

Cost Accounting Standards: Overview and Best Practices

Joseph G. Martinez
K. Tyler Thomas

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Agenda

- Introduction to the Cost Accounting Standards ("CAS")
 - Overview/Fundamental Requirements
 - Applicability
 - Standards
- CAS Disclosure Statements and Best Practices
- Managing CAS Noncompliances and Cost Impact Assessments
- Recent Developments

Overview

- CAS (48 C.F.R. Pt. 99): establishes cost accounting standards for determining the cost of "final cost objectives"
 - Governs the measurement, assignment and allocation of costs
 - Part of allowability
 - Including compliance with generally accepted accounting principles
 - Separate from cost principles
- Allocation of Costs
 - Cost allocation means "to assign an item of cost, or a group of items of cost, to one or more cost objectives"
 - CAS Preference for direct allocation
 - Fundamental Requirement: costs are allocated on causal or beneficial basis

Overview (cont.)

- Application
 - Requires "triggering" covered contract - \$7.5M
 - Then applies to all contracts in excess of \$750K unless an exemption applies
 - Exemptions include:
 - Competitive firm, fixed price
 - Commercial Items
 - Small Business Exempt
- Effect
 - Consistent application of compliant accounting practices
 - Price reductions for noncompliance; permits recovery under fixed-price contracts

Fundamental Requirements

- Disclose practices (when applicable)
- Follow consistently established cost accounting practices
 - Not just disclosed practices
 - May change prospectively or retroactively within same fiscal year with Administrative Contracting Officer (“ACO”) approval
 - Cost impact/price adjustment liability
- Comply with CAS in effect or as later modified (as applicable)
 - Type of CAS coverage

CAS Applicability

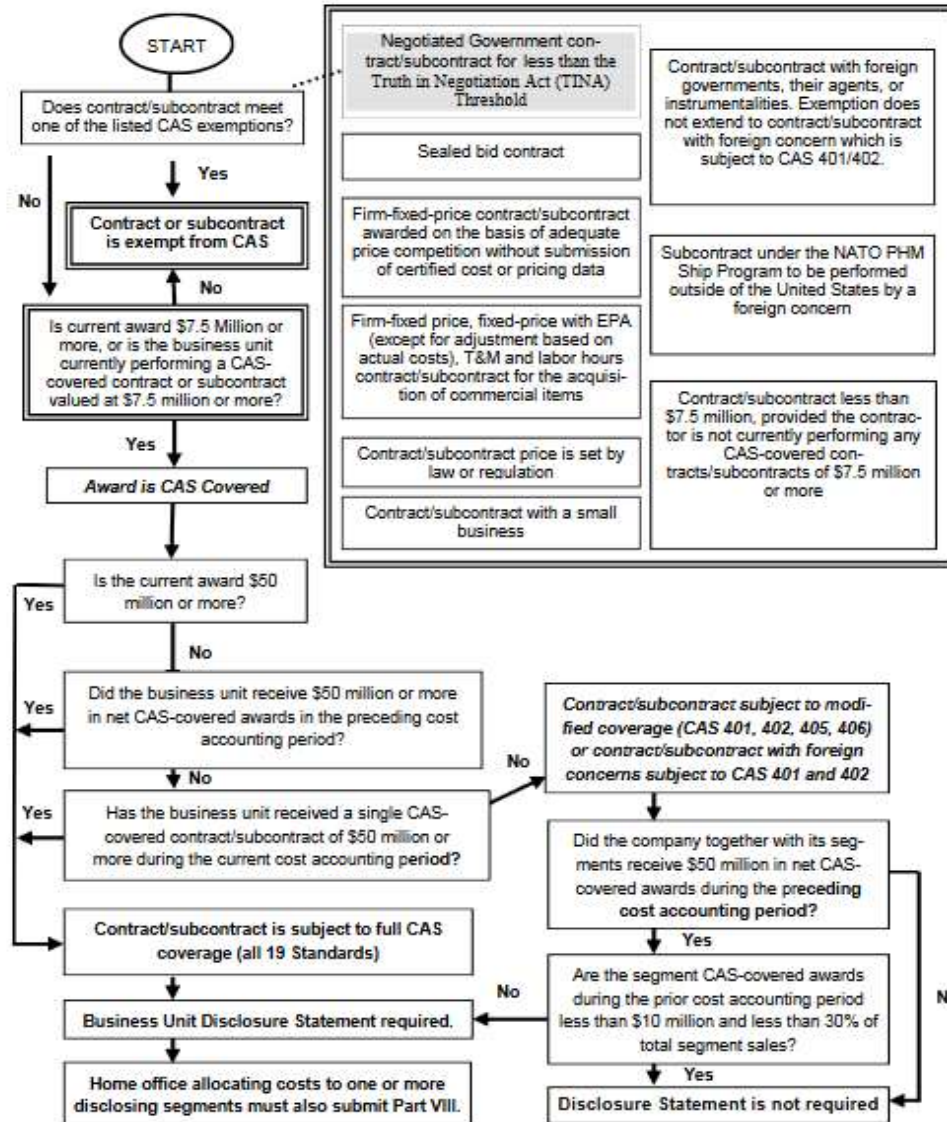
- Full v. modified CAS coverage
 - Full
 - Single CAS-covered contract award of \$50M or more during prior period; or
 - Business unit received \$50M or more in net CAS-covered prime and subcontract awards during prior period
 - Modified
 - CAS-covered contract award greater than \$7.5M (trigger), but less than \$50M in prior period; and
 - Business unit received less than \$50M in CAS-covered awards during prior period

