

# AMS CHANGE REQUEST (CR) COVERSHEET

**Change Request Number:** 14-81

**Date Received:** Sep 23, 2014

**Title:** Statute Updates - Guidance

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**Guidance and Policy must be submitted with separate CR coversheets**

Policy

**Or**

Procurement Guidance

Real Estate Guidance

Other Guidance

**Summary of Change:**

Update to various United States Code references

**Reason for Change:**

Currency with applicable statutes

**Development, Review, and Concurrence:**

Procurement Legal and Acquisition Policy Division. AGC-500 has confirmed that there are no substantive changes to the Procurement Integrity Act update in T3.1.8.

**Target Audience:**

Program offices and Acquisition Workforce

**Briefing Planned:** No.

**ASAG Responsibilities:** None.

**Section / Text Location:**

T3.1.8, T3.2.5 T3.3.2, T3.6.2, and T3.6.4. Also changes to "Solicitation, Offer, and Award" and "Agreement Regarding Conflict-of-Interest" forms.

**The redline version must be a comparison with the current published FAST version.**

I confirm I used the latest published version to create this change / redline

**Or**

This is new content

## Links:

<http://fast.faa.gov/ProcurementToolboxForms.cfm>

## Attachments:

Redline and final versions.

## Other Files:

N/A

## RedLines:

Revised: T3.1.8 Procurement Integrity Act > A Procurement Integrity > Act 1 Applicability

### T3.1.8 Procurement Integrity Act Revised 7/2006

## A Procurement Integrity Act

### 1 Applicability Revised 10/2010

As provided by 49 U.S.C. ~~Section 40122(g)(3) § 40110(d)(3), effective October 1, 1999~~, FAA is subject to the Procurement Integrity Act (the Act), (41 U.S.C. ~~Section 423 §§ 2101-2107~~). ~~Sections 2101, "Definitions," and 2106, "Reporting information believed to constitute evidence of offense," H~~however, ~~in 41 U.S.C. Section 423, subsections (f) Definitions and (g) Limitations on Protests~~, do not apply to FAA. Congress directed the FAA to adopt its own definitions in lieu of the definitions in ~~subsection (f) § 2101~~ of the Act, consistent with the intent of AMS and the Act. By memorandum dated July 14, 2000, the Administrator approved FAA's definitions. The FAA-specific definitions in this Procurement Guidance are to be substituted for ~~subsections (f) Definitions and (g) Limitation on Protests §§ 2101 and 2106~~.

### 2 FAA-Specific Definitions Revised 10/2010

*Under AMS, FAA-specific definitions are to be substituted for Procurement Integrity Act ~~subsection (f) "Definitions" and (g) "Limitation on Protests."~~ §§2101, "Definitions," and 2106, "Reporting information believed to constitute evidence of offense."*

#### FAA Definitions as Used in 41 U.S.C. ~~Section 423 §§ 2101-2107~~

(1) The term "contractor bid or proposal information" means any of the following information submitted to FAA as part of or in connection with a Screening Information Request (SIR) or an unsolicited proposal, to enter into an FAA procurement contract, if that information has not been previously made available to the public or disclosed publicly:

(A) Cost or pricing data (as defined in Appendix C of the AMS). (B) Indirect costs

and direct labor rates.

(C) Proprietary information about manufacturing processes, operations, or techniques marked by the contractor in accordance with applicable law or regulation.

(D) Information marked by the contractor in accordance with (1) AMS Clause 3.2.2.3-16, "Restricting ~~ion on~~ Disclosure and Use of Data," or (2) other applicable law and regulation.

(2) The term "source selection information" means any of the following information prepared for use by the FAA for the purpose of evaluating documentation, information, presentations, proposals, or binding offers which an offeror submits in response to a Screening Information Request (SIR), or in an unsolicited proposal, to enter into an FAA procurement contract, if that information has not been previously made available to the public or disclosed publicly:

(A) Proposed costs or prices submitted in response to a FAA SIR, or lists of those proposed costs or prices.

(B) Source selection plans.

(C) Technical evaluation plans.

(D) Technical evaluations of responses to SIRs or unsolicited proposals. (E) Cost or price evaluation plans.

(F) Cost or price evaluations of responses to SIRs or unsolicited proposals.

(G) Down select determinations identifying SIR responses that are most likely to receive contract award.

(H) Any ranking of offerors developed by the FAA during the source selection process. (I) The reports, evaluations and recommendations of source selection panels, boards, or advisory councils.

(J) Other information based on a case- by-case determination made by the FAA Acquisition Executive\*, his or her designee, or the Product or Service Team\*\*, that its disclosure would jeopardize the integrity or successful completion of the FAA procurement to which the information relates.

In addition, all source selection information should be clearly marked as such on the cover and throughout each individual document.

(3) The term "Federal agency" means the FAA.

(4) The term "Federal agency procurement" means the acquisition (by using competitive or non- competitive procedures and awarding a contract) of goods or services (including construction) from non-Federal sources by the FAA using appropriated funds.

(5) The term "contracting officer" means a person who, by appointment in accordance with FAA policy, has the authority to enter into a FAA contract on behalf of the Government and to make determinations and findings with respect to such contract.

(6) The term "protest" means a written objection by an interested party to the award or proposed award of a FAA procurement contract.

(7) The term "official" means the following:

(A) An employee of the FAA, as defined in the FAA's Personnel Management System.

(B) An officer (as defined in 5 U.S.C. [Section](#) 2104) of any non-FAA ~~f~~ederal agency (as

~~f~~Federal agency is defined in 40 U.S.C. [Section 472§ 102\(5\)](#).

(C) An employee (as defined in 5 U.S.C. [Section§ 2105](#)) of any non-FAA ~~f~~Federal agency (as ~~f~~Federal agency is defined in 40 U.S.C. [Section 472§102\(5\)](#)).

(D) A member of the uniformed services; (as defined in 5 U.S.C. [Section § 2101\(3\)](#)).

(8) The term "other applicable law or regulation" as used at 41 U.S.C. [Section 423\(e\)\(3\)\(A\)\(iv\) § 2105\(c\)\(1\)\(D\)](#), includes the FAA Personnel Management System.

(9) The term "Comptroller General of the United States," as used at 41 U.S.C. [Section 423\(h\)\(6\) §§ 2106 and 2107\(5\) and \(6\)](#), means the FAA Office of Dispute Resolution for Acquisition.

(10) The term "program manager" as used at 41 U.S.C. [Section 423\(d\)\(1\)\(B\) § 2104\(a\)\(2\)](#), includes a FAA Product or Service Team\*\* Lead or Acting Lead.

(11) The term "deputy program manager" as used at 41 U.S.C. [Section 423\(d\)\(1\)\(B\) § 2104\(a\)\(2\)](#); includes a Deputy or Acting Deputy to an FAA Product or Service Team\*\* Lead.

(12) The term "Federal Acquisition Regulation" as used at 41 U.S.C. [Section 423\(e\)\(3\)\(A\)\(iii\) § 2105\(c\)\(1\)\(C\)](#); means the FAA AMS.

\*The July 14, 2000, memo approving FAA definitions used "Associate Administrator for Research and Acquisitions." Due to organizational changes in 2006, this position was abolished. The FAA Acquisition Executive is an equivalent position.

\*\*The July 14, 2000, memo approving FAA definitions used the term "Integrated Product Team." Due to organizational changes, this term was not used after 2006. Product or Service Team is an [similar equivalent](#) structure.

### 3 Full Text of [Procurement Integrity Act](#), 41 U.S.C. [Section 423§§ 2101-2107](#) Added 10/2010

*Below is the full text of the Procurement Integrity Act, 41 U.S.C. [Section 423§§ 2101-2107](#) (omitting only its [subsections \(f\) and \(g\) §§ 2101 and 2106](#), which are not applicable to FAA). This Act, as it applies to the FAA, is to be read in conjunction with the FAA Procurement Integrity Act definitions (which are also shown in this Procurement Guidance Section). Please take special notice of 41 U.S.C. [Section 423\(h\) § 2107](#) below, which contains "savings provisions," or situations where the Procurement Integrity Act does **not** apply.*

#### Procurement Integrity Act, 41 U.S.C. [Section 423§§ 2101-2107](#)

#### ~~§ 423. Restrictions on disclosing and obtaining contractor bid or proposal information or source selection information~~

##### ~~(a) Prohibition on disclosing procurement information.~~

~~(1) A person described in paragraph (2) shall not, other than as provided by law, knowingly disclose contractor bid or proposal information or source selection information before the award of a Federal agency procurement contract to which the~~

information relates.

~~(2) Paragraph (1) applies to any person who—~~

~~(A) is a present or former official of the United States, or a person who is acting or has acted for or on behalf of, or who is advising or has advised the United States with respect to, a Federal agency procurement; and~~

~~(B) by virtue of that office, employment, or relationship has or had access to contractor bid or proposal information or source selection information.~~

~~(b) Prohibition on obtaining procurement information. A person shall not, other than as provided by law, knowingly obtain contractor bid or proposal information or source selection information before the award of a Federal agency procurement contract to which the information relates.~~

~~(c) Actions required of procurement officers when contacted by offerors regarding non-Federal employment.~~

~~(1) If an agency official who is participating personally and substantially in a Federal agency in a Federal agency procurement for a contract in excess of the simplified-acquisition threshold contracts or is contacted by a person who is a bidder or offeror in that Federal agency procurement regarding possible non-Federal employment for that official, the official shall—~~

~~(A) promptly report the contract in writing to the official's supervisor and to the designated agency ethics official (or designee) of the agency in which the official is employee; and~~

~~(B) (i) reject the possibility of non-Federal employment; or~~

~~(ii) disqualify himself or herself from further personal and substantial participation in that Federal agency procurement until such time as the agency has authorized the official to resume participation in such procurement, in accordance with the requirements of section 208 of title 18, United States Code, and applicable agency regulations on the grounds that—~~

~~(I) the person is no longer a bidder or offeror in that Federal agency procurement; or~~

~~(II) all discussions with the bidder or offeror regarding possible non-Federal employment have terminated without an agreement or arrangement for employment.~~

~~(2) Each report required by this subsection shall be retained by the agency for not less than two years following the submission of the report. All such reports shall be made available to the public upon request, except that any part of a report that is exempt from the disclosure requirements of section 552 of title 5, United States Code, under subsection (b)(1) of such section may be withheld from disclosure to the public.~~

~~(3) An official who knowingly fails to comply with the requirements of this subsection shall be subject to the penalties and administrative actions set forth in subsection (e).~~

~~(4) A bidder or offeror who engages in employment discussions with an official who is subject to the restrictions of this subsection, knowing that the official has not complied with subparagraph (A) or (B) of paragraph (1), shall be subject to the penalties and administrative actions set forth in subsection (e).~~

~~d) Prohibition on former official's acceptance of compensation from contractor.~~

~~(1) A former official of a Federal agency may not accept compensation from a contractor as an employee, officer, director, or consultant of the contractor within a period of one year after such former official—~~

~~(A) served, at the time of selection of the contractor or the award of a contract to that contractor, as the procuring contracting officer, the source selection authority, a member of the source selection evaluation board, or the chief of a financial or technical evaluation team in a procurement in which that contractor was selected for award of a contract in excess of \$10,000,000;~~

~~(B) served as the program manager, deputy program manager, or administrative contracting officer for a contract in excess of \$10,000,000 awarded to that contractor; or~~

~~(C) personally made for the Federal agency—~~

~~(i) a decision to award a contract, subcontract, modification of a contract or subcontract, or a task order or delivery order in excess of \$10,000,000 to that contractor;~~

~~(ii) a decision to establish overhead or other rates applicable to a contract or contracts for that contractor that are valued in excess of \$10,000,000;~~

~~(iii) a decision to approve issuance of a contract payment or payments in excess of \$10,000,000 to that contractor; or~~

~~(iv) a decision to pay or settle a claim in excess of \$10,000,000 with that contractor.~~

~~(2) Nothing in paragraph (1) may be construed to prohibit a former official of a Federal agency from accepting compensation from any division or affiliate of a contractor that does not produce the same or similar products or services as the entity of the contractor that is responsible for the contract referred to in subparagraph (A), (B), or (C) of such paragraph.~~

~~(3) A former official who knowingly accepts compensation in violation of this subsection shall be subject to penalties and administrative actions as set forth in subsection (e).~~

~~(4) A contractor who provides compensation to a former official knowing that such compensation is accepted by the former official in violation of this subsection shall be subject to penalties and administrative actions as set forth in subsection (e).~~

~~(5) Regulations implementing this subsection shall include procedures for an official or former official of a Federal agency to request advice from the appropriate designated agency ethics official regarding whether the official or former official is or would be precluded by this subsection from accepting compensation from a particular contractor.~~

~~(e) Penalties and administrative actions:~~

~~(1) Criminal penalties. Whoever engages in conduct constituting a violation of subsection (a) or (b) for the purpose of either—~~

~~(A) exchanging the information covered by such subsection for anything of value, or~~

~~(B) obtaining or giving anyone a competitive advantage in the award of a Federal agency procurement contract, shall be imprisoned for not more than 5 years or fined as provided under title 18, United States Code, or both.~~

~~(2) Civil penalties. The Attorney General may bring a civil action in an appropriate United States district court against any person who engages in conduct constituting a violation of subsection (a), (b), (c), or (d). Upon proof of such conduct by a preponderance of the evidence, the person is subject to a civil penalty of not more than \$50,000 for each violation plus twice the amount of compensation which the individual received or offered for the prohibited conduct. An organization that engages in such conduct is subject to a civil penalty of not more than \$500,000 for each violation plus twice the amount of compensation which the organization received or offered for the prohibited conduct.~~

~~(3) Administrative actions:~~

~~(A) If a Federal agency receives information that a contractor or a person has engaged in conduct constituting a violation of subsection (a), (b), (c), or (d), the Federal agency shall consider taking one or more of the following actions, as appropriate:~~

~~(i) Cancellation of the Federal agency procurement, if a contract has not yet been awarded.~~

~~(ii) Rescission of a contract with respect to which—~~

~~(I) the contractor or someone acting for the contractor has been convicted for an offense punishable under paragraph (1), or~~

~~(II) the head of the agency that awarded the contract has determined, based upon a preponderance of the evidence, that the~~

~~contractor or someone acting for  
the contractor has engaged in conduct  
constituting such an offense.~~

~~(iii) Initiation of suspension or debarment proceedings  
for the protection of the Government in accordance  
with procedures in the Federal Acquisition  
Regulation.~~

~~(iv) Initiation of adverse personnel action, pursuant to  
the procedures in chapter 75 of title 5, United States  
Code [5 USCS §§ 7501 et seq.], or other applicable law  
or regulation.~~

~~(B) If a Federal agency rescinds a contract pursuant to subparagraph  
(A) (ii), the United States is  
entitled to recover, in addition to any penalty prescribed by law, the  
amount expended under the contract.~~

~~(C) For purposes of any suspension or debarment proceedings initiated  
pursuant to subparagraph (A) (iii), engaging in conduct constituting an  
offense under subsection (a), (b), (c), or (d) affects the present  
responsibility of a Government contractor or subcontractor.~~

~~[paragraphs (f) and (g) omitted intentionally]~~

~~(h) Savings provisions. This section does not—~~

~~(1) restrict the disclosure of information to, or its receipt by, any person or class of  
persons authorized, in accordance with applicable agency regulations or procedures,  
to receive that information;~~

~~(2) restrict a contractor from disclosing its own bid or proposal information or the  
recipient from receiving that information;~~

~~(3) restrict the disclosure or receipt of information relating to a Federal agency  
procurement after it has been canceled by the Federal agency before contract award  
unless the Federal agency plans to resume the procurement;~~

~~(4) prohibit individual meetings between a Federal agency official and an offeror or  
potential offeror for, or a recipient of, a contract or subcontract under a Federal agency  
procurement, provided that unauthorized disclosure or receipt of contractor bid or  
proposal information or source selection information does not occur;~~

~~(5) authorize the withholding of information from, nor restrict its receipt by, Congress,  
a committee or subcommittee of Congress, the Comptroller General, a Federal agency,  
or an inspector general of a Federal agency;~~

~~(6) authorize the withholding of information from, nor restrict its receipt by, the  
Comptroller General of the United States in the course of a protest against the award  
or proposed award of a Federal agency procurement contract; or~~

~~(7) limit the applicability of any requirements, sanctions, contract; or penalties, and remedies established under any other law or regulation.~~

## § 2101. Definitions

[Omitted]

## § 2102. Prohibitions on disclosing and obtaining procurement information

(a) PROHIBITION ON DISCLOSING PROCUREMENT INFORMATION.—

(1) IN GENERAL.—Except as provided by law, a person described in paragraph (3) shall not knowingly disclose contractor bid or proposal information or source selection information before the award of a Federal agency procurement contract to which the information relates.

(2) EMPLOYEE OF PRIVATE SECTOR ORGANIZATION.—In addition to the restriction in paragraph (1), an employee of a private sector organization assigned to an agency under chapter 37 of title 5 shall not knowingly disclose contractor bid or proposal information or source selection information during the 3-year period after the employee's assignment ends, except as provided by law.

(3) APPLICATION.—Paragraph (1) applies to a person that—

(A) (i) is a present or former official of the Federal Government; or

(ii) is acting or has acted for or on behalf of, or who is advising or has advised the Federal Government with respect to, a Federal agency procurement; and

(B) by virtue of that office, employment, or relationship has or had access to contractor bid or proposal information or source selection information.

(b) PROHIBITION ON OBTAINING PROCUREMENT INFORMATION.—Except as provided by law, a person shall not knowingly obtain contractor bid or proposal information or source selection information before the award of a Federal agency procurement contract to which the information relates.

