''harmonize'' under PPA section 106(d) meant that it was Congress's intent that the Board adopt ERISA's minimum required contribution for measuring, assigning, and allocating pension costs to CAS-covered contracts. Further, these commenters stated that the plain meaning of ''harmonize,'' as defined in various dictionaries, would lead to an identical conclusion. The Board's review of the PPA, as well as its legislative history, did not reveal evidence of any such Congressional intent.

The Board has historically recognized that financial accounting policies and procedure, *i.e.,* GAAP, and tax accounting rules have inherently different goals from Government contract cost accounting that preclude their use for the appropriate measurement, assignment and allocation of pension costs for CAS. In the Board's view, PPA section 106 did not seek to change that historical recognition. Based on the Board's analysis, entirely adopting either financial accounting or tax accounting rules for CAS 412 and 413 would have resulted in inequities and unfairness to both contracting parties. The Board noted that the public commenters most directly affected by the CAS Pension Harmonization Rule tended to agree with the NPRM provisions, except for a few matters which are discussed later in this preamble.

The Board continues to believe that CAS 412 and 413 should reflect the continuing nature of the pension plan sponsored by a going concern, as well as the multi-year nature of the contractual relationship between the Government and contractors in the acquisition process. The CAS are intended to provide consistent and accurate cost data to determine the incurred cost for the current period and for the forward pricing of Government contracts over future years for multi-year contracts. With regard to pension accounting, both financial accounting and ERISA have taken a market-based approach toward pension liabilities, which are often referred to as ''mark-to-market'' liabilities. This approach is less predictable for purposes of projecting future costs than the going concern basis of CAS and, therefore, is less useful than CAS for forward pricing purposes for multi-year contracts.

The Board recognizes that contract cost accounting must address the risks to both the contractor and the Government associated with inadequate funding of a plan's current period settlement liability measured on a ''mark-to-market'' basis. This final rule addresses this risk by recognizing a minimum actuarial liability and minimum normal cost that is based on currently accrued benefits valued using the top three quality levels of investment grade corporate bond rates consistent with the PPA criteria as cited in the IRC at 26 U.S.C. 430(h)(2)(D)(i).

ERISA's ''funding target'' and ''target normal cost'' were introduced by the PPA and are mark-to-market values consistent with the measurement basis for the minimum actuarial liability and minimum normal cost. The CAS recognition of the minimum actuarial liability and minimum normal cost ensures that the annual pension cost as measured and assigned under CAS is at least sufficient to liquidate ERISA's target normal cost currently and the unfunded target liability on an amortized basis. Therefore, recognizing the minimum actuarial liability and minimum normal cost will reduce differences between the CAS assigned cost and the ERISA minimum required contribution, although the CAS assigned cost may sometimes exceed the ERISA minimum required contribution. Maintaining the going concern basis for Government contract costing will allow contractors to set multi-year funding goals that avoid undue volatility in cash flow requirements.

The Board was persuaded by public comments that the proposed threshold criteria (''triggers'') for recognition of the minimum actuarial liability and minimum normal cost were overly complex and might create inequities. The final rule only retains the criterion that assesses whether the sum of the minimum actuarial liability and minimum normal cost exceeds the sum of the actuarial accrued liability and normal cost. If the contractor computes pension costs on a composite basis for the plan as a whole, then the criterion should be examined at the plan level. However, if 9904.413–50(c)(2) or (3) require the contractor to separately compute pension costs for a segment, or if the contractor so elects, the criterion should be separately examined at the segment level. This may mean that some segments might use an actuarial accrued liability and normal cost to compute pension costs, and other segments might use the minimum actuarial liability and minimum normal cost. This ensures that variance in demographics or funding levels between different segments is recognized.

ERISA imposes minimum funding requirements on qualified defined benefit plans based on a conservative measurement of the plan's liability and normal cost. It should be noted that the measurement mandated for ERISA minimum funding approximates the value of a bond portfolio required to liquidate the stream of expected payments for accrued benefits if purchased in the current market. While the purchase of such a bond portfolio would not transfer all asset and demographic risks to a third party, this measurement emulates the costs of self-insuring the pension fund against the liability for accrued benefits and represents the mark-to-market (settlement) value without the premium charge for transfer of risk. The final rule requires that contract cost accounting for pension costs must recognize a mark-to-market (settlement) based liability and normal cost as minimum values for CAS. By doing so, the Board believes that any ERISA minimum required contribution in excess of the allocable contract pension cost amount will be reconciled and reflected in contract pricing in the near term because, by definition, the CAS liability and normal cost would be equal to or greater than the minimum values determined under the settlement liability. Furthermore, by recognizing the settlement liability and normal cost as minimum values, this final rule will benefit the procuring agencies, as well as taxpayers, by minimizing the Government's exposure to the financial risk of unfunded actuarial liabilities as funding progresses.

In order to promote equity and fairness in achieving an orderly change in the contract cost accounting for pension costs, this final rule retains the transition period consisting of five cost accounting periods, the Pension Harmonization Rule Transition Period, that will phase in recognition of any adjustment of the actuarial accrued liability and normal cost. This transition method will apply to all contractors with contracts subject to CAS 412 and 413.

Because modern actuarial software programs can value the same data set multiple times using different assumptions, the final rule is designed to allow companies to use the same actuarial methods and valuation software for ERISA, financial statements, and Government contract costing purposes. Except for the interest rate, the same general set of actuarial assumptions can be used for all three purposes. This will allow Government agencies and auditors to place reliance on externally verified data from ERISA and financial statement valuations while allowing contractors to avoid unnecessary additional actuarial effort and expense.

Summary of Final Rule

The primary harmonization provisions are consolidated within the ''CAS Pension Harmonization Rule'' at 9904.412–50(b)(7). This consolidation eliminates the need to revise many long-standing provisions of CAS 412 and clearly identifies the special accounting practices required for harmonization. Some revisions to other provisions of CAS 412 and 413 are also necessary to achieve the full result. These basic changes to CAS 412 and 413 are as follows:

(1) *Recognition of a ''minimum actuarial liability'' and ''minimum normal cost.''* CAS 412 and 413 continue to measure the actuarial accrued liability and normal cost based on a going concern basis using ''best-estimate'' actuarial assumptions, projected benefits, and the contractor's established immediate gain actuarial cost method. However, in order to ensure that the measured costs recognize the mark-to-market liability as a minimum value, the final rule requires that the measured pension cost must be determined using the minimum actuarial liability and minimum normal cost if a specific threshold criterion is met. That is, if the sum of the minimum actuarial liability and the minimum normal cost (as measured using current yield rates on the top three quality levels of investment-grade corporate bonds) exceeds the sum of actuarial accrued liability and normal cost (as measured using the expected rate of return on investments), the contractor must measure the pension cost for the period using the minimum actuarial liability and minimum normal cost. Furthermore, if the criterion is met, the minimum actuarial liability and minimum normal costs are used for all purposes of measurement, period assignment, and allocation under CAS 412. However, the minimum actuarial liability is not recognized for the purposes of 9904.413–50(c)(8), (9) and (12).

The minimum actuarial liability and minimum normal cost are measured under the accrued benefit cost method based on the current yield rate on the top three quality levels of investment-grade corporate bonds. Measuring the minimum actuarial liability and minimum normal cost on a current mark-to-market basis better aligns the CAS measurement with current accounting and economic theory. In addition, the minimum actuarial liability definition is consistent with the ERISA's funding target and the GAAP's ''accumulated benefit obligation.'' The minimum normal cost is similarly defined to be consistent with the ERISA's ''target normal cost'' and the GAAP's ''service cost'' (without salary projection).

(2) *Accelerated Gain and Loss Amortization.* The final rule accelerates the assignment of actuarial gains and losses to accounting periods by decreasing the amortization period from a fifteen-year to ten-year period. This accelerated assignment will reduce the period of deferral in cost recognition and is consistent with the shortest amortization period permitted for other portions of the unfunded actuarial liability (or actuarial surplus). Paragraph 9904.412–64–1(b)(5) of the transition provisions clarify that the ten-year amortization of gains and losses begins with the first cost accounting period this final rule is applicable to the contractor.

(3) *Mandatory Cessation of Benefit Accruals.* This final rule exempts any curtailment of benefit accrual required by ERISA from immediate adjustment under 9904.413–50(c)(12). Voluntary benefit curtailments will remain subject to immediate adjustment under 9904.413–50(c)(12).

(4) *Projection of Flat Dollar Benefits.* The final rule allows the projection of increases in specific dollar benefits granted under collective bargaining agreements. The recognition of such increases is limited to the average increase in such benefits over the preceding six years, limited to benefits governed by collective bargaining agreements. As with salary projections, the final rule will discontinue projection of these specific dollar benefit increases upon a segment closing, which uses the accrued benefit cost method to measure the actuarial accrued liability.

(5) *Present Value of Contributions Receivable.* For both qualified and nonqualified defined benefit plans, the final rule discounts contributions attributable to the prior accounting period but made after the asset valuation date, *i.e.,* the contribution receivable, at the expected rate of return on investments assumption that reflects long-term trends (assumed interest rate) from the date actually paid back to the valuation date. In considering the public comments on interest crediting on application of prepayment credits and the FAR 31.205–6(j)(2)(iii) quarterly funding requirement, the Board also reviewed the provisions on interest adjustments on pension costs, contributions receivable, prepayment credits, and unfunded pension costs. The assumed interest rate is used to adjust amounts not yet funded, such as receivable contributions, quarterly pension costs, and unfunded pension costs. This is consistent with the general provision of 9904.412–40(b)(2) that the assumed interest rate must be based on expected rates of return on investments, except for the interest rate used to measure the minimum actuarial liability and minimum normal cost. However, interest adjustments on invested monies, such as the prepayment credits, are adjusted at the actual rate of return on the assets.

(6) *Interest on Prepayments Credits.* Generally, the funding of pension plans is a financial management decision made by the contractor, and must satisfy the minimum funding requirements of ERISA. Thus, funding more than the pension cost measured and assigned under CAS is entirely possible. Funding in excess of the CAS assigned costs results in a prepayment for the purposes of CAS. Since all monies deposited into the funding agency are fungible and share equally in the fund's investment results, the prepayment is allocated a share of the investment earnings and administrative expenses on the same basis as all other invested monies. This recognition ensures that any investment gain or loss attributable to the assets accumulated by prepayments does not inequitably affect the gains and losses of the plan or any segments. A decision to fund in excess of the CAS assigned cost should have a neutral impact on Government contract costing, although it might have a transitory negative impact on the contractor's cash flow.

(7) *Transition Period to Phase In Minimum Actuarial Liability and Minimum Normal Cost Mitigates Initial Impact of the Potential Increase.* The changes to CAS 412 and 413 are phased in over a transition period consisting of five cost accounting periods, the Pension Harmonization Rule Transition Period. The phase in allows the cost impact of this final rule to be gradually recognized in the pricing and costing of CAS-covered and FAR-covered contracts alike. It also moderates the difference in the pension cost allocable to FAR-covered fixed price contracts entered into prior to the effective date of the CAS Pension Harmonization Rule that are not subject to equitable adjustment. The final rule was revised so that the transition period in the proposed rule is now a fixed schedule for the first five cost accounting periods, the Pension Harmonization Rule Transition Period, following the ''Implementation Date'' so that the transition does not extend unduly beyond the time needed for the contract pricing and budgetary systems to migrate from the existing rule to the CAS Pension Harmonization Rule. Also, the Board has modified the transition

schedule slightly to lessen the impact on contract prices and agency budgets in the near-term. To accomplish this, the difference between the minimum actuarial liability and the going concern actuarial accrued liability, and the difference between the minimum normal cost and the going concern normal cost, are recognized on a scheduled basis during the Pension Harmonization Rule Transition Period, the first five cost accounting periods that this rule is applicable. Under the revised schedule, 0% of the difference will be recognized in the First Cost Accounting Period, 25% in the Second Cost Accounting Period, 50% in the Third Cost Accounting Period, 75% in the Fourth Cost Accounting Period, and finally, 100% in the Fifth Cost Accounting Period. After the completion of the Pension Harmonization Rule Transition Period, 100% of the minimum actuarial liability and minimum normal cost are recognized, if applicable. While 0% of the difference is recognized in the First Cost Accounting Period, there will be other incremental differences, *e.g.,* the change to ten-year amortization of gains and losses.

(8) *Extended Illustrations.* Many illustrations in 9904.412–60 have been updated to reflect the proposed changes to CAS 412 and 413. To assist users with understanding how this final rule will function, examples have been added in a new section, ''9904.412–60.1 Illustrations—CAS Pension Harmonization Rule.'' This section presents illustrations showing the measurement and assignment of pension cost for a contractor's pension plan that meets the criterion of the 9904.412–50(b)(7) CAS Pension Harmonization Rule. The actuarial gain and loss recognition arising from the change in the liability basis (between using the actuarial accrued liability and the minimum actuarial liability) for computing pension cost is illustrated in 9904.412–60.1(d). This structural format differs from the format of 9904.412–60, Illustrations.

C. Public Comments to the Notice of Proposed Rulemaking

The Board received 20 public comments to the NPRM. These comments came from Federal agencies, contractors, professional and trade associations, actuaries, and individuals. As with the ANPRM and SDP, the Board found the public comments to be focused, well developed, and informative. The Board appreciates the efforts of all parties who submitted comments. The public comments to the NPRM may be viewed at: *http://www.whitehouse.gov/omb/casb_index_public_comments/*, or *http://www.regulations.gov.*

Summary of Public Comments

Many of the public commenters believed that, while the NPRM represented progress towards harmonizing the minimum required contribution under ERISA and reimbursable pension plan costs, the proposed three threshold criteria (''triggers'') for recognition of the minimum actuarial liability were an obstacle to adequate recognition of the contribution requirements of ERISA.

Some of the commenters continued to recommend that the Board accept the PPA's mark-to-market based accounting as the only basis for contract cost accounting. Several commenters believed that full harmonization could only be achieved by the direct recognition of mandatory prepayment credits. The public comments also included many detailed recommendations regarding how the proposed rule might be corrected or clarified.

Most of the public comments reiterated concerns that the differences between CAS and the PPA have the potential to cause cash flow problems for some Government contractors. Although there were diverse views on how to best achieve that goal, timely recognition of the ERISA minimum required contribution in contract costing was often recommended. Some commenters believed that section 106 of the PPA requires CAS 412 and 413 to be identical to PPA's minimum required contribution.

Many commenters believed that the Board should remove the proposed first threshold criterion, which some commenters referred to as ''trigger 1,'' that compared the pension cost measured on a going concern basis to the ERISA minimum required contribution. They noted that this criterion not only added complexity to the proposed rule, but also unnecessarily delayed the recovery of previously accumulated prepayment credits. Some of these comments also suggested that the Board remove the second threshold criterion (''trigger 2''), which compared the total liability for the period measured on a going concern basis (*i.e.,* the actuarial accrued liability and normal cost) to the total liability for the period measured on a mark-to-market basis (*i.e.,* the minimum actuarial liability and minimum normal cost). These commenters believe that the only necessary limitation on use of the minimum actuarial liability would occur when the pension cost measured on a going concern basis already exceeded the pension cost on a mark-to-market basis.

Many public comments objected to the segment closing and benefit curtailment provisions that excluded the recognition of the minimum actuarial liability. These commenters expressed their belief that such an exception could reverse the cost recovery and be non-compliant with the mandate of section 106 of the PPA.

Some public comments expressed a concern that the proposed transition rules would delay full recovery and believed that the Board should address contract cost accounting and not budgetary impacts. On the other hand, several commenters believed that the delay caused by the transitional phase in rule was a reasonable compromise that allowed the Government and contractors to gradually implement the effect of the magnitude of the cost increase on the forward pricing process.

This summary of the comments and responses form part of the Board's public record in promulgating this case and are intended to enhance the public's understanding of the Board's deliberations concerning the CAS Pension Harmonization Rule.

Responses to Specific Public Comments

Topic 1: Harmonization.

Comments: Some commenters focused on the meaning of the Congressional mandate under section 106 of the PPA, the proposed continued recognition of pension liabilities on a going concern basis, and the relationship between the pension cost for contract costing and the ERISA minimum required contribution. One commenter stated that ''By allowing the recognition of the MAL and MNC [*minimum actuarial liability and minimum normal cost*] (*sic*) in determining the CAS cost, without precondition, eventually the CAS assignable cost should catch up with the ERISA funding requirements and full harmonization should be reached.''

One public comment suggested that compliance with PPA section 106 required adoption of the measurement and period assignment provisions of the PPA. This commenter believes that the NPRM as proposed did not fully implement the mandate of section 106 because the Board did not adopt the measurement and amortization rules of the PPA. The commenter stated that *Webster's II New College Dictionary* (3d ed. 2005) defines ''harmonize'' and ''harmony'' to mean ''agreement.''

Two commenters argued that ''the best approach to harmonization would be to revamp CAS 412 and 413 to follow PPA, with modifications as necessary to meet the unique requirements of government contracts.'' One of these commenters quoted the Merriam-Webster's Online Dictionary which defines ''harmonize'' as ''to bring into consonance or accord.''

On the other hand, one commenter believed that harmonization is a more generalized goal meaning to achieve ''equity between the parties.'' And, another public commenter asked the Board to consider the language of section 106, which tells the Board to ''harmonize the [*ERISA minimum required contribution*] (*sic*) **and** government reimbursable pension plan costs, not harmonize CAS **with** the PPA.'' [Emphasis Added]

Three public commenters reminded the Board that the primary concern that prompted section 106 was the difference between the pension funding requirements imposed by ERISA and the delayed reimbursement of pension cost under contracts subject to CAS 412 and 413. Some commenters identified areas of concern that they believed were preventing the proposed rule from providing timely recovery of pension contributions.

Another public commenter reminded the Board that improving the timeliness of pension cost recovery was a goal of the NPRM writing that ''While pension funding rules have changed with the enactment of the PPA, this principle of equity—where the government does not excuse itself from requirements it is imposing on all plan sponsors—remains.'' This commenter believed that the CAS Pension Harmonization Rule, as proposed, failed to satisfy that objective and provided specific suggestions for improvement.

In contrast to the comments that the Board should fully adopt or more closely follow the measurement and amortization rules of the PPA, one commenter was concerned that ''the CAS Board is straying from the intent and historical precepts of contract cost accounting and veering toward tax-driven cash accounting.'' This commenter examined the goals of the Cost Accounting Standards vis-à-vis the goals of the PPA:

> As the Board's response notes, ''strictly tying pension accounting to settlement liabilities and current fair market values will cause volatility that will be counterproductive to predictability and disrupt the contract forward pricing process. Contract price predictability must remain a critical concern for the Board. ''

The commenter's letter continues:

> The long standing concept of accounting is that pension plans are presumed to continue absent evidence to the contrary. We understand that actuaries include assumptions concerning settlement payment (lump sum) elections by terminating and retiring employees—thus the likely risk of paying the extra settlement cost is already anticipated in actuarial measurements. Furthermore, the expected return on investment should reflect a contractor's investment policy for the plan, rather than theories of financial economics that are in vogue.

