

ENTERGY GULF STATES, INC.  
PUBLIC UTILITY COMMISSION OF TEXAS  
Docket No. 22356

Response of: Entergy Gulf States, Inc.  
to the Fifty Eighth Set of Data Requests  
of Requesting Party: Cities

Prepared By: Mark Young  
Sponsoring Witness: Robert Hahne  
Beginning Sequence No.  
Ending Sequence No.

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Question No.: CITIES 58 -5

Part No.:

Addendum:

Question:

Refer to Hahne rebuttal at RLH-1R. Identify the organization, legal status of, incorporation, affiliation of the Cost Accounting Standards Board (CASB). Make available a complete copy of the published standards of the organization.

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Response:

The Company objects to responding to this question, however, the Company will provide an answer to this question notwithstanding its objections and without waiving its rights.

The Cost Accounting Standards Board (CASB or Board) is an independent board within the Office of Management and Budget's Office of Federal Procurement Policy. The Board has exclusive statutory authority to make, promulgate, amend and rescind cost accounting standards.

The Cost Accounting Standards (CAS) were designed to achieve uniformity and consistency in the measurement, assignment, and allocation of costs to Government contracts. The basic principles set forth in the CAS, related to the measurement, assignment and allocation of costs, are applicable regardless of the entity whose costs are under consideration.

Excerpts from the CAS relied upon by Mr. Hahne in the development of his testimony were provided in Exhibit RLH-1R. Complete copies of the CAS referred to in Mr. Hahne's Exhibit RLH-1R are attached for your reference.

A complete copy of the CASB Standards and Regulations are printed in Title 48 of the Code of Federal Regulations, Chapter 99, and may be obtained by writing the Superintendent of Documents, U.S. Government Printing Office, Washington, DC 20402, or by calling the Washington, DC, ordering desk at area code (202) 783-3238.

9904.403 Allocation of home office expenses to segments.

9904.403-10 [Reserved]

Sec. 9904.403-20 Purpose.

(a) The purpose of this Cost Accounting Standard is to establish criteria for allocation of the expenses of a home office to the segments of the organization based on the beneficial or causal relationship between such expenses and the receiving segments. It provides for:

(1) Identification of expenses for direct allocation to segments to the maximum extent practical;

(2) Accumulation of significant nondirectly allocated expenses into logical and relatively homogeneous pools to be allocated on bases reflecting the relationship of the expenses to the segments concerned; and

(3) Allocation of any remaining or residual home office expenses to all segments.

Appropriate implementation of this Standard will limit the amount of home office expenses classified as residual to the expenses of managing the organization as a whole.

(b) This Standard does not cover the reallocation of a segment's share of home office expenses to contracts and other cost objectives.

Sec. 9904.403-30 Definitions.

(a) The following are definitions of terms which are prominent in this Standard. Other terms defined elsewhere in this part 99 shall have the meanings ascribed to them in those definitions unless paragraph (b) of this subsection, requires otherwise.

(1) Allocate means to assign an item of cost, or a group of items of cost, to one or more cost objectives. This term includes both direct assignments of cost and the reassignment of a share from an indirect cost pool.

(2) Home office means an office responsible for directing or managing two or more, but not necessarily all, segments of an organization. It typically establishes policy for, and provides guidance to the segments in their operations. It usually performs management, supervisory, or administrative functions, and may also perform service functions in support of the operations of the various segments. An organization which has intermediate levels, such as groups, may have several home offices which report to a common home office. An intermediate organization may be both a segment and a home office.

(3) Operating revenue means amounts accrued or charge to customers, clients, and tenants, for the sale of products manufactured or purchased for resale, for services, and for rentals of property held primarily for leasing to others. It includes both reimbursable costs and fees under cost-type contracts and percentage-of-completion sales accruals except that it includes only the fee for management contracts under which the contractor acts essentially as an agent of the Government in the erection or operation of Government-owned facilities. It excludes incidental interest, dividends, royalty, and rental income, and proceeds from the sale of assets used in the business.

(4) Segment means one of two or more divisions, product departments, plants, or other subdivisions of an organization reporting directly to a home office, usually identified with responsibility for profit and/or producing a product or service. The term includes Government-owned contractor-operated (GOCO) facilities, and joint ventures and subsidiaries (domestic and foreign) in which the organization has a majority ownership. The term also includes those joint ventures and subsidiaries (domestic and foreign) in which the organization has less than a majority of ownership, but over which it exercises control.

(5) Tangible capital asset means an asset that has physical substance, more than minimal value, and is expected to be held by an

enterprise for continued use or possession beyond the current accounting period for the services it yields.

(b) The following modifications of terms defined elsewhere in this Chapter 99 are applicable to this Standard: None.

Sec. 9904.403-40 Fundamental requirement.

(a)(1) Home office expenses shall be allocated on the basis of the beneficial

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or causal relationship between supporting and receiving activities. Such expenses shall be allocated directly to segments to the maximum extent practical. Expenses not directly allocated, if significant in amount and in relation to total home office expenses, shall be grouped in logical and homogeneous expense pools and allocated pursuant to paragraph (b) of this subsection. Such allocations shall minimize to the extent practical the amount of expenses which may be categorized as residual (those of managing the organization as a whole). These residual expenses shall be allocated pursuant to paragraph (c) of this subsection.

(2) No segment shall have allocated to it as an indirect cost, either through a homogeneous expense pool, or the residual expense pool, any cost, if other costs incurred for the same purpose have been allocated directly to that or any other segment.

(b) The following subparagraphs provide criteria for allocation of groups of home office expenses.

(1) Centralized service functions. Expenses of centralized service functions performed by a home office for its segments shall be allocated to segments on the basis of the service furnished to or received by each segment. Centralized service functions performed by a home office for its segments are considered to consist of specific functions which, but for the existence of a home office, would be performed or acquired by some or all of the segments individually. Examples include centrally performed personnel administration and centralized data processing.

(2) Staff management of certain specific activities of segments. The expenses incurred by a home office for staff management or policy guidance functions which are significant in amount and in relation to total home office expenses shall be allocated to segments receiving more than a minimal benefit over a base, or bases, representative of the total specific activity being managed. Staff management or policy guidance to segments is commonly provided in the overall direction or support of the performance of discrete segment activities such as manufacturing, accounting, and engineering (but see paragraph (b)(6) of this subsection).

(3) Line management of particular segments or groups of segments. The expense of line management shall be allocated only to the particular segment or group of segments which are being managed or supervised. If more than one segment is managed or supervised, the expense shall be allocated using a base or bases representative of the total activity of such segments. Line management is considered to consist of management or supervision of a segment or group of segments as a whole.

