



APR 8 2003

MEMORANDUM FOR RONALD POUSSARD  
DIRECTOR  
DEFENSE ACQUISITION REGULATIONS COUNCIL

FROM: RODNEY P. LANTIER, DIRECTOR *Rodney P. Lantier*  
REGULATORY AND FEDERAL ASSISTANCE  
PUBLICATIONS DIVISION

SUBJECT: FAR Case 2001-034, General Provisions of the Cost Principals

Attached are comments received on the subject FAR case published at 68 FR 5774; February 4, 2003. The comment closing date was April 7, 2003.

<u>Response Number</u>	<u>Date Received</u>	<u>Comment Date</u>	<u>Commenter</u>
2001-034-1	04/08/03	03/06/03	Larry Caton
2001-034-2	04/03/03	04/03/01	Lockheed Martin
2001-034-3	04/04/03	04/04/03	AIA

Attachments

3/6/03

To: General Services Administration  
FAR Secretariat (MVA)  
1800 F Street NW., Room 4035  
ATTN: Laurie Duarte  
Washington, DC 20405

2001-034-1

Subject: FAR case 2001-034

From: Larry Caton,  
Contract Specialist with CMS

The following are some observations from reading the proposed FAR change on special allocations for facilities contracts:

- 1) The overall objective of increasing consistency in regulation applicable to CAS and non-CAS covered contractors is a desirable change.
- 2) Why not make all CAS standards applicable to all FAR contracts and then exclude certain CAS standards that should not be applied to FAR contracts (like the requirement to file a disclosure statement). The approach of combining regulations would seem to make more sense, especially now that CAS has been re-codified into FAR. For example, make all contracts CAS covered and exempt certain classes of contracts from certain CAS standards were appropriate.
- 3) It does not seem right that non fully CAS covered facilities contracts would be entitled to a special allocation and other non fully CAS covered contracts would not. The special allocation should apply to all contracts and not just facilities contracts.
- 4) Increasing the consistency of terminology between CAS and FAR is very desirable.
- 5) The proposed special allocation change in FAR lacks the illustrations that are included in CAS. For example, CAS 410-60(g) makes the point that contract cost/activated that are outside the contractor's normal productive activity should be excluded from the G&A base.
- 6) The insertion of the word related in section 31.106-2 (b) (3) Special allocations, would make the statement clearer as follows: (3) Exclude the **related** allocation base data for the facilities contract from the base used to allocate the pool.
- 7) In section 31.203 (g), The use of the phrase "a base period" is misleading. We should use the same language that is in CAS 406, which uses the phrase "cost accounting periods". Furthermore, it appears we have two regulations on the same topic, when CAS 406 would work for both.

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**Anthony M. DiPasquale**  
Vice President  
Government Financial Management

April 3, 2003

General Services Administration  
FAR Secretariat (MVA)  
1800 F Street N.W., Rm. 4035  
Washington, D.C. 20405

Attn: Laurie Duarte

Subject: FAR Case 2001-034

Dear Ms. Duarte:

Lockheed Martin Corporation (LMC) appreciates the opportunity to comment on proposed revisions to the FAR General Provisions of the Cost Principles; Exceptions to General Rule on Allowability and Allocability; Direct Costs; and Indirect Costs. In addition, as the industry representative on the Cost Accounting Standards (CAS) Board, my comments reflect industry's perspective regarding CAS in FAR Cost Principles.

**General**

While there are some improvements in clarity and minimal streamlining (deletions), the net proposed revisions represent significant steps backwards in contract administration by adding prescriptive requirements and reducing contract administration flexibility. In addition, we continue to see more CAS type language being added to FAR Cost Principles. By law, the CAS Board governs the measurement, assignment and allocation of cost to cost objectives. FAR Cost Principles should be limited to matters of allowability and any inclusion of CAS in FAR should be by direct reference or quote. CAS language in FAR results in lowering the CAS threshold and is contrary to progressive initiatives such as DFARS Transformation.