CAS Applicability (cont.)

- Full v. modified coverage (cont.)
 - Full
 - Comply with all 19 Cost Accounting Standards
 - DS required
 - Modified
 - Comply with CAS 401, 402, 405 and 406
 - May require filing of DS
- Note: Some CAS requirements incorporated through cost principles

Figure 8-1-1
CAS Coverage and Disclosure Statement Determination

CAS Exemptions – 48 CFR 9903.201-1(b)



CAS Standards

- CAS provides 18 standards covering various practices
 - CAS 401 through 420 (no 416 and no 419)
- We have categorized into four types for discussion:
 - Consistency
 - Allocation
 - Compensation
 - Tangible Assets / Capital
- Based on "segments"
- Generally contractors have wide discretion to determine their cost accounting practices
- Government has burden of establishing any noncompliance

CAS - Consistency Standards*

- CAS 401 - Consistency in Estimating, Accumulating and Reporting Costs
- CAS 402 - Consistency in Allocating Costs Incurred for the Same Purpose
- CAS 405 - Accounting for Unallowable Costs
- CAS 406 - Cost Accounting Period

*These are the four standards that apply under modified CAS

CAS - Allocation Standards

- CAS 403 - Allocation of Home Office Expenses to Segments
- CAS 410 - Allocation of Business Unit G&A to Final Cost Objectives
- CAS 418 - Allocation of Direct and Indirect Costs
- CAS 420 - Accounting for IR&D/B&P Costs

CAS - Compensation Standards

- CAS 408 - Accounting for the Cost of Compensated Personal Absence
- CAS 415 - Accounting for the Cost of Deferred Compensation
- CAS 412 - Compensation and Measurement of Pension Costs
- CAS 413 - Adjustment and Allocation of Pension Costs

CAS - Tangible Assets and Capital Standards

- CAS 404 - Capitalization of Tangible Capital Assets
- CAS 407 - Use of Standard Costs for Direct Material and Direct Labor
- CAS 409 - Depreciation of Tangible Capital Assets
- CAS 411 - Account for Acquisition Costs of Material
- CAS 414 - Cost of Money as an Element of the Cost of Facilities Capital
- CAS 416 - Accounting for Insurance Costs
- CAS 417 - Cost of Money as an Element of the Cost of Capital Assets Under Construction

CAS Disclosure Statements

- What is it?
 - A written summary of a contractor's cost accounting practices set forth at 48 C.F.R. 9903.202-9
 - Standard form submitted for segments and home office units
 - DS Form, CASB DS-1
- Who must file?
 - Business unit receiving award of \$50M or more
 - Company, together with segments, receiving net awards in prior year of \$50M or more
 - Segments of the company allocating costs greater than TINA threshold, unless exempted or low amount of CAS business
 - Home office allocating material amount of costs to disclosing segments

CAS Disclosure Statements (cont.)

- Issues
 - Deviations from disclosed practices potential noncompliance
 - Lack of "adequate" DS may preclude contract award
 - Level of detail in continuation sheets
 - Frequency of amendments
 - Government views everything in DS as cost accounting practice
 - Subcontractor DS

CAS Disclosure Statements - Best Practices

- Best Practices for Developing and Submitting Disclosure Statements
 - Disclosure statement should contain a contractor's methods or techniques for allocating, assigning, and measuring costs
 - Appropriate level of detail
 - Lesser details – greater flexibility, but more potential for disagreement/confusion
 - Greater details – less flexibility, but potentially less government disagreement/confusion
 - DCAA likely to view anything contained in a DS as an accounting “method or technique”
 - Be wary of DCAA demands for revisions or resubmissions