(4) Central payments or accruals. Central payments or accruals which are made by a home office on behalf of its segments shall be allocated directly to segments to the extent that all such payments or accruals of a given type or class can be identified specifically with individual segments. Central payments or accruals are those which but for the existence of a number of segments would be accrued or paid by the individual segments. Common examples include centrally paid or accrued pension costs, group insurance costs, State and local income taxes and franchise taxes, and payrolls paid by a home office on behalf of its segments. Any such types of payments or accruals which cannot be identified specifically with individual segments shall be allocated to benefitted segments using an allocation base representative of the

factors on which the total payment is based.

(5) Independent research and development costs and bid and proposal costs. Independent research and development costs and bid and proposal costs of a home office shall be allocated in accordance with 9904.420.

(6) Staff management not identifiable with any certain specific activities of segments. The expenses incurred by a home office for staff management, supervisory, or policy functions, which are not identifiable to specific activities of segments shall be allocated in accordance with paragraph (c) of this subsection as residual expenses.

(c) Residual expenses. (1) All home office expenses which are not allocable in accordance with paragraph (a) of this subsection and paragraphs (b)(1) through (b)(5) of this subsection shall be deemed residual expenses. Typical residual expenses are those for the

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chief executive, the chief financial officer, and any staff which are not identifiable with specific activities of segments. Residual expenses shall be allocated to all segments under a home office by means of a base representative of the total activity of such segments, except where paragraph (c) (2) or (3) of this subsection applies.

(2) Residual expenses shall be allocated pursuant to 9904.403-50(c)(1) if the total amount of such expenses for the contractor's previous fiscal year (excluding any unallowable costs and before eliminating any amounts to be allocated in accordance with paragraph (c)(3) of this subsection) exceeds the amount obtained by applying the following percentage(s) to the aggregate operating revenue of all segments for such previous year: 3.35 percent of the first \$100 million; 0.95 percent of the next \$200 million; 0.30 percent of the next \$2.7 billion; 0.20 percent of all amounts over \$3 billion. The determination required by this paragraph for the 1st year the contractor is subject to this Standard shall be based on the pro forma application of this Standard to the home office expenses and aggregate operating revenue for the contractor's previous fiscal year.

(3) Where a particular segment receives significantly more or less benefit from residual expenses than would be reflected by the allocation of such expenses pursuant to paragraph (c) (1) or (2) of this subsection (see 9904.403-50(d)), the Government and the contractor may agree to a special allocation of residual expenses to such segment commensurate with the benefits received. The amount of a special allocation to any segment made pursuant to such an agreement shall be excluded from the pool of residual expenses to be allocated pursuant to paragraph (c) (1) or (2) of this subsection, and such segment's data shall be excluded from the base used to allocate this pool.

#### Sec. 9904.403-50 Techniques for application.

(a)(1) Separate expense groupings will ordinarily be required to implement 9904.403-40. The number of groupings will depend primarily on the variety and significance of service and management functions performed by a particular home office. Ordinarily, each service or management function will have to be separately identified for allocation by means of an appropriate allocation technique. However, it is not necessary to identify and allocate different functions separately, if allocation in accordance with the relevant requirements of 9904.403-40(b) can be made using a common allocation base. For example, if the personnel department of a home office provides personnel services for some or all of the segments (a centralized service function) and also established personnel policies for the same segments (a staff management function), the expenses of both functions could be allocated over the same base, such as the number of personnel, and the separate functions do not have to be identified.

(2) Where the expense of a given function is to be allocated by means of a particular allocation base, all segments shall be included in

the base unless:

(i) Any excluded segment did not receive significant benefits from, or contribute significantly to the cause of the expense to be allocated and,

(ii) Any included segment did receive significant benefits from or contribute significantly to the cause of the expense in question.

(b)(1) Section 9904.403-60 illustrates various expense pools which may be used together with appropriate allocation bases. The allocation of centralized service functions shall be governed by a hierarchy of preferable allocation techniques which represent beneficial or causal relationships. The preferred representation of such relationships is a measure of the activity of the organization performing the function. Supporting functions are usually labor-oriented, machine-oriented, or space-oriented. Measures of the activities of such functions ordinarily can be expressed in terms of labor hours, machine hours, or square footage. Accordingly, costs of these functions shall be allocated by use of a rate, such as a rate per labor hour, rate per machine hour or cost per square foot, unless such measures are unavailable or impractical to ascertain. In these latter cases the basis for allocation shall be a

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measurement of the output of the supporting function. Output is measured in terms of units of end product produced by the supporting function, as for example, number of printed pages for a print shop, number of purchase orders processed by a purchasing department, number of hires by an employment office.

(2) Where neither activity nor output of the supporting function can be practically measured, a surrogate for the beneficial, or causal relationship must be selected. Surrogates used to represent the relationship are generally measures of the activity of the segments receiving the service; for example, for personnel services reasonable surrogates would be number of personnel, labor hours, or labor dollars of the segments receiving the service. Any surrogate used should be a reasonable measure of the services received and, logically, should vary in proportion to the services received.

(c)(1) Where residual expenses are required to be allocated pursuant to 9904.403-40(c)(2), the three factor formula described below must be used. This formula is considered to result in appropriate allocations of the residual expenses of home offices. It takes into account three broad areas of management concern: The employees of the organization, the business volume, and the capital invested in the organization. The percentage of the residual expenses to be allocated to any segment pursuant to the three factor formula is the arithmetical average of the following three percentages for the same period.

(i) The percentage of the segment's payroll dollars to the total payroll dollars of all segments.

(ii) The percentage of the segment's operating revenue to the total operating revenue of all segments. For this purpose, the operating revenue of any segment shall include amounts charged to other segments and shall be reduced by amounts charged by other segments for purchases.

(iii) The percentage of the average net book value of the sum of the segment's tangible capital assets plus inventories to the total average net book value of such assets of all segments. Property held primarily for leasing to others shall be excluded from the computation. The average net book value shall be the average of the net book value at the beginning of the organization's fiscal year and the net book value at the end of the year.

(d) The following paragraphs provide guidance for implementing the requirements of 9904.403-40(c)(3).

(1) An indication that a segment received significantly less benefit in relation to other segments can arise if a segment, unlike all or most other segments, performs on its own many of the functions included in the residual expense. Another indication may be that, in relation to its

size, comparatively little or no costs are allocable to a segment pursuant to 9904.403-40(b) (1) through (5). Evidence of comparatively little communication or interpersonal relations between a home office and a segment, in relation to its size, may also indicate that the segment receives significantly less benefit from residual expenses. Conversely, if the opposite conditions prevail at any segment, a greater allocation than would result from the application of 9904.403-40(c) (1) or (2) may be indicated. This may be the case, for example, if a segment relies heavily on the home office for certain residual functions normally performed by other segments on their own.

(2) Segments which may require special allocations of residual expenses pursuant to 9904.403-40(c) (3) include, but are not limited to foreign subsidiaries, GOCO's, domestic subsidiaries with less than a majority ownership, and joint ventures.

(3) The portion of residual expenses to be allocated to a segment pursuant to 9904.403-40(c) (3) shall be the cost of estimated or recorded efforts devoted to the segments.