**Proposed 2.101 Definitions**

Instead of deleting the CAS definition of "indirect cost", the proposed language adds the CAS definition of "direct cost" to 2.101. Both terms are defined in CAS 418 and we suggest that a listing of such CAS terms in FAR direct the reader to the appropriate CAS. This suggestion, if employed broadly, eliminates redundancy and any inadvertent differences of interpretation when CAS is not directly quoted.

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*Proposed 31.106-2 Exceptions to General Rules on Allowability and Allocability*

The proposed title change from the above heading to “Special Allocations” begs the question as to whether FAR attempts to supercede CAS. The current clause with five paragraphs could have been deleted as part of streamlining. The material is adequately covered in CAS and FAR 31.109 (Advance Agreements). However, the proposed change adds prescriptive language and reverses who is responsible for determining special allocations.

At Proposed 31.106-2(b)(1), (2) and (3), language is added that prescribes the use of certain accounting methods for special allocations for “facilities contracts”. This includes the word “shall” that will lead to disagreements as to accounting decisions. This entire language should be deleted since CAS adequately covers the topic.

At proposed 31.106-2(c), the language flips the responsibility of accounting decisions from the contractor to the contracting officer. Specifically: “The Cognizant Federal agency is responsible for determining whether the conditions necessitating a special allocation exist and negotiating the terms of an advance agreement”, totally takes such accounting decisions out of the hands of contractors and directs the contracting officer to make the accounting decision and requires that the contracting officer must negotiate an advance agreement. This is clearly against public policy. In addition, advance agreements should always be optional, not mandatory. As proposed, what happens if the contractor does not agree to sign such an agreement as determined by the contracting officer? What is the remedy? The proposed language should be deleted.

At proposed 31.106-2(d) and (e), the language provides examples that are not all inclusive. CAS 404 covers this topic, and the proposed FAR language will cause disputes because of the differences in interpretation between CAS and FAR. As previously stated, the existing 31.106-2 should have been deleted under streamlining. If this suggestion is not adopted, then the proposed revisions should not be implemented because they will disturb clauses that are currently understood and have not generated disputes.

*Proposed 31.201-1 Composition of Total Cost*

At proposed 31.201-1(a), the language duplicates “standard cost” phrases at the beginning and end of the paragraph. Once again, FAR deals with allocability. Specifically, “standard cost” is fully defined and dealt with in CAS 407. There is no need to paraphrase CAS language or to eliminate the reference to CAS requirements.

*Proposed 31.201-2 Determining Allowability*

At proposed 31.201-2(a), the language constitutes a major change in determining allowability. The current language (“The factors to be considered in determining whether a cost is allowable include the following:”) is proposed to be replaced with language (“A cost is allowable only when all of the following requirements are met.”) that is overly prescriptive, limits contracting officer’s discretion, and violates the Guiding Principles (1.102), and Role of the Acquisition Team (1.102-4) found at the very beginning and heart of FAR. Specifically, the proposed

language does not “encourage innovation, and local adaptation where uniformity is not essential;” nor does it provide “the authority to the maximum extent practicable and consistent with the law, to determine the application of rules, regulations, and policies on a specific contract.” Further, it runs contrary to 1.102-4(e): “The FAR outlines procurement policies and procedures that are used by members of the Acquisition Team. If a policy or procedure, or a particular strategy or practice, is in the best interest of the Government and is not specifically addressed in the FAR, nor prohibited by law (statutes or case law), Executive order or other regulation, Government members of the Team should not assume it is prohibited. Rather, absence of direction should be interpreted as permitting the Team to innovate and use sound business judgment that is otherwise consistent with law and within the limits of their authority. Contracting officers should take the lead in encouraging business process innovations and ensuring that business decisions are sound.” LMC feels strongly that the proposed language must be dropped and that the existing language be retained.

