

## 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 revised, 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.

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