(e) Home office functions may be performed by an organization which for some purposes may not be a part of the legal entity with which the Government has contracted. This situation may arise, for example, in instances where the Government contracts directly with a corporation which is wholly or partly owned by another corporation. In this case, the latter corporation serves as a "home office," and

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the corporation with which the contract is made is a "segment" as those terms are defined and used in this Standard. For purposes of contracts subject to this Standard, the contracting corporation may only accept allocations from the other corporation to the extent that such allocations meet the requirements set forth in this Standard for allocation of home office expenses to segments.

#### Sec. 9904.403-60 Illustrations.

(a) The following table lists some typical pools, together with illustrative allocation bases, which could be used in appropriate circumstances:

Home office expense or function	Illustrative allocation bases
Centralized service functions:	
1. Personnel administration.....	1. Number of personnel, labor hours, payroll, number of hires.
2. Data processing services.....	2. Machine time, number of reports.
3. Centralized purchasing and subcontracting.	3. Number of purchase orders, value of purchases, number of items.
4. Centralized warehousing.....	4. Square footage, value of material, volume.
5. Company aircraft service.....	5. Actual or standard rate per hour, mile, passenger mile, or similar unit.
6. Central telephone service.....	6. Usage costs, number of instruments.

(b) The selection of a base for allocating centralized service functions shall be governed by the criteria established in 9904.403-50(b).

(c) The listed allocation bases in this section are illustrative.

Other bases for allocation of home office expenses to segments may be used if they are substantially in accordance with the beneficial or casual relationships outlined in 9904.403-40.

Home office expenses or function	Illustrative allocation bases
Staff management or specific activities:	
1. Personnel management.....	1. Number of personnel, labor hours, payroll, number of hires.
2. Manufacturing policies, (quality control, industrial engineering, production, scheduling, tooling, inspection and testing, etc.	2. Manufacturing cost input, manufacturing direct labor.
3. Engineering policies.....	3. Total engineering costs, engineering direct labor, number of drawings.
4. Material/purchasing policies....	4. Number of purchase orders, value of purchases.
5. Marketing policies.....	5. Sales, segment marketing costs.
Central payments or accruals:	
1. Pension expenses.....	1. Payroll or other factor on which total payment is based.
2. Group insurance expenses.....	2. Payroll or other factor on which total payment is based.
3. State and local income taxes and franchise taxes.	3. Any base or method which results in an allocation that equals or approximates a segment's proportionate share of the tax imposed by the jurisdiction in which the segment does business, as measured by the same factors used to determine taxable income for that jurisdiction.

#### Sec. 9904.403-61 Interpretation.

(a) Questions have arisen as to the requirements of 9904.403, Cost Accounting Standard, Allocation of Home Office Expenses to Segments, for the purpose of allocating State and local income taxes and franchise taxes based on income (hereinafter collectively referred to as income taxes) from a home office of an organization to its segments.

(b) By means of an illustrative allocation base in 9904.403-60, the Standard provides that income taxes are to be allocated by "any base or method which results in an allocation that equals or approximates a segment's proportionate share of the tax imposed by the jurisdiction in which the segment does business, as measured by the same factors used to determine taxable income for that jurisdiction." This provision contains two essential criteria for the allocation of income taxes from a home office to segments. First, the taxes of any particular jurisdiction are to be allocated only to those segments that do business in the taxing jurisdiction.

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Second, where there is more than one segment in a taxing jurisdiction, the taxes are to be allocated among those segments on the basis of "the same factors used to determine the taxable income for that jurisdiction." The questions that have arisen relate primarily to

whether segment book income or loss is a ``factor'' for this purpose.

(c) Most States tax a fraction of total organization income, rather than the book income of segments that do business within the State. The fraction is calculated pursuant to a formula prescribed by State statute. In these situations the book income or loss of individual segments is not a factor used to determine taxable income for that jurisdiction. Accordingly, in States that tax a fraction of total organization income, rather than the book income of segments within the State, such book income is irrelevant for tax allocation purposes. Therefore, segment book income is to be used as a factor in allocating income tax expense from a home office to segments only where this amount is expressly used by the taxing jurisdiction in computing the income tax.

9904.403-62 Exemption. [Reserved]

Sec. 9904.403-63 Effective date.

This Standard is effective as of April 17, 1992. Contractors with prior CAS-covered contracts with full coverage shall continue this Standard's applicability upon receipt of a contract to which this Standard is applicable. For contractors with no previous contracts subject to this Standard, this Standard shall be applied beginning with the contractor's next full fiscal year beginning after the receipt of a contract to which this Standard is applicable.

9904.404 Capitalization of tangible assets.

9904.404-10 [Reserved]

Sec. 9904.404.20 Purpose.

This Standard requires that, for purposes of cost measurement, contractors establish and adhere to policies with respect to capitalization of tangible assets which satisfy criteria set forth herein. Normally, cost measurements are based on the concept of enterprise continuity; this concept implies that major asset acquisitions will be capitalized, so that the cost applicable to current and future accounting periods can be allocated to cost objectives of those periods. A capitalization policy in accordance with this Standard will facilitate measurement of costs consistently over time.

Sec. 9904.404-30 Definitions.

(a) The following are definitions of terms which are prominent in this standard. Other terms defined elsewhere in this part 99 shall have the meanings ascribed to them in those definitions unless paragraph (b) of this subsection, requires otherwise.

(1) Asset accountability unit means a tangible capital asset which is a component of plant and equipment that is capitalized when acquired or whose replacement is capitalized when the unit is removed, transferred, sold, abandoned, demolished, or otherwise disposed of.

(2) Original complement of low cost equipment means a group of items acquired for the initial outfitting of a tangible capital asset or an operational unit, or a new addition to either. The items in the group individually cost less than the minimum amount established by the contractor for capitalization for the classes of assets acquired but in the aggregate they represent a material investment. The group, as a complement, is expected to be held for continued service beyond the current period. Initial outfitting of the unit is completed when the unit is ready and available for normal operations.

(3) Repairs and maintenance generally means the total endeavor to obtain the expected service during the life of tangible capital assets. Maintenance is the regularly recurring activity of keeping assets in normal or expected operating condition while repair is the activity of putting them back into such condition.

(4) Tangible capital asset means an asset that has physical



records are retained for 3 years after disposition of an asset in groups by year of disposition. An analysis of these retirements may be made by selecting the larger dollar items for each category of assets for which lives are to be determined (for example, at least 75 percent of the acquisition values retired each year). The cases cited above are only examples and many other examples could have been used. Also, in any example, a company's individual circumstances must be considered in order to take into account possible biased results because of changes in organizations, products, acquisition policies, economic factors, etc. The results from example (g)(5) of this subsection, for instance, might be substantially distorted if the 3-year period was unusual with respect to dispositions. Therefore, the examples are illustrative only and any sampling performed in compliance with this Standard should take into account all relevant information to ensure that reasonable results are obtained.