### Proposed 31.203 Indirect Costs

As previously stated, proposed revisions to this section fail to remove CAS from FAR. There are direct quotes from CAS 402 [e.g. 31.203(a) second sentence] and other CAS language that should be eliminated in the spirit of DFARS Transformation. A simple word count of this section shows the word “allocate” in various forms twenty times. Cost allocation is the responsibility of the CAS Board. In contrast, the word “allowable” is used once as is the word “unallowable”. Clearly, there has been no step forward to remove CAS from FAR, Part 31 - Cost Principles. We see no valid reason to replicate CAS in FAR. The result is to lower the CAS threshold, contrary to CAS Board actions, and public policy considerations.

At proposed 31.203(c), the language is modified to reflect the outcome of a court case (i.e., Martin Marietta – G & A costs) that sustained the Government’s position. While this is understandable, we see no FAR revision to reflect the outcome of another court case (i.e., Martin Marietta – Change in Accounting) where the Government’s position was not sustained. The Councils should treat both situations alike and not attempt to sway contracting officers in one direction or another by selectively adding the outcome of certain court cases.

At proposed 31.203(f)(2), the same language that is proposed at 31.106-2(c) is used (see previous comments to that section). Once again, the proposed language flips around the responsibilities of the contracting officer and the contractor with regard to accounting decision. The language also requires the contracting officer to obtain an advance agreement when, this too, is the responsibility of the contractor and the action should be optional, not mandatory. The language should be deleted with, at most, inclusion of a reference to see 31.109.

034-2

Summary

The proposed revisions in FAR Case 2001-34 (General Provisions of the Cost Principles, etc.) do not result in positive improvement to the contract administration process. Specifically:

- Instead of eliminating CAS from FAR, CAS type language is added.
- Instead of providing more flexibility to contracting officers, language is added that is prescriptive.
- Instead of maintaining the concept that it is the contractor's responsibility to design the accounting system, including the need for special allocations and advance agreements, language flips the responsibility to the contracting officer.
- Instead of equitably reflecting final case law decisions, language is added only where the Government's position was sustained.

LMC believes strongly that the proposed revisions conflict with the spirit and intent of DFARS Transformation, tread on the authority of the CAS Board, and are inconsistent with FAR Part-1 and public policy.

I would welcome further discussion of these matters if requested, and/or answer any questions. Please do not hesitate to call me at 301-897-6781.

Sincerely,



Anthony M. DiPasquale

2001-034-3



April 4, 2003

General Services Administration  
FAR Secretariat (MVA)  
ATTN: Laurie Duarte  
1800 F Street, NW, Room 4035  
Washington, DC 20405

RE: FAR Case 2001-034

Dear Ms. Duarte:

The Aerospace Industries Association (AIA) members agree with the Councils' efforts to streamline and clarify the FAR. We are pleased to have this opportunity to comment on the referenced Council's proposed rule that would amend the general provisions of the FAR cost principles.

We believe the proposed special allocations provisions within FAR 31.106 and FAR 31.203 are unnecessary, overly prescriptive and inconsistent with DOD efforts to streamline FAR. Special allocations are already addressed in the provisions of FAR 31.109. Also, the proposed revisions could be interpreted as requiring a special allocation even though such an allocation is not required or mandated by the provisions of the Cost Accounting Standards (e.g., CAS 418).

The proposed changes to FAR 31.201 have the effect of significantly changing the criteria for determining the allowability of a cost. The proposed change to FAR Part 31.201-2(a) changes allowability "factors to be considered" to "requirements." Industry is concerned this revision will have the unintended consequence of government auditors placing too great a focus on the criteria found in FAR 31.201-4 *Determining Allocability* in determining the allowability of costs assigned by the contractor to cost objectives and moving away from the provisions of CAS in making these determinations. This later condition conflicts with the DoD/Industry objective of minimizing the reference to or the effect of allocability provisions in the FAR cost principles. Therefore, industry strongly recommends this proposed revision to the FAR be withdrawn.