Several public commenters suggested that success in achieving harmonization should be measured by reduction in ''mandatory'' prepayment credits, where mandatory prepayments refers to minimum funding requirements in excess of the allocable pension costs measured and assigned in accordance with CAS 412 and 413. These commenters were not only concerned with the prospective harmonization of the contract cost with the ERISA minimum contribution once the CAS Pension Harmonization Rule was applicable, but also with a reduction in the substantive mandatory prepayment credits that had been accumulated since the passage of the PPA and the recent dramatic decline in asset values.

One public commenter stated this concern directly: ''Under the NPRM, there is no mechanism present to ensure that contractors will be able to assign mandatory prepayment credits.'' This commenter later continued: ''To eliminate these situations in which recovery of accumulated mandatory prepayment credits are indefinitely delayed, we ask the Board to reintroduce the mandatory prepayment credit mechanism that was contained in the ANPRM.''

Another commenter expressed the belief that: ''Without such amortization, [mandatory prepayment credits] (sic) are not recovered in a reasonable time period, and situations may arise where the balances are inaccessible.'' This commenter cautioned the Board that: ''Without these suggested changes, we respectfully submit that the Board will not have met its mandate under section 106 of the PPA.''

Response: As previously stated, the Board's review of the PPA, as well as its legislative history, did not reveal any expression of Congressional intent that ''harmonize'' under PPA section 106(d) requires the Board to adopt ERISA's minimum required contribution for measuring, assigning, and allocating pension costs to Government contracts. The Board's historical recognition that financial accounting and tax accounting rules have inherently different goals, that preclude them from being used for Government contract cost accounting, is well established. In the Board's view, PPA section 106 did not seek to change that historical recognition. Based on the Board's analysis, adopting either financial accounting or tax accounting rules for contract cost accounting purposes would have resulted in inequities to both contracting parties. The Board noted that the contracting parties most directly affected by the CAS Pension Harmonization Rule tended to agree with the general concepts articulated in the NPRM, except for a few matters which are dealt with later in this final rule.

The Board does not believe adopting tax accounting rules, which establish a funding range rather than an accrual for the period, is appropriate for contract cost accounting purposes. Recognition of the minimum actuarial liability is a reflection of the potential risk of inadequate funding imposed by the ''mark-to-market,'' *i.e.,* settlement liability, in the event that there is an immediate liquidation of the pension plan. To accomplish this, the minimum actuarial liability and minimum normal cost are treated as minimum values to the actuarial accrued liability and normal cost measurements. Apart from these minimum values, the measurement and period assignment rules continue to be based on the going concern concept wherein actuarial assumptions reflect long-term trends and avoid distortions caused by short-term fluctuations, which the Board has determined appropriate for contract cost accounting purposes. Furthermore, recognition of no less than the minimum actuarial liability and minimum normal cost for contract costing purposes ensures that over time the assignable pension cost is at least equal to the ERISA minimum required contribution computed using the funding target liability and target normal cost, which are mark-to-market values.

By ensuring that the pension cost measurement recognizes the minimum actuarial liability and minimum normal cost in a manner similar to the basis for the PPA's funding target and target normal cost, the Board believes that the final rule will over time accumulate contract pension costs that are at least equal to the accumulated value of the PPA minimum required contributions.

The Board agrees that timely recovery of the accumulated prepayments is essential to the degree practicable, but notes that there are some situations where recovery opportunities are limited, *i.e.,* overfunded plans with benefits that have been frozen. Section 106 of the PPA did not require direct reduction of accumulated prepayment credits when CAS is harmonized. However, the Board acknowledges the importance of such a reduction, and the final rule will improve recovery of accumulated prepayment credits through recognition of the higher of either the settlement or going concern liability.

Topic 2: Proposed Threshold Criteria

Comments: Several public commenters believed that the proposed rule was too complex because it combines going concern and settlement measurements. One public commenter expressed the belief that ''the Board's goal—to create a version of CAS that harmonizes with both the minimum funding requirements of PPA and the historical versions of CAS 412 and 413—is not viable.'' Another commenter believed that continuing to compute an actuarial accrued liability and normal cost measured using an expected rate of return on investments as the interest assumption, solely for Government cost accounting purposes, would add a layer of complexity and expense that is not warranted, and which could not be directly verified. And one public commenter remarked that the description of the ''minimum required amount'' needed clarification.

The industry associations were generally supportive of the proposed rule and believed that ''use of the new liability measure, the minimum actuarial liability (MAL), in conjunction with the existing actuarial accrued liability (AAL) provides for a balanced liability measurement despite varying economic circumstances and is a reasonable balance between long- and short-term approaches.'' Another commenter also gave general support for the rule as proposed, writing:

We understand that given the urgency of the mandate to harmonize CAS, the CASB has chosen an approach to make modifications to the existing CAS rules rather than undertake a complete overhaul of the rules. We understand and support this approach. In addition, we continue to support the CAS modifications to adopt the PPA-like minimum actuarial liability (MAL) and shorter ten-year amortization period for actuarial gains/losses in order to achieve harmonization.

In addition to the concern with complexity from using two different liability measures, a commenter found that imposition of a series of three threshold criteria as a prerequisite for recognizing the minimum actuarial liability and minimum normal cost values created a complexity that potentially would make the rule unmanageable.

First Threshold Criterion (''Trigger 1'')

The first of the proposed threshold criteria, *i.e.,* ''trigger 1,'' was the primary concern expressed in many public comments about the proposed rule. Most of the commenters believed that ''trigger 1'' prevented harmonization by limiting the periods during which the minimum actuarial liability could be recognized. Based on several analyses of ''trigger 1,'' these commenters concluded that ''trigger 1'' retarded the recovery of prepayments accumulated before and after the applicability of the CAS Pension Harmonization Rule.

Other concerns that were raised included the difficulty in predicting the minimum required contribution for forward pricing and the added volatility caused by using multiple ''triggers.'' These commenters uniformly urged the Board to eliminate ''trigger 1.''

One commenter offered the following observations to assuage the Board's concerns with inappropriate increases in contract pension costs:

But note that even with the elimination of this gateway, there would still be the five-year transition phase-in, the longer amortization period (a ten-year period versus the seven-year period in PPA), and greater asset smoothing than is permitted in PPA. These features will adequately control the cost increases that would otherwise be seen with a more direct and immediate harmonization.

Another commenter remarked that, if the Board had added to the NPRM the three ''trigger'' prerequisite for using the minimum actuarial liability and minimum normal cost as a way of responding to its comment on the ANPRM, then the commenter believed that its prior recommendation was not properly implemented in the NPRM:

In our ANPRM letter, we stated the following:

If the intent of the CAS Harmonization Rule is to adjust the CAS assignable costs so that the excess of the PPA funding requirements over the CAS assignable costs are recovered on a timely basis, increasing the regular AAL to the MAL when the CAS cost is already greater than the PPA funding requirement for a given year may not be necessary, particularly if there are no existing prepayment credits.

It appears that our suggestion was partly considered. However, Threshold Test 1 does not consider the existence of (mandatory) prepayment credits; it considers only the annual comparison of the minimum funding requirement and the regular CAS cost. As a result, it is too restrictive and will hinder full recovery of minimum funding requirements particularly for contractors who have been subject to the PPA requirements since 2008. Pension plans will eventually require funding contributions lower than CAS costs because the plans will become fully funded under the PPA earlier than when they will become fully funded under CAS. The plans will become fully funded under the PPA sooner because of the following reasons:

- The PPA became effective before the CAS Pension Harmonization Rule will become effective.
- The PPA has a 7-year amortization for unfunded liabilities, compared to the ten-year amortization period for gains/losses and even longer amortization periods for other amortization bases (*e.g.,* plan amendments, assumption changes, *etc.*) in the NPRM.
- The MAL and MNC are phased in and are not fully recognized during the transition period.

Thus, plans will fail the ''trigger 1'' threshold test before contractors can recover all of the minimum funding contributions required of them.

Second and Third Threshold Criteria (''Trigger 2 and Trigger 3'')

Several commenters recommended that the Board also eliminate ''trigger 2,'' which requires that the sum of the minimum actuarial liability (MAL) and the minimum normal cost (MNC) exceed the sum of the actuarial accrued liability (AL) and normal cost (NC) as a precondition for recognition of the minimum actuarial liability and minimum normal cost. The general recommendation was to retain only the final threshold criterion, *i.e.,* ''trigger 3'' and eliminate ''trigger 2'' because it was duplicative and added unnecessary complexity. One of these commenters believed that rather than comparing the liabilities and normal costs as a pre-condition, the rule should simply use the contract pension cost computed using the minimum actuarial liability and minimum normal cost as a minimum pension cost:

Considering the ANPRM's ''MAL > AL'' criterion and how it impacts the calculations, we recommended that *if no (mandatory) prepayment credits exist and if the regular CAS cost already exceeds the PPA minimum funding requirement,* then the CAS cost need not be adjusted to reflect the MAL and the MNC to result in an even higher CAS assignable cost. Our recommendation was intended for the specific—and less frequent—situations when CAS reimbursements will have already caught up with the ERISA required cash funding of the plan on a cumulative basis, *i.e.,* when there are no mandatory prepayment credits.

In our ANPRM comment letter, we also recommended considering a minimum CAS cost approach for harmonization, *in lieu of* the ''MAL > AL'' criterion. In other words, there is no need to impose a ''MAL > AL'' criterion when satisfaction of this criterion simply results in reflecting the MAL and the MNC as ''floor'' liabilities and normal costs in the calculations. Instead, we recommended directly calculating the CAS cost based on the MAL and MNC, and use the result as a floor for the CAS cost.

Some commenters made suggestions for improving the second criterion (''trigger 2'') if retained in the final rule. One commenter recommended that the final rule should ''provide that when ERISA or GAAP asset, liability, cost, or other values are to be used for CAS purposes, such values are per se CAS-compliant amounts. This will avoid unnecessary disputes with government auditors regarding whether these values are appropriate.''

Another public comment recommended that ''the Board restore the ANPRM interest rate definition as it provides the necessary leeway for contractors to set interest rates assumptions that will be more stable than rates tied to current periods. Along with this definition, it will be helpful to retain the NPRM provision allowing the PPA rates as a safe harbor option.'' The comment noted that the ANPRM required that the interest rate be based on ''high quality'' corporate bonds, rather than the NPRM requirement that the rate be based on ''investment grade'' bonds.

Response: The Board has been persuaded to eliminate the first threshold criterion (''trigger 1''), which was proposed in the NPRM, from the final rule. This test, which had been recommended in public comments to the ANPRM, adds complexity and inserts the vagaries of tax accounting into contract cost accounting.

The Board has reviewed the advantages and disadvantages of retaining either the second threshold criterion (''trigger 2'') or the third threshold criterion (''trigger 3'') as the single prerequisite for using recognition of the minimum actuarial liability and minimum normal cost. Based on this review, the Board has concluded the second criterion directly implements the Board's intent that the minimum actuarial liability and minimum normal cost are minimum values for the pension cost measurement. The Board also notes that unless the second criterion is satisfied, the effort needed to compute the contract pension cost using the minimum values is not necessary. Moreover, first determining which liability to use lessens the potential for computation errors because the contract pension cost needs to be computed once instead of twice. Therefore, the third threshold criterion, ''trigger 3,'' has also been eliminated.

The interest rate criteria used for measuring the minimum actuarial liability and minimum normal cost proposed in the NPRM referenced ''investment grade'' fixed-income investments, which infers the top four levels of investments (*e.g.,* Moody's Baa or higher) and differed from the ANPRM reference to ''high quality'' (*e.g.,* Moody's Aa or higher) fixed-income investments, which as used for GAAP is restricted to the top two levels of investments. The Board believes that the criterion of ''the top three quality levels of investment grade'' is appropriate because it is restricted to the higher tier ratings from the bond rating agencies, *e.g.,* Moody's' single ''A'' rated or higher, and is consistent with the investment quality required by the PPA as cited in 26 U.S.C. 430(h)(2)(D)(i). A lesser rated bond would pay more coupon interest, but the additional default risk is unacceptable for determining the contingent cost of liquidating all benefit obligations for contract cost accounting. The Board also believes that the criteria proposed in the NPRM permits less stringent interest rate criteria than the PPA. The final rule requirement for ''investment grade corporate bonds with varying maturities and that are in the top 3 quality levels available, such as Moody's' single 'A' rated or higher,'' supports consistency and is less likely to engender disputes. The ANPRM criteria relied upon GAAP requirements, which must reflect the expected rates at which the pension benefits could be effectively settled. The criteria used in this final rule, which is the slightly more stringent than the criteria proposed in the NPRM, should also satisfy the GAAP requirements.

The provisions of 9904.412–50(b)(7)(iii)(B) allows the contractor to elect to use investment grade corporate bond yield rates ''published or defined by the Secretary of the Treasury for determination of the minimum contribution required by ERISA'' as its established cost accounting practice for setting the interest to be used for 9904.412–50(b)(7)(iii)(A) purposes. This permits the PPA yield curve to be used as a ''safe harbor.'' The 9904.412–50(b)(7)(iii)(A) criteria is consistent with, although less stringent than, the discount rate used to compute the accrued benefit obligation as described by GAAP which refers to ''high quality'' (*e.g.,* Moody's Aa or higher) corporate bonds.

Because all other assumptions must be based on best estimate assumptions that reflect long-term trends in accordance with 9904.412–50(b)(4), this provision will preclude the use of the ''most valuable'' benefit assumptions, *i.e.,* most conservative assumptions used to value the funding target for an ''at risk'' plan, unless there is a persuasive actuarial study that supports such assumptions as appropriate based on the past experience and future expectations for the plan. All other actuarial assumptions are also required by 9904.412–50(b)(7)(iii)(D) to be the same as the assumptions used to compute the actuarial accrued liability on a going concern basis. Also, CAS 412 generally requires that the plan's liability be based on the terms of the written plan document, whereas GAAP requires that patterns of benefit improvements and other features of the ''substantive plan'' be recognized. These differences in the basis for measuring the liability for ERISA's funding target and GAAP's accrued benefit obligation can cause variances between those values and the minimum actuarial liability. Therefore the Board believes the automatic adoption of ERISA's funding target or GAAP's accrued benefit obligation is inappropriate.

Topic 3: Suggested Alternative Means of Achieving Harmonization

Comments: Several commenters continue to recommend that the Board replace the going concern basis for liability measurement with the current mark-to-market measurement adopted by Congress for the PPA, and by the Financial Accounting Standards Board for financial statement reporting and disclosure. These commenters believe that issues unique to contract cost accounting can be addressed through existing or modified provisions, *e.g.,* volatility might be addressed through longer amortization periods for contract costing purposes.

There were differing views presented as to whether the CAS should directly reference ERISA and GAAP liabilities or simply establish a mark-to-market measurement basis. Proponents of direct reference believed that direct adoption of ERISA or GAAP values would permit contractors and auditors to rely on values already subject to review by the Internal Revenue Service (IRS) or independent audit. However, the opponents of this approach noted differences in the criteria concerning assumptions and events that must be recognized, such as ''at risk'' status under ERISA or anticipation of plan changes that may occur under GAAP.

One commenter was concerned with switching back to a going concern liability basis when the ERISA or GAAP liability was fully funded. Besides the potential for complexity, the concern was that the proposed rule would impose a requirement to fund a contract cost for pensions in a period in which ERISA would have a lesser minimum required contribution or GAAP would recognize a lower pension expense.

Another commenter agreed that the Board should recognize the mark-to-market based liability, but recommended that the current going concern measurement basis be phased out over a five-year transition period. The commenter believed that once the entire transition period was completed, then contract cost accounting should rely solely on the mark-to-market based liability.

A different alternative to pension harmonization suggested by one commenter would be to retain exclusive use of the going concern basis for measuring pension liability, but allow the difference between the going concern actuarial accrued liability and the mark-to-market minimum actuarial liability during the initial year of harmonization to be amortized as the costs of a transitional ''special event.'' This commenter believes that this approach would greatly simplify harmonization while permitting the previously unrecognized portion of the mark-to-market liability to be included in contract costs.

The third alternative approach suggested came from a commenter who believed that the CAS should retain the going concern basis for measuring the liability, but that any excess of the ERISA minimum required contribution over the contract cost would be amortized over a relatively short period, such as a five-year period. This commenter also argued that certain contractors, whose business is predominantly from cost-based Government contracts, be permitted to recognize the full excess in the current period because they do not have a sufficient business base to subsidize the excess during the amortization period.

Response: The Board reiterates its belief that absent evidence to the contrary, defined benefit plans are ongoing commitments, and therefore contract costing should reflect the average cost based on expected average asset returns in the future. However, the Board believes that the mark-to-market liability must be recognized as a minimum value in order to reflect the risk that the pension plan may have to settle its liability for pension benefits. The suggested alternative for amortizaton of the initial excess of the minimum actuarial liability over the actuarial accrued liability might reduce the accumulated value of prepayment credits, but during extended periods of low bond rates, substantial prepayment credits could again accumulate.

The Board does not believe that the suggested amortizing of the PPA minimum required contribution in excess of the going concern pension cost is a viable solution. Adding such amortization to the current computations of CAS 412 and 413 adds complexities, whereas the going concern based pension cost does adjust to the PPA minimum required contribution over a period of time. The simplier approach of adopting the PPA minimum required contribution, but using a smoothing mechanism, was one of the many options included in the Staff Discussion Paper, but it was ultimately rejected by the Board due to concerns that minimum funding might not achieve adequate funding in every economic environment.

Topic 4: Proposed Accelerated Gain & Loss Amortization

Comments: Two commenters expressed their support for the proposed accelerated amortization of actuarial gains and losses over a ten-year period instead of the current fifteen-year period. As one commenter stated:

> We also believe the change in amortization period for actuarial gains and losses from a fifteen-year to ten-year period, while longer than the seven-year amortization period used for PPA, provides a reasonable balance between timely cost recovery and an acceptable level of volatility for pension costs measured for CAS.

However, one commenter objected to the imposition of an amortization period that exceeded the amortization period required for the ERISA minimum required contribution. This commenter was concerned that the minimum required contribution would not be fully recognized for CAS purposes for a decade.

In response to the Board's inquiry concerning whether there should be special recognition of a gain or loss from an exceptional event, two commenters opined that this issue was not directly tied to harmonization and should be addressed in a separate case. Another commenter expressed their belief that ''the proposed NPRM retains effective smoothing mechanisms for gains and losses, so alternative rules for exceptional gains or losses are unnecessary.'' They were also concerned about the introduction of a new issue this late in the promulgation process.

Two commenters found confusing the proposed language added to 9904.412–50(a)(1)(v) and 9904.412–50(b)(7) regarding the adjustment to the actuarial accrued liability based on the minimum actuarial liability. They asked for clarification of the Board's intent.

