



aronson LLC
ASSURANCE | TAX | CONSULTING

Cost Accounting Standards

404, 407, 409, and 411

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Principal Consultant

About Aronson LLC

- Thinking ahead for clients for more than 50 years
- 225+ professionals located in Rockville, MD
- 80+ professionals dedicated to supporting government contractors
- Aronson helps clients rethink the way they approach their business through innovative, industry-specific services and advice:
 - Audit, Assurance and Tax
 - Deltek Systems and Outsourcing
 - Financial and Contract Compliance
 - GSA Schedules
- www.aronsonllc.com/blogs/fedpoint/ – News and trends and insight for today's savvy government contractor



Adam D. Eastridge

Principal Consultant

- Adam D. Eastridge is a principal consultant in Aronson LLC's Government Contract Services Group. With more than 13 years of experience, he focuses on cost accounting standards (CAS), business systems, federal acquisition regulation (FAR), and audit support.
- Throughout his career, Adam has served the government contracting community in several capacities, holding positions at DCAA, a major defense contractor and several government contract consulting firms. This diverse experience gives him the ability to perform analysis with an understanding of the motivation of the stakeholders from each sector, and the consequences a decision will have on each stakeholder. As a result, Adam is adept at providing practical solutions that achieve positive results for his clients.
- Adam earned his bachelor's degree in accounting from Salisbury University in 2001.



Agenda

1. Refresher:
 - a) How to determine if your contract is subject to Full CAS Coverage
 - b) Definition of a cost accounting practice
2. CAS 404 - *Capitalization of tangible assets*
3. CAS 409 - *Depreciation of tangible capital assets*
4. CAS 407 - *Use of standard costs for direct material and direct labor*
5. CAS 411 - *Accounting for acquisition costs of material*



Full CAS Coverage (all 19 standards)

1. Current award is \$50M or more
2. Segment received \$50M or more in its preceding cost accounting period
3. Segment received \$50M or more in its current cost accounting period

Definition of a Cost Accounting Practice

1. Measurement of costs
2. Assignment of costs to cost accounting periods
3. Allocation of costs to cost objectives



CAS 404 - Capitalization of tangible assets

- CAS 404 pertains to the “measurement” of tangible assets
 - Reminder: a change in measurement is considered a cost accounting practice change.
- Definitions:
 - 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 service it yields.
 - 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.



CAS 404 - Capitalization of tangible assets

- Must have a written capitalization policy addressing:
 1. Amount of cost that will be capitalized (i.e. the acquisition cost)
 - Purchase price, plus
 - Costs necessary to put the asset into service
 2. Minimum service life (Can't exceed 2 years)
 3. Minimum acquisition cost (Can't exceed \$5,000)
 4. Other specific characteristics which are pertinent to capitalization policy decisions
 - For example: Class of asset
 5. Must require the identification of each asset in your books and records
 6. Original complement of low cost equipment
 - May use a higher minimum acquisition cost criteria
- Business combinations
 - Must limit the asset value to the value reported by the seller (i.e. no stepped up assets)
 - FAR 31.205-52 incorporates this requirement for ALL contracts, not just CAS covered contracts.



CAS 409 - Depreciation of tangible capital assets

- CAS 409 pertains to the “assignment” of costs.
 - Reminder: a change in assignment is considered a cost accounting practice change.
 - However, its important to differentiate a change in assignment from a change in estimate. A change in estimate is not considered a cost accounting practice change.
- Depreciation begins when the asset is in service

Service Life

- Estimated service life must be based on expected actual periods of usefulness
 - Must be supported by records
 - Can be adjusted for changes for physical and economic usefulness
 - Actual data not available when you receive your first CAS covered contract?
 - CAS 409 provides a two year grace period during which time you need to develop the estimated expected periods of usefulness based on actual and historical records
 - During the 2 years, one must use either the service life used for GAAP (if reasonable), or if that data isn't available, use a projection. However, the projection can not be less than the IRS asset guidelines.