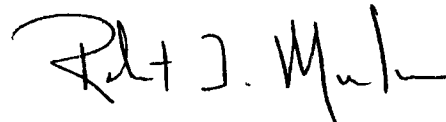
2001-034-3

Ms. Laurie Duarte  
April 7, 2003  
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We have provided our detailed concerns in the attachment to this letter. We strongly recommend that the proposed FAR revisions be amended to address our concerns. If all of our recommended changes as detailed in the attachment hereto, are not made, we request the proposed rule be withdrawn.

If you have any questions concerning our comments, please call Mr. Dick Powers of my staff on 703 358-1042. Dick can be reached by email at the following address: [powers@aia-aerospace.org](mailto:powers@aia-aerospace.org).

Sincerely,

A handwritten signature in black ink, appearing to read "R. T. Marlow". The signature is fluid and cursive, with a long horizontal stroke at the end.

Robert T. Marlow  
Vice President  
Government Division

Attachment



2001-034-3

## Schedule I

### Specific comments on revisions proposed under FAR Case 2001-034

#### FAR 31.106 Facilities contracts

- Proposed FAR 31.106-2 is at variance with the streamlining efforts that have been undertaken by the DAR Council. The concept of special allocations is already covered by FAR 31.109. Therefore, we recommend that this entire subsection be removed from the FAR. If the subsection must be retained, then we would recommend the following:
  - Revise the word “shall” in 31.106-2(b) to read “may” as the contractor is responsible for determining what accounting procedures and practices it will follow in conducting its business,
  - Eliminate 31.106-2(c) in its entirety and create new paragraph 31.106-2(b)(4), which states: “Negotiate an advance agreement with the cognizant Federal agency in accordance with 31.109 criteria.” As noted above, it is not the Government’s responsibility to make the determination and initiate negotiation efforts, as required by the proposed paragraph. By adding the above recommended statement under new (b)(4), the regulation writer makes it clear that it is the contractor’s responsibility to determine if conditions necessitating a special allocation exist.
  - Eliminate 31.106-2(d) and (e), the two paragraphs providing special allocation examples. Examples never cover all of a contractor’s accounting practices and these examples could lead to misleading determinations by the Government. In any event, the conceptual framework for the special allocation language is already covered in 31.109.

#### FAR 31.201 General:

- Proposed FAR 31.201-1(a) should have the phrase “...including standard costs properly adjusted for applicable variances.” deleted at the end of the paragraph. This language duplicates the first sentence of this subsection.
- In proposed FAR 31.201-2(a), the Councils have changed the whole concept of “allowability” by revising the words from “factors to be considered” to “when all of the following requirements are met.” The concept of allowability is different from the concept of “allocability.” The proposed language would allow government auditors to disregard CAS allocability requirements in seeking to prove that the Government was charged costs that were deemed unallocable to Government contracts. We strongly recommend that current language be retained, or the allocability sub-paragraphs (2) and (3) be deleted. In addition, the proposed language is not appropriate as it would require that for a cost to be allowable, all five criteria would have to be met, and all five are not necessarily present in all cases. For example, Item (5) “any limitation set forth in this subpart” is not applicable in every circumstance and Item (4) “terms of the contract,” as written, is not a requirement to be met.

#### FAR 31.203 Indirect costs:

- Proposed FAR 31.203(a) should add the words “two or more” before “final cost objectives” in the first sentence. This provides a necessary clarification.

2001-034-3

- Eliminate proposed FAR 31.203(d), (e), and (f) as the conceptual framework for special allocation language is already covered in 31.109. If the subsection must be retained, then we would recommend the following:
  - In the first sentence under (d), delete the remaining part of the sentence after the word “business.”
  - Under (f)(1), at the end of this paragraph, change the word “shall” to “may” as the contractor is responsible for determining what accounting procedures and practices it will follow in conducting its business.
  - Delete (f)(2) and add “Negotiate an advance agreement with the cognizant Federal agency in accordance with 31.109 criteria.” as a new subparagraph (f)(1)(iv). It is not the Government’s responsibility to make the determination and initiate negotiation efforts, as required by the proposed paragraph. By adding the above recommended statement under new (f)(1)(iv), the regulation writer makes it clear that it is the contractor’s responsibility to determine if conditions necessitating a special allocation exist.