## § 2103. Actions required of procurement officers when contacted regarding non-Federal employment

(a) ACTIONS REQUIRED.—An agency official participating personally and substantially in a Federal agency procurement for a contract in excess of the simplified acquisition threshold who contacts or is contacted by a person that is a bidder or offeror in that Federal agency procurement regarding possible non-Federal employment for that official shall—

(1) promptly report the contact in writing to the official's supervisor and to the designated agency ethics official (or designee) of the agency in which the official is employed; and

(2) (A) reject the possibility of non-Federal employment; or

(B) disqualify himself or herself from further personal and substantial participation in that Federal agency procurement until the agency authorizes the official to resume participation in the procurement, in accordance with the requirements of section 208 of title 18 and applicable agency regulations on the grounds that—

(i) the person is no longer a bidder or offeror in that Federal agency procurement; or

(ii) all discussions with the bidder or offeror regarding possible non-Federal employment have terminated without an agreement or arrangement for employment.

(b) RETENTION OF REPORTS.—The agency shall retain each report required by this section for not less than 2 years following the submission of the report. The reports shall be made available to the public on request, except that any part of a report that is exempt from the disclosure requirements of section 552 of title 5 under subsection (b)(1) of that section may be withheld from disclosure to the public.

(c) PERSONS SUBJECT TO PENALTIES.—The following are subject to the penalties and administrative actions set forth in section 2105 of this title:

(1) An official who knowingly fails to comply with the requirements of this section.

(2) A bidder or offeror that engages in employment discussions with an official who is subject to the restrictions of this section, knowing that the official has not complied with paragraph (1) or (2) of subsection (a).

#### **§ 2104. Prohibition on former official's acceptance of compensation from contractor**

(a) PROHIBITION.—A former official of a Federal agency may not accept compensation from a contractor as an employee, officer, director, or consultant of the contractor within one year after the official—

(1) served, when the contractor was selected or awarded a contract, as the procuring contracting officer, the source selection authority, a member of the source selection evaluation board, or the chief of a financial or technical evaluation team in a procurement in which that contractor was selected for award of a contract in excess of \$10,000,000;

(2) served as the program manager, deputy program manager, or administrative contracting officer for a contract in excess of \$10,000,000 awarded to that contractor; or

(3) personally made for the Federal agency a decision to—

(A) award a contract, subcontract, modification of a contract or subcontract, or a task order or delivery order in excess of \$10,000,000 to that contractor;

(B) establish overhead or other rates applicable to one or more contracts for that contractor that are valued in excess of \$10,000,000;

(C) approve issuance of one or more contract payments in excess of \$10,000,000 to that contractor; or

(D) pay or settle a claim in excess of \$10,000,000 with that contractor.

(b) WHEN COMPENSATION MAY BE ACCEPTED.—Subsection (a) does not prohibit a former official of a Federal agency from accepting compensation from a division or affiliate of a contractor that does not produce the same or similar products or services as the entity of the contractor that is responsible for the contract referred to in paragraph (1), (2), or (3) of subsection (a).

(c) IMPLEMENTING REGULATIONS.—Regulations implementing this section shall include procedures for an official or former official of a Federal agency to request advice from the appropriate designated agency ethics official regarding whether the official or former official is or would be precluded by this section from accepting compensation from a particular contractor.

(d) PERSONS SUBJECT TO PENALTIES.—The following are subject to the penalties and administrative actions set forth in section 2105 of this title:

(1) A former official who knowingly accepts compensation in violation of this section.

(2) A contractor that provides compensation to a former official knowing that the official accepts the compensation in violation of this section.

#### **§ 2105. Penalties and administrative actions**

(a) CRIMINAL PENALTIES.—A person that violates section 2102 of this title to exchange information covered by section 2102 of this title for anything of value or to obtain or give a person a competitive advantage in the award of a Federal agency procurement contract shall be fined under title 18, imprisoned for not more than 5 years, or both.

(b) CIVIL PENALTIES.—The Attorney General may bring a civil action in an appropriate district court of the United States against a person that engages in conduct that violates section 2102, 2103, or 2104 of this title. On proof of that conduct by a preponderance of the evidence—

(1) an individual is liable to the Federal Government for a civil penalty of not more than \$50,000 for each violation plus twice the amount of compensation that the individual received or offered for the prohibited conduct; and

(2) an organization is liable to the Federal Government for a civil penalty of not more than \$500,000 for each violation plus twice the amount of compensation that the organization received or offered for the prohibited conduct.

(c) ADMINISTRATIVE ACTIONS.—

(1) TYPES OF ACTION THAT FEDERAL AGENCY MAY TAKE.—A Federal agency that receives information that a contractor or a person has violated section 2102, 2103, or 2104 of this

title shall consider taking one or more of the following actions, as appropriate:

(A) Canceling the Federal agency procurement, if a contract has not yet been awarded.

(B) Rescinding a contract with respect to which—

(i) the contractor or someone acting for the contractor has been convicted for an offense punishable under subsection (a); or

(ii) the head of the agency that awarded the contract has determined, based on a preponderance of the evidence, that the contractor or a person acting for the contractor has engaged in conduct constituting the offense.

(C) Initiating a suspension or debarment proceeding for the protection of the Federal Government in accordance with procedures in the Federal Acquisition Regulation.

(D) Initiating an adverse personnel action, pursuant to the procedures in chapter 75 of title 5 or other applicable law or regulation.

(2) AMOUNT GOVERNMENT ENTITLED TO RECOVER.—When a Federal agency rescinds a contract pursuant to paragraph (1)(B), the Federal Government is entitled to recover, in addition to any penalty prescribed by law, the amount expended under the contract.

(3) PRESENT RESPONSIBILITY AFFECTED BY CONDUCT.—For purposes of a suspension or debarment proceeding initiated pursuant to paragraph (1)(C), engaging in conduct constituting an offense under section 2102, 2103, or 2104 of this title affects the present responsibility of a Federal Government contractor or subcontractor.

#### **§ 2106. Reporting information believed to constitute evidence of offense**

[Omitted]

#### **§ 2107. Savings provisions**

This chapter does not—

(1) restrict the disclosure of information to, or its receipt by, a person or class of persons authorized, in accordance with applicable agency regulations or procedures, to receive that information;

(2) restrict a contractor from disclosing its own bid or proposal information or the recipient from receiving that information;

(3) restrict the disclosure or receipt of information relating to a Federal agency procurement after it has been canceled by the Federal agency before contract award unless the Federal agency plans to resume the procurement;

(4) prohibit individual meetings between a Federal agency official and an offeror or potential offeror for, or a recipient of, a contract or subcontract under a Federal agency procurement, provided that unauthorized disclosure or receipt of contractor bid or proposal information or source selection information does not occur;

(5) authorize the withholding of information from, nor restrict its receipt by, Congress, a committee or subcommittee of Congress, the Comptroller General, a Federal agency, or an inspector general of a Federal agency;

(6) authorize the withholding of information from, nor restrict its receipt by, the Comptroller General in the course of a protest against the award or proposed award of a Federal agency procurement contract;

or

(7) limit the applicability of a requirement, sanction, contract penalty, or remedy established under another law or regulation.

**Revised : T3.2.5 - Contractor Ethical Guidelines > A Contractor Ethical Guidelines > 5 Subcontractor Kickbacks**

## 5 Subcontractor Kickbacks

As prescribed by the Anti-Kickback Act (41 U.S.C. ~~§§51-588701-8707~~), subcontractors are prohibited from making payments (or anything of value) and contractors from accepting payments (or anything of value) for the purpose of improperly obtaining or rewarding favorable treatment in connection with a prime contract or a subcontract relating to a prime contract.

### Revised : T3.3.2 - Contract Cost Principles > 2 Appendix - Selected Costs

## 2 Appendix - Selected Costs Revised 4/2013

This Appendix 2 does not cover every element of cost. Failure to include any item of cost does not imply that it is either allowable or unallowable. The determination of allowability must be based on the principles and standards in AMS Procurement Guidance T3.2.2 and the treatment of similar or related selected items.

### (1) *Public Relations and Advertising Costs.*

(a) “Public relations” means all functions and activities dedicated to:

(1) Maintaining, protecting, and enhancing the image of a concern or its products;

or

(2) Maintaining or promoting reciprocal understanding and favorable relations with the public at large, or any segment of the public. The term public relations includes activities associated with areas such as advertising, customer relations, etc.

(b) “Advertising” means the use of media to promote the sale of products or services and to accomplish the activities referred to in paragraph (d) of this subsection, regardless of the medium employed, when the advertiser has control over the form and content of what will appear, the media in which it will appear, and when it will appear. Advertising media include but are not limited to conventions, exhibits, free goods, samples, magazines, newspapers, trade papers, direct mail, dealer cards, window displays, outdoor advertising, radio, and television.

(c) Public relations and advertising costs include the costs of media time and space, purchased services performed by outside organizations, as well as the applicable portion of salaries, travel, and fringe benefits of employees engaged in the functions and activities identified in subparagraphs (e)(1) through (6).

(d) The only allowable advertising costs are those that are

(1) Specifically required by contract, or that arise from requirements of Government contracts, and that are exclusively for

(i) Acquiring scarce items for contract performance; or

(ii) Disposing of scrap or surplus materials acquired for contract performance;

(2) Costs of activities to promote sales of products normally sold to the U.S. Government, including trade shows, which contain a significant effort to promote exports from the United States. Such costs are allowable, notwithstanding subparagraphs (d)(1), (d)(3), (d)(4)(ii) and (d)(5) ( of this subsection). However, such costs do not include the costs of memorabilia (*e.g.*, models, gifts, and souvenirs), alcoholic beverages, entertainment, and physical facilities that are used primarily for entertainment rather than product promotion; or

(3) Allowable in accordance with Cost (31) Recruitment Costs. (e) Allowable

public relations costs include the following:

(1) Costs specifically required by contract. (2) Costs of

- (i) Responding to inquiries on company policies and activities;
- (ii) Communicating with the public, press, stockholders, creditors, and customers; and
- (iii) Conducting general liaison with news media and Government public relations officers, to the extent that such activities are limited to communication and liaison necessary to keep the public informed on matters of public concern such as notice of contract awards, plant closings or openings, employee layoffs or rehires, financial information, etc.

(3) Costs of participation in community service activities (*e.g.*, blood bank drives, charity drives, savings bond drives, disaster assistance, etc.).

(4) Costs of plant tours and open houses (but see subparagraph (d)(5) of this subsection).

(5) Costs of keel laying, ship launching, commissioning, and roll-out ceremonies, to the extent specifically provided for by contract.

(f) Unallowable public relations and advertising costs include the following:

(1) All public relations and advertising costs, other than those specified in subparagraphs (d) and (e) of this subsection, whose primary purpose is to promote the sale of products or services by stimulating interest in a product or product line (except for those costs made allowable under Cost (35), or by disseminating messages calling favorable attention to the contractor for purposes of enhancing the company image to sell the company's products or services.

(2) All costs of trade shows and other special events which do not contain a significant effort to promote the export sales of products normally sold to the U.S. Government.

(3) Costs of sponsoring meetings, conventions, symposia, seminars, and other special events when the principal purpose of the event is other than dissemination of technical information or stimulation of production.

(4) Costs of ceremonies such as

- (i) Corporate celebrations and
- (ii) New product announcements.

(5) Costs of promotional material, motion pictures, videotapes, brochures, handouts, magazines, and other media that are designed to call favorable attention to the contractor and its activities.

(6) Costs of souvenirs, models, imprinted clothing, buttons, and other mementos provided to customers or the public.

(7) Costs of memberships in civic and community organizations.

**(2) *Bad Debts.***

Bad debts, including actual or estimated losses arising from uncollectible accounts receivable due from customers and other claims, and any directly associated costs such as collection costs, and legal costs are unallowable.

**(3) *Bonding Costs.***

(a) Bonding costs arise when the Government requires assurance against financial loss to itself or others by reason of the act or default of the contractor. They arise also in instances where the contractor requires similar assurance. Included are such bonds as bid, performance, payment, advance payment, infringement, and fidelity bonds.

(b) Costs of bonding required pursuant to the terms of the contract are allowable.

(c) Costs of bonding required by the contractor in the general conduct of its business are allowable to the extent that such bonding is in accordance with sound business practice and the rates and premiums are reasonable under the circumstances.

**(4) *Compensation for Personal Services.***

(a) *General.* Compensation for personal services is allowable subject to the following general criteria and additional requirements contained in other parts of this cost principle:

(1) Compensation for personal services must be for work performed by the employee in the current year and must not represent a retroactive adjustment of prior years' salaries or wages (but see paragraphs (g), (h), (j), (k), (m), and (o) of this subsection).

(2) The total compensation for individual employees or job classes of employees must be reasonable for the work performed; however, specific restrictions on individual compensation elements apply when prescribed.

(3) The compensation must be based upon and conform to the terms and conditions of the contractor's established compensation plan or practice followed so consistently as to imply, in effect, an agreement to make the payment.

(4) No presumption of allowability will exist where the contractor introduces major revisions of existing compensation plans or new plans and the contractor has not provided the cognizant CO, either before implementation or within a reasonable period after it, an opportunity to review the allowability of the changes.

(5) Costs that are unallowable under other paragraphs of this Procurement Guidance Section T3.3.2 are not allowable under this subsection solely on the basis that they constitute compensation for personal services.

(6) (i) Compensation costs for certain individuals give rise to the need for special consideration. Such individuals include:

(A) Owners of closely held corporations, members of limited liability companies, partners, sole proprietors, or members of their immediate families; and

(B) Persons who are contractually committed to acquire a substantial financial interest in the contractor's enterprise.

(ii) For these individuals, compensation must- (A) Be reasonable

for the personal services rendered; and

(B) Not be a distribution of profits (which is not an allowable contract cost).

(iii) For owners of closely held companies, compensation in excess of the costs that are deductible as compensation under the Internal Revenue Code (26 U.S.C.) and regulations under it is unallowable.

(b) *Reasonableness-*

(1) *Compensation pursuant to labor-management agreements.* If costs of compensation established under "arm's length" labor-management agreements negotiated under the terms of the Federal Labor Relations Act or similar state statutes are otherwise allowable, the costs are reasonable unless, as applied to work in performing Government contracts, the costs are unwarranted by the character and circumstances of the work or discriminatory against the Government. The application of the provisions of a labor-management agreement designed to apply to a given set of circumstances and conditions of employment (*e.g.*, work involving extremely hazardous activities or work not requiring recurrent use of overtime) is unwarranted when applied to a Government contract involving significantly different circumstances and conditions of employment (*e.g.*, work involving less hazardous activities or work continually requiring use of overtime). It is discriminatory against the Government if it results in employee compensation (in whatever form or name) in excess of that being paid for similar non-Government work under comparable circumstances.

(2) *Compensation not covered by labor-management agreements.* Compensation for each employee or job class of employees must be reasonable for the work performed. Compensation is reasonable if the aggregate of each measurable and allowable element sums to a reasonable total. In determining the reasonableness of total compensation, consider only allowable individual elements of compensation. In testing the reasonableness of compensation for particular employees or job classes of employees, consider factors determined to be relevant by the contracting officer. Factors that may be relevant include, but are not limited to, conformity with compensation practices of other firms-

(i) Of the same size;

(ii) In the same industry;

(iii) In the same geographic area; and

(iv) Engaged in similar non-Government work under comparable circumstances.

(c) [Reserved]

(d) *Form of payment.*

(1) Compensation for personal services includes compensation paid or to be paid in the future to employees in the form of

- (i) Cash;
- (ii) Corporate securities, such as stocks, bonds, and other financial instruments (see paragraph (d)(2) of this subsection regarding valuation); or
- (iii) Other assets, products, or services.

(2) When compensation is paid with securities of the contractor or of an affiliate, the following additional restrictions apply:

- (i) Valuation placed on the securities is the fair market value on the first date the number of shares awarded is known, determined upon the most objective basis available.
- (ii) Accruals for the cost of securities before issuing the securities to the employees are subject to adjustment according to the possibilities that the employees will not receive the securities and that their interest in the accruals will be forfeited.

*(e) Income tax differential pay.*

(1) Differential allowances for additional income taxes resulting from foreign assignments are allowable.

(2) Differential allowances for additional income taxes resulting from domestic assignments are unallowable. (However, payments for increased employee income or Federal Insurance Contributions Act taxes incident to allowable reimbursed relocation costs are allowable under Cost (32).

*(f) Bonuses and incentive compensation.*

(1) Bonuses and incentive compensation are allowable provided the-

- (i) Awards are paid or accrued under an agreement entered into in good faith between the contractor and the employees before the services are rendered or pursuant to an established plan or policy followed by the contractor so consistently as to imply, in effect, an agreement to make such payment; and
- (ii) Basis for the award is supported.

(2) When the bonus and incentive compensation payments are deferred, the costs are subject to the requirements of paragraphs (f)(1) and (k) of this subsection.

*(g) Severance pay.*

(1) Severance pay is a payment in addition to regular salaries and wages by contractors to workers whose employment is being involuntarily terminated. Payments for early retirement incentive plans are covered in paragraph (j)(6) of this subsection.

(2) Severance pay is allowable only to the extent that, in each case, it is required by-

- (i) Law;
- (ii) Employer-employee agreement;
- (iii) Established policy that constitutes, in effect, an implied agreement on the contractor's part; or
- (iv) Circumstances of the particular employment.

(3) Payments made in the event of employment with a replacement contractor where continuity of employment with credit for prior length of service is preserved under substantially equal conditions of employment, or continued employment by the contractor at another facility, subsidiary, affiliate, or parent company of the contractor are not severance pay and are unallowable.