Response: The Board agrees that the wording of proposed 9904.412–50(a)(1)(v) should be further clarified. The adjustment language of the proposed 9904.412–50(a)(1)(v) was intended to identify the portion of the period gain or loss attributable to the change in liability measurement basis. The adjustment language was used in the proposed 9904.412–50(b)(7) to tie the gain and loss provision and the proposed 9904.412–64.1 transitional provisions together.

In the final rule, the proposal at 9904.412–50(a)(1)(v) of the NPRM for a specific adjustment of the actuarial accrued liability to become the minimum actuarial liability, or the normal cost to become the minimum normal cost, is no longer used and has been deleted. Paragraph 9904.412–50(b)(7)(ii) of the final rule provides for a direct computation of the minimum actuarial liability and minimum normal cost.

The Board understands that standard actuarial practice is to measure the expected unfunded actuarial liability by updating the unfunded actuarial liability from the prior period for interest and expected demographic changes. The current period experience gain or loss is simply the difference between the actual and expected unfunded actuarial liability. The normal gain and loss measurement will include the effects of a switch between bases for measuring the liability. The gain and loss measurement, when the measurement basis changes, is illustrated at 9904.412–60.1(d).

The adjustment language has been deleted from the transition rule at 9904.412–50(a)(1)(v) and 9904.412–50(b)(7). The provisions of 9904.412–64.1 have been revised to address the scheduled phase in of the mark-to-market based minimum actuarial liability and minimum normal cost, and govern only the first five cost accounting periods of the Pension Harmonization Rule Transition Period.

The amortization of the experience gain or loss that occurs between the prior and current valuations is an element of the current period cost. The gain or loss is measured as the difference between the expected and actual unfunded actuarial liability as of the valuation date. Although the source of the gain or loss is the actuarial experience during the prior period, the amortization installment of the gain/loss is included in the determination of the current year cost together with amortization of the other bases. To avoid any disputes, 9904.412–64.1(b)(5) has been added to clarify that the gain or loss measured in the First Cost Accounting Period of the Pension Harmonization Rule Transition Period, which is the first cost accounting period this final rule is applicable, shall be amortized over a ten-year period.

Topic 5: General References to ERISA

Comment: Two commenters believe that the general references to ERISA in the proposed rule should be modified to cite specific provisions of ERISA. They are concerned that confusion or disputes may arise because of the numerous provisions that form ERISA. They also note that many of the provisions that affect pension contribution requirements and limitations are addressed by 26 U.S.C. 401 through 436, which implement the tax treatment of the contribution amount.

In particular, one commenter was concerned the general reference to ERISA in 9904.412–50(b)(5) and Illustration 9904.412–60(b)(3) might not provide adequate guidance regarding the projection of increases in benefits that are not based on salaries and wages. The commenter wrote the following regarding 9904.412–50(b)(5):

> In my opinion, the reference above to ''ERISA'' is tied to the current ERISA Tax Deductible Limit as defined in the Pension Protection Act of 2006. The Act Title VIII, Pension Related Revenue Provisions, added section 801 which amended Internal Revenue Code [at 26 U.S.C.] Section 404 to increase the Tax Deductible Limit for Single Employer plans. These rules became effective in 2008. The above ERISA reference should be clarified to my interpretation since ERISA also has numerous provisions tied to Minimum Funding rules.

This commenter also suggested that the reference to ERISA in 9904.413–50(c)(12)(viii) should be clarified:

> Under (viii), in my opinion the requirement is tied to the new Internal Revenue Code [26 U.S.C.] Section 436 mandated cessation of benefit accruals due to funding target attainment percentage. This section was created by the Pension Protection Act of 2006 and should be clarified.

Response: The Board agrees that the references to ERISA proposed in the NPRM require that the user ascertain the relevant U.S.C., Title 26 provision. The Board reiterates its precept that tax accounting is inappropriate for contract costing. The Board continues to believe that replacing the general references to ERISA with specific U.S.C., Title 26 provisions is not desirable because it might require frequent updates to CAS 412 and 413 to the extent that ERISA and Title 26 of the U.S.C. are amended in the future. The Board acknowledges that the tax deductibility of pension contributions is governed by the IRC at Title 26 of the U.S.C, and has made conforming technical corrections to the existing and proposed rules in the promulgation of this final rule.

The Board agrees that the general reference to ERISA in 9904.412–50(b)(5) might create confusion as to the applicable provision of ERISA. In this case the provision was intended to refer to section 801(a) of the PPA, which is implemented by 26 U.S.C. 404(o)(3)(A)(ii)(II). To avoid confusion and disputes concerning the relevant ERISA coverage, the Board has replaced the general reference to ERISA with specific provisions that parallel 26 U.S.C. 404(o)(3)(A)(ii)(II).

This new language does not indicate a loosening of the restrictions on recognizing the costs for contingencies. Certain reasonably foreseeable contingencies, such as salary increases, may be recognized in contract costing. CAS 412 has always permitted the projection of a contingent liability for future salary increases but subject to the requirement that actuarial assumptions must be individually reasonable based on future expectations and grounded by past experience. Like 26 U.S.C. 404(o)(3)(A)(ii)(II), this final rule limits the basis for projection of the contingent liability for flat benefit increases to the historical data from the last six years, and adds the restriction that the benefits must be provided under a collective bargaining agreement. The formality of collective bargaining negotiations and agreements will provide verifiable evidence of the pattern of benefit improvements because such evidence may be lacking or subject to dispute in less formal situations.

Regarding the general reference to ERISA in 9904.413–50(c)(12)(viii), the Board is not adopting a specific concept from ERISA, but instead is providing an exemption for involuntary benefit curtailments imposed by an outside authority, *i.e.,* ERISA. Use of a general reference to ERISA in this provision allows the 9904.413–50(c)(12)(viii) exemption to continue to reflect benefit curtailments required by ERISA without requiring CAS 412 and 413 to be amended for future changes in ERISA. Moreover, this is neither a measurement nor a period assignment provision; rather, 9904.413–50(c)(12) requires an immediate adjustment of the unfunded actuarial liability or actuarial surplus when specific events occur, which are defined as a segment closing, benefit curtailment, or plan termination. The purpose of 9904.413–50(c)(12)(viii) is to provide an exemption from an otherwise required immediate adjustment.

Under the current ERISA provision, the contractor can provide that benefit accruals will automatically resume if the plan's funding level sufficiently improves within 12 months. If the funding level takes longer to improve, the contractor can amend the plan to reinstate the accruals once the plan attains an adequate level of funding. Because the contractor has not unilaterally decided to change the pension plan (from an ongoing plan that grants and accrues benefits for matching contract service to a frozen state where there is no expectation of future accruals), the Board believes an immediate settlement, or true up, of assets and liabilities is inappropriate and unnecessarily disruptive to contract pricing.

It is noteworthy that 9904.413–50(c)(12)(viii) was derived from the aforementioned ERISA provision which permits the restoration of benefit accruals if the required funding level is attained within 12 months. Otherwise, under the ERISA provision, a plan amendment would be required to restore the missed accruals, which would require amortization in accordance with 9904.412–50(a)(1)(iii). Under the amendments for the CAS Pension Harmonization Rule, the contractor can elect to continue to accrue benefits that are expected to be reinstated, and thereby continue to match the pension cost with the underlying activity. If the pension plan does not automatically restore the missed accruals, then the future reinstatement of the missed accruals is contingent upon future action by the contractor, and cannot be recognized until and unless the plan is amended to restore the missed benefit accruals.

In reviewing this provision for inclusion in the final rule, the Board considered whether the ''ERISA missed accrual'' was a liability to be recognized by the normal cost under CAS, which is the measurement of the actuarial present value of the annual benefit accrual. The Board has revised this provision to ensure that there is a strong expectation that benefit accruals will be incurred. First, the employee's right to the restoration of the benefit accrual must be included in the written plan documents. (See 9904.413.50(c)(12)(viii).) Second, the contractor cannot elect to anticipate the future accruals if there is evidence to the contrary, *e.g.,* there is consideration of eliminating the restoration provision by plan amendment or the entity is facing bankruptcy due to serious financial difficulties. Finally, as with all pension costs assigned to a current period, the pension cost must be funded by the contractor to be allocable, and thereby allowable, for reimbursement by the Government through contract pricing. Reimbursement to the contractor by the Government of its allocable share of the funded pension cost attributable to the ''ERISA missed accrual'' provides a funding source to improve the plan's funding level, which directly supports the goal of the PPA.

Topic 6: Proposed Accounting for Prepayments

Comments: Some commenters objected to the proposed revision to 9904.412–30(a)(23) and 9904.412–50(a)(4), which would adjust the prepayment credits based on investment returns and administrative expenses in accordance with 9904.413–50(c)(7). The commenters agreed that expenses associated with investment management are properly charged against the prepayment credits because the prepayments are part of the invested assets. However, the commenters believed that expenses associated with benefit administration should not be charged against prepayment credits which have not been allocated to benefit liability. As one public commenter explained:

We have several comments concerning proposed section 412–50(a)(4) which states that accumulated prepayment credits are to be adjusted for investment returns and administrative expenses. It seems reasonable to us that a proportional share of investment returns and investment related expenses should be allocated to the prepayment credit account, as a prepayment credit represents plan assets. As such, we agree that the prepayment credit should be allocated a proportional share of investment related administrative expenses. On the other hand, it does not seem reasonable that the prepayment credit should receive an allocation of any non-investment related administrative expenses (*e.g.,* for items such as plan administration, actuarial fees, and ERISA audits)—these types of expenses are not typically based on asset size, and the existence of a prepayment credit will not generally affect these fees.

To avoid confusion, one of the commenters recommended that 9904.412–30(a)(23) ''explicitly provide that the average rate of investment return for a year can be used to adjust all cash flows occurring in that year. This would eliminate the possibility that an auditor might require a contractor to measure investment returns within a plan year, which would be a difficult and expensive task.''

Several commenters believed that illustrations, in which the application of prepayment credits to fund the current pension cost on the first day of the plan year, might be misconstrued to be a cost measurement rule that might affect the allowability of interest on prepayment credits.

Two commenters were also concerned that the illustrations, in which the prepayment credits are accounted for separately from the segment accounting, might be read to require such accounting for prepayment credits. They believed that it was the contractor's prerogative to set the accounting practice on whether prepayment credits are identified by segment. Furthermore, they believe such a rule governing the accounting for prepayment credits was beyond the scope of harmonization.

Response: The Board understands that benefit-related expenses, such as PBGC premiums, fees for processing benefit payments, *etc.,* might not be directly associated to prepayment credits that have not been allocated towards the funding of benefits. The Board is concerned about the additional effort that would be required, and the potential for disputes, if contractors were required to separately identify administrative expenses as either investment-related or benefit-related. Furthermore, the Board views the monies deposited into the pension assets as fungible, *i.e.,* not individually identifiable. Besides, the Board notes that the PPA, as implemented by 26 U.S.C. 430(f)(8), adjusts the prefunding balance—which is the ERISA equivalent of the prepayment credit—at the rate of return on plan assets taking into account ''all contributions, disbursements, and other plan payments during such period.''

Topic 7: Actuarial Value of Assets

Comments: Three public comments questioned why the Board did not propose, as part of pension harmonization, the adoption of the PPA asset averaging method and 10% corridor around the market value of assets. The commenters believed that the proposed rule should have permitted adopting the PPA asset averaging method as part of the harmonization change so that the impact of the change in asset valuation method would be includable in the equitable adjustment claim. One commenter suggested that the 20% asset corridor be maintained to address the concerns with volatility.

One commenter questioned the illustration that implies a requirement that the prepayment be subtracted from the market value of assets before determining the actuarial value of assets as a requirement. In contrast the commenter noted that minimum funding requirements include the ERISA prefunding balance (prepayment) in the determination of the asset corridor. They asked that the Board clarify its intent and the proper treatment of the prepayment credit in the determination of the actuarial value of assets.

Response: The method of measuring the average value of assets (actuarial value of assets) under the PPA limits the expected rate of return on assets to the lower of the assumed rate of return on assets or the PPA interest rate for third segment. This limitation understates expected investment return when the prevailing yield curve rates are lower than the going concern expectations. However, the PPA average value of assets is not limited when the prevailing yield curve rates exceed the going concern expectations. The PPA average value of assets does not give equal treatment to gains and losses. When the PPA interest rates are lower than the going concern assumption, the required suppression of the expected return in investments can introduce an additional element of asset loss (or reduced gain) by understating the actuarial value of assets that would be developed on a going concern basis. However when the PPA interest rates are higher than the going concern assumption, there is no limit on the recognition expected investment earnings or losses. This added element of additional asset loss (or reduction in asset gain) does not comply with 9904.413–50(b)(2), which requires that the actuarial value of the assets ''be determined by the use of any recognized asset valuation method which provides equivalent recognition of appreciation and depreciation of the market value of the assets of the pension plan.'' The conditional limitation of the actuarial value of assets can also add some volatility and difficulty in forward pricing projections. And finally, the traditional equal recognition of gains and losses allows the contractor to follow its own decisions concerning investment policy without penalty for gains in excess of the current corporate bond rate. The Board believes that the existing provisions regarding the actuarial value of assets permit a wide variety of reasonable asset valuation methods to be used. A contractor may elect to use a 2-year asset averaging method with a 10% corridor around the market value of assets, but switching to such a method is not required to achieve harmonization.

The accounting for the prepayment credit in a separate side account is an example in the NPRM of a possible methodology for measuring the actuarial value of assets. And as explained above, any reasonable asset valuation method may be used as part of a consistently applied cost accounting practice. The Board does not believe any further modification to the rule, including illustrations, is necessary.

Topic 8: Discounting of Contributions Receivable

Comments: One public commenter asked the Board to clarify the proposed 9904.413–50(b)(6)(i) requiring contributions receivable to be discounted to the beginning of the cost accounting period at the applicable effective interest rate.

Response: The PPA requires that contributions made after the end of the plan year be adjusted for interest based on the ''effective interest rate.'' The PPA defines the ''effective interest rate'' as the single interest rate that will produce the same present value of accrued benefits as the duration-specific corporate bond yield rates. In reviewing the relationship of interest adjustments under the proposed harmonization rule to the Board's conceptual framework for harmonization and contract cost accounting, the Board believes the proposed rule was internally inconsistent. The general guiding principle for contract costing under harmonization is that the assumed interest rate, based on expected rates of return on investments, shall be used for all measurement purposes except the measurement of the minimum actuarial liability and minimum normal cost under 9904.412–50(b)(7)(ii).

Under the final rule, pension costs would be adjusted to the date of funding. Accumulated balances under 9904.412–50(a)(2) and amortization installments under 9904.412–50(a)(1) would be determined based on the assumed interest rate. Adjusting contributions receivable at the current corporate bond rate, which may not be representative of the expected earnings on the pension fund, is inconsistent with the assumed interest used for other measurements. Therefore, the Board has modified 9904.413–50(b)(6) to require that all contributions receivable be adjusted based on the assumed interest rate.

The harmonization rule adjusts amounts that have been deposited into the pension fund at the net rate of return on plan investments for the period.

Topic 9: Assignable Cost Limits

Comments: Some commenters recommended that the Board restore the ANPRM proposal for a buffer on the assignable cost limitation. The commenters did note that the 25% buffer proposed in the ANPRM was too large, and suggested that a 10% buffer would be sufficient to promote predictability while not permitting the accumulation of an excessive surplus.

Response: The Board recognizes that permitting a reasonable buffer in the assignable cost limitation has the advantage of dampening cost volatility for forward pricing purposes when the plan funding is close to the limit. However, the Board remains concerned that use of a buffer may result in the accumulation of excessive surplus assets. Currently the 9904.412–50(c)(2)(i) provision prohibiting the assignment of negative pension costs inhibits the Government's ability to recover an excessive asset surplus. Addressing the buffer concept and changing the zero dollar floor (9904.412–50(c)(2)(i)) are beyond the scope of harmonization. The Board believes these issues require further research because recognizing amounts in excess of measured cost has no precedent in the Cost Accounting Standards. The issue of excessive assets and the inclusion of a buffer in the assignable cost limitation must be considered together should the Board decide to open a new case on segment closing and other such adjustments.

Topic 10: Segment Closings and Benefit Curtailments

Comments: Many commenters objected to the proposed exclusion of the minimum actuarial liability from recognition for segment closings and benefit curtailment purposes under 9904.413–50(c)(12)(i). The commenters advised the Board of their strong belief that the proposed exclusion of the minimum actuarial liability in measuring the segment closing adjustment effectively reversed the CAS Pension Harmonization Rule. One public commenter summarized the objection as follows:

> The NPRM currently requires segment closing calculations to use the unadjusted Actuarial Accrued Liability (AAL), or the ongoing liability currently applicable in the existing CAS rules. We believe that the more appropriate measure of the liability in a segment closing calculation is the Minimum Accrued Liability (MAL) to achieve harmonization. The MAL, by its nature, is intended to reflect the present value of a pension plan if its obligations were settled at a particular point in time (*i.e.,* the segment closing date), while the AAL is reflective of an ongoing plan by incorporating long-term liability assumptions. The application of the AAL at segment closing effectively reverses the impact of harmonization that may have applied in prior periods since the final true-up of plan costs will revert back to the current (non-harmonized) CAS rules. We believe this is a fundamental flaw of the current NPRM that must be modified to ensure harmonization is achieved in the spirit of the mandate within the Pension Protection Act.

The following public commenter addressed the acceptance of risk by the contractor's decisions to settle or retain the benefit liability at segment closing:

> Looking from a theoretical standpoint, a segment closing should be based on a relatively risk-free basis, which essentially calls for the MAL to be used. If a contractor wishes to assume risks inherent in the investment of assets on a greater risk basis, then the contractor should absorb any losses as well as any gains that might arise.

Another commenter noted the relationship between the market value of assets, which is required in the measurement of the segment closing adjustment, and the minimum actuarial liability, which is not recognized:

> In order to harmonize pension cost, benefit curtailment and segment closing adjustments should be based on the difference between the Market Value of Assets (MVA) and the MAL. Both the MVA and the MAL are market-based measurements of the pension plan assets and obligations at the prevailing market conditions, and this basis is consistent with the requirements of the PPA.

One commenter asked that, in addition to mandatory benefit curtailments, voluntary benefit curtailments also should be exempted from the adjustment requirements of 9904.413–50(c)(12). The commenter argued that the required adjustment was disruptive and unnecessary if the segment was continuing and pension costs would continue to be charged to the contract.

There were three public comments concerning the proposed accounting for 9904.413–50(c)(12) adjustments in subsequent periods. These comments recommended revisions to the wording of 9904.413–50(c)(12)(ix). One commenter believed that the Board should consider addressing, in a future case on segment closings, subsequent actuarial gains for which the recovery of any excessive asset surplus is limited by the zero-dollar floor of 9904.412–50(c)(2)(i).