APR 17 2003

GSA Office of Governmentwide Policy

MEMORANDUM FOR RONALD POUSSARD  
DIRECTOR  
DEFENSE ACQUISITION REGULATIONS COUNCIL

FROM: RODNEY P. LANTIER, DIRECTOR *Rodney P. Lantier*  
REGULATORY AND FEDERAL ASSISTANCE  
PUBLICATIONS DIVISION

SUBJECT: FAR Case 2001-034, General Provisions of the Cost Principals

Attached is a additional comment received on the subject FAR case published at 68 FR 5774; February 4, 2003. The comment closing date was April 7, 2003.

<u>Response Number</u>	<u>Date Received</u>	<u>Comment Date</u>	<u>Commenter</u>
2001-034-4	04/15/03	04/09/03	NDIA
Attachment			



2001-034-4

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Web page: <http://www.ndia.org>

*The Voice of the Industrial Base*

April 9, 2003

General Services Administration  
FAR Secretariat (MVP)  
1800 F Street, N.W.  
Room 4035  
Washington, D.C. 20405

ATTN: Ms. Laurie Duarte

Subject: FAR Case 2001-034, General Provisions of the Cost Principles

Dear Ms. Duarte:

The National Defense Industrial Association (NDIA) is pleased to submit comments on the proposed rule to amend the general provisions of the Subpart 31.2 cost principles.

NDIA is a non-partisan, non-profit organization with a membership that includes over 900 companies – both large and small businesses – and more than 26,000 individuals. NDIA has specific interest in government policies and practices concerning the government's acquisition of goods and services. Our members, who provide a wide array of goods and services to the government, include some of the nation's largest defense contractors.

Our members oppose the proposed language of the FAR Case. We applaud previous and on-going efforts to streamline cost allowability regulations, such as removing excess language from 31.201-1 and separating CAS allocation requirements from procurement allowability policy. Rather than continue these efforts, the proposed rule appears to exacerbate confusion by moving CAS allocation concepts into allowability criteria of the FAR. The proposed changes reduce flexibility of the acquisition workforce and significantly impact small businesses.

In summary, the proposed changes significantly undercut the efforts of the past decade to streamline the cost principles and reduce the additional burdens imposed on sellers to the US Government. Our members are not aware of any compelling reason driving the need for such changes and, if the FAR Council has such a reason, it has omitted it from the promulgating comments. At a time when it our nation's security may depend on attracting non-traditional sellers to the Government marketplace, the proposed rules would make it less attractive for them to do so. Absent a compelling need for the changes, our members believe that the proposed language is bad public policy and requires substantial revision.

*"Publishers of National Defense Magazine"*

As a threshold proposition, we believe that the proposed changes, in their entirety, are unnecessary. FAR 31.109 already provides a mechanism for bilateral agreement with respect to the treatment of special or unusual costs. Although there is no suggestion that FAR 31.109 is inadequate or does not function in the manner intended, the changes now proposed would essentially displace that long-standing mechanism for disputes avoidance with a complex maze of provisions idiosyncratic to facilities contracts. A far simpler proposition would be to rely on FAR 31.109 as written, or alternative, to amend that provision by adding a new FAR 31.109(h)(17): “Special allocations of facilities costs.”

Beyond the foregoing comments with respect to the generally unnecessary nature of the proposed changes, our specific comments are as follows:

- 31.106-2—The entire proposed Subpart seems designed to reduce the flexibility of the parties to negotiate an equitable allocation of costs to the facility contract. We believe that the existing language (e.g., “A contractor's normal accounting practice for allocating indirect costs to the acquisition of contractor facilities may range from charging all these costs to this acquisition to not charging any. When necessary to produce an equitable result, the contractor's usual method of allocating indirect cost shall be varied, and appropriate adjustment shall be made to the pools of indirect cost and the bases of their distribution.”) provides sufficient guidance to the contracting parties without being overly restrictive. Moreover, the proposed language is redundant with existing language regarding advance agreements, found at 31.109.

