



ACQUISITION
TECHNOLOGY
AND LOGISTICS

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Ms. Lesley A. Field
Acting Chair
Cost Accounting Standards Board
Office of Federal Procurement Policy
725 17th Street, NW, Room 9013
Washington, DC 20503

JUN 17 2009

Dear Ms. Field:

The Department of Defense is pleased to have the opportunity to respond to your request for information regarding the retention or elimination or revision to the CAS exemption provided at 48 CFR 9903.201-1(b)(14) for contracts executed and performed entirely outside the United States, its territories, and possessions. We are providing a partial response now (see enclosure) with our comments as requested by your April 24, 2009 letter. The Army and the Air Force are gathering additional detail on the experiences with the Overseas Exemption and the volume of requests for the exemption. We will supplement this response when we have the data from the Army and Air Force.

We appreciate your consideration of our comments. Please direct any questions regarding this letter to Mr. H. Clyde Wray at 703-602-8387 or e-mail at Clyde.Wray@osd.mil.

Sincerely,

Shay D. Assad
Director, Defense Procurement
and Acquisition Policy

Enclosure:
As stated



Department of Defense
Responses to Questions Regarding the CAS Overseas Exemption

- 1. What is your experience with the overseas exemption? and**
- 2. How often has the overseas exemption been claimed?**

The Services are compiling data which the Department will forward when available on the specific experiences and number of exemptions granted based on the overseas exemption. This data will primarily be from the Army. Preliminary indications are that most of the exemption requests are at the subcontractor level where data is not readily available:

- The Navy reports no overseas exemptions granted since it deals overseas mostly in commercial activity, competitively awarded, or small dollar contracts that are exempt for other reasons.
- The Air Force reports 17 prime contractor overseas exemptions in the last three years but believes there are more at the subcontract level. The Air Force also believes that with its contingency contracting efforts that there will be increases for such exemptions in the future.
- The Army appears to have the largest number and dollar volume for such exemptions, but has not yet been able to compile its statistics.
- DCMA indicates that it is not staffed to administer CAS provisions overseas.

- 3. If the overseas exemption is eliminated, what problems will that cause you?**

- The Department anticipates that some host governments will consider that the imposition of CASB rules on accounting practices of foreign firms performing work entirely overseas is an infringement of their sovereignty. While this may not be accurate given the imposition of other US Government contracting rules on such firms, the change in the rule could trigger the host governments to react to the increase in rules imposed.
- There is some concern that imposition of additional rules on foreign firms may cause some of them to not bid on or not accept US Government contracts, lowering the resources available to perform the mission and lessening competition which affects contract prices. That could be a temporary or a sustained reduction.
- At least at first, and possibly on a sustained basis, the Department expects a significant increase in requests for CAS Waivers for firms that are now using the overseas exemption. The waiver process could significantly slow the contract award process. Since many of the overseas firms are involved in supporting activities in contingency activity areas, the tendency will be to find a way to continue to contract with firms that do not wish to contract under CASB rules.

- There may be an increase in proposed prices from firms previously exempt under the overseas exemption to account for additional risk due to potential cost impacts for noncompliances. These may be temporary increases until the firms can gage the additional cost risk. Also, there could be significant cost associated with changing accounting systems.

4. How does the overseas exemption help, or not help, to implement the CASB’s mandate “to achieve uniformity and consistency in the cost accounting standards governing measurement, assignment, and allocation of costs to contracts with the United States?”

- The more firms covered by the CASB rules, the more uniform and consistent the costs applied to US Government contracts will be.
- All exemptions to the CASB rules are due to cost benefit analysis of the costs to implement compared to the benefits of the more consistent cost treatment, or analysis of absolute need of the U.S. Government for contracts with firms who will not bid under CASB rules. As a class, there may be a good case to continue to exempt foreign firms performing overseas due to the administrative costs to both the U.S. Government and the contractor to enforce the rules, problems with host governments, and contractors who may choose not to bid on U.S. Government work.

5. What are the arguments for, and against, the requirement in the overseas exemption to require execution of the contract overseas?

- The execution location for a contract does not seem to be an important discriminator for application of CASB rules. With the current level of contractor mobility, electronic commerce, and global operations, the place of execution has less to do with contract operations or the accounting for the contract costs.
- The Department would recommend consideration of the location of the company headquarters and/or the location of its normal accounting operations as a better indicator of the need for an overseas exemption. A company incorporated and headquartered overseas, with its accounting operations overseas, and not performing CAS contracts within the U.S. has a much better argument for an exemption from CAS than a U.S. company, a company owned or controlled by a U.S. company, or a company using a U.S. accounting center or U.S. accounting software that is also used for CAS covered contracts.

6. What are the arguments for, and against, the requirement in the overseas exemption to require performance of the contract overseas?

- While the topic is an exemption for contracts performed overseas, the performance location for the contract is not as important as the ownership and control of the company and whether its accounting activities are already CAS covered for work performed elsewhere. If there is to be an exemption for work performed overseas, it should be limited to overseas companies without other CAS covered work.

In summary, the Department of Defense believes it would be in the best interests of the U.S. Government to continue to grant some form of class exemption to foreign firms doing business overseas. The current exemption should be changed from one based on place of contract execution and contract performance to one that identifies firms doing business overseas that are headquartered and operated from overseas. The exemption should be drafted to account for the extra costs to firms to implement the CASB rules and the extra administrative costs to the U.S. Government. If a firm has other CAS covered business through the parent company or its subsidiaries, the extra costs to implement and administer the CASB rules on overseas contracts are significantly reduced or eliminated. Overseas firms would continue to qualify for other exemptions and waivers as warranted.

Additional Comments:

If firms were no longer granted the overseas exemption, some of the firms no longer exempted would be smaller businesses where CAS coverage may not be justified by the benefits derived from coverage. The CASB should give consideration to exempting smaller overseas firms.

We noted that the Defense Contract Audit Agency (DCAA) on May 26, 2009 made a separate response directly to the CAS Board and in that response indicated that it considered the application of the current rule to U.S. companies to be clearly defined under the current rule. The Department is not confident that the application of the current exemption is as clearly defined as DCAA considers it, especially in relation to firms operating overseas that are owned or controlled by U.S. firms. DCAA believes that the allocation of Home Office costs to the overseas firm indicates that the contract performance is not entirely overseas. We are not confident that the meaning of the term “performance” in relation to a contract would be found to include corporate functions beyond the actual work required by the contract’s terms.