(4) Actual normal turnover severance payments shall be allocated to all work performed in the contractor's plant. However, if the contractor uses the accrual method to account for normal turnover severance payments, that method will be acceptable if the amount of the accrual is-

- (i) Reasonable in light of payments actually made for normal severances over a representative past period; and
- (ii) Allocated to all work performed in the contractor's plant.

(5) Abnormal or mass severance pay is of such a conjectural nature that accruals for this purpose are not allowable. However, the Government recognizes its obligation to participate, to the extent of its fair share, in any specific payment. Thus, the Government will consider allowability on a case-by-case basis.

(6) The costs of severance payments to foreign nationals employed under a service contract performed outside the United States are unallowable to the extent that such payments exceed amounts typically paid to employees providing similar services in the same industry in the United States. Further, all such costs of severance payments that are otherwise allowable are unallowable if the termination of employment of the foreign national is the result of the closing of, or the curtailment of activities at, a United States facility in that country at the request of the government of that country; this does not apply if the closing of a facility or curtailment of activities is made pursuant to a status-of-forces or other country-to-country agreement entered into with the government of that country before November 29, 1989. The head of the agency is permitted to waive these cost allowability limitations under certain circumstances.

(h) *Back pay*. Back pay is a retroactive adjustment of prior years' salaries or wages. Back pay is unallowable except as follows:

(1) Payments to employees resulting from underpaid work actually performed are allowable, if required by a negotiated settlement, order, or court decree.

(2) Payments to union employees for the difference in their past and current wage rates for working without a contract or labor agreement during labor management negotiation are allowable.

(3) Payments to nonunion employees based upon results of union agreement negotiation are allowable only if-

- (i) A formal agreement or understanding exists between management and the employees concerning these payments; or

(ii) An established policy or practice exists and is followed by the contractor so consistently as to imply, in effect, an agreement to make such payments.

(i) *Compensation and Price of Corporate Securities.* Compensation based on changes in the prices of corporate securities or corporate security ownership, such as stock options, stock appreciation rights, phantom stock plans, and junior stock conversions.

(1) Any compensation which is calculated, or valued, based on changes in the price of corporate securities is unallowable.

(2) Any compensation represented by dividend payments or which is calculated based on dividend payments is unallowable.

(3) If a contractor pays an employee in lieu of the employee receiving or exercising a right, option, or benefit which would have been unallowable under Cost (4)(d) "Compensation and Price of Corporate Securities," such payments are also unallowable.

(j) *Pension costs.*

(1) A pension plan is a deferred compensation plan. Additional benefits such as permanent and total disability and death payments and survivorship payments to beneficiaries of deceased employees may be treated as pension costs, provided the benefits are an integral part of the pension plan and meet all the criteria pertaining to pension costs.

(2) Pension plans are normally segregated into two types of plans: defined-benefit or defined-contribution pension plans. The cost of all defined-benefit pension plans shall be measured, allocated, and accounted for in compliance with the provisions of 48 CFR 9904.412, Cost Accounting Standard for composition and measurement of pension cost, and 48 CFR 9904.413, Adjustment and allocation of pension cost. The costs of all defined-contribution pension plans shall be measured, allocated, and accounted for in accordance with the provisions of 48 CFR 9904.412 and 48 CFR 9904.413. Pension costs are allowable subject to the referenced standards and the cost limitations and exclusions set forth in subparagraph (j)(2)(i) and in subparagraphs (j)(3) through (7) of this subsection.

(i) Except for nonqualified pension plans using the pay-as-you-go cost method, to be allowable in the current year, pension costs must be funded by the time set for filing of the Federal income tax return or any extension thereof. Pension costs assigned to the current year, but not funded by the tax return time, shall not be allowable in any subsequent year. For nonqualified pension plans using the pay-as-you-go cost method, to be allowable in the current year, pension costs must be allocated in the cost accounting period that the pension costs are assigned.

(ii) Pension payments must be reasonable in amount and must be paid pursuant to an agreement entered into in good faith between the contractor and employees before the work or services are performed; and the terms and conditions of the established plan. The cost of changes in pension plans that are discriminatory to the Government or are not intended to be applied consistently for all employees under similar circumstances in the future are not allowable.

(iii) Except as provided for early retirement benefits in subparagraph (j)(7) of this subsection, one-time-only pension supplements not available to all participants of the basic plan are not allowable as pension costs unless the supplemental benefits

represent a separate pension plan and the benefits are payable for life at the option of the employee.

(iv) Increases in payments to previously retired plan participants covering cost-of living adjustments are allowable if paid in accordance with a policy or practice consistently followed.

(3) *Defined-benefit Pension Plans.* This paragraph covers pension plans in which the benefits to be paid or the basis for determining such benefits are established in advance and the contributions are intended to provide the stated benefits. The cost limitations and exclusions pertaining to defined-benefit plans are as follows:

(i)

(A) Except for nonqualified pension plans, pension costs (see 48 CFR 9904.412-40(a)(1)) assigned to the current accounting period, but not funded during it, shall not be allowable in subsequent years (except that a payment made to a fund by the time set for filing the Federal income tax return or any extension thereof is considered to have been made during such taxable year). However, any portion of pension cost computed for a cost accounting period, that exceeds the amount required to be funded pursuant to a waiver granted under the provisions of the Employee's Retirement Income Security Act of 1974 (ERISA), will be allowable in those future accounting periods in which the funding of such excess amounts occurs (see 48 CFR 9904.412-50(c)(5)).

(B) For nonqualified pension plans, except those using the pay-as-you-go cost method, allowable costs are limited to the amount allocable in accordance with 48 CFR 9904.412-50(d)(2).

(C) For nonqualified pension plans using the pay- as-you-go cost method, allowable costs are limited to the amounts allocable in accordance with 48 CFR 9904.412-50(d)(3).

(ii) Any amount funded in excess of the pension cost assigned to a cost accounting period is not allowable and shall be accounted for as set forth at 48 CFR 9904.412-50(a)(4), and shall be allowable in the future period to which it is assigned, to the extent it is allocable, reasonable, and not otherwise unallowable.

(iii) Increased pension costs caused by delay in funding beyond 30 days after each quarter of the year to which they are assignable are unallowable. If a composite rate is used for allocating pension costs between the segments of a company and if, because of differences in the timing of the funding by the segments, an inequity exists, allowable pension costs for each segment will be limited to that particular segment's calculation of pension costs as provided for in 48 CFR 9904.413-50(c). Determinations of unallowable costs shall be made in accordance with the actuarial cost method used in calculating pension costs.

(iv) Allowability of the cost of indemnifying the Pension Benefit Guaranty Corporation (PBGC) under ERISA Section 4062 or 4064 arising from terminating an

employee deferred compensation plan will be considered on a case-by-case basis, provided that if insurance was required by the PBGC under ERISA Section 4023, it was so obtained and the indemnification payment is not recoverable under the insurance. Consideration under the foregoing circumstances will be primarily for the purpose of appraising the extent to which the indemnification payment is allocable to Government work. If a beneficial or other equitable relationship exists, the Government will participate in the indemnification payment to the extent of its fair share.

(iv) Increased pension costs resulting from the withdrawal of assets from a pension fund and transfer to another employee benefit plan fund, or transfer of assets to another account within the same fund, are unallowable except to the extent authorized by an advance agreement. If the withdrawal of assets from a pension fund is a plan termination under ERISA, the provisions of subparagraph (j)(6) of this subsection apply. The advance agreement shall

(A) State the amount of the Government's equitable share in the gross amount withdrawn or transferred; and

(B) Provide that the Government receive a credit equal to the amount of the Government's equitable share of the gross withdrawal or transfer.

(4) *Pension Adjustments and Asset Reversions.*

(i) For segment closings, pension plan terminations, or curtailment of benefits, the adjustment amount shall be the amount measured, assigned, and allocated in accordance with 48 CFR 9904.413-50(c)(12) for contracts and subcontracts that are subject to Cost Accounting Standards (CAS) Board rules and regulations (48 CFR Chapter 99). For contracts and subcontracts that are not subject to CAS, the adjustment amount shall be the amount measured, assigned, and allocated in accordance with 48 CFR 9904.413-50(c)(12), except the numerator of the fraction at 48 CFR 9904.413-50(c)(12)(vi) shall be the sum of the pension plan costs allocated to all non-CAS-covered contracts and subcontracts that are subject to subparagraph A.2 of Procurement Guidance Section T3.3.2 or for which cost or pricing data were submitted.

(ii) For all other situations where assets revert to the contractor, or such assets are constructively received by it for any reason, the contractor shall, at the Government's option, make a refund or give a credit to the Government for its equitable share of the gross amount withdrawn. The Government's equitable share shall reflect the Government's participation in pension costs through those contracts for which cost or pricing data were submitted or that are subject to this Procurement Guidance section 3.3.2. Excise taxes on pension plan asset reversions or withdrawals under this subparagraph (j)(4)(ii) are unallowable in accordance with Cost (38)(b)(6).

(5) *Defined-contribution Pension Plans.* This paragraph covers those pension plans in which the contributions are established in advance and the level of benefits is determined by the contributions made. It also covers profit sharing, savings plans, and other such plans, provided the plans fall within the definition of a pension plan in subparagraph (j)(1) of this subsection.

(i) Allowable pension cost is limited to the net contribution required to be made

for a cost accounting period after taking into account dividends and other credits, where applicable. However, any portion of pension cost computed for a cost accounting period that exceeds the amount required to be funded pursuant to a waiver granted under the provisions of ERISA will be allowable in those future accounting periods in which the funding of such excess amounts occurs (see 48 CFR 9904.412-50(c)(5)).

(ii) The provisions of subparagraphs (j)(3)(ii) and (iv) of this subsection apply to defined-contribution plans.

(6) *Pension Plans Using the Pay-as-you-go Cost method.* The cost of pension plans using the pay-as-you-go cost method shall be measured, allocated, and accounted for in accordance with 48 CFR 9904.412 and 9904.413. Pension costs for a pension plan using the pay-as-you-go cost method shall be allowable to the extent they are allocable, reasonable, and not otherwise unallowable.

(7) *Early retirement incentive plans.* An early retirement incentive plan is a plan under which employees receive a bonus or incentive, over and above the requirement of the basic pension plan, to retire early. These plans normally are not applicable to all participants of the basic plan and do not represent life income settlements, and as such would not qualify as pension costs. However, for contract costing purposes, early retirement incentive payments are allowable subject to the pension cost criteria contained in subparagraphs (j)(3)(ii) through (iv) provided

(i) The costs are accounted for and allocated in accordance with the contractor's system of accounting for pension costs;

(ii) The payments are made in accordance with the terms and conditions of the contractor's plan;

(iii) The plan is applied only to active employees. The cost of extending the plan to employees who retired or were terminated before the adoption of the plan is unallowable; and

(iv) The total of the incentive payments to any employee may not exceed the amount of the employee's annual salary for the previous fiscal year before the employee's retirement.

(8) *Employee Stock Ownership Plans (ESOP).*

(i) An ESOP is an individual stock bonus plan designed specifically to invest in the stock of the employer corporation. The contractor's contributions to an Employee Stock Ownership Trust (ESOT) may be in the form of cash, stock, or property. Costs of ESOP's are allowable subject to the following conditions:

(A) Contributions by the contractor in any one year may not exceed 15 percent (25 percent when a money purchase plan is included) of salaries and wages of employees participating in the plan in any particular year.

(B) The contribution rate (ratio of contribution to salaries and wages of participating employees) may not exceed the last approved contribution rate except when approved by the contracting officer

based upon justification provided by the contractor. When no contribution was made in the previous year for an existing ESOP, or

when a new ESOP is first established, and the contractor proposes to make a contribution in the current year, the contribution rate shall be subject to the contracting officer's approval.

(C) When a plan or agreement exists wherein the liability for the contribution can be compelled for a specific year, the expense associated with that liability is assignable only to that period. Any portion of the contribution not funded by the time set for filing of the Federal income tax return for that year or any extension thereof shall not be allowable in subsequent years.

(D) When a plan or agreement exists wherein the liability for the contribution cannot be compelled, the amount contributed for any year is assignable to that year provided the amount is funded by the time set for filing of the Federal income tax return for that year.

(E) When the contribution is in the form of stock, the value of the stock contribution shall be limited to the fair market value of the stock on the date that title is effectively transferred to the trust. Cash contributions shall be allowable only when the contractor furnishes evidence satisfactory to the contracting officer demonstrating that stock purchases by the ESOP are or will be at a fair market price; *e.g.*, makes arrangements with the trust permitting the contracting officer to examine purchases of stock by the trust to determine that prices paid are at fair market value. When excessive prices are paid, the amount of the excess will be credited to the same indirect cost pools that were charged for the ESOP contributions in the year in which the stock purchase occurs. However, when the trust purchases the stock with borrowed funds which will be repaid over a period of years by cash contributions from the contractor to the trust, the excess price over fair market value shall be credited to the indirect cost pools pro rata over the period of years during which the contractor contributes the cash used by the trust to repay the loan. When the fair market value of unissued stock or stock of a closely held corporation is not readily determinable, the valuation will be made on a case-by-case basis taking into consideration the guidelines for valuation used by the IRS.

(ii) Amounts contributed to an ESOP arising from either

(A) An additional investment tax credit (see 1975 Tax Reduction Act TRASOP's); or

(B) A payroll-based tax credit (see Economic Recovery Tax Act of 1981) are unallowable.

(iii) The requirements of subparagraph (j)(3)(ii) of this subsection are applicable to Employee Stock Ownership Plans.

(k) *Deferred Compensation Other Than Pensions.*

(1) Deferred compensation is an award given by an employer to compensate an employee in a future cost accounting period or periods for services rendered in one or more cost accounting periods before the date of receipt of compensation by the employee. Deferred compensation does not include the amount of year-end accruals for salaries, wages, or bonuses that are paid within a reasonable period of time after the end of a cost accounting period. Deferred awards are allowable

when they are based on current or future services. Awards made in periods subsequent to the period when the work being remunerated was performed are not allowable.

(2) The costs of deferred awards shall be measured, allocated, and accounted for in compliance with the provisions of 48 CFR 9904.415, Accounting for the Cost of Deferred Compensation.

(3) Deferred compensation payments to employees under awards made before the effective date of 48 CFR 9904.415 are allowable to the extent they would have been allowable under prior acquisition regulations.

(l) *Compensation Incidental to Business Acquisitions.* The following costs are unallowable: (1) Payments to

employees under agreements in which they receive special compensation, in excess of the contractor's normal severance pay practice, if their employment terminates following a change in the management control over, or ownership of, the contractor or a substantial portion of its assets.

(2) Payments to employees under plans introduced in connection with a change (whether actual or prospective) in the management control over, or ownership of, the contractor or a substantial portion of its assets in which those employees receive special compensation, which is contingent upon the employee remaining with the contractor for a specified period of time.

(m) *Fringe Benefits.*

(1) Fringe benefits are allowances and services provided by the contractor to its employees as compensation in addition to regular wages and salaries. Fringe benefits include, but are not limited to, the cost of vacations, sick leave, holidays, military leave, employee insurance, and supplemental unemployment benefit plans. Except as provided otherwise in subparagraph A.2 of Procurement Guidance T3.3.2. "Contracts with Commercial Organizations," the costs of fringe benefits are allowable to the extent that they are reasonable and are required by law, employer-employee agreement, or an established policy of the contractor.

(2) That portion of the cost of company-furnished automobiles that relates to personal use by employees (including transportation to and from work) is unallowable regardless of whether the cost is reported as taxable income to the employees (see Cost (43)(f)).

(n) *Employee Rebate and Purchase Discount Plans.* Rebates and purchase discounts, in whatever form, granted to employees on products or services produced by the contractor or affiliates are unallowable.

(o) *Postretirement Benefits Other Than Pensions (PRB).*

(1) PRB covers all benefits, other than cash benefits and life insurance benefits paid by pension plans, provided to employees, their beneficiaries, and covered dependents during the period following the employees' retirement. Benefits encompassed include, but are not limited to, postretirement health care; life insurance provided outside a pension plan; and other welfare benefits such as tuition assistance, day care, legal services, and housing subsidies provided after retirement.

(2) To be allowable, PRB costs must be reasonable and incurred pursuant to law, employer-employee agreement, or an established policy of the contractor. In addition, to be allowable, PRB costs must also be calculated in accordance with subparagraphs (o)(2)(i) or (iii) of this section.

(i) *Cash Basis.* Cost recognized as benefits when they are actually provided, must be paid to an insurer, provider, or other recipient for current year benefits or premiums.

(ii) *Terminal Funding.* If a contractor elects a terminal-funded plan, it does not accrue PRB costs during the working lives of employees. Instead, it accrues and pays the entire PRB liability to an insurer or trustee in a lump sum upon the termination of employees (or upon conversion to such a terminal-funded plan) to establish and maintain a fund or reserve for the sole purpose of providing PRB to retirees. The lump sum is allowable if amortized over a period of 15 years.

(iii) *Accrual Basis.* Accrual costing other than terminal funding must be measured and assigned according to Generally Accepted Accounting Principles and be paid to an insurer or trustee to establish and maintain a fund or reserve for the sole purpose of providing PRB to retirees. The accrual must also be calculated in accordance with generally accepted actuarial principles and practices as promulgated by the Actuarial Standards Board.

(3) To be allowable, costs must be funded by the time set for filing the Federal income tax return or any extension thereof. PRB costs assigned to the current year, but not funded or otherwise liquidated by the tax return time, shall not be allowable in any subsequent year.

(4) Increased PRB costs caused by delay in funding beyond 30 days after each quarter of the year to which they are assignable are unallowable.