9904.409-61 Interpretation. [Reserved]

Sec. 9904.409-62 Exemption.

This Standard shall not apply where compensation for the use of tangible capital assets is based on use rates or allowances provided by other appropriate Federal acquisition regulations such as those governing:

- (a) Educational institutions,
  - (b) State, local, and Federally recognized Indian tribal government,
- or
- (c) Construction equipment rates (See 48 CFR 31.105(d)).

Sec. 9904.409-63 Effective date.

- (a) This Standard is effective April 15, 1996.
- (b) This Standard shall be applied beginning with the contractor's next full cost accounting period beginning after the receipt of a contract or subcontract to which this Standard is applicable.
- (c) Contractors with prior CAS-covered contracts with full coverage shall continue to follow Standard 9904.409 in effect prior to April 15, 1996, until this Standard, effective April 15, 1996, becomes applicable after the receipt of a contract or subcontract to which this revised Standard applies.

[61 FR 5523, Feb. 13, 1996]

9904.410 Allocation of business unit general and administrative expenses to final cost objectives.

9904.410-10 [Reserved]

Sec. 9904.410-20 Purpose.

The purpose of this Cost Accounting Standard is to provide criteria for the allocation of business unit general and administrative (G&A) expenses to business unit final cost objectives based on their beneficial or causal relationship. These expenses represent the cost of the management and administration of the business unit as a whole. The Standard also provides criteria for the allocation of home office expenses received by a segment to the cost objectives of that segment. This Standard will increase the likelihood of achieving objectivity in the allocation of expenses to final cost objectives and comparability of cost data among contractors in similar circumstances.

Sec. 9904.410-30 Definitions.

- (a) The following are definitions of terms which are prominent in this standard. Other terms defined elsewhere in this part 99 shall have the meanings ascribed to them in those

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definitions unless paragraph (b) of this section, requires otherwise.

(1) Allocate means to assign an item of cost or a group of items of cost, to one or more cost objectives. This term includes both direct assignment of cost and the reassignment of a share from an indirect cost pool.

(2) Business unit means any segment of an organization, or an entire business organization which is not divided into segments.

(3) Cost input means the cost, except G&A expenses, which for contract costing purposes is allocable to the production of goods and services during a cost accounting period.

(4) Cost objective means a function, organizational subdivision, contract or other work unit for which cost data are desired and for which provision is made to accumulate and measure the cost of processes, products, jobs, capitalized projects, etc.

(5) Final cost objective means a cost objective which has allocated to it both direct and indirect costs, and, in the contractor's accumulation systems, is one of the final accumulation points.

(6) General and administrative (G&A) expense means any management, financial, and other expense which is incurred by or allocated to a business unit and which is for the general management and administration of the business unit as a whole. G&A expense does not include those management expenses whose beneficial or causal relationship to cost objectives can be more directly measured by a base other than a cost input base representing the total activity of a business unit during a cost accounting period.

(7) Segment means one of two or more divisions, product departments, plants, or other subdivisions of an organization reporting directly to a home office, usually identified with responsibility for profit and/or producing a product or service. The terms include Government-owned contractor-operated (GOCO) facilities, and joint ventures and subsidiaries (domestic and foreign) in which the organization has a majority ownership. The term also includes those joint ventures and subsidiaries (domestic and foreign) in which the organization has less than a majority of ownership, but over which it exercises control.

(b) The following modifications of terms defined elsewhere in this chapter 99 are applicable to this Standard: None.

#### Sec. 9904.410-40 Fundamental requirement.

(a) Business unit G&A expenses shall be grouped in a separate indirect cost pool which shall be allocated only to final cost objectives.

(b) (1) The G&A expense pool of a business unit for a cost accounting period shall be allocated to final cost objectives of that cost accounting period by means of a cost input base representing the total activity of the business unit except as provided in subparagraph (b) (2) of this subsection. The cost input base selected shall be the one which best represents the total activity of a typical cost accounting period.

(2) The allocation of the G&A expense pool to any particular final cost objectives which receive benefits significantly different from the benefits accruing to other final cost objectives shall be determined by special allocation (9904.410-50(j)).

(c) Home office expenses received by a segment shall be allocated to segment cost objectives as required by 9904.410-50(g).

(d) Any costs which do not satisfy the definition of G&A expense but which have been classified by a business unit as G&A expenses, can remain in the G&A expense pool unless they can be allocated to business unit cost objectives on a beneficial or causal relationship which is best measured by a base other than a cost input base.

#### Sec. 9904.410-50 Techniques for application.

(a) G&A expenses of a segment incurred by another segment shall be removed from the incurring segment's G&A expense pool. They shall be allocated to the segment for which the expenses were incurred on the basis of the beneficial or causal relationship between the expenses incurred and all benefiting or causing segments. If the expenses are incurred for two or more segments, they shall be allocated using

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an allocation base common to all such segments.

(b) The G&A expense pool may be combined with other expenses for allocation to final cost objectives provided that--

(1) The allocation base used for the combined pool is appropriate both for the allocation of the G&A expense pool under this Standard and for the allocation of the other expenses; and

(2) Provision is made to identify the components and total of the G&A expense pool separately from the other expenses in the combined pool.

(c) Expenses which are not G&A expenses and are insignificant in amount may be included in the G&A expense pool for allocation to final cost objectives.

(d) The cost input base used to allocate the G&A expense pool shall include all significant elements of that cost input which represent the total activity of the business unit. The cost input base selected to represent the total activity of a business unit during a cost accounting period may be: Total cost input; value-added cost input; or single element cost input. The determination of which cost input base best represents the total activity of a business unit must be judged on the basis of the circumstances of each business unit.

(1) A total cost input base is generally acceptable as an appropriate measure of the total activity of a business unit.

(2) Value-added cost input shall be used as an allocation base where inclusion of material and subcontract costs would significantly distort the allocation of the G&A expense pool in relation to the benefits received, and where costs other than direct labor are significant measures of total activity. A value-added cost input base is total cost input less material and subcontract costs.

(3) A single element cost input base; e.g., direct labor hours or direct labor dollars, which represents the total activity of a business unit may be used to allocate the G&A expense pool where it produces equitable results. A single element base may not produce equitable results where other measures of activity are also significant in relation to total activity. A single element base is inappropriate where it is an insignificant part of the total cost of some of the final cost objectives.

(e) Where, prior to the effective date of this Standard, a business unit's disclosed or established cost accounting practice was to use a cost of sales or sales base, that business unit may use the transition method set out in appendix A hereof.

(f) Cost input shall include those expenses which by operation of this Standard are excluded from the G&A expense pool and are not part of a combined pool of G&A expenses and other expenses allocated using the same allocation base.

(g)(1) Allocations of the home office expenses of:

(i) Line management of particular segments or groups of segments,

(ii) Residual expenses, and

(iii) Directly allocated expenses related to the management and administration of the receiving segment as a whole, shall be included in the receiving segment's G&A expense pool.