CAS Noncompliances

- FAR § 52.230-3(a)(4): permits the government to adjust a contract price if CAS noncompliance results in “any aggregate increased costs paid” by the government
- CAS may provide the government with an alternative argument for recovery
 - Permits the government to "re-open" fixed price contracts, so often attempt to assert CAS noncompliance in addition to unallowable costs
 - Any finding of unallowable costs may also result in noncompliance with CAS 405

Managing CAS Noncompliances

- Managing Noncompliances Combining Cost Impacts/Offsets
 - Offsetting increased costs with decreased costs from different/multiple changes or noncompliances
 - CAS and relevant contract clauses silent
 - FAR 30.606 prohibits offsetting, unless only combining increased costs
- Offset prohibitions permit “cherry picking” and potential government windfall
 - *Raytheon Co., Space & Airborne Sys.*, ASBCA Nos. 57801, *et al.*, 15-1 BCA ¶ 36,024
 - For agreements executed after Apr. 8, 2005, FAR 30.606 validly disallows such offsets
 - FAR 30.606 does not allow the government to double-recover for costs added to flexibly priced contracts and subtracted from fixed-price contracts

Managing CAS Noncompliances (cont.)

- Cost Impact Proposals
 - Show estimated increased or decreased costs
 - For each affected CAS-covered contract and subcontract
 - By contract type
 - By agency
 - Requires knowing what contracts were CAS covered and the basis of the pricing
 - Best practice is to maintain a current list of contracts that are subject to full or modified CAS coverage or exempt from CAS

Managing CAS Noncompliances (cont.)

- Two Types of Cost Impact Proposals
 - General Dollar Magnitude (“GDM”)
 - Should contain, at a minimum:
 - Estimate of the aggregate impact on CAS-covered contracts by contract type and by various departments/agencies
 - May use a variety of methods to determine the increase/decrease
 - Representative sample of affected CAS-covered contracts/subcontracts
 - Change in indirect rates multiplied by total estimated base
 - Any other method that provides a reasonable approximation of the total increase/decrease in cost for all affected contracts and subcontracts

Managing CAS Noncompliances (cont.)

- Two Types of Cost Impact Proposals (cont.)
 - Detailed Cost Impact (“DCI”)
 - Should contain data at the contract/subcontract level, including:
 - Fixed price
 - Target/estimated cost
 - Accumulated cost to date
 - Estimate to complete
 - Target profit or fee
 - Sharing ratio
 - Ceiling price
 - Period of performance
 - Profit or fee impact
 - Total increased/(decreased) cost to the government

Updates - NDAA FY 2017 Section 820

- There has been little activity in the last five years from the existing CASB which has prompted some of the changes addressed in Section 820
 - Adjusts the CAS Board's duties to ensure the CAS rely, to the maximum extent practicable, on GAAP
 - Requires the CAS Board to review disputes regarding the standards and consider whether greater clarity in the standards would avoid such disputes
 - Increases the value of contracts for which a CAS waiver may be granted to \$100,000,000
 - Revises DCAA acceptance of commercial audit findings

Updates - The Defense CAS Board

- The DOD CASB
 - Designated as an independent Board, 7 Members
 - The DOD CFO, after consultation with the DOD CASB, is to prescribe rules and procedures
 - Exclusive authority, with respect to DOD, to implement CAS to achieve uniformity and consistency
 - Authority to make recommendations to the CASB regarding changes
 - DOD CASB does not have authority to promulgate new standards
- Issues:
 - Potential for conflict when it comes to implementation
 - Effect unclear

Updates - Materiality

- COs abuse discretion when they fail to analyze the materiality of the cost impacts at issue in accordance with CAS 305, Materiality
- Materiality under CAS 305 is mandatory, but COs possess a great deal of discretion to consider the criteria where appropriate, and no one criterion is necessarily determinative

Raytheon Co., Space & Airborne Sys's, ASBCA No. 58068, 16-1 BCA ¶ 36,484

Updates - Not All Financial Accounting Issues Are CAS Governed

- Contractor classified a building lease as an operating lease
- Government failed to state a claim for a CAS 404 noncompliance because CAS 404, by its plain language, applies only to tangible capital assets and leases are intangible assets
- Also found that CAS Board intended to allow contractor to determine whether a lease should be treated as a capital lease or an operating lease

Exelis, Inc., ASBCA No. 60131, 16-1 BCA ¶ 36,485

Thank you

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Dentons US LLP
1400 Wewatta Street
Suite 700
Denver, CO 80202-5548
United States

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