(5) Costs of postretirement benefits in subdivision (o)(2)(iii) of this subsection attributable to past service ("transition obligation") as defined in Financial Accounting Standards Board Statement 106, paragraph 110, are allowable subject to the following limitation: The allowable amount of such costs assignable to a contractor fiscal year cannot exceed the amount of such costs which would be assigned to that contractor fiscal year under the delayed recognition methodology described in paragraphs 112 and 113 of Statement 106.

(6) The Government shall receive an equitable share of any amount of previously funded PRB costs which revert or inure to the contractor. Such equitable share shall reflect the Government's previous participation in PRB costs through those contracts for which cost or pricing data were required or which were subject to subparagraph A.2. "Contracts with Commercial Organization" of Procurement Guidance T3.3.2.

(p) *Limitation on Allowability of Compensation for Certain Contractor Personnel.*

(1) Costs incurred after January 1, 1998, for compensation of a senior executive in excess of the benchmark compensation amount determined applicable for the contractor fiscal year are unallowable. This limitation is the sole statutory limitation on allowable senior executive compensation costs incurred after

January 1, 1998, under new or previously existing contracts. This limitation applies whether or not the affected contracts were previously subject to a statutory limitation on such costs. (Note that pursuant to Section 804 of Pub. L. 105-261, the definition of "senior executive" in (p)(2)(ii) has been changed for compensation costs

incurred after January 1, 1999.

(2) As used in this paragraph:

(i) "Compensation" means the total amount of wages, salary, bonuses, deferred compensation (see subparagraph (k) of this subsection), and employer contributions to defined contribution pension plans (see subparagraphs (j)(5) and (j)(7) of this subsection), for the fiscal year, whether paid, earned, or otherwise accruing, as recorded in the contractor's cost accounting records for the fiscal year.

(ii) "Senior executive" means

(A) Prior to January 2, 1999;

(aa) The Chief Executive Officer (CEO) or any individual acting in a similar capacity at the contractor's headquarters;

(bb) The four most highly compensated employees in management positions at the contractor's headquarters, other than the CEO; and

(cc) If the contractor has intermediate home offices or segments that report directly to the contractor's headquarters, the five most highly compensated employees in management positions at each such intermediate home office or segment.

(B) Effective January 2, 1999, the five most highly compensated employees in management positions at each home office and each segment of the contractor, whether or not the home office or segment reports directly to the contractor's headquarters.

(iii) "Fiscal year" means the fiscal year established by the contractor for accounting purposes.

(iv) "Contractor's headquarters" means the highest organizational level from which executive compensation costs are allocated to Government contracts.

(q) *Employee Stock Ownership Plans (ESOP)*

(1) An ESOP is a stock bonus plan designed to invest primarily in the stock of the employer corporation. The contractor's contributions to an Employee Stock Ownership Trust (ESOT) may be in the form of cash, stock, or property.

(2) Costs of ESOPs are allowable subject to the following conditions: (i) For ESOPs that

meet the definition of a pension plan at,  
the contractor:

(A) Measures, assigns, and allocates the costs; and

(B) Funds the pension costs by the time set for filing of the Federal income tax return or any extension. Pension costs assigned to the current year, but not funded by the tax return time, are not allowable in any subsequent year.

- (ii) For ESOPs that do not meet the definition of a pension plan, the contractor measures, assigns, and allocates costs in accordance with 48 CFR 9904.415.
- (iii) Contributions by the contractor in any one year that exceed the deductibility limits of the Internal Revenue Code for that year are unallowable.
- (iv) When the contribution is in the form of stock, the value of the stock contribution is limited to the fair market value of the stock on the date that title is effectively transferred to the trust.
- (v) When the contribution is in the form of cash:
  - (A) Stock purchases by the ESOP in excess of fair market value are unallowable; and
  - (B) When stock purchases are in excess of fair market value, the contractor must credit the amount of the excess to the same indirect cost pools that were charged for the ESOP contributions in the year in which the stock purchase occurs. However, when the trust purchases the stock with borrowed funds which will be repaid over a period of years by cash contributions from the contractor to the trust, the contractor shall credit the excess price over fair market value to the indirect cost pools pro rata over the period of years during which the contractor contributes the cash used by the trust to repay the loan.
- (vi) When the fair market value of unissued stock or stock of a closely held corporation is not readily determinable, the valuation will be made on a case-by-case basis taking into consideration the guidelines for valuation used by the IRS.

## **(5) Contingencies.**

- (a) "Contingency," as used in this subpart, means a possible future event or condition arising from presently known or unknown causes, the outcome of which is indeterminable at the present time.
- (b) Costs for contingencies are generally unallowable for historical costing purposes because such costing deals with costs incurred and recorded on the contractor's books. However, in some cases, as for example, terminations, a contingency factor may be recognized when it is applicable to a past period to give recognition to minor unsettled factors in the interest of expediting settlement.
- (c) In connection with estimates of future costs, contingencies fall into two categories:
  - (1) Those that may arise from presently known and existing conditions, the effects of which are foreseeable within reasonable limits of accuracy; *e.g.*, anticipated costs of rejects and defective work. Contingencies of this category are to be included in the estimates of future costs so as to provide the best estimate of performance cost.

(2) Those that may arise from presently known or unknown conditions, the effect of which cannot be measured so precisely as to provide equitable results to the contractor and to the Government; *e.g.*, results of pending litigation. Contingencies of this category are to be excluded from cost estimates under the several items of cost, but should be disclosed separately (including the basis upon which the contingency is computed) to facilitate the negotiation of appropriate contractual coverage.

**(6) Contributions or Donations.**

Contributions or donations, including cash, property and services, regardless of recipient, are unallowable, except as provided in Cost (1)(c)(3).

**(7) Cost of Money**

(a) *General.* Cost of money:

(1) Is an imputed cost that is not a form of interest on borrowings [see Cost (17)]; (2) Is an "incurred cost" for cost-reimbursement purposes under applicable cost-reimbursement contracts and for progress payment purposes under fixed-price contracts; and

(3) Refers to-

- (i) Facilities capital cost of money (48 CFR 9904.414); and
- (ii) Cost of money as an element of the cost of capital assets under construction (48 CFR 9904.417).

(b) Cost of money is allowable, provided-

- (1) It is measured, assigned, and allocated to contracts in accordance with 48 CFR 9904.414 or measured and added to the cost of capital assets under construction in accordance with 48 CFR 9904.417, as applicable;
- (2) The requirements of Cost (48), which limit the allowability of cost of money, are followed; and
- (3) The estimated facilities capital cost of money is specifically identified and proposed in cost proposals relating to the contract under which the cost is to be claimed.

(c) Actual interest cost in lieu of the calculated imputed cost of money is unallowable.

**(8) Depreciation.**

(a) Depreciation on a contractor's plant, equipment, and other capital facilities is an allowable contract cost, subject to the limitations contained in this cost principle. For tangible personal property, only estimated residual values that exceed 10 percent of the capitalized cost of the asset need be used in establishing depreciable costs. Where either the declining balance method of depreciation or the class life asset depreciation range system is used, the residual value need not be deducted from capitalized cost to determine depreciable costs. Depreciation cost that would significantly reduce the book value of a tangible capital asset below its residual value is unallowable.

(b) Contractors having contracts subject to 48 CFR 9904.409, Depreciation of Tangible Capital Assets, shall adhere to the requirement of that standard for all fully CAS-covered contracts and may elect to adopt the standard for all other contracts. All requirements of 48 CFR 9904.409 are applicable if the election is made, and contractors must continue to follow it until notification of final acceptance of all deliverable items on all open negotiated Government

contracts.

(c) For contracts to which 48 CFR 9904.409 is not applied, except as indicated in paragraphs (g) and (h) of this subsection, allowable depreciation shall not exceed the amount used for financial accounting purposes, and shall be determined in a manner consistent with the depreciation policies and procedures followed in the same segment on non-Government business.

(d) Depreciation, rental, or use charges are unallowable on property acquired from the Government at no cost by the contractor or by any division, subsidiary, or affiliate of the contractor under common control.

(e) The depreciation on any item which meets the criteria for allowance at price under Cost (23)(e) may be based on that price, provided the same policies and procedures are used for costing all business of the using division, subsidiary, or organization under common control.

(f) No depreciation or rental is allowed on property fully depreciated by the contractor or by any division, subsidiary, or affiliate of the contractor under common control. However, a reasonable charge for using fully depreciated property may be agreed upon and allowed. In determining the charge, consideration shall be given to cost, total estimated useful life at the time of negotiations, effect of any increased maintenance charges or decreased efficiency due to age, and the amount of depreciation previously charged to Government contracts or subcontracts.

(g) Whether or not the contract is otherwise subject to CAS, the requirements of Cost (48) shall be observed.

(h) In the event of a write-down from carrying value to fair value as a result of impairments caused by events or changes in circumstances, allowable depreciation of the impaired assets is limited to the amounts that would have been allowed had the assets not been written down [see Cost (13)(h)]. However, this does not preclude a change in depreciation resulting from other causes such as permissible changes in estimates of service life, consumption of services, or residual value.

(i) In the event the contractor reacquires property involved in a sale and leaseback arrangement, allowable depreciation of reacquired property shall be based on the net book value of the asset as of the date the contractor originally became a lessee of the property in the sale and leaseback arrangement:

(1) Adjusted for any allowable gain or loss; and

(2) Less any amount of depreciation expense included in the calculation of the amount that would have been allowed had the contractor retained title.

j. A "capital lease," as defined in Statement of Financial Accounting Standard No. 13 (FAS-13), Accounting for Leases, is subject to the requirements of this cost principle. FAS-13 requires that capital leases be treated as purchased assets, *i.e.*, be capitalized, and the capitalized value of such assets be distributed over their useful lives as depreciation charges or over the leased life as amortization charges, as appropriate, except that:

(1) Lease costs under a sale and leaseback arrangement are allowable up to the amount that would have been allowed had the contractor retained title to the asset; and

(2) If it is determined that the terms of the capital lease have been significantly affected by the fact that the lessee and lessor are related, depreciation charges are not allowable in excess of those that would have occurred if the lease contained terms consistent with those found in a lease between unrelated parties.

### **(9) Economic Planning Costs.**

Economic planning costs are the costs of general long-range management planning that is concerned with the future overall development of the contractor's business and that may take into account the eventual possibility of economic dislocations or fundamental alterations in those markets in which the contractor currently does business. Economic planning costs are allowable. Economic planning costs do not include organization or reorganization costs covered by Cost.(24). See Cost (35) for market planning costs other than economic planning costs.

**(10) *Employee Morale, Health, Welfare, Food Service, and Dormitory Costs and Credits.***

(a) Aggregate costs incurred on activities designed to improve working conditions, employer- employee relations, employee morale, and employee performance (less income generated by these activities) are allowable, subject to the limitations contained in this subsection. Some examples of allowable activities are-

(1) House publications; (2) Health clinics;

(3) Wellness/fitness centers;

(4) Employee counseling services; and

(5) Food and dormitory services for the contractor's employees at or near the contractor's facilities. These services include-

(i) Operating or furnishing facilities for cafeterias, dining rooms, canteens, lunch wagons, vending machines, living accommodations; and

(ii) Similar types of services.

(b) *Costs of Gifts Are Unallowable.* (Gifts do not include awards for performance or awards made in recognition of employee achievements pursuant to an established contractor plan or policy.)

(c) Costs of recreation are unallowable, except for the costs of employees' participation in company sponsored sports teams or employee organizations designed to improve company loyalty, team work, or physical fitness.

(d)

(1) The allowability of food and dormitory losses are determined by the following factors:

(i) Losses from operating food and dormitory services are allowable only if the contractor's objective is to operate such services on a break-even basis.

(ii) Losses sustained because food services or lodging accommodations are furnished without charge or at prices or rates which obviously would not be conducive to the accomplishment of the objective in paragraph (d)(1)(i) of this subsection are not allowable, except as described in paragraph (d)(1)(iii) of this subsection.

(iii) A loss may be allowed to the extent that the contractor can demonstrate that unusual circumstances exist such that even with efficient management, operating the services on a break-even basis would require charging inordinately high prices, or prices or rates higher than those charged by commercial establishments offering the same services in the same geographical areas. The following are examples of unusual circumstances:

(A) The contractor must provide food or dormitory services at remote

locations where adequate commercial facilities are not reasonably available.

(B) The contractor's charged (but unproductive) labor costs would be excessive if the services were not available.

(C) If cessation or reduction of food or dormitory operations will not otherwise yield net cost savings.

(2) Costs of food and dormitory services shall include an allocable share of indirect expenses pertaining to these activities.

(e) When the contractor has an arrangement authorizing an employee association to provide or operate a service, such as vending machines in the contractor's plant, and retain the profits, such profits shall be treated in the same manner as if the contractor were providing the service (but see subparagraph (f) of this subsection).

(f) Contributions by the contractor to an employee organization, including funds from vending machine receipts or similar sources, are allowable only to the extent that the contractor demonstrates that an equivalent amount of the costs incurred by the employee organization would be allowable if directly incurred by the contractor.

**(11) *Entertainment Costs.*** Costs of amusement, diversions, social activities, and any directly associated costs such as tickets to shows or sports events, meals, lodging, rentals, transportation, and gratuities are unallowable. Costs made specifically unallowable under this cost principle are not allowable under any other cost principle. Costs of membership in social, dining, or country clubs or other organizations having the same purposes are also unallowable, regardless of whether the cost is reported as taxable income to the employees.

**(12) *Fines, Penalties, and Mischarging Costs.***

(a) Costs of fines and penalties resulting from violations of, or failure of the contractor to comply with, Federal, State, local, or foreign laws and regulations, are unallowable except when incurred as a result of compliance with specific terms and conditions of the contract or written instructions from the contracting officer.

(b) Costs incurred in connection with, or related to, the mischarging of costs on Government contracts are unallowable when the costs are caused by, or result from, alteration or destruction of records, or other false or improper charging or recording of costs. Such costs include those incurred to measure or otherwise determine the magnitude of the improper charging, and costs incurred to remedy or correct the mischarging, such as costs to rescreen and reconstruct records.

**(13) *Gains and Losses on Disposition or Impairment of Depreciable Property or Other Capital Assets.***

(a) Gains and losses from the sale, retirement, or other disposition [but see Cost (16)] of depreciable property shall be included in the year in which they occur as credits or charges to the cost grouping(s) in which the depreciation or amortization applicable to those assets was included [but see subparagraph (d) of this subsection]. However, no gain or loss shall be recognized as a result of the transfer of assets in a business combination . See subparagraph Cost (48), "Asset Valuations Resulting from Business Combinations."

(b) Notwithstanding the provisions in paragraph (c) of this subsection, when costs of depreciable property are subject to the sale and leaseback limitations:

(1) The gain or loss is the difference between the net amount realized and the undepreciated balance of the asset on the date the contractor becomes a lessee; and

(2) When the application of (b)(1) of this subsection results in a loss:

(i) The allowable portion of the loss is zero if the fair market value exceeds the undepreciated balance of the asset on the date the contractor becomes a lessee; and

(ii) The allowable portion of the loss is limited to the difference between the fair market value and the undepreciated balance of the asset on the date the contractor becomes a lessee if the fair market value is less than the undepreciated balance of the asset on the date the contractor becomes a lessee.

(c) Gains and losses on disposition of tangible capital assets, including those acquired under capital leases, shall be considered as adjustments of depreciation costs previously recognized. The gain or loss for each asset disposed of is the difference between the net amount realized, including insurance proceeds from involuntary conversions, and its undepreciated balance. The gain recognized for contract costing purposes shall be limited to the difference between the acquisition cost (or for assets acquired under a capital lease, the value at which the leased asset is capitalized) of the asset and its undepreciated balance (except see subdivisions (c)(2)(i) or (ii) of this section).

(d) Special considerations apply to an involuntary conversion which occurs when a contractor's property is destroyed by events over which the owner has no control, such as fire, windstorm, flood, accident, theft, etc., and an insurance award is recovered. The following govern involuntary conversions:

(1) When there is a cash award and the converted asset is not replaced, gain or loss shall be recognized in the period of disposition. The gain recognized for contract costing purposes shall be limited to the difference between the acquisition cost of the asset and its undepreciated balance.

(2) When the converted asset is replaced, the contractor shall either

(i) Adjust the depreciable basis of the new asset by the amount of the total realized gain or loss; or

(ii) Recognize the gain or loss in the period of disposition, in which case the Government shall participate to the same extent as outlined in subparagraph (d)(1) of this subsection.

(e) Gains and losses on the disposition of depreciable property shall not be recognized as a separate charge or credit when

(1) Gains and losses are processed through the depreciation reserve account and reflected in the depreciation allowable under Cost.(8); or

(2) The property is exchanged as part of the purchase price of a similar item, and the gain or loss is taken into consideration in the depreciation cost basis of the new item.

(f) Gains and losses arising from mass or extraordinary sales, retirements, or other disposition other than through business combinations shall be considered on a case-by-case basis.

(g) Gains and losses of any nature arising from the sale or exchange of capital assets other than depreciable property shall be excluded in computing contract costs.

(h) With respect to long-lived tangible and identifiable intangible assets held for use, no loss shall be allowed for a write-down from carrying value to fair value as a result of impairments caused by events or changes in

circumstances (*e.g.*, environmental damage, idle facilities arising from a declining business base, etc.). If depreciable property or other capital assets have been written down from carrying value to fair value due to impairments, gains or losses upon disposition shall be the amounts that would have been allowed had the assets not been written down.

**(14) *Idle Facilities and Idle Capacity Costs.***

(a) "Costs of idle facilities or idle capacity," as used in this subsection, means costs such as maintenance, repair, housing, rent, and other related costs; *e.g.*, property taxes, insurance, and depreciation.

(1) "Facilities," as used in this subsection, means plant or any portion thereof (including land integral to the operation), equipment, individually or collectively, or any other tangible capital asset, wherever located, and whether owned or leased by the contractor.