Most significantly, our members are disagree with the proposed language at 31.106-2(c) that would suggest that special allocations require advance Government approval—(e.g., “The cognizant Federal agency is responsible for determining whether the conditions necessitating a special allocation exist...”). While the Government may have the responsibility of evaluating a contractor’s cost accounting practices for allowability and allocability, it is clearly the contractor’s responsibility to establish those cost accounting practices and to initiate an advance agreement when it deems circumstances ripe for doing so. We believe that inclusion of this prescriptive language into the final rule may create confusion as it provides for a potential conflict with existing CAS language at, for example, CAS 418-50(f), which states, “Where a particular cost objective ... receives significantly more or less benefit from an indirect cost pool ... the Government and contractor *may agree* to a special allocation ...” (emphasis added).

Additionally, the proposed rule would bring in advanced cost allocation concepts, such as special allocations, and make those concepts mandatory for any business to which the Subpart applies, without regard to the business’s CAS coverage status. Compliance with the full range of CAS requirements requires sophisticated and costly cost accounting systems. Small businesses generally lack such systems and would be forced to comply with the proposed requirements even though they are otherwise exempt from CAS. This seems counter to the trend that increases the CAS coverage threshold in order to reduce burdens on smaller businesses and to attract non-traditional sellers into the Government marketplace. Our members urge that the

034-4

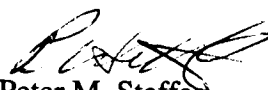
proposed mandatory cost allocation concepts be left in CAS where they will be applicable in accordance with CAS coverage requirements.

In summary, the proposed 31.106-2 language is redundant, overly prescriptive, and may well lead to CAS/FAR conflicts. We urge that the entire Subpart be deleted from the final rule.

- 31.201-2(a)—The proposed language removes contracting officer discretion to determine, on a case-by-case basis, what costs are allowable by introducing overly prescriptive language. We believe that this change, which eliminates contracting officer discretion to weigh the various factors in making the decision regarding cost allowability, conflicts with recent initiatives to reduce administrative oversight—as well as conflicting with other FAR guidance, such as 1.102-2. (E.g., “The System must provide uniformity where it contributes to efficiency or where fairness or predictability is essential. The System should also, however, encourage innovation, and local adaptation where uniformity is not essential.” (FAR 1.102-2(b)(2)).) The current language gives contracting officers discretion to determine cost allowability by weighing the various factors and we urge that this discretion be retained.
- 31.203—Again, we believe that the proposed language is overly restrictive and may lead to conflicts between CAS and FAR during implementation. We are particularly concerned by the proposed language at 31.203(f)(1) and (f)(2), which make special allocations mandatory through the use of the word “shall” and, like the proposed language at 31.106(2), that would suggest that special allocations are solely at the discretion of the Government. Our members believe that a contractor’s cost accounting practices are determined by the contractor and not by the cognizant federal agency official or contracting officer. We further believe that the proposed language may conflict with existing the CAS requirements of CAS 418 by making mandatory what is currently discretionary.

We continue to recommend a greater emphasis on identifying and removing Subpart 31.205 language that is not required by statute—an effort we believe to be consistent with the current DFARS transformation initiative. While resource constraints obviously preclude reformatting all cost principles at once, we believe that the current FAR case provides an excellent opportunity to reformat, streamline and clarify the existing language. We encourage the FAR Council to reconsider its draft language, which eliminates current flexibility and contracting officer discretion in favor of prescriptive language that appears to be a “step backwards” for acquisition reform. If further information is required, please contact NDIA Procurement Division Director Ruth Franklin at (703) 247-2598 or at [rfranklin@ndia.org](mailto:rfranklin@ndia.org).

Sincerely,



Peter M. Steffes  
Vice President, Government Policy