Response: The Board limited its proposed amendment to 9904.413–50(c)(12) to the exemption of benefit curtailments mandated by ERISA. Currently such benefit curtailments are addressed by 26 U.S.C.436. The Board recognizes that there are issues concerning the risks and rewards of settling or retaining the benefit liability upon the occurrence of a segment closing or benefit curtailment. There is also a potential that an analysis would demonstrate that the risks and rewards will vary depending upon market and economic conditions at the time of the segment closing or benefit curtailment.

The Board believes that any changes to the current provisions of 9904.413–50(c)(12), including the provision at 9904.413–50(c)(12)(ix) that was proposed in the NPRM, must be based on a full consideration of these issues. Unintended consequences might arise if all the issues are not fully vetted. The Board believes that the issues and problems with the current segment closing and benefit curtailment provisions are beyond the scope of pension harmonization required under section 106, and should be addressed in a separate case, which the Board is considering. Accordingly, the Board has deleted the proposed provision at 9904.413–50(c)(12)(ix) from the final rule.

In reviewing the relationship of the segment closing liability to the liability used to compute annual pension costs, the Board noted that transfers of participants to other segments, including inactive segments, might be an integral part of winding down a segment's workforce prior to a segment closing. To fully respond to the public comments, the Board considered whether the asset transfers associated with participant transfers should be based on the same liability as used for 9904.413–50(c)(12) purposes, that is, the actuarial accrued liability determined under the accrued benefit cost method rather than the contractor's normal funding method. In the preamble to the 1995 amendments to CAS 412 and 413 (60 FR 16534, March 30, 1995), the Board noted that it was adding this distinction for the liability to be used to transfer assets because of its relationship to segment closings:

> Under the revised definition of a segment closing, some employees may remain in a segment performing non-Government work while other employees may be transferred to other segments. For consistency, the provisions for transfers of either active or retired participants specify that the assets transferred must equal the actuarial accrued liability determined under the accrued benefit cost method.

Therefore, the Board believes that to be consistent with the exemption of 9904.413–50(c)(12) from 9904.412–50(b)(7), the liability to be used to transfer assets under 9904.413–50(c)(8) and (9) should be likewise exempt. While participant and associated assets transfers also effect the measurement of ongoing pension costs, the Board believes that this treatment has the additional benefit of preserving assets within the segment in which they were accumulated. In the 1995 preamble, the Board explained its view on the impact of future costs of participant and associated asset transfers:

> If plan participants remain employed by the contractor, whether in the same or another segment, the Board believes the responsibility for future salary increases, which are attributable to future productivity, merit, and inflation, belongs to the future customers that benefit from the participants' continued employment.

Furthermore, because asset transfers under 9904.413–50(c)(8) and (9) are based on the liability measured by the accrued benefit cost method, rather than the established funding method, the Board has added to these paragraphs clarifying language regarding which actuarial assumptions are appropriate. This clarification was not previously necessary because all assumptions were required to reflect long-term trends.

Topic 11: Illustrations

Comments: Two commenters recommended that the Board eliminate proposed harmonization illustrations that ''do not focus on unique features of the rule and that could imply acceptance of tax accounting.'' They believed that, not only were the portions of the illustration related to ERISA measurements unnecessary, as ERISA is amended in the future, these illustrations could also become confusing and obsolete.

Response: The Board agrees and has limited the harmonization illustrations to those that demonstrate the measurement and assignment of the pension cost under this final rule.

Topic 12: Transition Rule

Comments: The comments from the industry associations were supportive of the proposed 9904.412–64.1 transition rule:

> We understand the transition rules are intended to mitigate any abrupt increase in costs as a result of the final rules to allow the Government to manage agency budgets. We continue to agree that this is an important reason to use such a transition and support the duration selected. In addition, we believe the phase-in will reduce the monetary amounts and number of equitable adjustments resulting from this required change in CAS, thereby lessening the opportunities for disagreements.

The associations believed that their support for the proposed rule and the transition provision was demonstrated by their acceptances of a further delay in the timeliness of cost recovery and prolonged negative cash flow burden. Other commenters were also supportive of the proposed transition.

However, two commenters believed that it was inappropriate for the Board to propose a transition rule to address the Government's budgetary concerns. One commenter opined that:

> * * * [there] will be significant gaps between CAS pension costs and the PPA funding requirements, gaps that do not exist for businesses selling commercially. These gaps will have detrimental cash flow and profit impacts on contractors because they will be required to fund shortfalls over a shorter period than they will be able to recover associated costs from the Government.

The other commenter believed it was appropriate to include the proposed transition to allow both parties to the contract a means of managing the forward pricing process and equitable adjustments from the expected large change in pension costs.

On the other hand, a joint public comment from several of the Government's military agencies expressed their belief that the magnitude of the potential pension cost increases requires a longer transition period in order to properly manage the impact on budgets and existing contracts.

Response: The Board determined that a transition period was necessary to implement the CAS Pension Harmonization Rule in a fair and equitable manner, as it has done with previous promulgations. In any attempt to promote fairness and equity, the Board would necessarily take into account the nature of the Government acquisition process, which includes the budgetary process. The Board believes that this transition period was necessary to allow the cost impact of this final rule to be gradually recognized in the pricing and costing of CAS-covered and FAR-covered contracts alike. It also moderates the difference in the pension cost allocable to FAR-covered fixed price contracts entered into prior to the effective date of the CAS Pension Harmonization Rule that are not subject to equitable adjustment.

Topic 13: Effective Date of the Final Rule and Its Applicability to Contracts

Comments: Many contractors recommended that the Board allow sufficient time to modify cost projections and permit contract cost negotiation to accommodate the change in accounting practice that would be required by the final rule. There was general agreement that the final rule should not be effective prior to January 1, 2011, and that the effective date should be delayed for 60 days from the publication of the final rule. Some of the commenters noted that delayed effective and applicability dates might ease the impact of equitable adjustments.

Response: The Board has considered the comments regarding the effective date of the final rule. This final rule is being published after January 1, 2011, which is later than the effective date mandated by section 106 of the PPA, but provides the relief requested in the public comments to delay the effective and applicability dates. The Board decided to delay the effective date for 60 days after publication to permit time for contractors to make the necessary changes to the actuarial valuation and cost projection systems. Furthermore, to ensure that no contractor becomes immediately applicable to the final rule, the implementation date is the first cost accounting period after June 30, 2012. The Board agrees that such a delay will eliminate a portion of the equitable adjustment claims for contractors that report on a calendar year basis.

Topic 14: Guidance on Equitable Adjustments

Comments: Two commenters requested that the Board provide guidance on the calculation of the cost impact for equitable adjustment. The commenters believed such guidance was important to avoid having different interpretations that would lead to disputes over equitable adjustments. One of the commenters asked that the Board explicitly identify what constitutes a mandatory cost accounting practice change due to the CAS Pension Harmonization Rule.

Response: The Board believes that the final rule changes cost accounting practices contained in CAS 412 and 413 that are necessary to implement the CAS Pension Harmonization Rule required by section 106 of the PPA. Whether a particular accounting practice has changed, the actual determination of the cost impact and the processing of equitable adjustments are matters for CAS administration as may be undertaken by the contracting parties for CAS-covered contracts. Therefore, this final rule is limited to contract cost accounting and does not include any guidance on the administration of the change in cost accounting practice; the Board urges the Federal agency heads to issue the necessary policies and procedures.

Topic 15: Request for Additional Opportunities for Public Comment

Comments: Several commenters recommended that the Board republish the CAS Pension Harmonization Rule as a second NPRM if substantive changes are made to the rule. The commenters believed that a second NPRM would be advantageous given the complexity and cost impact of the proposed changes.

Response: The Board believes that the conceptual basis that underpinned the NPRM has been extended to the final rule. While the elimination of the threshold criteria of ''trigger 1'' and ''trigger 3'' have greatly reduced the wording and complexity of 9904.412–50(b)(7), the basic concepts for establishing a harmonization prerequisite have not changed. This final rule does not add any substantive changes to how the CAS Pension Harmonization Rule is implemented. Therefore, the Board believes that a second NPRM is not necessary, and after consideration of the public comments to the NPRM, the Board is publishing the CAS Pension Harmonization Rule as a final rule.

D. Paperwork Reduction Act

The Paperwork Reduction Act, Public Law 96–511, does not apply to this final rule because this rule imposes no additional paperwork burden on offerors, affected contractors and subcontractors, or members of the public which requires the approval of OMB under 44 U.S.C. 3501, *et seq.* The records required by this final rule are those normally maintained by contractors and subcontractors who claim reimbursement of costs under Government contracts.

E. Executive Order 12866, the Congressional Review Act, and the Regulatory Flexibility Act

Because the affected contractors and subcontractors are those who are already subject to CAS 412 and 413, the economic impact of the promulgation of this CAS Pension Harmonization Rule as a final rule on contractors and subcontractors is expected to be minor. As a result, the Board has determined that this final rule will not result in the promulgation of an ''economically significant rule'' under the provisions of Executive Order 12866, and that a regulatory impact analysis will not be required. For the same reason, the Administrator of the Office of Information and Regulatory Affairs has determined that this final rule is not a ''major rule'' under the Congressional Review Act, 5 U.S.C. Chapter 8. Furthermore, this final rule does not have a significant effect on a substantial number of small entities because small businesses are exempted from the application of the Cost Accounting Standards. Therefore, this final rule does not require a regulatory flexibility analysis under the Regulatory Flexibility Act of 1980, 5 U.S.C. chapter 6.

List of Subjects in 48 CFR 9904

Government Procurement, Cost Accounting Standards.

Daniel I. Gordon,
Chair, Cost Accounting Standards Board.

For the reasons set forth in this preamble, Chapter 99 of Title 48 of the Code of Federal Regulations is amended as set forth below:

PART 9904—COST ACCOUNTING STANDARDS

■ 1. The authority citation for Part 9904 continues to read as follows:

Authority: Pub. L. 111–350, 124 Stat. 3677, 41 U.S.C. 1502 [formerly Pub. L. 100–679, 102 Stat 4056, 41 U.S.C. 422].

■ 2. Section 9904.412–30 is amended by revising paragraphs (a)(1), (8), (9), and (23) to read as follows:

9904.412–30 Definitions.

(a) * * *

(1) *Accrued benefit cost method* means an actuarial cost method under which units of benefits are assigned to each cost accounting period and are valued as they accrue, that is, based on the services performed by each employee in the period involved. The measure of normal cost under this method for each cost accounting period is the present value of the units of benefit deemed to be credited to employees for service in that period. The measure of the actuarial accrued liability at a plan's measurement date is the present value of the units of benefit credited to employees for service prior to that date. (This method is also known as the Unit Credit cost method without salary projection.)

* * * * *

(8) *Assignable cost deficit* means the increase in unfunded actuarial liability that results when the pension cost computed for a qualified defined-benefit pension plan exceeds the maximum tax-deductible amount for the cost accounting period determined in accordance with the Internal Revenue Code at Title 26 of the U.S.C.

(9) *Assignable cost limitation* means the excess, if any, of the actuarial accrued liability and the normal cost for the current period over the actuarial value of the assets of the pension plan.

* * * * *

(23) *Prepayment credit* means the amount funded in excess of the pension cost assigned to a cost accounting period that is carried forward for future recognition. The Accumulated Value of Prepayment Credits means the value, as of the measurement date, of the prepayment credits adjusted for income and expenses in accordance with 9904.413–50(c)(7) and decreased for amounts used to fund pension costs or liabilities, whether assignable or not.

* * * * *

■ 3. Section 9904.412–40 is amended by adding paragraph (b)(3) to read as follows:

9904.412–40 Fundamental requirement.

* * * * *

(b) * * *

(3) For qualified defined benefit pension plans, the measurement of pension costs shall recognize the requirements of 9904.412–50(b)(7) for periods beginning with the ''Applicability Date of the CAS Pension Harmonization Rule.'' However, paragraphs 9904.413–50(c)(8), (9) and (12) are exempt from the requirements of 9904.412–50(b)(7).

* * * * *

■ 4. In 9904.412–50, paragraphs (a)(2), (4) and (6); (b)(5); and (c)(1), (2) and (5) are revised, and paragraph (b)(7) is added to read as follows:

9904.412–50 Techniques for application.

(a) * * *

(2)(i) Except as provided in 9904.412–50(d)(2), any portion of unfunded actuarial liability attributable to either pension costs applicable to prior years that were specifically unallowable in accordance with then existing Government contractual provisions or pension costs assigned to a cost accounting period that were not funded in that period, shall be separately identified and eliminated from any unfunded actuarial liability being amortized pursuant to paragraph (a)(1) of this subsection.

(ii) Such portions of unfunded actuarial liability shall be adjusted for interest based on the interest assumption established in accordance with 9904.412–50(b)(4) without regard to 9904.412–50(b)(7). The contractor may elect to fund, and thereby reduce, such portions of unfunded actuarial liability and future interest adjustments thereon. Such funding shall not be recognized for purposes of 9904.412–50(d).

* * * * *

(4) Any amount funded in excess of the pension cost assigned to a cost accounting period shall be accounted for as a prepayment credit. The accumulated value of such prepayment credits shall be adjusted for income and expenses in accordance with 9904.413–50(c)(7) until applied towards pension cost in a future accounting period. The accumulated value of prepayment credits shall be reduced for portions of the accumulated value of prepayment credits used to fund pension costs or to fund portions of unfunded actuarial liability separately identified and maintained in accordance with 9904.412–50(a)(2). The accumulated value of any prepayment credits shall be excluded from the actuarial value of the assets used to compute pension costs for purposes of this Standard and Cost Accounting Standard 9904.413.

* * * * *

(6) For purposes of this Standard, defined-benefit pension plans funded exclusively by the purchase of individual or group permanent insurance or annuity contracts, and thereby exempted from the minimum funding requirements implemented by the Employee Retirement Income Security Act of 1974 (ERISA), 29 U.S.C. 1001 *et seq.,* as amended, shall be treated as defined-contribution pension plans. However, all other defined-benefit pension plans administered wholly or in part through insurance company contracts shall be subject to the provisions of this Standard relative to defined-benefit pension plans.

(b) * * *

(5) Pension cost shall be based on provisions of existing pension plans. This shall not preclude contractors from making salary projections for plans whose benefits are based on salaries and wages, or from considering improved benefits for plans which provide that such improved benefits must be made. For qualified defined benefit plans whose benefits are subject to a collectively bargained agreement(s) and whose benefits are not based on salaries and wages, the contractor may recognize benefit improvements expected to occur in succeeding plan years determined on the basis of the average annual increase in benefits over the 6 immediately preceding plan years.

* * * * *

(7) *CAS Pension Harmonization Rule:* For qualified defined benefit pension plans, the pension cost shall be determined in accordance with the provisions of paragraph (b)(7)(i) of this section.

(i) In any period that the sum of the minimum actuarial liability and the minimum normal cost exceeds the sum of the actuarial accrued liability and the normal cost, the contractor shall measure and assign the pension cost for the period in accordance with 9904.412 and 9904.413 by using the minimum actuarial liability and minimum normal cost as the actuarial accrued liability and normal cost, respectively, for all purposes unless otherwise excepted.

(ii) Special definitions to be used for this paragraph:

(A) The *minimum actuarial liability* shall be the actuarial accrued liability measured under the accrued benefit cost method and using an interest rate assumption as described in 9904.412–50(b)(7)(iii).

(B) The *minimum normal cost* shall be the normal cost measured under the accrued benefit cost method and using an interest rate assumption as described in 9904.412–50(b)(7)(iii). Anticipated administrative expense for the period shall be recognized as a separate incremental component of normal cost.

(iii) Actuarial Assumptions: The actuarial assumptions used to measure the minimum actuarial liability and minimum normal cost shall meet the following criteria:

(A) The interest assumption used to measure the pension cost for the current period shall reflect the contractor's best estimate of rates at which the pension benefits could effectively be settled based on the current period rates of return on investment grade fixed-income investments of similar duration to the pension benefits and that are in the top 3 quality levels available, *e.g.,* Moody's' single ''A'' rated or higher;

(B) The contractor may elect to use the same rate or set of rates, for investment grade corporate bonds of similar duration to the pension benefits, as may be published by the Secretary of the Treasury and used for determination of the minimum contribution required by ERISA. The contractor's cost accounting practice includes the election of the specific published rate or set of rates and must be consistently followed;

(C) For purposes of 9904.412–50(b)(7)(ii)(A) and (B), use of current period rates of return on investment grade corporate bonds of similar duration to the pension benefits shall not violate the provisions of 9904.412–40(b)(2) and 9904.412–50(b)(4) regarding the interest rate used to measure the minimum actuarial liability and minimum normal cost; and

(D) All actuarial assumptions, other than interest assumptions, used to measure the minimum actuarial liability and minimum normal cost shall be the same as the assumptions used elsewhere in this Standard.

(c) * * *

(1) Amounts funded in excess of the pension cost assigned to a cost accounting period pursuant to the provisions of this Standard shall be accounted for as a prepayment credit and carried forward to future accounting periods.

(2) For qualified defined-benefit pension plans, the pension cost measured for a cost accounting period is assigned to that period subject to the following adjustments, in order of application:

(i) Any amount of pension cost measured for the period that is less than zero shall be assigned to future accounting periods as an assignable cost credit. The amount of pension cost assigned to the period shall be zero.

(ii) When the pension cost equals or exceeds the assignable cost limitation:

(A) The amount of pension cost, adjusted pursuant to paragraph (c)(2)(i) of this subsection, shall not exceed the assignable cost limitation,

(B) All amounts described in 9904.412–50(a)(1) and 9904.413–50(a), which are required to be amortized, shall be considered fully amortized, and

(C) Except for portions of unfunded actuarial liability separately identified and maintained in accordance with 9904.412–50(a)(2), any portion of unfunded actuarial liability, which occurs in the first cost accounting period after the pension cost has been limited by the assignable cost limitation, shall be considered an actuarial gain or loss for purposes of this Standard. Such actuarial gain or loss shall exclude any increase or decrease in unfunded actuarial liability resulting from a plan amendment, change in actuarial assumptions, or change in actuarial cost method effected after the pension cost has been limited by the assignable cost limitation.

(iii) An amount of pension cost of a qualified pension plan, adjusted pursuant to paragraphs (c)(2)(i) and (ii) of this subsection that exceeds the sum of (A) the maximum tax-deductible amount, determined in accordance with the Internal Revenue Code at Title 26 of the U.S.C., and (B) the accumulated value of prepayment credits, shall be assigned to future accounting periods as an assignable cost deficit. The amount of pension cost assigned to the current period shall not exceed the sum of the maximum tax-deductible amount and the accumulated value of prepayment credits.

* * * * *

(5) Any portion of pension cost measured for a cost accounting period and adjusted in accordance with 9904.412–50(c)(2) that exceeds the amount required to be funded pursuant to a waiver granted under the provisions of ERISA shall not be assigned to the current period. Rather, such excess shall be treated as an assignable cost deficit, except that it shall be assigned to future cost accounting periods using the same amortization period as used for ERISA purposes.