CAS 409 - *Depreciation of tangible capital assets*

- **Depreciation Method**

- Use the method used for financial accounting purposes, unless:
 - Doesn't reflect expected consumption
 - Method is unacceptable for federal income tax purposes
- Accelerated method is appropriate where the expected consumption is significantly greater in the early years of asset life
- Straight line method is appropriate where the expected consumption is level over the asset life

- **Residual Value**

- Must be determined for all assets
- For personal property: only residual value exceeding 10% of the capitalized cost must be deducted



CAS 409 - *Depreciation of tangible capital assets*

- **Gains/Losses**

- Shall be limited to the difference between the original acquisition cost and the undepreciated balance
- Must be included in the year of the disposition
- Shall be allocated in the same manner as the depreciation cost has or would have been allocated. If the amount is immaterial, the amount can be included in an appropriate cost pool

- **Direct Cost**

- Depreciation can only be charged direct if such charges are based on usage



CAS 407 - Use of standard costs for direct material and direct labor

- Reminder: changing from actual cost to standard cost and vice-versa is considered a change in accounting practice (i.e. change in measurement)
- Definition:
 - Production unit: means a grouping of activities which either uses homogeneous inputs of direct material and direct labor or yields homogeneous outputs such that the costs or statistics related to these homogeneous inputs or outputs are appropriate as bases for allocating variances.
- Standard costs may be used for estimating, accumulating, and reporting costs of direct material and direct labor only when all of the following criteria are met:
 1. Standard costs are entered into the books of account.
 2. Standard costs and related variances are appropriately accounted for at the level of the production unit.
 3. Practices with respect to the setting and revising of standards, use of standard costs, and disposition of variances are stated in writing and are consistently followed.



CAS 407 - Use of standard costs for direct material and direct labor

Labor

- Labor categories:
 - Functions performed within that category must be similar and the employees involved must be interchangeable.
- Labor-cost variances
 - Shall be recognized at the time labor cost is introduced into production units. Labor-rate variances and labor-time variances may be combined into one labor-cost variance account.

Material

- Material-price variances may be recognized either at the time purchases of material are entered into the books of account
 - Where variances are recognized at the time purchases of material are entered into the books of account, they shall be accumulated separately by homogeneous groupings of material.
 - shall be allocated, at least annually, to items in purchased-items inventory and to production units receiving items from that homogeneous grouping of material. If, insignificant the cost may be included in appropriate indirect cost pools for allocation to applicable cost objectives
 - The price variances and material-quantity variances may be combined into one material-cost variance account



CAS 407 - Use of standard costs for direct material and direct labor

Allocation of variances accumulated by production unit

- Variances must be allocated to cost objectives (including ending in-process inventory) at least annually.
 - Where a variance related to material is allocated, the allocation shall be on the basis of the material cost at standard, or, where outputs are homogeneous, on the basis of units of output.
 - Where a variance related to labor is allocated, the allocation shall be on the basis of the labor cost at standard or labor hours at standard or, where outputs are homogeneous, on the basis of units of output
- Variances which are immaterial may be included in appropriate indirect cost pools for allocation to applicable cost objectives



CAS 411 - Accounting for acquisition costs of material

- The contractor shall have, and consistently apply, written statements of accounting policies and practices for accumulating the costs of material and for allocating costs of material to cost objectives
- The cost of material which is used solely in performing indirect functions, or is not a significant element of production cost, whether or not incorporated in an end product, may be allocated to an indirect cost pool.
- Material cost shall be the acquisition cost of a category of material
 - Must account for all discounts and credits. These must be charged to the same cost objective the material was charged to
- Direct charge (not through an inventory account)
 - Must identify the contract when the material is purchased



CAS 411 - Accounting for acquisition costs of material

- **Direct charge through an Inventory account**
 - Must use either:
 1. First in first out
 2. Last in first out
 3. Moving average
 4. Weighted average, or
 5. Standard cost



Next Session – March 2015

- Allocations
 - 412 Composition and measurement of pension costs
 - 413 Adjustment an allocation pension costs
 - 414 Cost of money
 - 417 Cost of money (assets under construction)



Points of Contact

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