(2) Any separate allocation of the expenses of home office centralized service functions, staff management of specific activities of segments, and central payments or accruals, which is received by a segment, shall be allocated to the segment cost objectives in proportion to the beneficial or causal relationship between the cost objectives and

the expense if such allocation is significant in amount. Where a beneficial or causal relationship for the expense is not identifiable with segment cost objectives, the expense may be included in the G&A expense pool.

(h) Where a segment performs home office functions and also performs as an operating segment having a responsibility for final cost objectives, the expense of the home office functions shall be segregated. These expenses shall be allocated to all benefiting or causing segments, including the segment performing the home office functions, pursuant to disclosed or established accounting practices for the allocation of home office expenses to segments.

(i) For purposes of allocating the G&A expense pool, items produced or worked on for stock or product inventory shall be accounted for as final cost

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objectives in accordance with the following paragraphs:

(1) Where items are produced or worked on for stock or product inventory in a given cost accounting period, the cost input to such items in that period shall be included only once in the computation of the G&A expense allocation base and in the computation of the G&A expense allocation rate for that period and shall not be included in the computation of the base or rate for any other cost accounting period.

(2) A portion of the G&A expense pool shall be allocated to items produced or worked on for stock or product inventory in the cost accounting period or periods in which such items are produced at the rates determined for such periods except as provided in subparagraph (i) (3) of this subsection.

(3) Where the contractor does not include G&A expense in inventory as part of the cost of stock or product inventory items, the G&A rate of the cost accounting period in which such items are issued to final cost objectives may be used to determine the G&A expenses applicable to issues of stock or product inventory items.

(j) Where a particular final cost objective in relation to other final cost objectives receives significantly more or less benefit from G&A expense than would be reflected by the allocation of such expenses using a base determined pursuant to paragraph (d) of this subsection, the business unit shall account for this particular final cost objective by a special allocation from the G&A expense pool to the particular final cost objective commensurate with the benefits received. The amount of a special allocation to any such final cost objective shall be excluded from the G&A expense pool required by 9904.410-40(a), and the particular final cost objective's cost input data shall be excluded from the base used to allocate this pool.

#### Sec. 9904.410-60 Illustrations.

(a) Business Unit A has been including the cost of scientific computer operations in its G&A expense pool. The scientific computer is used predominantly for research and development, rather than for the management and administration of the business unit as a whole. The costs of the scientific computer operation do not satisfy the Standard's definition of G&A expense; however, they may remain in the G&A expense pool unless they can be allocated to business unit cost objectives on a beneficial or causal relationship which is best measured by a base other than a cost input base representing the total activity of a business unit during a cost accounting period.

(b) Segment B performs a budgeting function, the cost of which is included in its G&A expense pool. This function includes the preparation of budgets for another segment. The cost of preparing the budgets for the other segment should be removed from B's G&A expense pool and transferred to the other segment.

(c) (1) Business Unit C has a personnel function which is divided

into two parts: A vice president of personnel who establishes personnel policy and overall guidance, and a personnel department which handles hirings, testing, evaluations, etc. The expense of the vice president is included in the G&A expense pool. The expense of the personnel department is allocated to the other indirect cost pools based on the beneficial or causal relationship between that expense and the indirect cost pools. This procedure is in compliance with the requirements of this Standard.

(2) Business Unit C has included selling costs as part of its G&A expense pool. Unit C wishes to continue to include selling costs in its G&A pool. Under the provisions of this Standard, Unit C may continue to include selling costs in its G&A pool, and these costs will be allocated over a cost input base selected in accordance with the provisions of 9904.410-50(d).

(3) Business Unit C has included IR&D and B&P costs in its G&A expense pool. Unit C has used a cost of sales base to allocate its G&A expense pool. As of January 1, 1978 (assumed for purposes of this illustration), the date on which Unit C must first allocate its G&A expense pool in accordance with the requirements of this Standard, Unit C has among its final cost objectives several cost reimbursement contracts and fixed price contracts subject to the CAS clause (referred to as the

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preexisting contracts). If Unit C chooses to use the transition method in 9904.410-50(e):

(i) Unit C shall allocate IR&D and B&P costs during the transition period (from January 1, 1978, to and including the cost accounting period during which the preexisting contracts are completed), to the preexisting contracts as part of its G&A expense pool using a cost of sales base pursuant to 9904.410-50(e) and appendix A to 9904.410.

(ii) During the transition period such costs, as part of the G&A expense pool, shall be allocated to new cost reimbursement contracts and new fixed price contracts subject to the CAS clause using a cost input base as required by 9904.410-50 (d) and (e) and appendix A to 9904.410.

(iii) Beginning with the cost accounting period after the transition period the IR&D and B&P costs, as part of the G&A expense pool, shall be allocated to all final cost objectives using a cost input base as required by 9904.410-50(d). If Unit C chooses not to use the transition method in 9904.410-50(e), the contractual provision requiring appropriate equitable adjustment of the prices of affected prime contracts and subcontracts will be implemented.

(4) Business Unit C has accounted for and allocated IR&D and B&P costs in a cost pool separate and apart from the G&A expense pool. Unit C may continue to account for these costs in a separate cost pool under the provision of this Standard. If Unit C is to use a total cost input base, these costs when accounted for and allocated in a cost pool separate and apart from the G&A expense pool will become part of the total cost input base used by Unit C to allocate the G&A expense pool.

(5) Business Unit C has included selling costs as part of its G&A expense pool. Unit C has used a cost of sales base to allocate the G&A expense pool. Unit C desires to continue to allocate selling costs using the costs of sales base. Under the provisions of this Standard, Unit C would account for selling costs as a cost pool separate and apart from the G&A expense pool, and continue to allocate these costs over a cost of sales base. If Unit C uses a total cost input base to allocate the G&A expense pool, the selling costs will become part of the total cost input base.

(d)(1) Business Unit D has accounted for selling costs in a cost pool separate and apart from its G&A expense pool and has allocated these costs using a cost of sales base. Under the provisions of this Standard, Unit D may continue to account for those costs in a separate pool and allocate them using a cost of sales base. Unit D has a total

cost input base to allocate its G&A expense pool. The selling costs will become part of the cost input base used by Unit D to allocate the G&A expense pool.

(2) During a cost accounting period, Business Unit D buys \$2,000,000 of raw materials. At the end of that cost accounting period, \$500,000 of raw materials inventory have not been charged out to contracts or other cost objectives. The \$500,000 of raw materials are not part of the total cost input base for the cost accounting period, because they have not been charged to the production of goods and services during that period. If all of the \$2,000,000 worth of raw material had been charged to cost objectives during the cost accounting period, the cost input base for the allocation of the G&A expense pool would include the entire \$2,000,000.