* * * * *

■ 5. Section 9904.412–60 is amended by revising paragraphs (b)(2) and (3), (c)(1) through (6), (c)(13), and (d)(4) to read as follows:

9904.412–60 Illustrations.

* * * * *

(b) * * *

(2) For several years Contractor H has had an unfunded nonqualified pension plan which provides for payments of $200 a month to employees after retirement. The contractor is currently making such payments to several retired employees and recognizes those payments as its pension cost. The contractor paid monthly annuity benefits totaling $24,000 during the current year. During the prior year, Contractor H made lump sum payments to irrevocably settle the benefit liability of several participants with small benefits. The annual installment to amortize these lump sum payments over fifteen years at the interest rate assumption, which is based on expected rate of return on investments and complies with 9904.412–40(b)(2) and 9904.412–50(b)(4), is $5,000. Since the plan does not meet the criteria set forth in 9904.412–50(c)(3)(ii), pension cost must be accounted for using the pay-as-you-go cost method. Pursuant to 9904.412–50(b)(3), the amount of assignable cost allocable to cost objectives of that period is $29,000, which is the sum of the amount of benefits actually paid in that period ($24,000) and the second annual installment to amortize the prior year's lump sum settlements ($5,000).

(3) Contractor I has two qualified defined-benefit pension plans that provide for fixed dollar payments to hourly employees.

(i) Under the first plan, in which the benefits are not subject to a collective bargaining agreement, the contractor's actuary believes that the contractor will be required to increase the level of benefits by specified percentages over the next several years based on an established pattern of benefit improvements. In calculating pension costs for this first plan, the contractor may not assume future benefits greater than that currently required by the plan.

(ii) With regard to the second plan, a collective bargaining agreement negotiated with the employees' labor union provides that pension benefits will increase by specified percentages over the next several years. Because the improved benefits are required to be made, the contractor can consider not only benefits increases required by the collective bargaining agreement, but may also consider subsequent benefit increases based on the average increase in benefits during the previous 6 years in computing pension costs for the current cost accounting period in accordance with 9904.412–50(b)(5). The contractor shall limit projected benefits to the increases specified in the provisions of the existing plan, as amended by the collective bargaining agreement, in accordance with 9904.412–50(b)(5).

* * * * *

(c) * * *

(1) Contractor J maintains a qualified defined-benefit pension plan. The actuarial accrued liability for the plan is $20 million and is measured by the minimum actuarial liability in accordance with 9904.412–50(b)(7)(ii) since the criterion of 9904.412–50(b)(7(i) has been satisfied. The actuarial value of the assets of $18 million is subtracted from the actuarial accrued liability of $20 million to determine the total unfunded actuarial liability of $2 million. Pursuant to 9904.412–50(a)(1), Contractor J has identified and is amortizing twelve separate portions of unfunded actuarial liabilities. The sum of the unamortized balances for the twelve separately maintained portions of unfunded actuarial liability equals $1.8 million. In accordance with 9904.412–50(a)(2), the contractor has separately identified, and eliminated from the computation of pension cost, $200,000 attributable to a pension cost assigned to a prior period that was not funded. The sum of the twelve amortization bases maintained pursuant to 9904.412–50(a)(1) and the amount separately identified under 9904.412–50(a)(2) equals $2 million ($1,800,000 + 200,000). Because the sum of all identified portions of unfunded actuarial liability equals the total unfunded actuarial liability, the plan is in actuarial balance and Contractor J can assign pension cost to the current cost accounting period in accordance with 9904.412–40(c).

(2) Contractor K's pension cost computed for 2017, the current year, is $1.5 million. This computed cost is based on the components of pension cost described in 9904.412–40(a) and 9904.412–50(a) and is measured in accordance with 9904.412–40(b) and 9904.412–50(b). The assignable cost limitation, which is defined at 9904.412–30(a)(9), is $1.3 million. In accordance with the provisions of 9904.412–50(c)(2)(ii)(A), Contractor K's assignable pension cost for 2017 is limited to $1.3 million. In addition, all amounts that were previously being amortized pursuant to 9904.412–50(a)(1) and 9904.413–50(a) are considered fully amortized in accordance with 9904.412–50(c)(2)(ii)(B). The following year, 2018, Contractor K computes an unfunded actuarial liability of $4 million. Contractor K has not changed his actuarial assumptions nor amended the provisions of his pension plan. Contractor K has not had any pension

costs disallowed or unfunded in prior periods. Contractor K must treat the entire $4 million of unfunded actuarial liability as an actuarial loss to be amortized over a ten-year period beginning in 2018 in accordance with 9904.412–50(c)(2)(ii)(C) and 9904.413–50(a)(2)(ii).

(3) Assume the same facts shown in illustration 9904.412–60(c)(2), except that in 2016, the prior year, Contractor K's assignable pension cost was $800,000, but Contractor K only funded and allocated $600,000. Pursuant to 9904.412–50(a)(2), the $200,000 of unfunded assignable pension cost was separately identified and eliminated from other portions of unfunded actuarial liability. This portion of unfunded actuarial liability was adjusted for 8% interest, which is the interest assumption for 2016 and 2017, and was brought forward to 2017 in accordance with 9904.412–50(a)(2). Therefore, $216,000 ($200,000 × 1.08) is excluded from the amount considered fully amortized in 2017. The next year, 2018, Contractor K must eliminate $233,280 ($216,000 × 1.08) from the $4 million so that only $3,766,720 is treated as an actuarial loss in accordance with 9904.412–50(c)(2)(ii)(C).

(4) Assume, as in 9904.412–60(c)(2), the 2017 pension cost computed for Contractor K's qualified defined-benefit pension plan is $1.5 million and the assignable cost limitation is $1.7 million. The accumulated value of prepayment credits is $0. However, because of the limitation on tax-deductible contributions imposed by the Internal Revenue Code at Title 26 of the U.S.C., Contractor K cannot fund more than $1 million without incurring an excise tax, which 9904.412–50(a)(5) does not permit to be a component of pension cost. In accordance with the provisions of 9904.412–50(c)(2)(iii), Contractor K's assignable pension cost for the period is limited to $1 million. The $500,000 ($1.5 million − $1 million) of pension cost not funded is reassigned to the next ten cost accounting periods beginning in 2018 as an assignable cost deficit in accordance with 9904.412–50(a)(1)(vi).

(5) Assume the same facts for Contractor K in 9904.412–60(c)(4), except that the accumulated value of prepayment credits equals $700,000. Therefore, in addition to the $1 million tax-deductible contribution which was deposited on the first day of the plan year, Contractor K could apply up to $700,000 of the accumulated value of prepayment credits towards the pension cost computed for the period. In accordance with the provisions of 9904.412–50(c)(2)(iii), the amount of pension cost assigned to the current period shall not exceed $1,700,000, which the sum of the $1 million maximum tax-deductible amount and $700,000 accumulated value of prepayment credits. Contractor K's assignable pension cost for the period is the full $1.5 million computed for the period. A new prepayment credit of $200,000 is created by the excess funding after applying sum of the $1 million contribution and $700,000 accumulated value of prepayment credits towards the $1.5 million assigned pension cost ($700,000 + $1,000,000 − $1,500,000). The $200,000 of remaining accumulated value of prepayment credits is adjusted for $14,460 of investment income allocated in accordance with 9904.412–50(a)(4) and 9904.413–50(c)(7) and the sum of $214,460 is carried forward until needed in future accounting periods in accordance with 9904.412–50(a)(4) and 9904.412–50(c)(1).

(6) Assume the same facts for Contractor K in 9904.412–60(c)(4), except that the 2017 assignable cost limitation is $1.3 million and the accumulated value of prepayment credits is $0. Pension cost of $1.5 million is computed for the cost accounting period, but the assignable cost is limited to $1.3 million in accordance with 9904.412–50(c)(2)(ii)(A). Pursuant to 9904.412–50(c)(2)(ii)(B), all existing amortization bases maintained in accordance with 9904.412–50(a)(1) are considered fully amortized. The assignable cost of $1.3 million is then compared to the maximum tax-deductible amount of $1 million. Pursuant to 9904.412–50(c)(2)(iii), Contractor K's assignable pension cost for the period is limited to $1 million. The $300,000 ($1.3 million − $1 million) excess of the assignable cost limitation over the tax-deductible maximum is assigned to future periods as an assignable cost deficit.

* * * * *

(13) The assignable pension cost for Contractor O's qualified defined-benefit plan is $600,000. For the same period Contractor O contributes $700,000 which is the minimum funding requirement under ERISA. In addition, there exists $75,000 of unfunded actuarial liability that has been separately identified pursuant to 9904.412–50(a)(2). Contractor O may use $75,000 of the contribution in excess of the assignable pension cost to fund this separately identified unfunded actuarial liability, if he so chooses. The effect of the funding is to eliminate the unassignable $75,000 portion of unfunded actuarial liability that had been separately identified and thereby eliminated from the computation of pension costs. Contractor O shall then account for the remaining $25,000 ([$700,000 − $600,000] − $75,000) of excess contribution as a prepayment credit in accordance with 9904.412–50(a)(4).

(d) * * *

(4) Again, assume the set of facts in 9904.412–60(d)(2) except that, Contractor P's contribution to the Trust is $105,000 based on an interest assumption of 8%, which is based on the expected rate of return on investments and complies with 9904.412–40(b)(2) and 9904.412–50(b)(4). Under the provisions of 9904.412–50(d)(2) the entire $100,000 is allocable to cost objectives of the period. In accordance with the provisions of 9904.412–50(c)(1) Contractor P has funded $5,000 ($105,000 − $100,000) in excess of the assigned pension cost for the period. The $5,000 shall be accounted for as a prepayment credit. Pursuant to 9904.412–50(a)(4), the $5,000 shall be adjusted for an allocated portion of the total investment income and expenses in accordance with 9904.412–50(a)(4) and 9904.413–50(c)(7). Allocated earnings and expenses, and the prepayment credits, shall be excluded from the actuarial value of assets used to compute the next year's pension cost. For the current period the net return on assets attributable to investment income and expenses was 6.5%. Therefore, the accumulated value of prepayment credits of $5,325 (5,000 × 1.065) may be used to fund the next year's assigned pension cost, if needed.

* * * * *

■ 6. Section 9904.412–60.1 is added to read as follows:

9904.412–60.1 Illustrations—CAS Pension Harmonization Rule.

The following illustrations address the measurement, assignment and allocation of pension cost on or after the Applicability Date of the CAS Harmonization Rule. The illustrations present the measurement, assignment and allocation of pension cost for a contractor that separately computes pension costs by segment or aggregation of segments. The actuarial gain and loss recognition of changes between measurements based on the actuarial accrued liability, determined without regard to the provisions of 9904.412–50(b)7) and the minimum actuarial liability are illustrated in 9904.412–60.1(d). The structural format for

9904.412.60.1 differs from the format for 9904.412–60.

(a) *Description of the pension plan, actuarial assumptions and actuarial methods used for 9904.412–60.1 Illustrations.* (1) *Introduction:* Harmony Corporation has a defined-benefit pension plan covering employees at seven segments, of which some segments have contracts that are subject to this Standard and 9904.413, while other segments perform commercial work only. The demographic experience regarding employee terminations for employees of Segment 1 is materially different from that of the other six segments so that pursuant to 9904.413–50(c)(2)(iii) the contractor must separately compute the pension cost for Segment 1. Because the factors comprising pension cost for Segments 2 through 7 are relatively equal, the contractor computes pension cost for these six segments in the aggregate and allocates the aggregate cost to segments on a composite basis. Inactive employees are retained in the segment from which they terminated employment. The contractor has received its annual actuarial valuation for its qualified defined benefit pension plan, which bases the pension benefit on the employee's final average salary.

(2) *Actuarial Methods and Assumptions:* (i) *Salary Projections:* As permitted by 9904.412–50(b)(5), the contractor includes a projection of future salary increases and uses the projected unit credit cost method, which is an immediate gain actuarial cost method that satisfies the requirements of 9904.412–40(b)(1) and 50(b)(1), for measuring the actuarial accrued liability and normal cost. The contractor uses the accrued benefit cost method (also known as the unit credit cost method without projection) to measure the minimum actuarial liability and minimum normal cost. The accrued benefit cost method satisfies 9904.412–50(b)(7)(ii) as well as 9904.412–40(b)(1) and 50(b)(1).

(ii) *Interest Rates:* (A) Assumed interest rate used to measure the actuarial accrued liability and normal cost: The contractor's basis for establishing the expected rate of return on investments assumption satisfies the criteria of 9904.412–40(b)(2) and 9904.412–50(b)(4). This is referred to as the ''assumed interest rate'' for purposes of this illustration.

(B) Corporate bond rate used to measure the minimum actuarial liability and minimum normal cost: For purposes of measuring the minimum actuarial liability and minimum normal cost the contractor has elected to use a specific set of investment grade corporate bond yield rates published by the Secretary of the Treasury for ERISA's minimum funding requirements. The basis for establishing the set of corporate bond rates meets the requirements of 9904.412–50(b)(7)(iii)(A) as permitted by 9904.412–50(b)(7)(iii)(B). This set of rates is referred to as the ''corporate bond rates'' for purposes of this illustration.

(iii) *Mortality:* The mortality assumption is based on a table of generational mortality rates published by the Secretary of the Treasury and reflects recent mortality improvements. This table satisfies 9904.412–40(b)(2) which requires assumptions to ''represent the contractor's best estimates of anticipated experience under the plan, taking into account past experience and reasonable expectations.'' The specific table used for each valuation shall be identified.

(iv) *Termination of Employment:* The termination of employment (turnover) assumption is based on an experience study of Harmony Company employee terminations or causes other than retirement. Because the experience for Segment 1 was materially different from the experience for the rest of the company, the termination of employee assumption for Segment 1 was developed based on the experience of that segment only in accordance with 9904.413–50(c)(2)(iii). The termination of employment experiences for each of Segments 2 through 7 were materially similar, and therefore the termination of employee assumption for Segments 2 through 7 was developed based on the experiences of those segments in the aggregate.

(v) *Actuarial Value of Assets:* The valuation of the actuarial value of assets used for CAS 412 and 413 is based on a recognized smoothing technique that ''provides equivalent recognition of appreciation and depreciation of the market value of the assets of the pension plan.'' The disclosed method also constrains the asset value to a corridor bounded by 80% to 120% of the market value of assets. This method for measuring the actuarial value of assets satisfies the provisions of 9904.413–50(b)(2).

(b) *Measurement of Pension Costs.* Based on the pension plan, actuarial methods and actuarial assumptions described in 9904.412–60.1(a), the Harmony Corporation determines that the pension plan, as well as Segment 1 and Segments 2 through 7, have unfunded actuarial liabilities and measures its pension cost for plan year 2017 as follows:

(1) *Asset Values:* (i) *Market Values of Assets:* The contractor accounts for the market value of assets in accordance with 9904.413–50(c)(7). The contractor has elected to separately identify the accumulated value of prepayment credits from the assets allocated to segments. The accumulated value of prepayment credits are adjusted in accordance with 9904.412–50(a)(4) and 9904.413–50(c)(7). The market value of assets as of January 1, 2017, including the accumulated value of prepayment credits, is summarized in Table 1.

TABLE 1—JANUARY 1, 2017, MARKET VALUE OF ASSETS

	Total plan	Segment 1	Segments 2 through 7	Accumulated prepayments	Note
Market Value of Assets	$14,257,880	$1,693,155	$11,904,328	$660,397	1

Note 1: Information taken directly from the actuarial valuation report prepared for CAS 412 and 413 purposes and supporting documentation.

(ii) *Actuarial Value of Assets:* Based on the contractor's disclosed asset valuation method, and recognition of the asset gain or loss, which is the difference between the expected income, based on the assumed interest rate, which complies with 9904.412–40(b)(2) and 9904.412–50(b)(4), and the actual income, including realized and unrealized appreciation and depreciation for the current and four prior periods as required by 9904.413–40(b), is delayed and amortized over a five-year period. The portion of the appreciation and depreciation that is deferred until future periods is subtracted from the market value of assets to determine the actuarial value of assets for CAS 412 and 413 purposes. The actuarial value of assets cannot be less than 80%, or more than 120%, of the market value of assets. The development of the actuarial value of assets for the total plan, as well as for

Segment 1 and Segments 2 through 7, as of January 1, 2017 is shown in Table 2.

TABLE 2—JANUARY 1, 2017, ACTUARIAL VALUE OF ASSETS

	Total plan	Segment 1	Segments 2 through 7	Accumulated prepayments	Note
Market Value at January 1, 2017	$14,257,880	$1,693,155	$11,904,328	$660,397	1
Total Deferred Appreciation	(37,537)	(4,398)	(31,400)	(1.739)	2
Unlimited Actuarial Value of Assets	14,220,343	1,688,757	11,872,928	658,658	
CAS 413 Asset Corridor 80% of Market Value of Assets	11,406,304	1,354,524	9,523,462	528,318	
Market Value at January 1, 2017	14,257,880	1,693,155	11,904,328	660,397	1
120% of Market Value of Assets	17,109,456	2,031,786	14,285,194	792,476	
CAS Actuarial Value of Assets	14,220,343	1,688,757	11,872,928	658,658	3, 4

Note 1: See Table 1.
Note 2: Information taken directly from the actuarial valuation report prepared for CAS 412 and 413 purposes and supporting documentation.
Note 3: CAS Actuarial Value of Assets cannot be less than 80% of Market Value of Assets or more than 120% of Market Value of Assets.
Note 4: The Actuarial Value of Assets are used in determination of any Unfunded Actuarial Liability or Unfunded Actuarial Surplus regardless of whether the liability is based on the actuarial accrued liability measured without regard to 9904.412–50(b)(7) or minimum actuarial liability measured in accordance with 9904.412–50(b)(7).

(2) *Liabilities and Normal Costs:* (i) *Actuarial Accrued Liabilities and Normal Costs:* Based on the plan population data and the disclosed methods and assumptions for CAS 412 and 413 purposes, the contractor measures the actuarial accrued liability and normal cost on a going concern basis using an assumed interest rate that satisfies the requirements of 9904.412–40(b)(2) and 9904.412–50(b)(4). The actuarial accrued liability and normal cost for each segment are measured based on the termination of employment assumption unique to that segment. The actuarial accrued liability and normal cost for the total plan is the sum of the actuarial accrued liability and normal cost for the segments. The actuarial accrued liability and normal cost are shown in Table 3.

TABLE 3—ACTUARIAL ACCRUED LIABILITIES AND NORMAL COSTS AS OF JANUARY 1, 2017

	Total plan	Segment 1	Segments 2 through 7	Notes
Actuarial Accrued Liability (AAL)	$16,325,000	$2,100,000	$14,225,000	1
Normal Cost	910,700	89,100	821,600	1
Expense Load on Normal Cost				2 1, 2

Note 1: Information taken directly from the actuarial valuation report prepared for CAS 412 and 413 purposes and supporting documentation. The actuarial accrued liability and normal cost are computed using the assumed interest rate in accordance with 9904.412–40(b)(2) and 9904.412.50(b)(4).
Note 2: Expected administrative expenses are implicitly recognized as part of the assumed interest rate.

