

**DENTONS**



# Cost Accounting Standards: Overview and Best Practices

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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

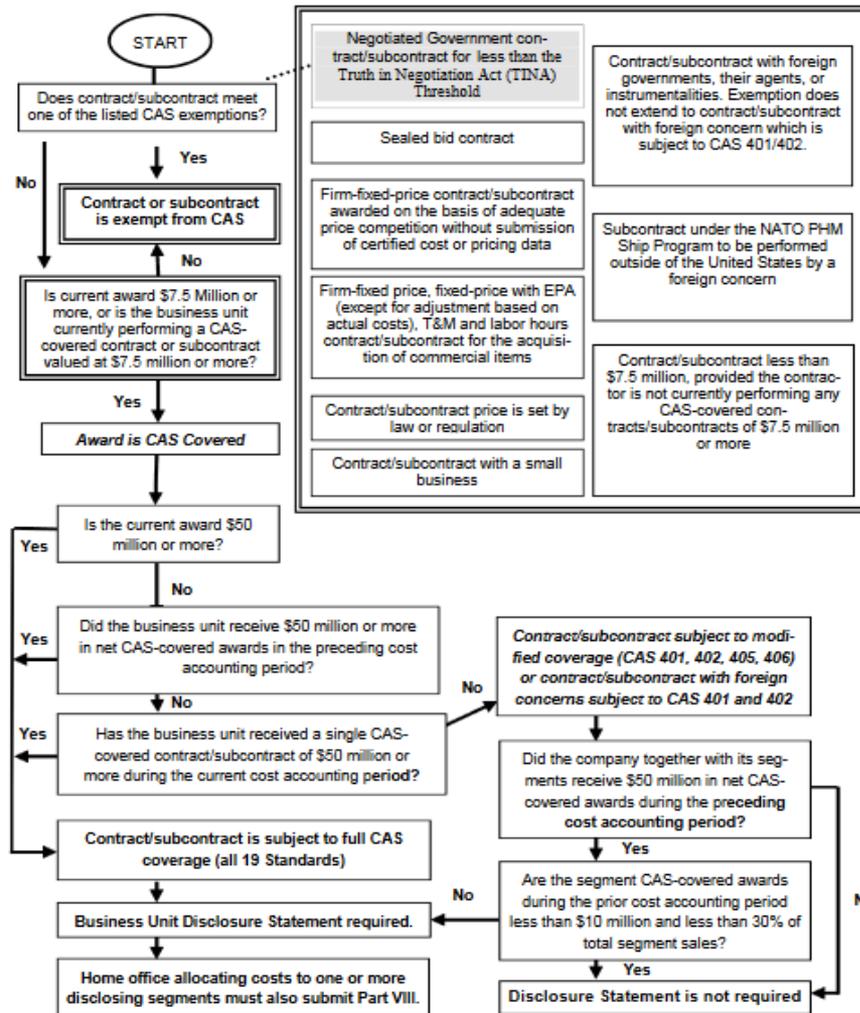
- Full v. modified CAS coverage
  - Full
    - Single CAS-covered contract award of \$50M or more during prior period; or
    - Business unit received \$50M or more in net CAS-covered prime and subcontract awards during prior period
  - Modified
    - CAS-covered contract award greater than \$7.5M (trigger),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