(3) Business Unit D manufactures a variety of testing devices. During a cost accounting period, Unit D acquires and uses a small building, constructs a small production facility using its own resources, and keeps for its own use one unit of a testing device that it manufactures and sells to its customers. The acquisition cost of the building is not part of the total cost input base; however, the depreciation taken on the building would be part of the total cost input base. The costs of construction of the small production facility are not part of the total cost input base. The requirements of 9904.404 provide that those G&A expenses which are identifiable with the constructed asset and are material in amount shall be capitalized as part of the cost of the production facility. If there are G&A expenses material in amount and identified with the constructed asset, these G&A expenses would be removed from the G&A expense pool prior to the allocation of

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this pool to final cost objectives. The cost of the testing device shall be part of the total cost input base per the requirements of 9904.404 which provides that the costs of constructed assets identical with the contractor's regular product shall include a full share of indirect cost.

(e)(1) Business Unit E produces Item Z for stock or product inventory. The business unit does not include G&A expense as part of the inventory cost of these items for costing or financial reporting purposes. A production run of these items occurred during Cost Accounting Period 1. A number of the units produced were not issued during Period 1 and are issued in Period 2. However, those units produced in Period 1 shall be included in the cost input of that period for calculating the G&A expense allocation base and shall not be included in the cost input of Period 2.

(2) Business Unit E should apply the G&A expense rate of Period 1 to those units of Item Z issued during Period 1 and may apply the rate of Period 2 to the units issued in Period 2.

(3) If the practice of Business Unit E is to include G&A expense as part of the cost of stock or product inventory, the inventory cost of all units of Item Z produced in Period 1 and remaining in inventory at the end of Period 1, should include G&A expense using the G&A rate of Period 1.

(f)(1) Business Unit F produced Item X for stock or product inventory. The business unit does not include G&A expense as part of the inventory cost of these items. A production run of these items was started, finished, and placed into inventory in a single cost accounting period. These items are issued during the next cost accounting period.

(2) The cost of items produced for stock or product inventory should be included in the G&A base in the same year they are produced. The cost of such items is not to be included in the G&A base on the basis of when they are issued to final cost objectives. Therefore, the time of issuance of these items from inventory to a final cost objective is irrelevant in computing the G&A base.

(g) The normal productive activity of Business Unit G includes the

construction of base operating facilities for others. Unit G uses a total cost input base to allocate G&A expense to final cost objectives. As part of a contract to construct an operating facility, Unit G agrees to acquire a large group of trucks and other mobile equipment to equip the base operating facility. Unit G does not usually supply such equipment. The cost of the equipment constitutes a significant part of the contract cost. A special G&A allocation to this contract shall be agreed to by the parties if they agree that in the circumstances the contract as a whole receives substantially less benefit from the G&A expense pool than that which would be represented by a cost allocation based on inclusion of the contract cost in the total cost input base.

(h)(1) The home office of Segment H separately allocates to benefiting or causing segments significant home office expenses of staff management functions relative to manufacturing, staff management functions relative to engineering, central payment of health insurance costs, and residual expenses. Segment H receives these expenses as separate allocations and maintains three indirect cost pools; i.e., G&A expense, manufacturing overhead, and engineering overhead; all home office expenses allocated to Segment H are included in Segment H's G&A expense pool.

(2) This accounting practice of Segment H does not comply with 9904.410-50(g)(2). Home office residual expenses should be in the G&A expense pool, and the expenses of the staff management functions relative to manufacturing and engineering should be included in the manufacturing overhead and engineering overhead pools, respectively. The health insurance costs should be allocated in proportion to the beneficial and causal relationship between these costs and Segment H's cost objectives.

9904.410-61 Interpretation. [Reserved]

#### Sec. 9904.410-62 Exemption.

This Standard shall not apply to contracts and grants with state, local, and Federally recognized Indian tribal governments.

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#### Sec. 9904.410-63 Effective date.

This Standard is effective as of April 17, 1992. Contractors with prior CAS-covered contracts with full coverage shall continue this Standard's applicability upon receipt of a contract to which this Standard is applicable. For contractors with no previous contracts subject to this Standard, this Standard shall be applied beginning with the contractor's next full fiscal year beginning after the receipt of a contract to which this Standard is applicable.

#### Appendix A to 9904.410--Transition From a Cost of Sales or Sales Base to a Cost Input Base

A business unit may use the method described below for transition from the use of a cost of sales or sales base to a cost input base.

(1) Calculate the cost of sales or sales base in accordance with the cost accounting practice disclosed or established prior to the date established by 9904.410-80(b) of the original Cost Accounting Standard.

(2) Calculate the G&A expense allocation rate using the base determined in subparagraph (1) of this appendix and use that rate to allocate from the G&A expense pool to the final cost objectives which were in existence prior to the date on which the business unit must first allocate costs in accordance with the requirements of this Cost Accounting Standard.

(3) Calculate a cost input base in compliance with 9904.410-50(d).

(4) Calculate the G&A expense rate using the base determined in subparagraph (3) of this appendix and use that rate to allocate from the

subject to this Standard, this Standard shall be applied beginning with the contractor's next full fiscal year beginning after the receipt of a contract to which this Standard is applicable.

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9904.418 Allocation of direct and indirect costs.

9904.418-10 [Reserved]

Sec. 9904.418-20 Purpose.

The purpose of this Cost Accounting Standard is to provide for consistent determination of direct and indirect costs; to provide criteria for the accumulation of indirect costs, including service center and overhead costs, in indirect cost pools; and, to provide guidance relating to the selection of allocation measures based on the beneficial or causal relationship between an indirect cost pool and cost objectives. Consistent application of these criteria and guidance will improve classification of costs as direct and indirect and the allocation of indirect costs.

Sec. 9904.418-30 Definitions.

(a) The following are definitions of terms which are prominent in this Standard. Other terms defined elsewhere in this chapter 99 shall have the meanings ascribed to them in those definitions unless paragraph (b) of this subsection, requires otherwise.

(1) Allocate means to assign an item of cost, or a group of items of cost, to one or more cost objectives. This term includes both direct assignment of cost and the reassignment of a share from an indirect cost pool.

(2) Direct cost means any cost which is identified specifically with a particular final cost objective. Direct costs are not limited to items which are incorporated in the end product as material or labor. Costs identified specifically with a contract are direct costs of that contract. All costs identified specifically with other final cost objectives of the contractor are direct costs of those cost objectives.

(3) Indirect cost means any cost not directly identified with a single final cost objective, but identified with two or more final cost objectives or with at least one intermediate cost objective.

(4) Indirect cost pool means a grouping of incurred costs identified with two or more cost objectives but not identified specifically with any final cost objective.

(b) The following modifications of terms defined elsewhere in this chapter 99 are applicable to this Standard: None.

Sec. 9904.418-40 Fundamental requirements.

(a) A business unit shall have a written statement of accounting policies and practices for classifying costs as direct or indirect which shall be consistently applied.

(b) Indirect costs shall be accumulated in indirect cost pools which are homogeneous.