(ii) Likewise, based on the plan population data and the disclosed methods and assumptions for CAS 412 and 413 purposes, the contractor measures the minimum actuarial liability and minimum normal cost using a set of investment grade corporate bond yield rates published by the Secretary of the Treasury that satisfy the requirements of 9904.412–50(b)(7)(iii). The minimum actuarial liability and minimum normal cost for each segment are measured based on the termination of employment assumption for that segment. The minimum actuarial liability and minimum normal cost for the total plan is the sum of the actuarial accrued liability and normal cost for the segments as shown in Table 4.

TABLE 4—MINIMUM ACTUARIAL LIABILITIES AND MINIMUM NORMAL COSTS AS OF JANUARY 1, 2017

	Total plan	Segment 1	Segments 2 through 7	Notes
Minimum Actuarial Liability	$16,636,000	$2,594,000	$14,042,000	1
Minimum Normal Cost	942,700	102,000	840,700	1
Expense Load on Minimum Normal Cost	82,000	8,840	73,160	1, 2

Note 1: Plan level information taken directly from the actuarial valuation report prepared for ERISA purposes and supporting documentation and equals the sum of the data for the segments. Data for the segments is taken directly from the actuarial valuation report prepared for CAS 412 and 413 purposes and supporting documentation.
Note 2: Anticipated annual administrative expenses are separately recognized as an incremental component of minimum normal cost in accordance with 9904.412–50(b)(7)(ii)(B).

(3) *CAS Pension Harmonization Test:* (i) In accordance with 9904.412–50(b)(7)(i), the contractor compares the sum of the actuarial accrued liability and normal cost plus any expense load, to the sum of the minimum actuarial liability and minimum normal cost plus any expense load. Because the contractor separately computes pension costs by segment, or aggregation of segments, the applicability of 9904.412–50(b)(7)(i) is determined separately for

Segment 1 and Segments 2 through 7. See Table 5, which shows the application of the provisions of 9904.412–50(b)(7)(i), *i.e.,* the CAS pension harmonization test.

TABLE 5—CAS PENSION HARMONIZATION TEST AT JANUARY 1, 2017

	Total plan	Segment 1	Segments 2 through 7	Notes
	(Note 1)	(Note 2)	(Note 2)	
"Going Concern" Liability for Period:	....	....	....	3
Actuarial Accrued Liability	....	$2,100,000	$14,225,000	4
Normal Cost	....	89,100	821,600	4
Expense Load on Normal Cost	....	....	....	4, 5
Total Liability for Period	....	2,189,100	15,046,600	....
Minimum Liability for Period:				
Minimum Actuarial Liability	....	2,594,000	14,042,000	6
Minimum Normal Cost	....	102,000	840,700	6
Expense Load on Minimum Normal Cost	....	8,840	73,160	6, 7
Total Minimum Liability for Period	....	2,704,840	14,955,860	....

Note 1: Because the contractor determines pension costs separately for Segment 1 and Segments 2 through 7, the data for the Total Plan is not needed for purposes of the 9904.412–50(b)(7)(i) determination.

Note 2: Because the contractor determines pension cost separately for Segment 1 and Segments 2 through 7, the 9904.412–50(b)(7) CAS Pension Harmonization test is applied at the segment level to determine the larger of the Total Liability for Period or the Total Minimum Liability for Period. For Segment 1, the larger Total Minimum Liability for Period determines the measurement basis for the liability and normal cost. For Segments 2 through 7, the larger Total Liability for Period determines the measurement basis for the liability and normal cost.

Note 3: The actuarial accrued liability and normal cost plus any expense load are computed using interest assumptions based on long-term expectations in accordance with 9904.412–40(b)(2) and 9904.412–50(b)(4). For purposes of Illustration 9904.412–60.1(b), the sum of these amounts are referred to as the "Going Concern" Liability for the Period.

Note 4: See Table 3.

Note 5: Because the contractor's assumed interest rate implicitly recognizes expected administrative expenses there is no explicit amount added to the normal cost.

Note 6: See Table 4.

Note 7: The contractor explicitly identifies the expected expenses as a separate component of the minimum normal cost, as required by 9904.412–50(b)(7)(ii)(B).

(ii) As shown in Table 5 for Segment 1, the total minimum liability for the period (minimum actuarial liability and minimum normal cost) of $2,704,840 exceeds the total liability for the period (actuarial accrued liability and normal cost) of $2,189,100. Therefore, the contractor must measure the pension cost for Segment 1 using the minimum actuarial liability and minimum normal cost as the values of the actuarial accrued liability and normal cost in accordance with 9904.412–50(b)(7)(i). In other words, the contractor substitutes the minimum actuarial liability and minimum normal cost for the actuarial accrued liability and normal cost.

(iii) Conversely, as shown in Table 5 for Segments 2 through 7, the total liability for the period of $15,046,600 exceeds the total minimum liability for the period of $14,955,860 for Segments 2 through 7. Therefore, the contractor must measure the pension cost using the actuarial accrued liability and normal cost without regard for the minimum actuarial liability and minimum normal cost.

(4) *Measurement of Current Period Pension Cost:* (i) To determine the pension cost for Segment 1, the contractor measures the unfunded actuarial liability, pension cost without regard to 9904.412–50(c)(2) limitations, and the assignable cost limitation using the actuarial accrued liability and normal cost as measured by the minimum actuarial liability and minimum normal cost, respectively, which are based on the accrued benefit cost method. This measurement complies with the requirements of 9904.412–50(b)(7) and the definition of actuarial accrued liability, 9904.412–30(a)(2) and normal cost, 9904.412–30(a)(18).

(ii) To determine the pension cost for Segments 2 through 7, the contractor measures the unfunded actuarial liability, pension cost without regard to 9904.412–50(c)(2) limitations, and the assignable cost limitation using the actuarial accrued liability and normal cost based on the projected unit credit cost method, which is the contractor's established cost accounting method and the contractor's assumed interest rate based on long-term trends as required by 9904.412–50(b)(4).

(iii) Unfunded Actuarial Liability (Table 6):

TABLE 6—UNFUNDED ACTUARIAL LIABILITY AS OF JANUARY 1, 2017

	Total plan	Segment 1	Segments 2 through 7	Notes
	(Note 1)			
Actuarial Accrued Liability	$16,819,000	$ 2,594,000	$14,225,000	2
CAS Actuarial Value of Assets	(13,561,685)	(1,688,757)	(11,872,928)	3
Unfunded Actuarial Liability	3,257,315	905,243	2,352,072	....

Note 1: Because the contractor determines pensions separately for Segment 1 and Segments 2 through 7, the values are the sum of the values for Segment 1 and Segments 2 through 7.

Note 2: For Segment 1, the actuarial accrued liability is measured by the accrued benefit cost method as required by 9904.412–50(b)(7), *i.e.,* the minimum actuarial liability as described in 9904.412–50(b)(7)(ii). See Table 4. For Segments 2 through 7, the actuarial accrued liability is measured by the projected unit credit cost method, which is the contractor's established actuarial cost method since these the 9904.412–50(b)(7)(i) criterion was not met for these segments. See Table 3.

Note 3: See Table 2. The CAS Actuarial Value of Assets is used regardless of the basis for determining the liabilities. The CAS Actuarial Value of Assets allocated to Segment 1 and Segments 2 through 7 excludes the accumulated value of prepayment credits as required by 9904.412–50(a)(4).

(iv) Measurement of the Adjusted Pension Cost (Table 7):

TABLE 7—MEASUREMENT OF PENSION COST AT JANUARY 1, 2017

	Total plan	Segment 1	Segments 2 through 7	Notes
	(Note 1)			
Normal Cost	....	$ 102,000	$821,600	2
Expense Load on Normal Cost	....	8,840	....	2, 3
Amortization Installments	....	140,900	366,097	4
Measured Pension Cost	1,439,437	251,740	1,187,697	....

Note 1: Because the contractor separately computes pension cost for Segment 1 and Segments 2 through 7, only the total pension cost is shown.

Note 2: For Segment 1, the normal cost is measured by the accrued benefit cost method as required by 9904.412–50(b)(7), *i.e.,* the minimum normal cost as described in 9904.412–50(b)(7)(ii). See Table 4. For Segments 2 through 7, the normal cost is measured by the contractor's established immediate gain cost method since these the 9904.412–50(b)(7)(i) criterion was not met for these segments. See Table 3.

Note 3: Because the criterion of 9904.412–50(b)(7)(i) was met for Segment 1, the Normal Cost is measured by the Minimum Normal Cost, which explicitly identifies the expected expenses as a separate component of the minimum normal cost in accordance with 9904.412–50(b)(7)(ii)(B). See Table 4. For Segments 2 through 7, the normal cost is measured by the contractor's established immediate gain cost method, which implicitly recognizes expenses as a decrement to expected assumed interest rate, since the 9904.412–50(b)(7)(i) criterion was not met for these segments. See Table 3.

Note 4: Net amortization installment based on the unfunded actuarial liability of $3,257,315 ($905,243 for Segment 1, and $2,352,072 for Segments 2 through 7) and the contractor's assumed interest rate in compliance with 9904.412–40(b)(2) and 9904.412–50(b)(4). See Table 6.

(c) *Assignment of Pension Cost.* In 9904.412–60.1(b), the Harmony Corporation measured the total pension cost to be $1,439,437 ($251,740 for Segment 1 and $1,187,697 for Segments 2 through 7). The contractor must now determine if any of the limitations of 9904.412–50(c)(2) apply at the segment level.

(1) *Zero Dollar Floor:* The contractor compares the measured pension cost to a zero dollar floor as required by 9904.412–50(c)(2)(i). In this case, the measured pension cost is greater than zero and no assignable cost credit is established. See Table 8.

TABLE 8—CAS 412–50(c)(2)(i) ZERO DOLLAR FLOOR AS OF JANUARY 1, 2017

	Total plan	Segment 1	Segments 2 through 7	Notes
	(Note 1)			
Measured Pension Cost ≥ $0	....	$251,740	$1,187,697	2
Assignable Cost Credit	....	....	....	3

Note 1: Because the provisions of CAS 412–50(c)(2)(i) are applied at the segment level, no values are shown for the Total Plan.

Note 2: See Table 7. The Assignable Pension Cost in accordance with 9904.412–50(c)(2)(i) is the greater of zero or the Harmonized Pension Cost.

Note 3: There is no Assignable Cost Credit since the Measured Pension Cost is greater than zero.

(2) *Assignable Cost Limitation:* (i) As required by 9904.412–50(c)(2)(ii), the contractor measures the assignable cost limitation amount. The pension cost assigned to the period cannot exceed the assignable cost limitation amount. Because the measured pension cost for Segment 1 met the harmonization criterion of 9904.412–50(b)(7)(i), the assignable cost limitation is based on the sum of the actuarial accrued liability and normal cost plus expense load, using the accrued benefit cost method in accordance with 9904.412–50(b)(7)(ii). Therefore, the actuarial accrued liability and normal cost plus expense load are measured by the minimum actuarial liability and minimum normal cost plus expense load. See Table 9.

TABLE 9—CAS 412–50(c)(2)(ii) ASSIGNABLE COST LIMITATION AS OF JANUARY 1, 2017

	Total plan	Segment 1	Segments 2 through 7	Notes
	(Note 1)			
Actuarial Accrued Liability	....	$2,594,000	$14,225,000	2
Normal Cost	....	102,000	821,600	3
Expense Load on Normal Cost	....	8,840	....	4

TABLE 9—CAS 412–50(c)(2)(ii) ASSIGNABLE COST LIMITATION AS OF JANUARY 1, 2017—Continued

	Total plan	Segment 1	Segments 2 through 7	Notes
	(Note 1)			
Total Liability for Period	....	$2,704,840	$15,046,600	....
CAS Actuarial Value of Plan Assets	....	(1,688,757)	(11,872,928)	5
(A) Assignable Cost Limitation Amount	....	$1,016,083	$3,173,672	6
(B) 412–50(c)(2)(i) Assigned Cost	....	$251,740	$1,187,697	7
(C) 412–50(c)(2)(ii) Assigned Cost	$1,439,437	$251,740	$1,187,697	8

Note 1: Because the assignable cost limitation is applied at the segment level when pension costs are separately calculated by segment or aggregation of segments, no values are shown for the Total Plan other than the Assigned Cost after consideration of the Assignable Cost Limit.
Note 2: For Segment 1, the actuarial accrued liability is measured by the accrued benefit cost method as required by 9904.412–50(b)(7), *i.e.,* the minimum actuarial liability as described in 9904.412–50(b)(7)(ii)(A). See Table 4. For Segments 2 through 7, the actuarial accrued liability is measured by the contractor's established immediate gain cost method since these the 9904.412–50(b)(7)(i) criterion was not met for these segments. See Table 3.
Note 3: For Segment 1, the normal cost is measured by the accrued benefit cost method as required by 9904.412–50(b)(7), *i.e.,* the minimum normal cost as described in 9904.412–50(b)(7)(ii)(B). See Table 4. For Segments 2 through 7, the normal cost is measured by the contractor's established immediate gain cost method since these the 9904.412–50(b)(7)(i) criterion was not met for these segments. See Table 3.
Note 4: For Segment 1, the normal cost is measured by the accrued benefit cost method as required by 9904.412–50(b)(7), *i.e.,* the minimum normal cost as described in 9904.412–50(b)(7)(ii)(B), which explicitly identifies the expected expenses as a separate component of the minimum normal cost. See Table 4. For Segments 2 through 7, the normal cost is measured by the contractor's established immediate gain cost method, which implicitly recognizes expenses as a decrement to the assumed interest rate since these the 9904.412–50(b)(7)(i) criterion was not met for these segments. See Table 3.
Note 5: See Table 2. The CAS Actuarial Value of Assets is used regardless of the basis for determining the liabilities. The CAS Actuarial Value of Assets allocated to Segment 1 and Segments 2 through 7 excludes the accumulated value of prepayment credits as required by 9904.412–50(a)(4).
Note 6: The Assignable Cost Limitation cannot be less than $0.
Note 7: See Illustration 9904.412–60.1(c)(1), Table 8.
Note 8: Lesser of lines (A) or (B).

(ii) As shown in Table 9, the contractor determines that the measured pension costs for Segment 1 and Segments 2 through 7 do not exceed the assignable cost limitation and are not limited.

(3) *Measurement of Tax-Deductible Limitation on Assignable Pension Cost:* (i) Finally, after limiting the measured pension cost in accordance with 9904.412–50(c)(2)(i) and (ii), the contractor checks to ensure that the total assigned pension cost will not exceed $15,674,697, which is the sum of the maximum tax-deductible contribution ($15,014,300), which is developed in the actuarial valuation prepared for ERISA, and the accumulated value of prepayment credits ($660,397) shown in Table 1. Since the tax-deductible contribution and accumulated value of prepayment credits are maintained for the plan as a whole, these values are allocated to segments based on the assignable pension cost after adjustment, if any, for the assignable cost limitation in accordance with 9904.413–50(c)(1)(ii). See Table 10.

TABLE 10—CAS 412–50(c)(2)(iii) TAX-DEDUCTIBLE LIMITATION AS OF JANUARY 1, 2017

	Total plan	Segment 1	Segments 2 through 7	Notes
Maximum Tax-deductible Amount	$15,014,300	$2,625,818	$12,388,482	1, 2
Accumulated Prepayment Credits	660,397	115,495	544,902	3, 4
(A) 412–50(c)(2)(iii) Limitation	$15,674,697	$2,741,313	$12,933,384	....
(B) 412–50(c)(2)(ii) Assigned Cost	$1,439,437	$251,740	$1,187,697	5
Assigned Pension Cost	$1,439,437	$251,740	$1,187,697	6

Note 1: The Maximum Deductible Amount for the Total Plan is obtained from the valuation report prepared for ERISA purposes.
Note 2: The Maximum Tax-deductible Amount for the Total Plan is allocated to segments based on the assigned cost after application of 9904.412–50(c)(2)(ii) in accordance with 9904.413–50(c)(1)(i) for purposes of this assignment limitation test.
Note 3: The Accumulated Prepayment Credits for the Total Plan are allocated to segments based on the assigned cost after application of 9904.412–50(c)(2)(ii) in accordance with 9904.413–50(c)(1)(i) for purposes of this assignment limitation test.
Note 4: See Table 1.
Note 5: See Table 9.
Note 6: Lesser of lines (A) or (B).

(ii) For Segment 1, the assignable pension cost of $251,740, measured after considering the assignable cost limitation, does not exceed the 9904.412–50(c)(2)(iii) limit of $2,716,649. For Segments 2 through 7, the assignable pension cost of $1,187,697, measured after considering the assignable cost limitation, does not exceed the 9904.412–50(c)(2)(iii) limit of $12,958,048.

(d) *Actuarial Gain and Loss—Change in Liability Basis.* (1) Assume the same facts shown in 9904.412–60.1(b) for Segment 1 of the Harmony Corporation for 2017. Table 11 shows the actuarial liabilities and normal costs plus any expense loads for Segment 1 for 2016 through 2018.

TABLE 11—SUMMARY OF LIABILITIES FOR SEGMENT 1 AS OF JANUARY 1

	2016	2017	2018	Notes
"Going Concern" Liabilities for the Period:				
Actuarial Accrued Liability	$1,915,000	$2,100,000	$2,305,000	1
Normal Cost	89,600	89,100	99,500	1
Expense Load on Normal Cost	....	....	....	1, 2
Total Liability for Period	$2,004,600	$2,189,100	$2,404,500	....
Minimum Liabilities for the Period:				
Minimum Actuarial Liability	$1,901,000	$2,594,000	$2,212,000	3
Minimum Normal Cost	83,800	102,000	96,500	3
Expense Load on Minimum Normal Cost	8,300	8,840	9,300	3, 4
Total Minimum Liability for Period	$1,993,100	$2,704,840	$2,317,800	....
Interest Basis as Determined by Segment's Liabilities for Period	9904.412–50(b)(4)	9904.412–50(b)(7)(iii)	9904.412–50(b)(4)	5

Note 1: See Table 3 for 2017 values. For 2016 and 2018, the data for Segment 1 is taken directly from the actuarial valuation report prepared for CAS 412 and 413 purposes and supporting documentation, including subtotals of the data by segment.

Note 2: Because the contractor's interest assumption, which satisfies the requirements of 9904.412–40(b)(2) and 9904.412–50(b)(4), implicitly recognizes expected administrative expenses there is no explicit amount shown for the normal cost.