(2) "Idle capacity," as used in this subsection, means the unused capacity of partially used facilities. It is the difference between that which a facility could achieve under 100 percent operating time on a one-shift basis, less operating interruptions resulting from time lost for repairs, setups, unsatisfactory materials, and other normal delays, and the extent to which the facility was actually used to meet demands during the accounting period. A multiple-shift basis may be used in the calculation instead of a one-shift basis if it can be shown that this amount of usage could normally be expected for the type of facility involved.

(3) "Idle facilities," as used in this subsection, means completely unused facilities that are excess to the contractor's current needs.

(b) The costs of idle facilities are unallowable unless the facilities

(1) Are necessary to meet fluctuations in workload; or

(2) Were necessary when acquired and are now idle because of changes in requirements, production economies, reorganization, termination, or other causes which could not have been reasonably foreseen. (Costs of idle facilities are allowable for a reasonable period, ordinarily not to exceed 1 year, depending upon the initiative taken to use, lease, or dispose of the idle facilities (but see Cost (39)).

(c) Costs of idle capacity are costs of doing business and are a factor in the normal fluctuations of usage or overhead rates from period to period. Such costs are allowable provided the capacity is necessary or was originally reasonable and is not subject to reduction or elimination by subletting, renting, or sale, in accordance with sound business, economics, or security practices. Widespread idle capacity throughout an entire plant or among a group of assets having substantially the same function may be idle facilities.

(d) Any costs to be paid directly by the Government for idle facilities or idle capacity reserved for defense mobilization production shall be the subject of a separate agreement.

**(15) *Independent Research and Development and Bid and Proposal Costs.***

(a) *Definitions.*

(1) "Applied research," as used in this subsection, means that effort which (1) normally follows basic research, but may not be severable from the related basic research, (2) attempts to determine and exploit the potential of scientific discoveries or improvements in technology, materials, processes, methods, devices, or techniques, and (3) attempts to advance the state of the art. Applied research does not include efforts whose principal aim is design, development, or test of specific items or services to be considered for sale; these efforts are within the definition of the term "development,"

defined in this subsection.

(2) "Basic research," as used in this subsection, means that research which is directed toward increase of knowledge in science. The primary aim of basic research is a fuller knowledge or understanding of the subject under study, rather than any practical application thereof.

(3) "Bid and proposal (B&P) costs," as used in this subsection, means the costs incurred in preparing, submitting, and supporting bids and proposals (whether or not solicited) on potential Government or non-Government contracts. The term does not include the costs of effort sponsored by a grant or cooperative agreement, or required in the performance of a contract.

(4) "Company," as used in this subsection, means all divisions, subsidiaries, and affiliates of the contractor under common control.

(5) "Development," as used in this subsection, means the systematic use, under whatever name, of scientific and technical knowledge in the design, development, test, or evaluation of a potential new product or service (or of an improvement in an existing product or service) for the purpose of meeting specific performance requirements or objectives. Development includes the functions of design engineering, prototyping, and engineering testing. Development excludes

(i) Subcontracted technical effort which is for the sole purpose of developing an additional source for an existing product, or

(ii) Development effort for manufacturing or production materials, systems, processes, methods, equipment, tools, and techniques not intended for sale.

(iii) "Independent research and development (IR&D)," as used in this subsection, means a contractor's IR&D cost that consists of projects falling within the four following areas: (1) basic research, (2) applied research, (3) development, and (4) systems and other concept formulation studies. The term does not include the costs of effort sponsored by a grant or required in the performance of a contract. IR&D effort shall not include technical effort expended in developing and preparing technical data specifically to support submitting a bid or proposal.

(iv) "Systems and other concept formulation studies," as used in this subsection, means analyses and study efforts either related to specific IR&D efforts or directed toward identifying desirable new systems, equipment or components, or modifications and improvements to existing systems, equipment, or components.

(b) *Composition and Allocation of Costs.* The requirements of 48 CFR 9904.420, Accounting for independent research and development costs and bid and proposal costs, are incorporated in their entirety and shall apply as follows

(1) *Fully-CAS-covered contracts.* Contracts that are fully-CAS-covered shall be subject to all requirements of 48 CFR 9904.420.

(2) *Modified CAS-covered and Non-CAS-covered Contracts.* Contracts that are not CAS-covered or that contain terms or conditions requiring modified CAS coverage shall be subject to all requirements of 48 CFR 9904.420 except 48 CFR 9904.420-50(e)(2) and 48 CFR 9904.420-50(f)(2), which are not then applicable. However, non-CAS-covered or modified CAS-covered contracts awarded at a time the contractor has CAS-covered contracts requiring compliance with 48 CFR 9904.420, shall be subject to all the requirements of 48 CFR 9904.420. When the

requirements of 48 CFR 9904.420-50(e)(2) and 48 CFR 9904.420-50(f)(2) are not applicable, the following apply:

(i) IR&D and B&P costs shall be allocated to final cost objectives on the same basis of allocation used for the G&A expense grouping of the profit center in which the costs are incurred. However, when IR&D and B&P costs clearly benefit other profit centers or benefit the entire company, those costs shall be allocated through the G&A of the other profit centers or through the corporate G&A, as appropriate.

(ii) If allocations of IR&D or B&P through the G&A base do not provide equitable cost allocation, the contracting officer may approve use of a different base.

(c) *Allowability.* Except as provided in subparagraphs (d) and (e) of this subsection, or as provided in agency regulations, costs for IR&D and B&P are allowable as indirect expenses on contracts to the extent that those costs are allocable and reasonable.

(d) *Deferred IR&D costs.*

(1) IR&D costs that were incurred in previous accounting periods are unallowable, except when a contractor has developed a specific product at its own risk in anticipation of recovering the development costs in the sale price of the product provided that

(i) The total amount of IR&D costs applicable to the product can be identified;

(ii) The proration of such costs to sales of the product is reasonable;

(iii) The contractor had no Government business during the time that the costs were incurred or did not allocate IR&D costs to Government contracts except to prorate the cost of developing a specific product to the sales of that product; and

(iv) No costs of current IR&D programs are allocated to Government work except to prorate the costs of developing a specific product to the sales of that product.

(2) When deferred costs are recognized, the contract (except firm-fixed-price and fixed-price with economic price adjustment) will include a specific provision setting forth the amount of deferred IR&D costs that are allocable to the contract. The negotiation memorandum will state the circumstances pertaining to the case and the reason for accepting the deferred costs.

(e) *Cooperative Arrangements.*

(1) IR&D costs may be incurred by contractors working jointly with one or more non-Federal entities pursuant to a cooperative arrangement (for example, joint ventures, limited partnerships, teaming arrangements, and collaboration and consortium arrangements). IR&D costs also may include costs contributed by contractors in performing cooperative research and development agreements, or similar arrangements, entered into under

(i) Section 12 of the Stevenson-Wydler Technology Transfer Act of 1980 (15 U.S.C. 3710(a));

(ii) Sections 203(c)(5) and (6) of the National Aeronautics and Space Act of 1958, as amended (42 U.S.C. 2473(c)(5) and (6));

(iii) 10 U.S.C. 2371 for the Defense Advanced Research Projects Agency; or

(iv) Other equivalent authority.

(2) IR&D costs incurred by a contractor pursuant to these types of cooperative arrangements should be considered as allowable IR&D costs if the work performed would have been allowed as contractor IR&D had there been no cooperative arrangement.

(3) Costs incurred in preparing, submitting, and supporting offers on potential cooperative arrangements are allowable to the extent they are allocable, reasonable, and not otherwise unallowable.

**(16) Insurance and Indemnification.**

(a) Insurance by purchase or by self-insuring includes

(1) Coverage the contractor is required to carry or to have approved, under the terms of the contract; and

(2) Any other coverage the contractor maintains in connection with the general conduct of its business.

(b) For purposes of applying the provisions of this subsection, the Government considers insurance provided by captive insurers (insurers owned by or under control of the contractor) as self-insurance, and charges for it shall comply with the provisions applicable to self-insurance costs in this subsection. However, if the captive insurer also sells insurance to the general public in substantial quantities and it can be demonstrated that the charge to the contractor is based on competitive market forces, the Government will consider the insurance as purchased insurance.

(c) Whether or not the contract is subject to CAS, self-insurance charges are allowable subject to paragraph (e) of this subsection and the following limitations:

(1) The contractor shall measure, assign, and allocate costs in accordance with 48 CFR 9904.416, Accounting for Insurance Costs.

(2) The contractor shall comply with Procurement Guidance T3.4.1. However, approval of a contractor's insurance program does not constitute a determination as to the allowability of the program's cost.

(3) If purchased insurance is available, any self-insurance charge plus insurance administration expenses in excess of the cost of comparable purchased insurance plus associated insurance administration expenses is unallowable.

(4) Self-insurance charges for risks of catastrophic losses are unallowable.

(d) Purchased insurance costs are allowable, subject to paragraph (e) of this subsection and the following limitations:

(1) For contracts subject to full CAS coverage, the contractor shall measure, assign, and allocate costs in accordance with 48 CFR 9904.416.

(2) For all contracts, premiums for insurance purchased from fronting insurance companies (insurance

companies not related to the contractor but who reinsure with a captive insurer of the contractor) are unallowable to the extent they exceed the sum of

- (i) The amount that would have been allowed had the contractor insured directly with the captive insurer; and
- (ii) Reasonable fronting company charges for services rendered.

(3) Actual losses are unallowable unless expressly provided for in the contract, except-

- (i) Losses incurred under the nominal deductible provisions of purchased insurance, in keeping with sound business practice, are allowable; and
- (ii) Minor losses, such as spoilage, breakage, and disappearance of small hand tools that occur in the ordinary course of business and that are not covered by insurance, are allowable.

(e) Self-insurance and purchased insurance costs are subject to the cost limitations in the following paragraphs:

(1) Costs of insurance required or approved pursuant to the contract are allowable.

(2) Costs of insurance maintained by the contractor in connection with the general conduct of its business are allowable subject to the following limitations:

(i) Types and extent of coverage shall follow sound business practice, and the rates and premiums shall be reasonable.

(ii) Costs allowed for business interruption or other similar insurance shall be limited to exclude coverage of profit.

(iii) The cost of property insurance premiums for insurance coverage in excess of the acquisition cost of the insured assets is allowable only when the contractor has a formal written policy assuring that in the event the insured property is involuntarily converted, the new asset shall be valued at the book value of the replaced asset plus or minus adjustments for differences between insurance proceeds and actual replacement cost. If the contractor does not have such a formal written policy, the cost of premiums for insurance coverage in excess of the acquisition cost of the insured asset is unallowable.

(iv) Costs of insurance for the risk of loss of, or damage to, Government property are allowable only to the extent that the contractor is liable for such loss or damage and such insurance does not cover loss or damage which results from willful misconduct or lack of good faith on the part of any of the contractor's directors or officers, or other equivalent representatives.

(v) Costs of insurance on the lives of officers, partners, proprietors, or employees are allowable only to the extent that the insurance represents additional compensation [see Procurement Guidance T3.3.2].

(3) The cost of insurance to protect the contractor against the costs of correcting its own defects in materials and workmanship is unallowable. However, insurance costs to cover fortuitous or casualty losses resulting from defects in materials or workmanship are allowable as a

normal business expense.

(4) Premiums for retroactive or backdated insurance written to cover losses that have occurred and are known are unallowable.

(5) The Government is obligated to indemnify the contractor only to the extent authorized by law, as expressly provided for in the contract, except as provided in paragraph (d)(3) of this subsection.

(6) Late premium payment charges related to employee deferred compensation plan insurance incurred pursuant to Section 4007 (29 U.S.C. 1307) or Section 4023 (29 U.S.C. 1323) of the Employee Retirement Income Security Act of 1974 are unallowable.

**(17) Interest and Other Financial Costs.** Interest on borrowings (however represented), bond discounts, costs of financing and refinancing capital (net worth plus long-term liabilities), legal and professional fees paid in connection with preparing prospectuses, costs of preparing and issuing stock rights, and directly associated costs are unallowable except for interest assessed by State or local taxing authorities under the conditions specified in Cost (38) [but see Cost (25)].

**(18) Labor Relations Costs.** (a) Costs incurred in maintaining satisfactory relations between the contractor and its employees, (other than those made unallowable in paragraph (b) of this section), including costs of shop stewards, labor management committees, employee publications, and other related activities, are allowable.

(b) As required by Executive Order 13494, Economy in Government Contracting, costs of any activities undertaken to persuade employees, of any entity, to exercise or not to exercise, or concerning the manner of exercising, the right to organize and bargain collectively through representatives of the employees' own choosing are unallowable. Examples of unallowable costs in paragraph (b) of this section include, but are not limited to, the costs of—

(1) Preparing and distributing materials;

(2) Hiring or consulting legal counsel or consultants;

(3) Meetings (including paying the salaries of the attendees at meetings held for this purpose);  
and

(4) Planning or conducting activities by managers, supervisors, or union representatives during work hours.

**(19) Lobbying and Political Activity Costs.**

(a) Costs associated with the following activities are unallowable:

(1) Attempts to influence the outcomes of any Federal, State, or local election, referendum, initiative, or similar procedure, through in kind or cash contributions, endorsements, publicity, or similar activities;

(2) Establishing, administering, contributing to, or paying the expenses of a political party, campaign, political action committee, or other organization established for the purpose of influencing the outcomes of elections;

(3) Any attempt to influence

(i) The introduction of Federal, state, or local legislation, or

(ii) The enactment or modification of any pending Federal, state, or local

legislation through communication with any member or employee of the Congress or state legislature (including efforts to influence state or local officials to engage in similar lobbying activity), or with any government official or employee in connection with a decision to sign or veto enrolled legislation;

(4) Any attempt to influence

(i) The introduction of Federal, state, or local legislation, or

(ii) The enactment or modification of any pending Federal, state, or local legislation by preparing, distributing or using publicity or propaganda, or by urging members of the general public or any segment thereof to contribute to or participate in any mass demonstration, march, rally, fund raising drive, lobbying campaign or letter writing or telephone campaign;

(5) Legislative liaison activities, including attendance at legislative sessions or committee hearings, gathering information regarding legislation, and analyzing the effect of legislation, when such activities are carried on in support of or in knowing preparation for an effort to engage in unallowable activities; or

(6) Costs incurred in attempting to improperly influence, either directly or indirectly, an employee or officer of the Executive branch of the Federal Government to give consideration to or act regarding a regulatory or contract matter.

(b) The following activities are excepted from the coverage of (a) of this section: (1) Providing a

technical and factual presentation of information on a topic directly related to the performance of a contract through hearing testimony, statements or letters to the Congress or a state legislature, or subdivision, member, or cognizant staff member thereof, in response to a documented request (including a Congressional Record notice requesting testimony or statements for the record at a regularly scheduled hearing) made by the recipient member, legislative body or subdivision, or a cognizant staff member thereof; provided such information is readily obtainable and can be readily put in deliverable form; and further provided that costs under this section for transportation, lodging or meals are unallowable unless incurred for the purpose of offering testimony at a regularly scheduled Congressional hearing pursuant to a written request for such presentation made by the Chairman or Ranking Minority Member of the Committee or Subcommittee conducting such hearing.

(2) Any lobbying made unallowable by subparagraph (a)(3) of this subsection to influence state or local legislation in order to directly reduce contract cost, or to avoid material impairment of the contractor's authority to perform the contract.

(3) Any activity specifically authorized by statute to be undertaken with funds from the contract.

(c) When a contractor seeks reimbursement for indirect costs, total lobbying costs shall be separately identified in the indirect cost rate proposal, and thereafter treated as other unallowable activity costs.

(d) Contractors shall maintain adequate records to demonstrate that the certification of costs as being allowable or unallowable.

(e) Existing procedures should be utilized to resolve in advance any significant questions or disagreements concerning the interpretation or application of this subsection.

**(20) *Losses on Other Contracts.*** An excess of costs over income under any other contract (including the contractor's contributed portion under cost-sharing contracts) is unallowable.

**(21) *RESERVED***

**(22) *Manufacturing and Production Engineering Costs.***

(a) The costs of manufacturing and production engineering effort as described in (1) through (4) of this subparagraph are all allowable:

(1) Developing and deploying new or improved materials, systems, processes, methods, equipment, tools and techniques that are or are expected to be used in producing products or services;

(2) Developing and deploying pilot production lines;

(3) Improving current production functions, such as plant layout, production scheduling and control, methods and job analysis, equipment capabilities and capacities, inspection techniques, and tooling analysis (including tooling design and application improvements); and

(4) Material and manufacturing producibility analysis for production suitability and to optimize manufacturing processes, methods, and techniques.

(b) This cost principle does not cover

(1) Basic and applied research effort (as defined in Cost (15)(1)) related to new technology, materials, systems, processes, methods, equipment, tools and techniques. Such technical effort is governed by Cost (15), Independent Research and Development and Bid and Proposal Costs; and

(2) Development effort for manufacturing or production materials, systems, processes, methods, equipment, tools, and techniques that are intended for sale is also governed by Cost (15).

(c) Where manufacturing or production development costs are capitalized or required to be capitalized under the contractor's capitalization policies, allowable cost will be determined in accordance with the requirements of Cost (8), "Depreciation".

**(23) *Material Costs.***

(a) Material costs include the costs of such items as raw materials, parts, subassemblies, components, and manufacturing supplies, whether purchased or manufactured by the contractor, and may include such collateral items as inbound transportation and in-transit insurance. In computing material costs, the contractor shall consider reasonable overruns, spoilage, or defective work (unless otherwise provided in any contract provision relating to inspecting and correcting defective work).