(c) Pooled costs shall be allocated to cost objectives in reasonable proportion to the beneficial or causal relationship of the pooled costs to cost objectives as follows:

(1) If a material amount of the costs included in a cost pool are costs of management or supervision of activities involving direct labor or direct material costs, resource consumption cannot be specifically identified with cost objectives. In that circumstance, a base shall be used which is representative of the activity being managed or supervised.

(2) If the cost pool does not contain a material amount of the costs of management or supervision of activities involving direct labor or



direct material costs, resource consumption can be specifically identified with cost objectives. The pooled cost shall be allocated based on the specific identifiability of resource consumption with cost objectives by means of one of the following allocation bases:

- (i) A resource consumption measure,
- (ii) An output measure, or
- (iii) A surrogate that is representative of resources consumed.

The base shall be selected in accordance with the criteria set out in 9904.418-50(e).

(d) To the extent that any cost allocations are required by the provisions of other Cost Accounting Standards, such allocations are not subject to the provisions of this Standard.

(e) This Standard does not cover accounting for the costs of special facilities where such costs are accounted for in separate indirect cost pools.

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Sec. 9904.418-50 Techniques for application.

(a) Determination of direct cost and indirect cost. (1) The business unit's written policy classifying costs as direct or indirect shall be in conformity with the requirements of this Standard.

(2) In accounting for direct costs a business unit shall use actual costs, except that--

(i) Standard costs for material and labor may be used as provided in 9904.407; or

(ii) An average cost or pre-established rate for labor may be used provided that:

(A) The functions performed are not materially disparate and employees involved are interchangeable with respect to the functions performed, or

(B) The functions performed are materially disparate but the employees involved either all work in a single production unit yielding homogeneous outputs, or perform their respective functions as an integral team.

Whenever average cost or pre-established rates for labor are used, the variances, if material, shall be disposed of at least annually by allocation to cost objectives in proportion to the costs previously allocated to these cost objectives.

(3) Labor or material costs identified specifically with one of the particular cost objectives listed in paragraph (d)(3) of this subsection shall be accounted for as direct labor or direct material costs.

(b) Homogeneous indirect cost pools. (1) An indirect cost pool is homogeneous if each significant activity whose costs are included therein has the same or a similar beneficial or causal relationship to cost objectives as the other activities whose costs are included in the cost pool. It is also homogeneous if the allocation of the costs of the activities included in the cost pool result in an allocation to cost objectives which is not materially different from the allocation that would result if the costs of the activities were allocated separately.

(2) An indirect cost pool is not homogeneous if the costs of all significant activities in the cost pool do not have the same or a similar beneficial or causal relationship to cost objectives and, if the costs were allocated separately, the resulting allocation would be materially different. The determination of materiality shall be made using the criteria provided in 9903.305.

(3) A homogeneous indirect cost pool shall include all indirect costs identified with the activity to which the pool relates.

(c) Change in allocation base. No change in an existing indirect cost pool allocation base is required if the allocation resulting from the existing base does not differ materially from the allocation that

results from the use of the base determined to be most appropriate in accordance with the criteria set forth in paragraphs (d) and (e) of this subsection. The determination of materiality shall be made using the criteria provided in Subpart 9903.305.

(d) Allocation measures for an indirect cost pool which includes a material amount of the costs of management or supervision of activities involving direct labor or direct material costs. (1) The costs of the management or supervision of activities involving direct labor or direct material costs do not have a direct and definitive relationship to the benefiting cost objectives and cannot be allocated on measures of a specific beneficial or causal relationship. In that circumstance, the base selected to measure the allocation of the pooled costs to cost objectives shall be a base representative of the activity being managed or supervised.

(2) The base used to represent the activity being managed or supervised shall be determined by the application of the criteria below. All significant elements of the selected base shall be included.

(i) A direct labor hour base or direct labor cost base shall be used, whichever in the aggregate is more likely to vary in proportion to the costs included in the cost pool being allocated, except that:

(ii) A machine-hour base is appropriate if the costs in the cost pool are comprised predominantly of facility-related costs, such as depreciation, maintenance, and utilities; or

(iii) A units-of-production base is appropriate if there is common production of comparable units; or

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(iv) A material cost base is appropriate if the activity being managed or supervised is a material-related activity.

(3) Indirect cost pools which include material amounts of the costs of management or supervision of activities involving direct labor or direct material costs shall be allocated to:

(i) Final cost objectives;

(ii) Goods produced for stock or product inventory;

(iii) Independent research and development and bid and proposal projects;

(iv) Cost centers used to accumulate costs identified with a process cost system (i.e., process cost centers);

(v) Goods or services produced or acquired for other segments of the contractor and for other cost objectives of a business unit; and

(vi) Self-construction, fabrication, betterment, improvement, or installation of tangible capital assets.

(e) Allocation measures for indirect cost pools that do not include material amounts of the costs of management or supervision of activities involving direct labor or direct material costs. Homogeneous indirect cost pools of this type have a direct and definitive relationship between the activities in the pool and benefiting cost objectives. The pooled costs shall be allocated using an appropriate measure of resource consumption. This determination shall be made in accordance with the following criteria taking into consideration the individual circumstances:

(1) The best representation of the beneficial or causal relationship between an indirect cost pool and the benefiting cost objectives is a measure of resource consumption of the activities of the indirect cost pool.

(2) (i) If consumption measures are unavailable or impractical to ascertain, the next best representation of the beneficial or causal relationship for allocation is a measure of the output of the activities of the indirect cost pool. Thus, the output is substituted for a direct measure of the consumption of resources.

(ii) The use of the basic unit of output will not reflect the proportional consumption of resources in circumstances in which the level of resource consumption varies among the units of output produced.

Where a material difference will result, either the output measure shall be modified or more than one output measure shall be used to reflect the resources consumed to perform the activity.

(3) If neither resources consumed nor output of the activities can be measured practically, a surrogate that varies in proportion to the services received shall be used to measure the resources consumed. Generally, such surrogates measure the activity of the cost objectives receiving the service.

(4) Allocation of indirect cost pools which benefit one another may be accomplished by use of:

(i) The cross-allocation (reciprocal) method,  
(ii) The sequential method, or  
(iii) Another method the results of which approximate those achieved by either of the methods in subdivisions (e)(4)(i) or (e)(4)(ii) of this subsection.

(5) Where the activities represented by an indirect cost pool provide services to two or more cost objectives simultaneously, the cost of such services shall be prorated between or among the cost objectives in reasonable proportion to the beneficial or causal relationship between the services and the cost objectives.

(f) Special allocation. Where a particular cost objective in relation to other cost objectives receives significantly more or less benefit from an indirect cost pool than would be reflected by the allocation of such costs using a base determined pursuant to paragraphs (d) and (e) of this subsection, the Government and contractor may agree to a special allocation from that indirect cost pool to the particular cost objective commensurate with the benefits received. The amount of a special allocation to any such cost objective made pursuant to such an agreement shall be excluded from the indirect cost pool and the particular cost objective's allocation base data shall be excluded from the base used to allocate the pool.