Note 3: See Table 4 for 2017 values. For 2016 and 2018, the data for Segment 1 is taken directly from the actuarial valuation report prepared for ERISA purposes and supporting documentation, including subtotals of the data by segment. The values for 2016 are based on the transitional minimum actuarial liability and transitional minimum normal cost measured in accordance with 9904.412–64.1(a) and (b).

Note 4: For purposes of determining minimum normal cost, the contractor explicitly identifies the expected administrative expense as a separate component as required by 9904.412–50(b)(7)(ii)(B).

Note 5: For determining the pension cost for the period, the measurements are based on the actuarial accrued liability and normal cost unless the total minimum liability for the period exceeds the "Going Concern" total liability for the period. The measurement basis was separately determined for each segment in accordance with 9904.412–50(b)(7)(i).

(2) For 2016, the sum of the minimum actuarial liability and minimum normal cost does not exceed the sum of the actuarial accrued liability and normal cost. Therefore the criterion of 9904.412–50(b)(7)(i) is not met, and the actuarial accrued liability and normal cost are used to compute the pension cost for 2016. For 2017, the sum of the minimum actuarial liability and minimum normal cost exceeds the sum of the actuarial accrued liability and normal cost, and therefore the pension cost is computed using minimum actuarial liability and minimum normal cost as required by 9904.412–50(b)(7)(i). For 2018, the sum of the minimum actuarial liability and minimum normal cost does not exceed the sum of the actuarial accrued liability and normal cost, and the actuarial accrued liability and normal cost are used to compute the pension cost for 2018 because the criterion of 9904.412–50(b)(7)(i) is not met. Table 12 shows the measurement of the unfunded actuarial liability for 2016 through 2018.

TABLE 12—UNFUNDED ACTUARIAL LIABILITY FOR SEGMENT 1 AS OF JANUARY 1

	2016	2017	2018	Notes
Current Year Actuarial Liability Basis	9904.412–50(b)(4)	9904.412–50(b)(7)(iii)	9904.412–50(b)(4)	1
Actuarial Accrued Liability	$1,915,000	$2,594,000	$2,305,000	1
CAS Actuarial Value of Assets	(1,500,000)	(1,688,757)	(1,894,486)	2
Unfunded Actuarial Liability (Actual)	$415,000	$905,243	$410,514	....

Note 1: See Table 11.

Note 2: The 2017 CAS Actuarial Value of Assets is developed in Table 2. For 2016 and 2018, the Actuarial Value of Assets for Segment 1 is taken directly from the actuarial valuation report prepared for CAS 412 and 413 purposes and supporting documentation.

(3) Except for changes in the value of the assumed interest rate used to measure the minimum actuarial liability and minimum normal cost, there were no changes to the pension plan's actuarial assumptions or actuarial cost methods during the period of 2016 through 2018. The contractor's actuary measured the expected unfunded actuarial liability and determined the actuarial gain or loss for 2017 and 2018 as shown in Table 13.

TABLE 13—MEASUREMENT OF ACTUARIAL GAIN OR LOSS FOR SEGMENT 1 AS OF JANUARY 1

	2016	2017	2018	Notes
Actual Unfunded Actuarial Liability	(Note 1)	$905,243	$410,514	2
Expected Unfunded Actuarial Liability	....	(381,455)	(848,210)	3
Actuarial Loss (Gain)	....	$523,788	$(437,696)	....

Note 1: The determination of the actuarial gain or loss that occurred during 2015 and measured on 2016 is outside the scope of this Illustration.

Note 2: See Table 12.

Note 3: Information taken directly from the actuarial valuation report prepared for CAS 412 and 413 purposes and supporting documentation. The expected unfunded actuarial liability is based on the prior unfunded actuarial liability updated based on the assumed interest rate in compliance with 9904.412–40(b)(2) and 9904.412–50(b)(4). Note that in accordance with 9904.412–50(b)(7)(iii)(D), the corporate bond yield rate is only used to determine the minimum actuarial liability but not to adjust the liability for the passage of time.

(4) According to the actuarial valuation report, the 2017 actuarial loss of $523,788 includes a $494,000 actuarial loss due to a change in measurement basis from using an actuarial accrued liability of $2,100,000 to using a minimum actuarial liability of $2,594,000, including the effect of any change in the interest rate basis. (See Table 11 for the actuarial accrued liability and the minimum actuarial liability.) The $494,000 loss ($2,594,000–$2,100,000) due to the change in the liability basis is amortized as part of the total actuarial loss of $523,788 over a ten-year period in accordance with 9904.412–50(a)(1)(v) and 9904.413–50(a)(2)(ii). Similarly, the next year's valuation report shows a 2018 actuarial gain of $437,696, which includes a $93,000 actuarial gain ($2,305,000–$2,212,000) due to a change from a minimum actuarial liability back to a an actuarial accrued liability basis, which includes the effect of any change in interest rate basis. The $93,000 gain due the change in the liability basis will be amortized as part of the total $437,696 actuarial gain over a ten-year period in accordance with 9904.412–50(a)(1) and 9904.413–50(a)(2)(ii).

■ 7. Section 9904.412–63 is revised to read as follows:

9904.412–63 Effective Date.

(a) This Standard is effective as of February 27, 2012, hereafter known as the ''Effective Date'', and is applicable for cost accounting periods after June 30, 2012, hereafter known as the ''Implementation Date.''

(b) Following receipt of a contract or subcontract subject to this Standard on or after the Effective Date, contractors shall follow this Standard, as amended, beginning with its next cost accounting period beginning after the later of the Implementation Date or the receipt date of a contract or subcontract to which this Standard is applicable in accordance with paragraph (a) of this section. The first day of the cost accounting period that this Standard, as amended, is first applicable to a contractor or subcontractor is the ''Applicability Date of the CAS Pension Harmonization Rule'' for purposes of this Standard. Prior to the Applicability Date of the CAS Pension Harmonization Rule, contractors or subcontractors shall follow the Standard in 9904.412 in effect prior to the Effective Date.

(1) Following the award of a contract or subcontract subject to this Standard received on or after the Effective Date, contractors with contracts or subcontracts subject to this Standard that were received prior to the Effective Date shall continue to follow the Standard in 9904.412 in effect prior to the Effective Date. Beginning with the Applicability Date of the CAS Pension Harmonization Rule, such contractors shall follow this Standard, as amended, for all contracts or subcontracts subject to this Standard.

(2) Following the award of a contract or subcontract subject to this Standard received during the period beginning on or after the date published in the **Federal Register** and ending before the Effective Date, contractors shall follow the Standard in 9904.412 in effect prior to the Effective Date. If another contract or subcontract, subject to this Standard, is received on or after the Effective Date, the provisions of 9904.412–63(b)(1) shall apply.

■ 8. Section 9904.412–64.1 is added to read as follows:

9904.412–64.1 Transition Method for the CAS Pension Harmonization Rule.

Contractors or subcontractors that become subject to the Standard, as amended, during the Pension Harmonization Transition Period shall recognize the change in cost accounting method in accordance with paragraphs (a) and (b).

(a) The Pension Harmonization Rule Transition Period is the five cost accounting periods beginning with a contractor's first cost accounting period beginning after June 30, 2012, and is independent of the receipt date of a contract or subcontract subject to this Standard. The Pension Harmonization Rule Transition Period begins on the first day of a contractor's first cost accounting period that begins after June 30, 2012.

(b) Phase in of the Minimum Actuarial Liability and Minimum Normal Cost. During each successive accounting period of Pension Harmonization Rule Transition Period, the contractor shall recognize on a scheduled basis the amount by which the minimum actuarial liability differs from the actuarial accrued liability; and the amount by which the sum of the minimum normal cost plus any expense load differs from the sum of the normal cost plus any expense load.

(1) For purposes of determining the amount of the difference, the minimum actuarial liability and minimum normal cost shall be measured in accordance with 9904.412–50(b)(7)(ii).

(2) During each successive accounting period of the Pension Harmonization Rule Transition Period, the transitional minimum actuarial liability shall be set equal to the actuarial accrued liability adjusted by an amount equal to the difference between the minimum actuarial liability and actuarial accrued liability, multiplied by the scheduled applicable percentage for that period. The sum of the transitional minimum normal cost plus any expense load shall be set equal to the sum of normal cost plus any expense load, adjusted by an amount equal to the difference between the minimum normal cost and the normal cost, plus expense loads, multiplied by the scheduled applicable percentage for that period.

(3) The scheduled applicable percentages for each successive accounting period of the Pension Harmonization Rule Transition Period are as follows: 0% for the First Cost Accounting Period, 25% for the Second Cost Accounting Period, 50% for the Third Cost Accounting Period, 75% for the Fourth Cost Accounting Period, and 100% for the Fifth Cost Accounting Period.

(4) The transitional minimum actuarial liability and transitional minimum normal cost measured in accordance with this provision shall be used for purposes of the 9904.412–50(b)(7) minimum actuarial liability and minimum normal cost.

(5) The actuarial gain or loss attributable to experience since the prior valuation, measured as of the First Cost Accounting Period of the Pension Harmonization Rule Transition Period, shall be amortized over a ten-year period in accordance with 9904.413–50(a)(2)(ii).

(c) Transition Illustration. Assume the same facts for the Harmony Corporation in Illustration 9904.412–60.1(a) and (b), except that this is the Fourth Cost Accounting Period of the Pension Harmonization Rule Transition Period. As in Illustration 9904.412–60.1(a) and (b), the contractor separately computes pension costs for Segment 1, and computes pension costs for Segments 2 through 7 in the aggregate. The contractor has two actuarial valuations prepared: one measures the actuarial accrued liability and normal cost using the contractor's expected rate of return on investments assumption, in accordance with 9904.412–40(b)(2) and

9904.412–50(b)(4), and the other valuation measures the minimum actuarial liability and minimum normal cost based on the assumed current yields on investment quality corporate bonds in accordance with 9904.412–50(b)(7)(iii)(A). The actuarial valuations present the values subtotaled for each segment and in total for the plan as a whole.

(1) The contractor applies 9904.412–64.1(b) as follows:

(i) (A) For Segment 1, the $494,000 ($2,594,000—$2,100,000) difference between the minimum actuarial liability and the actuarial accrued liability is multiplied by 75%. Therefore for Segment 1, the minimum actuarial liability for purposes of 9904.412–50(b)(7) is adjusted to a transitional minimum actuarial liability of $2,470,500 ($2,100,000 + [75% × $494,000]).

(B) For Segments 2 through 7, the ($183,000) difference ($14,042,000 – $14,225,000) between the minimum actuarial liability and the actuarial accrued liability is multiplied by 75%. For Segment 2 through 7, the minimum actuarial liability for purposes of 9904.412–50(b)(7) is adjusted to a transitional minimum actuarial liability of $14,115,200 ($14,087,750 + [75% × ($183,000)]).

(C) The computation of the transitional minimum actuarial liability that incrementally recognizes the difference between the minimum actuarial liability and the actuarial accrued liability for Segment 1, and for Segments 2 through 7, is shown in Table 1 below:

TABLE 1—DEVELOPMENT OF TRANSITIONAL MINIMUM ACTUARIAL LIABILITY FOR FOURTH TRANSITION PERIOD

	Total plan	Segment 1	Segments 2 through 7	Notes
	(Note 1)			
Minimum Actuarial Liability		$2,594,000	$14,042,000	2
		(2,100,000)	(14,225,000)	3
Actuarial Accrued Liability Difference		$494,000	$(183,000)	4
Phase In Percentage (Period 4)		75%	75%	5
Phase In Liability Difference		$370,500	$(137,250)	6
Actuarial Accrued Liability		2,100,000	14,225,000	6
Transitional Minimum: Actuarial Liability		$2,470,500	$14,087,750	

Note 1: The values for the Total Plan are not shown because the 9904.412–50(b)(7)(i) threshold criterion is applied separately for each segment.

Note 2: See Illustration 9904.412–60.1(b)(2)(ii), Table 4.

Note 3: See Illustration 9904.412–60.1(b)(2)(i), Table 3.

Note 4: The phase in percentage will be applied to positive or negative differences in the actuarial liabilities, since the purpose of the phase in is to incrementally move the measurement away from the actuarial accrued liability to the minimum actuarial liability, regardless of the direction of the movement.

Note 5: Appropriate transition percentage for the Fourth Cost Accounting Period of the Pension Harmonization Rule Transition Period as stipulated in 9904.412–64.1(b)(3).

Note 6: The actuarial accrued liability is adjusted by the phase in difference between liabilities, either positive or negative, in accordance with 9904.412–64.1(b)(2).

(ii) (A) For Segment 1, the $21,740 ($110,840–$89,100) difference between the minimum normal cost and the normal cost, plus expense loads, is multiplied by 75%. Therefore for Segment 1, the minimum normal cost plus expense load, for purposes of 9904.412–50(b)(7), is adjusted to a transitional minimum normal cost plus expense load of $105,405 ($89,100 + [75% × $21,740]).

(B) For Segments 2 through 7, the 92,260 ($913,860–$821,600) difference between the minimum normal cost and the normal cost, plus expense loads, is multiplied by 75%. Therefore, for Segments 2 through 7, the minimum normal cost for purposes of 9904.412–50(b)(7) is adjusted to a transitional minimum normal cost plus expense load of $890,795 ($821,600 + [75% × $92,260]).

(C) The computation of the transitional minimum normal cost plus expense load for Segment 1, and for Segments 2 through 7, is shown in Table 2 below:

TABLE 2—DEVELOPMENT OF TRANSITIONAL MINIMUM NORMAL COST FOR FOURTH TRANSITION PERIOD

	Total plan	Segment 1	Segments 2 through 7	Notes
	(Note 1)			
Minimum Normal Cost		$102,000	$840,700	2
Expense Load on Normal Cost		8,840	73,160	2, 3
Minimum Normal Cost Plus Expense Load		$110,840	$913,860	2
Normal Cost Plus Expense Load		(89,100)	(821,600)	4
Difference		$21,740	$92,260	5
Phase In Percentage (Period 4)		75%	75%	6
Phase In Normal Cost Difference		$16,305	$69,195	7
Normal Cost Plus Expense Load		89,100	821,600	7
Transitional Minimum:				

TABLE 2—DEVELOPMENT OF TRANSITIONAL MINIMUM NORMAL COST FOR FOURTH TRANSITION PERIOD—Continued

	Total plan	Segment 1	Segments 2 through 7	Notes
Normal Cost Plus Expense Load		$105,405	$890,795	

Note 1: The values for the Total Plan are not shown because the 9904.412–50(b)(7)(i) threshold criterion is applied separately for each segment.
Note 2: See Illustration 9904.412–60.1(b)(2)(ii), Table 4.
Note 3: For minimum normal cost valuation purposes, the contractor explicitly identifies the expected administrative expenses as a separate component of minimum normal cost.
Note 4: See Illustration 9904.412–60.1(b)(2)(i), Table 3. Expected expenses are implicitly recognized as part of the contractor's expected rate of return on investments assumption.
Note 5: The phase in percentage will be applied to positive and negative differences in the normal costs plus expense loads, since the purpose of the phase in is to incrementally move the measurement from the normal cost plus expense load, to the minimum normal cost plus expense load, regardless of the direction of the movement.
Note 6: Appropriate transition percentage for the Fourth Cost Accounting Period of the Pension Harmonization Rule Transition Period stipulated in 9904.412–64.1(b)(3).
Note 7: The sum of the normal cost plus expense load is adjusted by the phase in difference between normal costs, either positive or negative, in accordance with 9904.412–64.1(b)(2).

(2) The contractor applies the provisions of with 9904.412–50(b)(7)(i) using the transitional minimum actuarial liability and transitional minimum normal cost plus expense load, in accordance with 9904.412–64.1(b)(4).

(i) The comparison of the sum of the actuarial accrued liability and normal cost plus expense load, and the sum of the transitional minimum actuarial liability and minimum normal cost plus expense load, for Segment 1, and for Segments 2 through 7, is summarized in Table 3 below:

TABLE 3—SUMMARY OF LIABILITY AND NORMAL COST VALUES FOR FOURTH TRANSITION PERIOD

	Total plan	Segment 1	Segments 2 through 7	Notes
	(Note 1)			
"Going Concern" Liabilities for Period:				
Actuarial Accrued Liability		$2,100,000	$14,225,000	2
Normal Cost Plus Expense Load		89,100	821,600	3
Total Liability for Period		2,189,100	15,046,600	
Transitional Minimum Liabilities for the Period:				
Transitional Minimum Actuarial Liability		2,470,500	14,087,750	1
Transitional Minimum Normal Cost Plus Expense Load		105,405	890,795	3
Total Transitional Minimum Liability for Period		2,575,905	14,978,545	4

Note 1: The values for the Total Plan are not shown because the 9904.412–50(b)(7)(i) threshold criterion is applied separately for each segment.
Note 2: See Table 1.
Note 3: See Table 2.
Note 4: If the threshold criterion is met, then the pension cost for the period is measured based on the Transitional Minimum Actuarial Liability and Transition Normal Cost Plus Expense Load.

(ii) For Segment 1, the Total Transitional Minimum Liability for the Period of $2,575,905 exceeds the total liability for the period of $2,189,100. (See Table 3.) Therefore, in accordance with 9904.412–50(b)(7)(i), the pension cost for Segment 1 is measured using the actuarial accrued liability and normal cost as measured by the transitional minimum actuarial liability and transitional minimum normal cost, which are based on the accrued benefit cost method. This measurement complies with the requirements of 9904.412–50(b)(7) and with the definition of actuarial accrued liability, 9904.412–30(a)(2), and normal cost, 9904.412–30(a)(18).

(iii) For Segments 2 through 7, the total liability for the period of $15,046,600 exceeds the Total Transitional Minimum Liability for the Period of $14,978,545. (See Table 3.) Therefore, in accordance with 9904.412–50(b)(7)(i), the pension cost for Segment 2 through 7 is measured using the actuarial accrued liability and normal cost, which are based on the projected benefit cost method.

(3) The contractor computes the pension cost for the period in accordance with the provisions of 9904.412–50(b)(7)(i), which considers the transitional minimum actuarial liability and transitional minimum normal cost plus expense load, in accordance with 9904.412–64.1(b).

(i) The contractor computes the unfunded actuarial liability as shown in Table 4 below:

TABLE 4—UNFUNDED ACTUARIAL LIABILITY FOR FOURTH TRANSITION PERIOD

	Total Plan	Segment 1	Segments 2 through 7	Notes
	(Note 1)			
Actuarial Accrued Liability		$2,470,500	$14,225,000	2

TABLE 4—UNFUNDED ACTUARIAL LIABILITY FOR FOURTH TRANSITION PERIOD—Continued

	Total Plan	Segment 1	Segments 2 through 7	Notes
CAS Actuarial Value of Assets	....	(1,688,757)	(11,872,928)	3
Unfunded Actuarial Liability	....	781,743	2,352,072	

Note 1: The values for the Total Plan are not shown because the 9904.412–50(b)(7)(i) threshold criterion is applied separately for each segment.