(b) The contractor shall-

(1) Adjust the costs of material for income and other credits, including available trade discounts, refunds, rebates, allowances, and cash discounts, and credits for scrap, salvage, and material returned to vendors; and

(2) Credit such income and other credits either directly to the cost of the material or allocate such income and other credits as a credit to indirect costs. When the contractor can demonstrate that

failure to take cash discounts was reasonable, the contractor does not need to credit lost discounts.

- (c) Reasonable adjustments arising from differences between periodic physical inventories and book inventories may be included in arriving at costs; provided such adjustments relate to the period of contract performance.
- (d) When materials are purchased specifically for and are identifiable solely with performance under a contract, the actual purchase cost of those materials should be charged to the contract. If material is issued from stores, any generally recognized method of pricing such material is acceptable if that method is consistently applied and the results are equitable.
- (e) Allowance for all materials, supplies and services that are sold or transferred between any divisions, subdivisions, subsidiaries, or affiliates of the contractor under a common control shall be on the basis of cost incurred in accordance with this subpart. However, allowance may be at price when-
  - (1) It is the established practice of the transferring organization to price interorganizational transfers at other than cost for commercial work of the contractor or any division, subsidiary or affiliate of the contractor under a common control; and
  - (2) The item being transferred qualifies for an exception and the contracting officer has not determined the price to be unreasonable.
- (f) When a commercial item under paragraph (e) of this subsection is transferred at a price based on a catalog or market price, the contractor-

- (1) Should adjust the price to reflect the quantities being acquired; and
- (2) May adjust the price to reflect the actual cost of any modifications necessary because of contract requirements.

**(24) Organization Costs.**

(a) Except as provided in subparagraph (b) of this subsection, expenditures in connection with (1) planning or executing the organization or reorganization of the corporate structure of a business, including mergers and acquisitions, (2) resisting or planning to resist the reorganization of the corporate structure of a business or a change in the controlling interest in the ownership of a business, and (3) raising capital (net worth plus long-term liabilities), are unallowable. Such expenditures include but are not limited to incorporation fees and costs of attorneys, accountants, brokers, promoters and organizers, management consultants and investment counselors, whether or not employees of the contractor. Unallowable "reorganization" costs include the cost of any change in the contractor's financial structure, excluding administrative costs of short-term borrowings for working capital, resulting in alterations in the rights and interests of security holders, whether or not additional capital is raised.

(b) The cost of activities primarily intended to provide compensation will not be considered organizational costs subject to this subsection, but will be governed by Cost (4). These activities include acquiring stock for

- (1) Executive bonuses,
- (2) Employee savings plans, and
- (3) Employee stock ownership plans.

**(25) Other Business Expenses.** The following types of recurring costs are allowable:

(a) Registry and transfer charges resulting from changes in ownership of securities issued by the contractor.

- (b) Cost of shareholders' meetings.
- (c) Normal proxy solicitations.
- (d) Preparing and publishing reports to shareholders.
- (e) Preparing and submitting required reports and forms to taxing and other regulatory bodies. (f) Incidental costs of directors' and committee meetings.
- (g) Other similar costs.

**(26) *Plant Protection Costs.*** Costs of items such as

- (a) Wages, uniforms, and equipment of personnel engaged in plant protection, (b) Depreciation on plant protection capital assets, and
- (c) Necessary expenses to comply with military requirements, are allowable.

**(27) *Patent Costs.***

(a) The following patent costs are allowable to the extent that they are incurred as requirements of a Government contract [but see Cost (30)]:

(1) Costs of preparing invention disclosures, reports, and other documents. (2) Costs for searching the art to the extent necessary to make the invention disclosures.

(3) Other costs in connection with the filing and prosecution of a United States patent application where title or royalty-free license is to be conveyed to the Government.

(b) General counseling services relating to patent matters, such as advice on patent laws, regulations, clauses, and employee agreements, are allowable [but see Cost (30)].

(c) Other than those for general counseling services, patent costs not required by the contract are unallowable. [See also Cost (34)].

**(28) *Plant Reconversion Costs.*** Plant reconversion costs are those incurred in restoring or rehabilitating the contractor's facilities to approximately the same condition existing immediately before the start of the Government contract, fair wear and tear excepted. Reconversion costs are unallowable except for the cost of removing Government property and the restoration or rehabilitation costs caused by such removal. However, in special circumstances where equity so dictates, additional costs may be allowed to the extent agreed upon before costs are incurred.

Care should be exercised to avoid duplication through allowance as contingencies, additional profit or fee, or in other contracts.

**(29) *Precontract Costs.*** Precontract costs are those incurred before the effective date of the contract directly pursuant to the negotiation and in anticipation of the contract award when such incurrence is necessary to comply with the proposed contract delivery schedule. Such costs are allowable to the extent that they would have been allowable if incurred after the date of the contract.

**(30) Professional and Consultant Service Costs.**

(a) *Definition.* "Professional and consultant services", as used in this subpart, are those services rendered by persons who are members of a particular profession or possess a special skill and who are not officers or employees of the contractor. Examples include those services acquired by contractors or subcontractors in order to enhance their legal, economic, financial, or technical positions. Professional and consultant services are generally acquired to obtain information, advice, opinions, alternatives, conclusions, recommendations, training, or direct assistance, such as studies, analyses, evaluations, liaison with Government officials, or other forms of representation.

(b) Costs of professional and consultant services are allowable subject to this subparagraph and subparagraphs (c) through (f) of this subsection when reasonable in relation to the services rendered and when not contingent upon recovery of the costs from the Government [but see Costs (27) and (44)].

(c) Costs of professional and consultant services performed under any of the following circumstances are unallowable:

(1) Services to improperly obtain, distribute, or use information or data protected by law or regulation .

(2) Services that are intended to improperly influence the contents of solicitations, the evaluation of proposals or quotations, or the selection of sources for contract award, whether award is by the Government, or by a prime contractor or subcontractor.

(3) Any other services obtained, performed, or otherwise resulting in violation of any statute or regulation prohibiting improper business practices or conflicts of interest.

(4) Services performed which are not consistent with the purpose and scope of the services contracted for or otherwise agreed to.

(d) In determining the allowability of costs (including retainer fees) in a particular case, no single factor or any special combination of factors is necessarily determinative. However, the contracting officer shall consider the following factors, among others:

(1) The nature and scope of the service rendered in relation to the service required.

(2) The necessity of contracting for the service, considering the contractor's capability in the particular area.

(3) The past pattern of acquiring such services and their costs, particularly in the years prior to the award of Government contracts.

(4) The impact of Government contracts on the contractor's business.

(5) Whether the proportion of Government work to the contractor's total business is such as to influence the contractor in favor of incurring the cost, particularly when the services rendered are not of a continuing nature and have little relationship to work under Government contracts.

(6) Whether the service can be performed more economically by employment rather than by contracting.

(7) The qualifications of the individual or concern rendering the service and the customary fee charged, especially on non-Government contracts.

(8) Adequacy of the contractual agreement for the service (*e.g.*, description of the service, estimate of time required, rate of compensation, termination provisions).

(e) Retainer fees, to be allowable, must be supported by evidence that

(1) The services covered by the retainer agreement are necessary and customary; (2) The level of

past services justifies the amount of the retainer fees (if no services were rendered, fees are not automatically unallowable);

(3) The retainer fee is reasonable in comparison with maintaining an in-house capability to perform the covered services, when factors such as cost and level of expertise are considered; and

(4) The actual services performed are documented in accordance with subparagraph (f) of this subsection.

(f) Fees for services rendered shall be allowable only when supported by evidence of the nature and scope of the service furnished. [See also Cost (35)]. However, retainer agreements generally are not based on specific statements of work. Evidence necessary to determine that work performed is proper and does not violate law or regulation shall include

(1) Details of all agreements (*e.g.*, work requirements, rate of compensation, and nature and amount of other expenses, if any) with the individuals or organizations providing the services and details of actual services performed;

(2) Invoices or billings submitted by consultants, including sufficient detail as to the time expended and nature of the actual services provided; and

(3) Consultants' work products and related documents, such as trip reports indicating persons visited and subjects discussed, minutes of meetings, and collateral memoranda and reports.

**(31) *Recruitment Costs.***

(a) Subject to subparagraph (b) of this subsection, the following costs are allowable: (1) Costs of help-wanted advertising.

(2) Costs of operating an employment office needed to secure and maintain an adequate labor force.

(3) Costs of operating an aptitude and educational testing program. (4) Travel costs of employees engaged in recruiting personnel.

(5) Travel costs of applicants for interviews.

(6) Costs for employment agencies, not in excess of standard commercial rates. (b) Help-wanted

advertising costs are unallowable if the advertising

(1) Does not describe specific positions or classes of positions; or

(2) Includes material that is not relevant for recruitment purposes, such as extensive illustrations or descriptions of the company's products or capabilities.

**(32) Relocation Costs.**

(a) Relocation costs are costs incident to the permanent change of assigned work location (for a period of 12 months or more) of an existing employee or upon recruitment of a new employee. The following types of relocation costs are allowable as noted, subject to the limitations in paragraphs (b) and (f) of this subsection:

(1) Costs of travel of the employee and members of the employee's immediate family [see Cost (43)] and transportation of the household and personal effects to the new location.

(2) Costs of finding a new home, such as advance trips by the employee or the spouse, or both, to locate living quarters, and temporary lodging during the transition period for the employee and members of the employee's immediate family.

(3) Closing costs incident to the disposition of the actual residence owned by the employee when notified of the transfer (*e.g.*, brokerage fees, legal fees, appraisal fees, points, and finance charges), except that these costs, when added to the costs described in paragraph (a)(4) of this subsection, shall not exceed 14 percent of the sales price of the property sold.

(4) Continuing costs of ownership of the vacant former actual residence being sold, such as maintenance of building and grounds (exclusive of fixing up expenses), utilities, taxes, property insurance, and mortgage interest, after the settlement date or lease date of a new permanent residence, except that these costs, when added to the costs described in paragraph (a)(3) of this subsection, shall not exceed 14 percent of the sales price of the property sold.

(5) Other necessary and reasonable expenses normally incident to relocation, such as disconnecting and connecting household appliances; automobile registration; driver's license and use taxes; cutting and fitting rugs, draperies, and curtains; forfeited utility fees and deposits; and purchase of insurance against damage to or loss of personal property while in transit.

(6) Costs incident to acquiring a home in the new work location, except that- (i) These costs are not allowable for existing employees or newly recruited employees who were not homeowners before the relocation; and

(ii) The total costs shall not exceed 5 percent of the purchase price of the new home.

(7) Mortgage interest differential payments, except that these costs are not allowable for existing or newly recruited employees who, before the relocation, were not homeowners and the total payments are limited to an amount determined as follows:

(i) The difference between the mortgage interest rates of the old and new residences times the current balance of the old mortgage times 3 years.

(ii) When mortgage differential payments are made on a lump-sum basis and the employee leaves or is transferred again in less than 3 years, the amount initially recognized shall be proportionately adjusted to reflect payments only for the actual time of the relocation.

(8) Rental differential payments covering situations where relocated employees retain ownership of

a vacated home in the old location and rent at the new location. The rented quarters at the new location must be comparable to those vacated, and the allowable differential payments may not exceed the actual rental costs for the new home, less the fair market rent for the vacated home times 3 years.

(9) Costs of canceling an unexpired lease.

(10) Payments for increased employee income or Federal Insurance Contributions Act (26 U.S.C. chapter 21) taxes incident to allowable reimbursed relocation costs.

(11) Payments for spouse employment assistance.

(b) The costs described in paragraph (a) of this subsection must also meet the following criteria to be considered allowable:

(1) The move must be for the benefit of the employer.

(2) Reimbursement must be in accordance with an established policy or practice that is consistently followed by the employer and is designed to motivate employees to relocate promptly and economically.

(3) The costs must not be otherwise unallowable under Procurement Guidance Section T3.3.2.

(4) Amounts to be reimbursed shall not exceed the employee's actual expenses, except that for miscellaneous costs of the type discussed in paragraph (a)(5) of this subsection, a flat amount, not to exceed \$5,000, may be allowed in lieu of actual costs.

(5) Reimbursement on a lump-sum basis may be allowed for any of the following relocation costs when adequately supported by data on the individual elements (*e.g.*, transportation, lodging, and meals) comprising the build-up of the lump-sum amount to be paid based on the circumstances of the particular employee's relocation:

(i) Costs of finding a new home.

(ii) Costs of travel to the new location (but not costs for the transportation of household goods).

(iii) Costs of temporary lodging.

(iv) When reimbursement on a lump-sum basis is used, any adjustments to reflect actual costs are unallowable.

(c) The following types of costs are unallowable:

(1) Loss on the sale of a home.

(2) Costs incident to acquiring a home in the new location as follows: (i) Real estate brokers' fees and commissions.

(ii) Costs of litigation.

- (iii) Real and personal property insurance against damage or loss of property.
- (iv) Mortgage life insurance.
- (v) Owner's title policy insurance when such insurance was not previously carried by the employee on the old residence. (However, the cost of a mortgage title policy is allowable.)
- (vi) Property taxes and operating or maintenance costs.

(3) Continuing mortgage principal payments on a residence being sold.

(4) Costs incident to furnishing equity or nonequity loans to employees or making arrangements with lenders for employees to obtain lower-than-market rate mortgage loans.

(d) If relocation costs for an employee have been allowed either as an allocable indirect or direct cost, and the employee resigns within 12 months for reasons within the employee's control, the contractor shall refund or credit the relocation costs to the Government.

(e) Subject to the requirements of subparagraphs (a) through (d) of this section, the costs of family movements and of personnel movements of a special or mass nature are allowable. The cost, however, should be assigned on the basis of work (contracts) or time period benefited.

(f) Relocation costs (both outgoing and return) of employees who are hired for performance on specific contracts or long-term field projects are allowable if

(1) The term of employment is 12 months or more;

(2) The employment agreement specifically limits the duration of employment to the time spent on the contract or field project for which the employee is hired;

(3) The employment agreement provides for return relocation to the employee's permanent and principal home immediately prior to the outgoing relocation, or other location of equal or lesser cost; and

(4) The relocation costs are determined under the rules of subparagraphs (a) through (d) of this section. However, the costs to return employees, who are released from employment upon completion of field assignments pursuant to their employment agreements, are not subject to the refund or credit requirement of subparagraph (d).

### **(33) Rental Costs.**

(a) This subsection is applicable to the cost of renting or leasing real or personal property acquired under "operating leases" as defined in Statement of Financial Accounting Standards No. 13 (FAS-13), Accounting for Leases. Compliance with A.2.e.(8)(m) requires that assets acquired by means of capital leases, as defined in FAS-13, shall be treated as purchased assets; *i.e.*, be capitalized and the capitalized value of such assets be distributed over their useful lives as depreciation charges, or over the lease term as amortization charges, as appropriate (but see subparagraph (b)(4) of this section).

(b) The following costs are allowable:

(1) Rental costs under operating leases, to the extent that the rates are reasonable at the time of the

lease decision, after consideration of

- (i) Rental costs of comparable property, if any; (ii) Market conditions in the area;
- (iii) The type, life expectancy, condition, and value of the property leased;
- (iv) Alternatives available; and
- (v) Other provisions of the agreement.

(2) Rental costs under a sale and leaseback arrangement only up to the amount the contractor would be allowed if the contractor retained title.

(3) Charges in the nature of rent for property between any divisions, subsidiaries, or organizations under common control, to the extent that they do not exceed the normal costs of ownership, such as depreciation, taxes, insurance, facilities capital cost of money, and maintenance (excluding interest or other unallowable costs pursuant to this Procurement Guidance Section T3.3.2), provided that no part of such costs shall duplicate any other allowed cost. Rental cost of personal property leased from any division, subsidiary, or affiliate of the contractor under common control, that has an established practice of leasing the same or similar property to unaffiliated lessees shall be allowed in accordance with subparagraph (b)(1) of this subsection.

(4) Rental costs under leases entered into before March 1, 1970 for the remaining term of the lease (excluding options not exercised before March 1, 1970) to the extent they would have been allowable under Defense Acquisition Regulation (formerly ASPR) 15-205.34 or Federal Procurement Regulations section 1-15.205-34 in effect January 1, 1969.

(c) The allowability of rental costs under unexpired leases in connection with terminations is treated in (39) of this subsection.

**(34) *Royalties and Other Costs for Use of Patents.***

(a) Royalties on a patent or amortization of the cost of purchasing a patent or patent rights necessary for the proper performance of the contract and applicable to contract products or processes are allowable unless

- (1) The Government has a license or the right to a free use of the patent;
- (2) The patent has been adjudicated to be invalid, or has been administratively determined to be invalid;
- (3) The patent is considered to be unenforceable; or
- (4) The patent is expired.

(b) Care should be exercised in determining reasonableness when the royalties may have been arrived at as a result of less-than-arm's-length bargaining; *e.g.*, royalties

- (1) Paid to persons, including corporations, affiliated with the contractor; (2) Paid to

unaffiliated parties, including corporations, under an agreement entered into in contemplation that a Government contract would be awarded; or

(3) Paid under an agreement entered into after the contract award.

(c) In any case involving a patent formerly owned by the contractor, the royalty amount allowed should not exceed the cost which would have been allowed had the contractor retained title.

(d) See A.1.(i) regarding advance agreements.

**(35) *Selling Costs.***

(a) "Selling" is a generic term encompassing all efforts to market the contractor's products or services, some of which are covered specifically in other subsections of A.2.e. The costs of any selling efforts other than those addressed in this cost principle are unallowable.

(b) Selling activity includes the following broad categories:

(1) *Advertising.* Advertising is defined at Cost (1), and advertising costs are subject to the allowability provisions of Cost (1)(b).