(g) Use of preestablished rates for indirect costs. (1) Preestablished rates, based on either forecasted actual or standard cost, may be used in allocating an indirect cost pool.

(2) Preestablished rates shall reflect the costs and activities anticipated for

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the cost accounting period except as provided in paragraph (g)(3) of this subsection. Such preestablished rates shall be reviewed at least annually, and revised as necessary to reflect the anticipated conditions.

(3) The contracting parties may agree on preestablished rates which are not based on costs and activities anticipated for a cost accounting period. The contractor shall have and consistently apply written policies for the establishment of these rates.

(4) Under paragraphs (g)(2) and (3) of this subsection where variances of a cost accounting period are material, these variances shall be disposed of by allocating them to cost objectives in proportion to the costs previously allocated to these cost objectives by use of the preestablished rates.

(5) If preestablished rates are revised during a cost accounting period and if the variances accumulated to the time of the revision are significant, the costs allocated to that time shall be adjusted to the amounts which would have been allocated using the revised preestablished rates.

Sec. 9904.418-60 Illustrations.

(a) Business Unit A has various classifications of engineers whose time is spent in working directly on the production of the goods or services called for by contracts and other final cost objectives. In keeping with its written policy, detailed time records are kept of the

hours worked by these engineers, showing the job/account numbers representing various cost objectives. On the basis of these detailed time records, Unit A allocates the labor costs of these engineers as direct labor costs of final cost objectives. This practice is in accordance with the requirements of 9904.418-50(a)(1).

(b) Business Unit B has a fabrication department, employees of which perform various functions on units of the work-in-process of multiple final cost objectives. These employees are grouped by labor skills and are interchangeable within the skill grouping. The average wage rate for each group is multiplied by the hours worked on each cost objective by employees in that group. The contractor classifies these costs as direct labor costs of each final cost objective. This cost accounting treatment is in accordance with the provisions of 9904.418-50(a)(2)(ii)(B).

(c) Business Unit C accumulates the costs relating to building ownership, maintenance, and utility into one indirect cost pool designated "Occupancy Costs" for allocation to cost objectives. Each of these activities has the same or a similar beneficial or causal relationship to the cost objectives occupying a space. Unit C's practice is in conformance with the provisions of 9904.418-50(b)(1).

(d) Business Unit D includes the indirect costs of machining and assembling activities in a single manufacturing overhead pool. The machining activity does not have the same or similar beneficial or causal relationship to cost objectives as the assembling activity. Also, the allocation of the cost of the machining activity to cost objectives would be significantly different if allocated separately from the cost of the assembling activity. Unit D's single manufacturing overhead pool is not homogeneous in accordance with the provisions of 9904.418-50(b), and separate pools must be established in accordance with 9904.418-40(b).

(e) In accordance with 9904.418-50(b)(3), Business Unit E includes all the cost of occupancy in an indirect cost pool. In selecting an allocation measure for this indirect cost pool, the contractor establishes that it is impractical to ascertain a measurement of the consumption of resources in relation to the use of facilities by individual cost objectives. An output base, the number of square feet of space provided to users, can be measured practically; however, the cost to provide facilities is significantly different for various types of facilities such as warehouse, factory, and office and each type of facility requires a different level of resource consumption to provide the same number of square feet of usable space. Allocation on a basic unit measure of square feet of space occupied will not adequately reflect the proportional consumption of resources. Unit E establishes a weighted square foot measure for allocating occupancy costs, which reflects the different levels of resource consumption required to provide the different types of facilities.

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This practice is in conformance with provisions of 9904.418-50(e)(2)(iii).

(f) Business Unit F has an indirect cost pool containing a significant amount of material-related costs. The contractor allocates these costs between his machining overhead cost pool and his assembly overhead cost pool. The business unit finds it impractical to use an allocation measure based on either consumption or output. The business unit selects a dollars of material-issued base which varies in proportion to the services rendered. The dollars of material-issued base is a surrogate base which conforms to the provisions of 9904.418-50(e)(3).

(g) Business Unit G has a machining activity for which it develops a separate overhead rate, using direct labor cost as the allocation base. The machining activity occasionally does significant amounts of work for other activities of the business unit. The labor used in doing the work for other activities is of the same nature as that used for contract

work. However, the machining labor for other activities is not included in the base used to allocate the overhead costs of the machining activity. This practice is not in conformance with 9904.418-50(d)(2). Unit G must include the cost of labor doing work for the other activities in the allocation base for the machining activity indirect cost pool.

(h) Business Unit H accounts for the costs of company aircraft in a separate homogeneous indirect cost pool and allocates the cost to benefiting cost objectives using flight hours. Unit H prorates the cost of a single flight between benefiting cost objectives whenever simultaneous services have been rendered. Manager of Contract 2 learns of the trip and goes along with Manager of Contract 1. Unit H prorates the cost of the trip between Contract 1 and Contract 2. This practice is in conformance with the provision of 9904.418-50(e)(5).

(i) During a cost accounting period, Business Unit I allocates the cost of its flight services indirect cost pool to other indirect cost pools and final cost objectives using a preestablished rate. The preestablished rate is based on an estimate of the actual costs and activity for the cost accounting period. For the cost accounting period, Unit I establishes a rate of \$200 per hour for use of the flight services activity. In March, the contractor's operating environment changes significantly; the contractor now expects a significant increase in the cost of this activity during the remainder of the year. Unit I estimates the rate for the entire cost accounting period to be \$240 an hour. Pursuant to the provisions of 9904.418-50(g)(4), the Business Unit may revise its rate to the expected \$240 an hour. If the accumulated variances are significant, the business unit must also adjust the costs previously allocated to reflect the revised rates.  
9904.418-61 Interpretation. [Reserved]

#### Sec. 9904.418-62 Exemptions.

This Standard shall not apply to contracts and grants with state, local, and Federally recognized Indian tribal governments.

#### Sec. 9904.418-63 Effective date.

This Standard is effective as of April 17, 1992. Contractors with prior CAS-covered contracts with full coverage shall continue this Standard's applicability upon receipt of a contract to which this Standard is applicable. For contractors with no previous contracts subject to this Standard, this Standard shall be applied beginning with the contractor's second full fiscal year beginning after the receipt of a contract to which this Standard is applicable.

9904.420 Accounting for independent research and development costs and bid and proposal costs.

9904.420-10 [Reserved]

#### Sec. 9904.420-20 Purpose.

The purpose of this Cost Accounting Standard is to provide criteria for the accumulation of independent research and development costs and bid and proposal costs and for the allocation of such costs to cost objectives based on the beneficial or causal relationship between such costs and cost objectives. Consistent application of these criteria will improve cost allocation.

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#### Sec. 9904.420-30 Definitions.

(a) The following are definitions of terms which are prominent in this Standard. Other terms defined elsewhere in this Chapter 99 shall have the meanings ascribed to them in those definitions unless paragraph