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FACT ...

The fact that CAS 415 now applies to all ESOPs (pension and non-pension) does not change the fact that a pension ESOP is governed by FAR 52.216-7. Although the CAS Board actions have improved life in terms of accounting for ESOPs, the CAS Board has no authority to change FAR 52.216-7.

Government Contracts Consulting

Provided by Beason & Nalley, Inc.

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ESOP (EMPLOYEE STOCK OWNERSHIP PLANS) FINAL RULE DEFINING CAS APPLICABILITY

As published in the Federal Register, May 1, 2008, ESOPs, effective for contracts awarded after June 2, 2008, are subject to CAS 415, Accounting for the cost of deferred compensation. Previously, ESOPs considered to be pension ESOPs were subject to CAS 412 (also incorporated by reference into FAR 31.205-6(j)); hence, it did not matter if a contract was CAS covered or not CAS covered). Regarding the change, the effective date is actually somewhat complicated giving recognition to the existence (or potential existence) of advance agreements which would remain in

effect unless modified to incorporate the revised requirements of CAS. Further, the earliest effective date is the start of the cost accounting period beginning after receipt of a CAS covered contract (after June 2, 2008 which means that a calendar year contractor will likely have an effective

FURTHER MORE...

Further, the earliest effective date is the start of the cost accounting period beginning after receipt of a CAS covered contract (after June 2, 2008 which means that a calendar year contractor will likely have an effective date of January 1, 2009).

date of January 1, 2009). Because CAS and FAR are separate regulatory bodies, it isn't clear if and how the CAS change impacts the allowable cost and payment clause, FAR 52.216-7(b)(2) which limits reimbursement (for employer contributions to employee pension plans) until actually paid unless funding is no less than quarterly's. Typically, ESOPs are not funded on a quarterly basis; hence, billable/reimbursable when actually paid. The fact that CAS 415 now applies to all ESOPs (pension and non-pension) does not change the fact that a pension ESOP is governed by FAR 52.216-7. Although the CAS Board actions have improved life in terms of accounting for ESOPs, the CAS Board has no authority to change FAR 52.216-7.

CAS BOARD AND HARMONIZATION OF CAS 412-413 WITH PENSION PROTECTION ACT (PPA)

The CAS Board is required by the PPA to harmonize CAS 412 and 413 with the PPA no later than January 1, 2010. Although this requirement (Congressional mandate) applies to eligible government contractors (defined as those whose primary work is subject to FAR/DFARS FAR with such revenues exceeding \$5 billion annually), it would be impractical if not unprecedented for the “harmonization” to exclude other government contractors who all face dual, but inconsistent regulations (PPA/ERISA and CAS/FAR). In July 2007, the CAS Board issued its Staff Discussion Paper inviting public comments to facilitate the CAS Board action to harmonize CAS 412 and 413 with the PPA. In the interim, DOD (DPAP, now DPAPSS) has very clearly stated that increased costs for anticipated changes to the CAS shall not be included in any contract, forward pricing rates or re-opener clauses allowing adjustment at a later date (reference to a December 22, 2006 Memorandum). DPAPSS recently reaffirmed this policy in response to an industry request that DPAPSS request that the CAS Board temporarily waive the requirements of CAS 412 and 413. Although DOD’s reaffirmation is wholly consistent with its December 2006 memorandum, it and the CAS Board Staff Discussion Paper suggest that harmonization will unlikely equal synchronization because of one major obstacle:



affordability. The government can afford to require companies to increase pension funding because it ultimately shifts the net financial burden from the government to the corporate community. In contrast, it is not affordable to allow those increased pension costs to become increased contract costs on DOD contracts at a time when DOD budgets are expected to significantly decline. Not that affordability equals sound cost allocability principles, but affordability is a reality whereas principles are a theory. In this context, so too is the concept of fair and reasonable price a “theory” and not a “reality”.

THE LATEST AUDIT QUEST, “IN SEARCH OF EARMARKS”

In April DCAA issued an Audit Alert “Lobbying Costs Related to Legislative Earmarks” noting that lobbying costs are unallowable under

FAR 31.205-22. To help its auditors connect the dots, DCAA explains that a legislative earmark refers to a Congressional provision directing funds to be spent on specific projects. Interestingly enough, the source for DCAA’s explanation appears to be Wikipedia and DCAA curiously avoided using the OMB definition (at the same Wikipedia page) “earmarks are funds provided by the Congress for projects of programs where the congressional direction circumvents Executive Branch merit-based or competitive allocation processes, or

DEFINITION ...

Regardless of the precise definition, earmarks are the subject of an audit alert because earmarks implicate lobbying as the most likely originating activity leading to the earmarked appropriations.



specifies the location or recipient, or otherwise curtails the ability of the Executive Branch to manage critical aspects of the funds allocation process". Regardless of the precise definition, earmarks are the subject of an audit alert because earmarks implicate lobbying as the most likely originating activity leading to the earmarked appropriations. The DCAA hypothesis and a very sound hypothesis is that some amount of lobbying activity (thus unallowable costs) will be associated with a contract or subcontract representing an earmarked project. Hence, auditors are already asking contractors for additional contract/subcontract data; specifically, the identity of those tied to congressional earmarks. Unless a contractor tracks that in its contracts database, it's arguable that a contractor has no contractual obligation to determine and to identify those which trace back to earmarked funds. Nonetheless, the audit inquiry

will be forthcoming and it should be recognized that unallowable lobbying costs are expressly unallowable and subject to penalties (FAR 42.709).

READER INPUTS FOR FUTURE NEWSLETTERS

Beason & Nalley develops its topics based upon recent regulation, publicly accessible government policies and our experience in assisting clients with regulatory compliance. However, we are also interested in the ongoing compliance experiences of our readers; hence, we invite your input in terms of suggestions for topics based upon your compliance experiences. Suggested topics along with any background information (i.e., your experience) should be sent to sbaker@beasonnalley.com.

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FAR Part 31 Cost Principles Training Course

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Brief Synopsis:

This one-day comprehensive course will enable audience participants to understand relevance, applicability, and compliance features of the most important cost principles provisions, and to understand the trap doors and problem issues that can arise when failing to comply with these important cost guidelines.

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Instructors

Mike Steen

Darryl Walker

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