(2) *Corporate image enhancement.* Corporate image enhancement activities, including broadly targeted sales efforts, other than advertising, are included within the definition of public relations at Cost (1)(a), and the costs of such efforts are subject to the allowability provisions at Cost (1)(a)

(3) *Bid and proposal costs.* Bid and proposal costs are defined at Cost (15) and are subject to the allowability provisions of that subsection.

(4) *Market planning.* Market planning involves market research and analysis and general management planning concerned with development of the contractor's business. Long-range market planning costs are subject to the allowability provisions of Cost (9). Other market planning costs are allowable.

(5) *Direct selling.* Direct selling efforts are those acts or actions to induce particular customers to purchase particular products or services of the contractor. Direct selling is characterized by person-to-person contact and includes such efforts as familiarizing a potential customer with the contractor's products or services, conditions of sale, service capabilities, etc. It also includes negotiation, liaison between customer and contractor personnel, technical and consulting efforts, individual demonstrations, and any other efforts having as their purpose the application or adaptation of the contractor's products or services for a particular customer's use. The cost of direct selling efforts is allowable.

(c) Notwithstanding any other provision of this subsection, sellers' or agents' compensation, fees, commissions, percentages, retainer or brokerage fees, whether or not contingent upon the award of contracts, are allowable only when paid to bona fide employees or established commercial or selling agencies maintained by the contractor for the purpose of securing business.

**(36) *Service and Warranty Costs.*** Service and warranty costs include those arising from fulfillment of any contractual obligation of a contractor to provide services such as installation, training, correcting defects in the products, replacing defective parts, and making refunds in the case of inadequate performance. When not inconsistent with the terms of the contract, such service and warranty costs are allowable. However, care should be exercised to

avoid duplication of the allowance as an element of both estimated product cost and risk.

**(37) *Special Tooling and Special Test Equipment Costs.***

(a) The terms "special tooling" and "special test equipment" are defined in AMS Procurement Guidance T3.10.3.

(b) The cost of special tooling and special test equipment used in performing one or more Government contracts is allowable and shall be allocated to the specific Government contract or contracts for which acquired, except that the cost of

(1) Items acquired by the contractor before the effective date of the contract (or replacement of such items), whether or not altered or adapted for use in performing the contract, and

(2) Items which the contract schedule specifically excludes, shall be allowable only as depreciation or amortization.

(c) When items are disqualified as special tooling or special test equipment because with relatively minor expense they can be made suitable for general purpose use and have a value as such commensurate with their value as special tooling or special test equipment, the cost of adapting the items for use under the contract and the cost of returning them to their prior configuration are allowable.

**(38) *Taxes.***

(a) The following types of costs are allowable:

(1) Federal, State, and local taxes, except as otherwise provided in subparagraph (b) of this section that are required to be and are paid or accrued in accordance with generally accepted accounting principles. Fines and penalties are not considered taxes.

(2) Taxes otherwise allowable under subparagraph (a)(1) of this section, but upon which a claim of illegality or erroneous assessment exists; provided the contractor, before paying such taxes

(i) Promptly requests instructions from the contracting officer concerning such taxes; and

(ii) Takes all action directed by the contracting officer arising out of subparagraph (2)(1) of this section or an independent decision of the Government as to the existence of a claim of illegality or erroneous assessment, to

(A) Determine the legality of the assessment or

(B) Secure a refund of such taxes.

(3) Pursuant to subparagraph (a)(2) of this section, the reasonable costs of any action taken by the contractor at the direction or with the concurrence of the contracting officer. Interest or penalties incurred by the contractor for non- payment of any tax at the direction of the contracting officer or by reason of the failure of the contracting officer to ensure timely direction after a prompt request.

(4) The Environmental Tax found at section 59A of the Internal Revenue Code, also called the "Superfund Tax."

(b) The following types of costs are not allowable: (1) Federal income

and excess profits taxes.

(2) Taxes in connection with financing, refinancing, refunding operations, or reorganizations [see Costs (17) and (24)].

(3) Taxes from which exemptions are available to the contractor directly, or available to the contractor based on an exemption afforded the Government, except when the contracting officer determines that the administrative burden incident to obtaining the exemption outweighs the corresponding benefits accruing to the Government. When partial exemption from a tax is attributable to Government contract activity, taxes charged to such work in excess of that amount resulting from application of the preferential treatment are unallowable. These provisions intend that tax preference attributable to Government contract activity be realized by the Government. The term "exemption" means freedom from taxation in whole or in part and includes a tax abatement or reduction resulting from mode of assessment, method of calculation, or otherwise.

(4) Special assessments on land that represent capital improvements.

(5) Taxes (including excises) on real or personal property, or on the value, use, possession or sale thereof, which is used solely in connection with work other than on Government contracts (see subparagraph (c) of this section).

(6) Any excise tax in subtitle D, chapter 43 of the Internal Revenue Code of 1986, as amended. That chapter includes excise taxes imposed in connection with qualified pension plans, welfare plans, deferred compensation plans, or other similar types of plans.

(7) Income tax accruals designed to account for the tax effects of differences between taxable income and pretax income as reflected by the books of account and financial statements.

(8) Any tax imposed under 26 U.S.C. 5000C (Imposition of Tax on Certain Foreign Procurements)

(c) Taxes on property used solely in connection with either non-Government or Government work should be considered directly applicable to the respective category of work unless the amounts involved are insignificant or comparable results would otherwise be obtained; *e.g.*, taxes on contractor-owned work-in-process which is used solely in connection with non-Government work should be allocated to such work; taxes on contractor-owned work-in-process inventory (and Government-owned work-in-process inventory when taxed) used solely in connection with Government work should be charged to such work. The cost of taxes incurred on property used in both Government and non-Government work shall be apportioned to all such work based upon the use of such property on the respective final cost objectives.

(d) Any taxes, interest, or penalties that were allowed as contract costs and are refunded to the contractor shall be credited or paid to the Government in the manner it directs. If a contractor or subcontractor obtains a foreign tax credit that reduces its U.S. Federal income tax because of the payment of any tax or duty allowed as contract costs, and if those costs were reimbursed by a foreign government, the amount of the reduction shall be paid to the Treasurer of the United States at the time the Federal income tax return is filed. However, any interest actually paid or credited to a contractor incident to a refund of tax, interest, or penalty shall be paid or credited to the Government only to the extent that such interest accrued over the period during which the contractor had been reimbursed by the Government for the taxes, interest, or penalties.

**(39) Termination Costs.** Contract terminations generally give rise to the incurrence of costs or the need for special treatment of costs that would not have arisen had the contract not been terminated. The following cost principles peculiar to termination situations are to be used in conjunction with the other cost principles in this Procurement Guidance Section T3.3.2:

(a) *Common items.* The costs of items reasonably usable on the contractor's other work shall not be allowable unless the contractor submits evidence that the items could not be retained at cost without sustaining a loss. The contracting officer should consider the contractor's plans and orders for current and planned production when determining if items can reasonably be used on other work of the contractor. Contemporaneous purchases of common items by the contractor shall be regarded as evidence that such items are reasonably usable on the contractor's other work. Any acceptance of common items as allocable to the terminated portion of the contract should be limited to the extent that the quantities of such items on hand, in transit, and on order are in excess of the reasonable quantitative requirements of other work.

(b) *Costs Continuing After Termination.* Despite all reasonable efforts by the contractor, costs which cannot be discontinued immediately after the effective date of termination are generally allowable. However, any costs continuing after the effective date of the termination due to the negligent or willful failure of the contractor to discontinue the costs shall be unallowable.

(c) *Initial Costs.* Initial costs, including starting load and preparatory costs, are allowable as follows:

(1) Starting load costs not fully absorbed because of termination are nonrecurring labor, material, and related overhead costs incurred in the early part of production and result from factors such as

- (i) Excessive spoilage due to inexperienced labor;
- (ii) Idle time and subnormal production due to testing and changing production methods;
- (iii) Training; and
- (iv) Lack of familiarity or experience with the product, materials, or manufacturing processes.

(2) Preparatory costs incurred in preparing to perform the terminated contract include such costs as those incurred for initial plant rearrangement and alterations, management and personnel organization, and production planning. They do not include special machinery and equipment and starting load costs.

(3) When initial costs are included in the settlement proposal as a direct charge, such costs shall not also be included in overhead. Initial costs attributable to only one contract shall not be allocated to other contracts.

(4) If initial costs are claimed and have not been segregated on the contractor's books, they shall be segregated for settlement purposes from cost reports and schedules reflecting that high unit cost incurred during the early stages of the contract.

(5) If the settlement proposal is on the inventory basis, initial costs should normally be allocated on the basis of total end items called for by the contract immediately before termination; however, if the contract includes end items of a diverse nature, some other equitable basis may be used, such as machine or labor hours.

(d) *Loss of Useful Value.* Loss of useful value of special tooling, and special machinery and equipment is generally allowable, provided

(1) The special tooling, or special machinery and equipment is not reasonably capable of use in the other work of the contractor;

(2) The Government's interest is protected by transfer of title or by other means deemed appropriate by the contracting officer; and

(3) The loss of useful value for any one terminated contract is limited to that portion of the acquisition cost which bears the same ratio to the total acquisition cost as the terminated portion of the contract bears to the entire terminated contract and other Government contracts for which the special tooling, or special machinery and equipment was acquired.

(e) *Rental Under Unexpired Leases.* Rental costs under unexpired leases, less the residual value of such leases, are generally allowable when shown to have been reasonably necessary for the performance of the terminated contract, if

(1) The amount of rental claimed does not exceed the reasonable use value of the property leased for the period of the contract and such further period as may be reasonable; and

(2) The contractor makes all reasonable efforts to terminate, assign, settle, or otherwise reduce the cost of such lease.

(f) *Alterations of Leased Property.* The cost of alterations and reasonable restorations required by the lease may be allowed when the alterations were necessary for performing the contract.

(g) *Settlement Expenses.*

(1) Settlement expenses, including the following, are generally allowable: (i) Accounting,

legal, clerical, and similar costs reasonably necessary for

(A) The preparation and presentation, including supporting data, of settlement claims to the contracting officer; and

(B) The termination and settlement of subcontracts.

(ii) Reasonable costs for the storage, transportation, protection, and disposition of property acquired or produced for the contract.

(iii) Indirect costs related to salary and wages incurred as settlement expenses in (i) and (ii); normally, such indirect costs shall be limited to payroll taxes, fringe benefits, occupancy costs, and immediate supervision costs.

(2) If settlement expenses are significant, a cost account or work order shall be established to separately identify and accumulate them.

(h) *Subcontractor Claims.* Subcontractor claims, including the allocable portion of the claims common to the contract and to other work of the contractor, are generally allowable. An appropriate share of the contractor's indirect expense may be allocated to the amount of settlements with subcontractors; provided, that the amount allocated is reasonably proportionate to the relative benefits received and is otherwise consistent with Procurement Guidance T3.3.2. The indirect expense so allocated shall exclude the same and similar costs claimed directly or indirectly as settlement expenses.

**(40) Trade, Business, Technical and Professional Activity Costs.** The following types of costs are allowable:

(a) Memberships in trade, business, technical, and professional organizations. (b) Subscriptions to trade, business, professional, or other technical periodicals.

(c) When the principal purpose of a meeting, convention, conference, symposium, or seminar is the dissemination of trade, business, technical or professional information or the stimulation of production or improved productivity

(1) Costs of organizing, setting up, and sponsoring the meetings, conventions, symposia, etc., including rental of meeting facilities, transportation, subsistence, and incidental costs;

(2) Costs of attendance by contractor employees, including travel costs [see Cost (43)]; and

(3) Costs of attendance by individuals who are not employees of the contractor, provided

(i) Such costs are not also reimbursed to the individual by the employing company or organization, and

(ii) The individuals attendance is essential to achieve the purpose of the conference, meeting, convention, symposium, etc.

#### **(41) Training and Education Costs.**

(a) *Allowable Costs.* Training and education costs are allowable to the extent indicated below. (b) *Vocational*

*Training.* Costs of preparing and maintaining a noncollege level program of instruction, including but not limited to on-the-job, classroom, and apprenticeship training, designed to increase the vocational effectiveness of employees, are allowable. These costs include

(1) Salaries or wages of trainees (excluding overtime compensation),

(2) Salaries of the director of training and staff when the training program is conducted by the contractor,

(3) Tuition and fees when the training is in an institution not operated by the contractor, and/or

(4) Training materials and textbooks.

(c) *Part-time College Level Education.* Allowable costs of part-time college education at an undergraduate or postgraduate level, including that provided at the contractor's own facilities, are limited to

(1) Fees and tuition charged by the educational institution, or, instead of tuition, instructors' salaries and the related share of indirect cost of the educational institution, to the extent that the sum thereof is not in excess of the tuition that would have been paid to the participating educational institution;

(2) Salaries and related costs of instructors who are employees of the contractor;

(3) Training materials and textbooks; and

(4) Straight-time compensation of each employee for time spent attending classes during working hours not in excess of 156 hours per year where circumstances do not permit the operation of classes or attendance at classes after regular working hours. In unusual cases, the period may be extended (see subparagraph (h) of this subsection).

(d) *Full-time Education.* Costs of tuition, fees, training materials and textbooks (but not subsistence, salary, or any other emoluments) in connection with full-time education, including that provided at the contractor's own facilities, at a postgraduate but not undergraduate college level, are allowable only when the course or degree pursued is related to the field in which the employee is working or may reasonably be expected to work and are limited to a total period not to exceed 2 school years or the length of the degree program, whichever is less, for each employee so trained.

(e) *Specialized Programs.* Costs of attendance of up to 16 weeks per employee per year at specialized programs specifically designed to enhance the effectiveness of managers or to prepare employees for such positions are allowable. Such costs include enrollment fees and related charges and employees' salaries, subsistence, training materials, textbooks, and travel. Costs allowable under this paragraph do not include costs for courses that are part of a degree- oriented curriculum, which are only allowable pursuant to subparagraphs (c) and (d) of this subsection.

(f) *Other Expenses.* Maintenance expense and normal depreciation or fair rental on facilities owned or leased by the contractor for training purposes are allowable in accordance with Costs (8), (14), (21) and (33).

(g) *Grants.* Grants to educational or training institutions, including the donation of facilities or other properties, scholarships, and fellowships are considered contributions and are unallowable.

(h) *Advance Agreements.*

(1) Training and education costs in excess of those otherwise allowable under subparagraphs (c) and (d) of this subsection, including subsistence, salaries or any other emoluments, may be allowed to the extent set forth in an advance agreement. To be considered for an advance agreement, the contractor must demonstrate that the costs are consistently incurred under an established managerial, engineering, or scientific training and education program, and that the course or degree pursued is related to the field in which the employees are now working or may reasonably be expected to work. Before entering into the advance agreement, the contracting officer shall give consideration to such factors as

- (i) The length of employees' service with the contractor; (ii) Employees' past performance and potential;
- (iii) Whether employees are in formal development programs; and
- (iv) The total number of participating employees.

(2) Any advance agreement must include a provision requiring the contractor to refund to the Government training and education costs for employees who resign within 12 months of completion of such training or education for reasons within an employee's control.

(i) *Training or Education Costs for Other Than Bona Fide Employees.* Costs of tuition, fees, textbooks, and similar or related benefits provided for other than bona fide employees are unallowable, except that the costs incurred for educating employee dependents (primary and secondary level studies) when the employee is working in a foreign country where public education is not available and where suitable private education is inordinately expensive may be included in overseas differential.

(j) *Employee Dependent Education Plans.* Costs of college plans for employee dependents are unallowable.

**(42) RESERVED**

**(43) Travel Costs.**

**(a) Costs for Transportation, Lodging, Meals, and Incidental Expenses.**

(1) Costs incurred by contractor personnel on official company business are allowable, subject to the limitations contained in this subsection. Costs for transportation may be based on mileage rates, actual costs incurred, or on a combination thereof, provided the method used results in a reasonable charge. Costs for lodging, meals, and incidental expenses may be based on per diem, actual expenses, or a combination thereof, provided the method used results in a reasonable charge.

(2) Except as provided in subparagraph (a)(3) of this subsection, costs incurred for lodging, meals, and incidental expenses (as defined in the regulations cited in (a)(2)(i) through (iii) of this subparagraph) shall be considered to be reasonable and allowable only to the extent that they do not exceed on a daily basis the maximum per diem rates in effect at the time of travel as set forth in the

(i) Federal Travel Regulations, (Stock No. 922-002-00000-2) prescribed by the [General Services Administration](#), for travel in the conterminous 48 United States, available on a subscription basis from the: Superintendent of Documents, U.S. Government Printing Office, Washington, DC 20402;

(ii) [Department of Defense](#) Per Diem, Travel and Transportation Allowance Committee (PDTATAC) bulletins, for travel in Alaska, Hawaii, The Commonwealth of Puerto Rico, and territories and possessions of the United States, available in the Federal Register (or in the Section 925 Supplement to the guidance cited under (a)(2)(iii) below); or

(iii) Standardized Regulations (Government Civilians, Foreign Areas), Section 925, "Maximum Travel Per Diem Allowances for Foreign Areas," (Stock No. 744-008-00000-0) prescribed by the [Department of State](#), for travel in areas not covered in (a)(2)(i) and (ii) of this subparagraph, available on a subscription basis from the: Superintendent of Documents, U.S. Government Printing Office, Washington, DC 20402.

(3) In special or unusual situations, actual costs in excess of the above-referenced maximum per diem rates are allowable provided that such amounts do not exceed the higher amounts authorized for Federal civilian employees as permitted in the regulations referenced in (a)(2)(i), (ii), or (iii) of this subsection. For such higher amounts to be allowable, all of the following conditions must be met:

(i) One of the conditions warranting approval of the actual expense method, as set forth in the regulations referenced in subparagraphs (a)(2)(i), (ii), or (iii) of this subsection, must exist.