Note 2: Because the Pension Harmonization criterion of 9904.412–50(b)(7)(i) has been met for Segment 1, the actuarial accrued liability is measured by the transitional minimum actuarial liability as required by 9904.412–64.1(b)(4). See Table 3. Because the Pension Harmonization criterion of 9904.412–50(b)(7)(i) was not satisfied for Segments 2 through 7, the actuarial accrued liability is based on the actuarial assumptions that reflect long-term trends in accordance with 9904.412–50(b)(4), *i.e.,* the transitional minimum actuarial liability does not apply.

Note 3: See Illustration 9904.412–60.1(b)(1)(ii), Table 2.

(ii) Measurement of the Pension Cost for the current period (Table 5):

TABLE 5—PENSION COST FOR FOURTH TRANSITION PERIOD

	Total plan	Segment 1	Segments 2 through 7	Notes
	(Note 1)			
Normal Cost Plus Expense Load	....	$105,405	$821,600	2
Amortization Installments	....	101,990	314,437	3, 4
Pension Cost Computed for the Period	1,343,432	207,395	1,136,037	

Note 1: Except for the Total Pension Cost Computed for the Period, the values for the Total Plan are not shown because the 9904.412–50(b)(7)(i) threshold criterion is applied separately for each segment.

Note 2: See Table 3. Because the Pension Harmonization criterion of 9904.412–50(b)(7)(i) has been met for Segment 1, the sum of the normal cost plus the expense load is measured by the sum of the transitional minimum normal cost plus the expense load, as required by 9904.412–64.1(a). Because the Pension Harmonization criterion of 9904.412–50(b)(7)(i) was not satisfied for Segments 2 through 7, the sum of the normal cost plus any applicable expense load is based on the contractor's actuarial assumptions reflecting long-term trends in accordance with 9904.412–40(b)(2) and 9904.412–50(b)(4), *i.e.,* the transitional minimum normal cost plus the expense load does not apply.

Note 3: Net amortization installment based on the unfunded actuarial liability of $781,743 for Segment 1, and $2,352,072 for Segments 2 through 7, including an interest equivalent on the unamortized portion of such liability. See Table 4. The interest adjustment is based on the contractor's interest rate assumption in compliance with 9904.412–40(b)(2) and 9904.412–50(b)(4).

Note 4: See 9904.64–1(c)(4) for details concerning the recognition of the unfunded actuarial liability during the first Pension Harmonization Rule Transition Period.

(4) The Silvertone Corporation separately computes pension costs for Segment 1, and computes pension costs for Segments 2 through 7 in the aggregate.

(i) For the First Cost Accounting Period of the Pension Harmonization Rule Transition Period, the difference between the actuarial accrued liability and the minimum actuarial liability, and the difference between the normal cost and the minimum normal cost, are multiplied by 0%. Therefore the transitional minimum actuarial liability and transitional minimum normal are equal to the actuarial accrued liability and normal cost. The total transitional minimum liability for the period does not exceed the total liability for the period in conformity with the criterion of 9904.412–50(b)(7)(i). Therefore, the pension cost for the First Cost Accounting Period of the Pension Harmonization Rule Transition Period is computed using the actuarial accrued liability and normal cost.

(ii) The actuarial gain attributable to experience during the prior period that is measured for the cost accounting period is amortized over a ten-year period in accordance with 9904.412–50(a)(1)(v) and 9904.413–50(a)(2)(ii).

(iii) The contractor computes the pension cost for First Cost Accounting Period of the Pension Harmonization Rule Transition Period as shown in Table 6 below.

TABLE 6—COMPUTATION OF THE PENSION FOR THE FIRST TRANSITION PERIOD

	Total plan	Segment 1	Segments 2 through 7	Notes
	(Note 1)			
Amortization of Unfunded Liability Net Amortization Installment from Prior Periods	....	$81,019	$523,801	2
January 1, 2013, Actuarial Loss (Gain) Amortization Installment	....	(9,369)	(68,740)	3
Net Amortization Installment	....	71,650	455,061	....
Normal Cost plus expense load	....	78,400	715,000	4
Pension Cost Computed for the Period	....	150,050	1,170,061	

Note 1: The values for the Total Plan are not shown because the 9904.412–50(b)(7)(i) threshold criterion is applied separately for each segment.

Note 2: Amortization installments of actuarial gains and losses, and other portions of the unfunded actuarial liability identified prior to January 1, 2013, in accordance with 9904.412–50(a)(1)(v) and 9904.413–50(b)(2)(ii), including an interest adjustment based on the contractor's long-term interest assumption in compliance with 9904.412–40(b)(2) and 9904.412–50(b)(4).

Note 3: The actuarial gains for both Segment 1, and Segments 2 through 7, as measured as of January 1, 2013, are amortized over a ten-year period in accordance with 9904.413–50(a)(2)(ii) and 9904.412–64–1(b)(4). Note that although the source of the actuarial gains was the deviation between assumed and actual changes during the prior period, the gain is measured on January 1, 2013, and so the ten-year amortization period applies in the current period, including an interest adjustment based on the contractor's long-term interest assumption in compliance with 9904.412–40(b)(2) and 9904.412–50(b)(4).

Note 4: For the first period of the Pension Harmonization Rule transition period, the adjustment to the sum of the actuarial accrued liability and normal cost is adjusted by $0. Therefore the sum of the transitional minimum actuarial liability and transitional minimum normal cost plus expense load is equal to the sum of the actuarial accrued liability and normal cost plus expense load, and the criterion of 9904.412–50(b)(7)(i) was not met for either Segment 1, or Segments 2 through 7. The sum of the normal cost plus expense load is based on the sum of the going concern normal cost plus expense load.

■ 9. Section 9904.413–30 is amended by revising paragraphs (a)(1) and (16) to read as follows:

9904.413–30 Definitions.

(a) * * *

(1) *Accrued benefit cost method* means an actuarial cost method under which units of benefits are assigned to each cost accounting period and are valued as they accrue; that is, based on the services performed by each employee in the period involved. The measure of normal cost under this method for each cost accounting period is the present value of the units of benefit deemed to be credited to employees for service in that period. The measure of the actuarial accrued liability at a plan's measurement date is the present value of the units of benefit credited to employees for service prior to that date. (This method is also known as the Unit Credit cost method without salary projection.)

* * * * *

(16) *Prepayment credit* means the amount funded in excess of the pension cost assigned to a cost accounting period that is carried forward for future recognition. The Accumulated Value of Prepayment Credits means the value, as of the measurement date, of the prepayment credits adjusted for income and expenses in accordance with 9904.413–50(c)(7) and decreased for amounts used to fund pension costs or liabilities, whether assignable or not.

* * * * *

■ 10. Section 9904.413–40 is amended by revising paragraph (c) to read as follows:

9904.413–40 Fundamental requirement.

* * * * *

(c) *Allocation of pension cost to segments.* Contractors shall allocate pension costs to each segment having participants in a pension plan.

(1) A separate calculation of pension costs for a segment is required when the conditions set forth in 9904.413–50(c)(2) or (3) are present. When these conditions are not present, allocations may be made by calculating a composite pension cost for two or more segments and allocating this cost to these segments by means of an allocation base.

(2) When pension costs are separately computed for a segment or segments, the provisions of Cost Accounting Standard 9904.412 regarding the assignable cost limitation shall be based on the actuarial value of assets, actuarial accrued liability and normal cost for the segment or segments for purposes of such computations. In addition, for purposes of 9904.412–50(c)(2)(iii), the amount of pension cost assignable to a segment or segments shall not exceed the sum of:

(i) The maximum tax-deductible amount computed for the plan as a whole, and

(ii) The accumulated value of prepayment credits not already allocated to segments apportioned among the segment(s).

■ 11. Section 9904.413–50 is amended by revising paragraphs (a)(2), (c)(1)(i) and (c)(7), (8), and (9) and adding paragraphs (b)(6) and (c)(12)(viii) to read as follows:

9904.413–50 Techniques for application.

(a) * * *

* * * * *

(2) Actuarial gains and losses shall be amortized as required by 9904.412–50(a)(1)(v).

(i) For periods beginning prior to the ''Applicability Date of the CAS Pension Harmonization Rule,'' actuarial gains and losses determined under a pension plan whose costs are measured by an immediate-gain actuarial cost method shall be amortized over a fifteen-year period in equal annual installments, beginning with the date as of which the actuarial valuation is made.

(ii) For periods beginning on or after the ''Applicability Date of the CAS Pension Harmonization Rule,'' such actuarial gains and losses shall be amortized over a ten-year period in equal annual installments, beginning with the date as of which the actuarial valuation is made.

(iii) The installment for a cost accounting period shall consist of an element for amortization of the gain or loss, and an element for interest on the unamortized balance at the beginning of the period. If the actuarial gain or loss determined for a cost accounting period is not material, the entire gain or loss may be included as a component of the current or ensuing year's pension cost.

* * * * *

(b) * * *

(6) The market value of the assets of a pension plan shall include the present value of contributions received after the date the market value of plan assets is measured.

(i) The assumed rate of interest, established in accordance with 9904.412–40(b)(2) and 9904.412–50(b)(4), shall be used to determine the present value of such receivable contributions as of the valuation date.

(ii) The market value of plan assets measured in accordance with paragraphs (b)(6)(i) of this section shall be the basis for measuring the actuarial value of plan assets in accordance with this Standard.

(c) * * *

(1) * * *

(i) When apportioning to the segments the sum of (A) the maximum tax-deductible amount, which is determined for a qualified defined-benefit pension plan as a whole pursuant to the Internal Revenue Code at Title 26 of the U.S. C., as amended, and (B) the accumulated value of the prepayment credits not already allocated to segments, the contractor shall use a base that considers the otherwise assignable pension costs or the funding levels of the individual segments.

* * * * *

(7) After the initial allocation of assets, the contractor shall maintain a record of the portion of subsequent contributions, permitted unfunded accruals, income, benefit payments, and expenses attributable to the segment, and paid from the assets of the pension plan. Income shall include a portion of any investment gains and losses attributable to the assets of the pension plan. Income and expenses of the pension plan assets shall be allocated to the segment in the same proportion that

the average value of assets allocated to the segment bears to the average value of total pension plan assets, including the accumulated value of prepayment credits, for the period for which income and expenses are being allocated.

(8) If plan participants transfer among segments, contractors need not transfer assets or actuarial accrued liabilities, unless a transfer is sufficiently large to distort the segment's ratio of pension plan assets to actuarial accrued liabilities determined using the accrued benefit cost method. If assets and liabilities are transferred, the amount of assets transferred shall be equal to the actuarial accrued liabilities transferred, determined using the accrued benefit cost method and long-term assumptions in accordance with 9904.412–40(b)(2) and 9904.412–50(b)(4).

(9) Contractors who separately calculate the pension cost of one or more segments may calculate such cost either for all pension plan participants assignable to the segment(s) or for only the active participants of the segment(s). If costs are calculated only for active participants, a separate segment shall be created for all of the inactive participants of the pension plan and the cost thereof shall be calculated. When a contractor makes such an election, assets shall be allocated to the segment for inactive participants in accordance with paragraphs (c)(5), (6), and (7) of this subsection. When an employee of a segment becomes inactive, assets shall be transferred from that segment to the segment established to accumulate the assets and actuarial liabilities for the inactive plan participants. The amount of assets transferred shall be equal to the actuarial accrued liabilities, determined under the accrued benefit cost method and long-term assumptions in accordance with 9904.412–40(b)(2) and 9904.412–50(b)(4), for these inactive plan participants. If inactive participants become active, assets and liabilities shall similarly be transferred to the segments to which the participants are assigned. Such transfers need be made only as of the last day of a cost accounting period. The total annual pension cost for a segment having active employees shall be the amount calculated for the segment and an allocated portion of the pension cost calculated for the inactive participants. Such an allocation shall be on the same basis as that set forth in paragraph (c)(1) of this subsection.

* * * * *

(12) * * *

(viii) If a benefit curtailment is caused by a cessation of benefit accruals mandated by the Employee Retirement Income Security Act of 1974 (ERISA), 29 U.S.C. 1001 *et seq.,* as amended based on the plan's funding level, then no adjustment for the curtailment of benefit pursuant to this paragraph (c)(12) is required. Instead, the curtailment of benefits shall be recognized as follows:

(A) If the written plan document provides that benefit accruals are nonforfeitable once employment service has been rendered, and shall be retroactively restored if, and when, the benefit accrual limitation ceases, then the contractor may elect to recognize the expected benefit accruals in the actuarial accrued liability and normal cost during the period of cessation for the determination of pension cost in accordance with the provisions of 9904–412 and 413.

(B) Otherwise, the curtailment of benefits shall be recognized as an actuarial gain or loss for the period. The subsequent restoration of missed benefit accruals shall be recognized as an actuarial gain or loss in the period in which the restoration occurs.

■ 12. Section 9904.413–60 is amended by revising paragraphs (a) and (c)(12) and (18) and adding paragraphs (b)(3) and (c)(26) to read as follows:

9904.413–60 Illustrations.

(a) *Assignment of actuarial gains and losses.* Contractor A has a defined-benefit pension plan whose costs are measured under an immediate-gain actuarial cost method. The contractor makes actuarial valuations every other year. In the past, at each valuation date, the contractor has calculated the actuarial gains and losses that have occurred since the previous valuation date, and has merged such gains and losses with the unfunded actuarial liabilities that are being amortized. Pursuant to 9904.413–40(a), the contractor must make an actuarial valuation annually, and any actuarial gains or losses measured must be separately amortized over a specific period of years beginning with the period for which the actuarial valuation is made in accordance with 9904.413–50(a)(1) and (2). If the actuarial gain or loss is measured for a period beginning prior to the ''Applicability Date for the CAS Pension Harmonization Rule,'' the gain or loss shall be amortized over a fifteen-year period. For gains and losses measured for periods beginning on or after the ''Applicability Date for the CAS Pension Harmonization Rule,'' the gain or loss shall be amortized over a ten-year period.

(b) * * *

(3) Assume that besides the market value of assets of $10 million that Contractor B has on the valuation date of January 1, 2017, the contractor makes a contribution of $100,000 on July 1, 2017, to cover its prior year's pension cost. For ERISA purposes, the contractor measures $98,000 as the present value of the contribution on January 1, 2017, and therefore recognizes $10,098,000 as the market value of assets. The contractor must also use this market value of assets for contract costing purposes as required by 9904.413–50(b)(6)(ii). The actuarial value of assets on January 1, 2017, must also reflect $98,000 as the present value of the July 1, 2017, contribution of $100,000.

(c) * * *

(12) Contractor M sells its only Government segment. Through a contract novation, the buyer assumes responsibility for performance of the segment's Government contracts. Just prior to the sale, the actuarial accrued liability under the actuarial cost method in use is $18 million, and the market value of assets allocated to the segment of $22 million. In accordance with the sales agreement, Contractor M is required to transfer $20 million of plan assets to the new plan sponsored by the buyer. In determining the segment closing adjustment under 9904.413–50(c)(12), the actuarial accrued liability and the market value of assets are reduced by the amounts transferred to the buyer's new plan in accordance with the terms of the sales agreement. The adjustment amount, which is the difference between the remaining assets ($2 million) and the remaining actuarial liability ($0), is $2 million.

* * * * *

(18) Contractor Q terminates its qualified defined-benefit pension plan without establishing a replacement plan. At termination, the market value of assets is $85 million. All obligations for benefits are irrevocably transferred to an insurance company by the purchase of annuity contracts at a cost of $55 million, which thereby determines the actuarial liability in accordance with 9904.413–50(c)(12)(i). The contractor receives a reversion of $30 million ($85 million − $55 million). The adjustment is equal to the reversion amount, which is the excess of the market value of assets over the actuarial liability. However, the Internal Revenue Code imposes a 50% excise tax of $15 million (50% of $30 million) on the reversion amount. In accordance with 9904.413–50(c)(12)(vi), the $30 million adjustment amount is reduced by the $15 million excise tax. Pursuant to 9904.413–50(c)(12)(vi), a share of the $15 million net adjustment ($30 million − $15 million) shall be allocated,

without limitation, as a credit to CAS-covered contracts.

* * * * *

(26) Assume the same facts as Illustration 9904.413–60(c)(20), except that ERISA required Contractor R to cease benefit accruals. In this case, the segment closing adjustment is exempted by 9904.413–50(c)(12)(viii). If the written plan document provides that benefit accruals will automatically be retroactively reinstated when permitted by ERISA, then the pension cost measured pursuant to CAS 412 and this Standard for contract costing purposes may continue to recognize the benefit accruals, if the contractor has so elected. If there is evidence that the contractor might revoke the plan provision to restore the missed benefit accruals, then the contractor shall not make such election. Otherwise, the pension cost measured pursuant to CAS 412 and this Standard shall not recognize any benefit accruals until, and unless, the plan is subsequently amended to reinstate the accruals. Furthermore, when the plan is amended, the change in the actuarial accrued liability shall be measured as an actuarial gain or loss, and amortized in accordance with 9904.412–50(a)(1)(v) and 9904.413–50(a)(2)(ii).

■ 13. Section 9904.413–63 is revised to read as follows:

9904.413–63 Effective Date.

(a) This Standard is effective as February 27, 2012, hereafter known as the ''Effective Date'', and is applicable for cost accounting periods after June 30, 2012, hereafter known as the ''Implementation Date.''

(b) Following receipt of a contract or subcontract subject to this Standard on or after the Effective Date, contractors shall follow this Standard, as amended, beginning with its next cost accounting period beginning after the later of the Implementation Date or the receipt date of a contract or subcontract to which this Standard is applicable in accordance with this paragraph (a). The first day of the cost accounting period that this Standard, as amended, is first applicable to a contractor or subcontractor is the ''Applicability Date of the CAS Pension Harmonization Rule'' for purposes of this Standard. Prior to the Applicability Date of the CAS Pension Harmonization Rule, contractors or subcontractors shall follow the Standard in 9904.413 in effect prior to the Effective Date.

(1) Following the award of a contract or subcontract subject to this Standard received on or after the Effective Date, contractors with contracts or subcontracts subject to this Standard that were received prior to the Effective Date shall continue to follow the Standard in 9904.413 in effect prior to the Effective Date. Beginning with the Applicability Date of the CAS Pension Harmonization Rule, such contractors shall follow this Standard, as amended, for all contracts or subcontracts subject to this Standard.

(2) Following the award of a contract or subcontract subject to this Standard received during the period beginning on or after the date published in the **Federal Register** and ending before the Effective Date, contractors shall follow the Standard in 9904.413 in effect prior to the Effective Date. If another contract or subcontract, subject to this Standard, is received on or after the Effective Date, the provisions of 9904.413–63(b)(1) shall apply.

■ 14. Section 9904.413–64.1 is added to read as follows:

9904.413–64.1 Transition Method for the CAS Pension Harmonization Rule.

The transition method for the CAS Pension Harmonization Rule under this Standard shall be in accordance with 9904.412.64.1 Transition Method for CAS Pension Harmonization Rule.

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