(ii) A written justification for use of the higher amounts must be approved by an officer of the contractor's organization or designee to ensure that the authority is properly administered and controlled to prevent abuse.

(iii) If it becomes necessary to exercise the authority to use the higher actual expense method repetitively or on a continuing basis in a particular area, the contractor must obtain advance approval from the contracting officer.

(iv) Documentation to support actual costs incurred shall be in accordance with the contractor's established practices, subject to subparagraph (a)(7) of this subsection, and provided that a receipt is required for each expenditure of \$75.00 or more. The approved justification required by subparagraph (a)(3)(ii) and, if applicable, subparagraph (a)(3)(iii) of this subsection must be retained.

(4) Subparagraphs (a)(2) and (a)(3) of this subsection do not incorporate the regulations cited in subdivisions (a)(2)(i), (ii), and (iii) of this subsection in their entirety. Only the maximum per diem rates, the definitions of lodging, meals, and

incidental expenses, and the regulatory coverage dealing with special or unusual situations are incorporated herein.

(5) An advance agreement with respect to compliance with subparagraphs (a)(2) and (a)(3) of this subsection may be useful and desirable.

(6) The maximum per diem rates referenced in subparagraph (a)(2) of this subsection generally would not constitute a reasonable daily charge

(i) When no lodging costs are incurred; and/or

(ii) On partial travel days (*e.g.*, day of departure and return). Appropriate downward adjustments from the maximum per diem rates would normally be required under these circumstances. While these adjustments need not be calculated in accordance with the applicable Federal Travel Regulations, they must result in a reasonable charge.

(7) Costs shall be allowable only if the following information is documented

(i) Date and place (city, town, or other similar designation) of the expenses;

(ii) Purpose of the trip; and

(iii) Name of person on trip and that person's title or relationship to the contractor.

(b) Travel costs incurred in the normal course of overall administration of the business are allowable and shall be treated as indirect costs.

(c) Travel costs directly attributable to specific contract performance are allowable and may be charged to the contract.

(d) Airfare costs in excess of the lowest-priced airfare available to the contractor during normal business hours are unallowable except when the lowest priced airfare require circuitous routing, require travel during unreasonable hours, excessively prolong travel, result in increased cost that would offset transportation savings, are not reasonably adequate for the physical or medical needs of the traveler, or are not reasonably available to meet mission requirements. However, in order for airfare costs in excess of the above airfare to be allowable, the applicable condition(s) set forth above must be documented and justified.

(e)

(1) "Cost of travel by contractor-owned, -leased, or -chartered aircraft," as used in this paragraph, includes the cost of lease, charter, operation (including personnel), maintenance, depreciation,

insurance, and other related costs.

(2) The costs of travel by contractor-owned, -leased, or -chartered aircraft are limited to the standard airfare described in subparagraph (d) of this subsection for the flight destination unless travel by such aircraft is specifically required by contract specification, term, or condition, or a higher amount is approved by the contracting officer. A higher amount may be agreed to when one or more of the circumstances for justifying higher than standard airfare listed in subparagraph (d) of this subsection are applicable, or when an advance agreement under subparagraph (e)(3) of this subsection has been executed. In all cases, travel by contractor-owned, -leased, or -chartered aircraft must be fully documented and justified. For each contractor-owned, -leased, or -chartered aircraft used for any business purpose which is charged or allocated, directly or indirectly, to a Government contract, the contractor must maintain and make available manifest/logs for all flights on such company aircraft. As a minimum, the manifest/log shall indicate

- (i) Date, time, and points of departure; (ii) Destination, date, and time of arrival;
- (iii) Name of each passenger and relationship to the contractor; (iv) Authorization for trip; and
- (v) Purpose of trip.

(3) Where an advance agreement is proposed, consideration may be given to the following:

- (i) Whether scheduled commercial airlines or other suitable, less costly, travel facilities are available at reasonable times, with reasonable frequency, and serve the required destinations conveniently.
- (ii) Whether increased flexibility in scheduling results in time savings and more effective use of personnel that would outweigh additional travel costs.

(f) Costs of contractor-owned or -leased automobiles, as used in this subparagraph, include the costs of lease, operation (including personnel), maintenance, depreciation, insurance, etc. These costs are allowable, if reasonable, to the extent that the automobiles are used for company business. That portion of the cost of company-furnished automobiles that relates to personal use

by employees (including transportation to and from work) is compensation for personal services and is unallowable as stated in Cost (4)(m)(2).

#### ***(44) Costs Related to Legal and Other Proceedings.***

##### ***(a) Definitions***

(1) "Conviction," as used in this subsection, is defined in T3.2.2.7, A.2.e.

(2) "Costs" include, but are not limited to, administrative and clerical expenses; the costs of legal services, whether performed by in-house or private counsel; the costs of the services of accountants, consultants, or others retained by the contractor to assist it; costs of employees, officers, and directors; and any similar costs incurred before, during, and after commencement of a judicial or administrative proceeding which bears a direct relationship to the proceeding.

(3) "Fraud," as used in this subsection, means

- (i) Acts of fraud or corruption or attempts to defraud the Government or to corrupt its agents,
- (ii) Acts which constitute a cause for debarment or suspension under Procurement Guidance Section T3.2.2.7 and
- (iii) Acts which violate the False Claims Act, 31 U.S.C., sections 3729-3731, or the Anti-Kickback Act, 41 U.S.C., ~~sections 51 and 54~~ [§ 8702](#).

(4) "Penalty," does not include restitution, reimbursement, or compensatory damages.

(5) "Proceeding," includes an investigation.

(b) Costs incurred in connection with any proceeding brought by a Federal, State, local, or foreign government for violation of, or a failure to comply with, law or regulation by the contractor (including its agents or employees), or costs incurred in connection with any proceeding brought by a third party in the name of the United States under the False Claims Act, 31 U.S.C. 3730, are unallowable if the result is

(1) In a criminal proceeding, a conviction;

(2) In a civil or administrative proceeding, either a finding of contractor liability where the proceeding involves an allegation of fraud or similar misconduct or imposition of a monetary penalty where the proceeding does not involve an allegation of fraud or similar misconduct;

(3) A final decision by an appropriate official of an executive agency to

- (i) Debar or suspend the contractor; (ii) Rescind

or void a contract; or

- (iii) Terminate a contract for default by reason of a violation or failure to comply with a law or regulation.

(4) Disposition of the matter by consent or compromise if the proceeding could have led to any of the outcomes listed in subparagraphs (b)(1) through (3) of this subsection (but see subparagraphs (c) and (d) of this subsection); or

(5) Not covered by subparagraphs (b)(1) through (4) of this subsection, but where the underlying alleged contractor misconduct was the same as that which led to a different proceeding whose costs are unallowable by reason of subparagraphs (b)(1) through (4) of this subsection.

(c)

(1) To the extent they are not otherwise unallowable, costs incurred in connection with any proceeding under subparagraph (b) of this subsection commenced by the United States that is resolved by consent or compromise pursuant to an agreement entered into between the contractor and the United States, and which are unallowable solely because of subparagraph (b) of this subsection, may be allowed to the extent specifically provided in such agreement

(2) In the event of a settlement of any proceeding brought by a third party under the False Claims Act in which the United States did not intervene, reasonable costs incurred by the contractor in connection with such a proceeding, that are not otherwise unallowable by regulation or by separate agreement with the United States, may be allowed if the contracting officer, in consultation with his or her legal advisor, determines that there was very little likelihood that the third party would have been successful on the merits.

(d) To the extent that they are not otherwise unallowable, costs incurred in connection with any proceeding under paragraph (b) of this subsection commenced by a State, local, or foreign government may be allowable when the contracting officer (or other official specified in agency procedures) determines, that the costs were incurred either:

(1) As a direct result of a specific term or condition of a Federal contract; or

(2) As a result of compliance with specific written direction of the cognizant contracting officer.

(e) Costs incurred in connection with proceedings described in subparagraph (b) of this subsection, but which are not made unallowable by that subparagraph, may be allowable to the extent that:

(1) The costs are reasonable in relation to the activities required to deal with the proceeding and the underlying cause of action;

(2) The costs are not otherwise recovered from the Federal Government or a third party, either directly as a result of the proceeding or otherwise; and

(3) The percentage of costs allowed does not exceed the percentage determined to be appropriate considering the complexity of procurement litigation, generally accepted principles governing the award of legal fees in civil actions involving the United States as a party, and such other factors as may be appropriate. Such percentage shall not exceed 80 percent. Agreements reached under subparagraph (c) of this subsection shall be subject to this limitation. If, however, an agreement described in subparagraph (c)(1) of this subsection explicitly states the amount of otherwise allowable incurred legal fees and limits the allowable recovery to 80 percent or less of the stated legal fees, no additional limitation need be applied. The amount of reimbursement allowed for legal costs in connection with any proceeding described in subparagraph (c)(2) of this subsection shall be determined by the cognizant contracting officer, but shall not exceed 80 percent of otherwise allowable legal costs incurred.

(f) Costs not covered elsewhere in this subsection are unallowable if incurred in connection with: (1) Defense against

Federal Government claims or appeals or the prosecution of claims or appeals against the Federal Government.

(2) Organization, reorganization, (including mergers and acquisitions) or resisting mergers and acquisitions [see also Cost (24)].

(3) Defense of antitrust suits.

(4) Defense of suits brought by employees or ex-employees of the contractor under section 2 of the Major Fraud Act of 1988 where the contractor was found liable or settled.

(5) Costs of legal, accounting, and consultant services and directly associated costs incurred in connection with the defense or prosecution of lawsuits or appeals between contractors arising from either

- (i) An agreement or contract concerning a teaming arrangement, a joint venture, or similar arrangement of shared interest; or
- (ii) Dual sourcing, coproduction, or similar programs, are unallowable, except when

(A) Incurred as a result of compliance with specific terms and conditions of the contract or written instructions from the contracting officer, or

(B) When agreed to in writing by the contracting officer.

(6) Patent infringement litigation, unless otherwise provided for in the contract. (7) Representation of,

or assistance to, individuals, groups, or legal entities which the contractor is not legally bound to provide, arising from an action where the participant was convicted of violation of a law or regulation or was found liable in a civil or administrative proceeding.

(8) Protests of Federal Government solicitations or contract awards, or the defense against protests of such solicitations or contract awards, unless the costs of defending against a protest are incurred pursuant to a written request from the cognizant contracting officer.

(g) Costs which may be unallowable under Cost (44), including directly associated costs, shall be segregated and accounted for by the contractor separately. During the pendency of any proceeding covered by subparagraph (b) and subparagraphs (f)(4) and (f)(7) of this subsection, the contracting officer shall generally withhold payment of such costs. However, if in the best interests of the Government, the contracting officer may provide for conditional payment upon provision of adequate security, or other adequate assurance, and agreement by the contractor to repay all unallowable costs, plus interest, if the costs are subsequently determined to be unallowable.

**(45) *Research and Development Costs.*** "Research and development," as used in this subsection, means the type of technical effort which is described in Cost (15) but sponsored by a grant or required in performance of a contract . When costs are incurred in excess of either the price of a contract or amount of a grant for research and development effort, the excess is unallowable under any other Government contract.

**(46) *Goodwill.***

Goodwill, an unidentifiable intangible asset, originates under the purchase method of accounting for a business combination when the price paid by the acquiring company exceeds the sum of the identifiable individual assets acquired less liabilities assumed, based upon their fair values. The excess is commonly referred to as goodwill. Goodwill may arise from the acquisition of a company as a whole or a portion thereof. Any costs for amortization, expensing, write-off, or write-down of goodwill (however represented) are unallowable.

**(47) *Costs of Alcoholic Beverages.*** Costs of alcoholic beverages are unallowable.

**(48) *Asset Valuations Resulting from Business Combinations.***

(a) For tangible capital assets, when the purchase method of accounting for a business combination is used, whether or not the contract or subcontract is subject to CAS, the allowable depreciation and cost of money shall be based on the capitalized asset values measured and assigned in accordance with 48 CFR 9904.404-50(d), if allocable, reasonable, and not otherwise unallowable.

(b) For intangible capital assets, when the purchase method of accounting for a business combination is used,

allowable amortization and cost of money shall be limited to the total of the amounts that would have been allowed had the combination not taken place.

## Revised: T3.6.2 - Labor Laws > 9 Service Contracts/Service Contract

### 9 Service Contracts/Service Contract Act Revised 7/2007

a. *General.* The Service Contract Act of 1965; (41 U.S.C. ~~351, §§-et seq.~~ 6701-6707), selected provisions of the Fair Labor Standards Act of 1938, as amended (29 U.S.C. § 201; et seq.), and related Department of Labor regulations (29 CFR ~~P~~parts 4, 6, 8, 541, and 1925) apply to service contracts.

b. *Service Contract Act.* The Service Contract Act (SCA) applies to contracts if the principal purpose is to furnish services in the U.S. through the use of service employees, unless exempted. Service contracts over \$2,500 must contain mandatory provisions regarding minimum wages and fringe benefits, safe and sanitary working conditions, notification to employees of the minimum allowed compensation, and a statement of equivalent Federal employee classifications and wage rates. Additionally, the SCA limits the term of service contracts to 5 years (41 U.S.C. ~~§353.~~ 6707(d)).

c. *Exemptions from SCA.* The SCA does not apply to: (1) Contracts

performed outside of the U.S.; (2) Contracts less ~~thatt~~than \$2,500;

(3) Construction, alteration, or repair of public buildings or public works, including painting and decorating;

(4) Dismantling, demolition or removal of improvements when part of a construction contract;

(5) Work performed by a regular dealer or manufacturer (in accordance with the Walsh-Healey Public Contracts Act). Service contracts for remanufacturing of equipment may be subject to Walsh-Healey Public Contracts Act, rather than the SCA, if the work is so extensive as to be equivalent to manufacturing. Remanufacturing is considered to be major overhaul or modification of equipment, material, or an item which involves: (a) complete or substantial teardown to the component level; (b) substantially all of the parts are reworked and/or replaced, or outmoded parts are replaced; (c) the equipment is reassembled; and (d) the work is performed at a facility operated by the contractor. Remanufacturing does not include repair of damaged equipment or routine maintenance unless there is complete teardown, rework, and reassembly;

(6) Transporting freight or personnel by vessel, aircraft, bus, truck, express, railroad, or oil or gas pipeline where published tariff rates are in effect;

(7) Contracts for furnishing of services by radio, telephone, telegraph, or cable companies subject to the Communications Act of 1934;

(8) Public utility services;

(9) Employment contracts with an individual(s) (rather than a firm with multiple employees);

(10) Contracts with common carriers for the carriage of mail by rail, air (except air star routes), bus, and ocean vessel, where such carriage is performed on regularly-scheduled runs of the trains, airplanes, buses, and vessels over regularly established routes and accounts for a substantial portion of the carrier's revenues;

(11) Carriage of freight or personnel if subject to regulated rates in section 10721 of the Interstate Commerce Act;

(12) Contracts principally for maintenance, calibration, or repair of automated data processing equipment, office information/word processing systems, scientific and medical equipment, and office/business equipment (if services are performed by the manufacturer or supplier of the equipment), subject to the following: (a) the equipment is commercially available; (b) the price of services is based on established catalog or market prices; (c) employees used for Government contracts and commercial contracts are under the same overall compensation plan; and (d) the contractor certifies in the contract to the aforementioned conditions; or

(13) *Employees* who are bona fide executive, administrative or professional employees (as defined and implemented in 29 CFR 541). Some support service contracts involve professional employees who may be exempt from SCA requirements. Professionals are those employees having recognizable status based on acquiring professional knowledge through prolonged study, such as accountancy, actuarial computation, architecture, dentistry, engineering, law, medicine, nursing, pharmacy, the sciences (such as biology, chemistry, physics, and teaching). To be a professional employee, a person must be involved essentially in discharging professional duties and exercising judgment.

d. *Examples of Contracts Covered by SCA*

The following examples, while not definitive or exclusive, illustrate some of the types of services that have been found to be covered by the SCA (see 29 CFR 4.130 for additional examples):

(1) Motor pool operation, parking, taxicab, and ambulance services; (2) Packing, crating, and storage;

(3) Custodial, janitorial, housekeeping, and guard services; (4) Food service and lodging;

(5) Snow, trash, and garbage removal;

(6) Some support services at Government installations, including grounds maintenance and landscaping;

(9) Certain specialized services requiring specific skills, such as drafting, illustrating, graphic arts, stenographic reporting, or mortuary services;

(10) Electronic equipment maintenance and operation and engineering support services;

(11) Maintenance and repair of all types of equipment, for example, aircraft, engines, electrical motors, vehicles, and electronic, telecommunication, office and related business and construction equipment;

(12) Operation, maintenance, or logistics support of a Government facility; (13) Data collection, processing and analysis services;

e. *Determining SCA Applicability.* Prior to issuing a screening information request, the CO should determine SCA applicability to the particular acquisition and anticipated categories of contractor employees. If the SCA applies to any anticipated categories of employees, the CO will request a wage determination from DOL.

## **Revised: T3.6.4 Foreign Acquisition > 1 Applicability of Buy**

### **1 Applicability of Buy American** Added 10/2012

- a. FAA-specific Buy American provisions (49 U.S.C. §50101) apply when acquiring steel or manufactured products, as described in Section 4 below. In many instances, the Buy American Act (41 U.S.C. §~~40a~~ [8301-8305](#)) requirements for supplies and construction will only apply when acquiring raw and unmanufactured materials.
- b. Canadian and Mexican steel and manufactured products under certain conditions, and civil aircraft and related supplies of countries that are parties to the Agreement on Civil Aircraft, are treated as domestic for purposes of FAA Buy American and the Buy American Act. See Section 7 Trade Agreements below.