

# FORVIS



## **CAS: The Series – Episode 8: *COM and Standard Costs – CAS 407,414, 417***

A 12-part webinar series on the Cost Accounting Standards

# Your Instructors



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# Agenda

- Layout of the series
- CAS 407 – Use of Standard Costs for Direct Material & Labor
- CAS 414 – Cost of Money as an Element of the Cost of Facilities Capital
- CAS 417 – Cost of Money as an Element of the Cost of Capital Assets Under Construction

# Polling Question

Where are you working from today?

1. Home or alternate work location
2. My company office
3. A different work location
4. Traveling
5. Other

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# Layout of the Series

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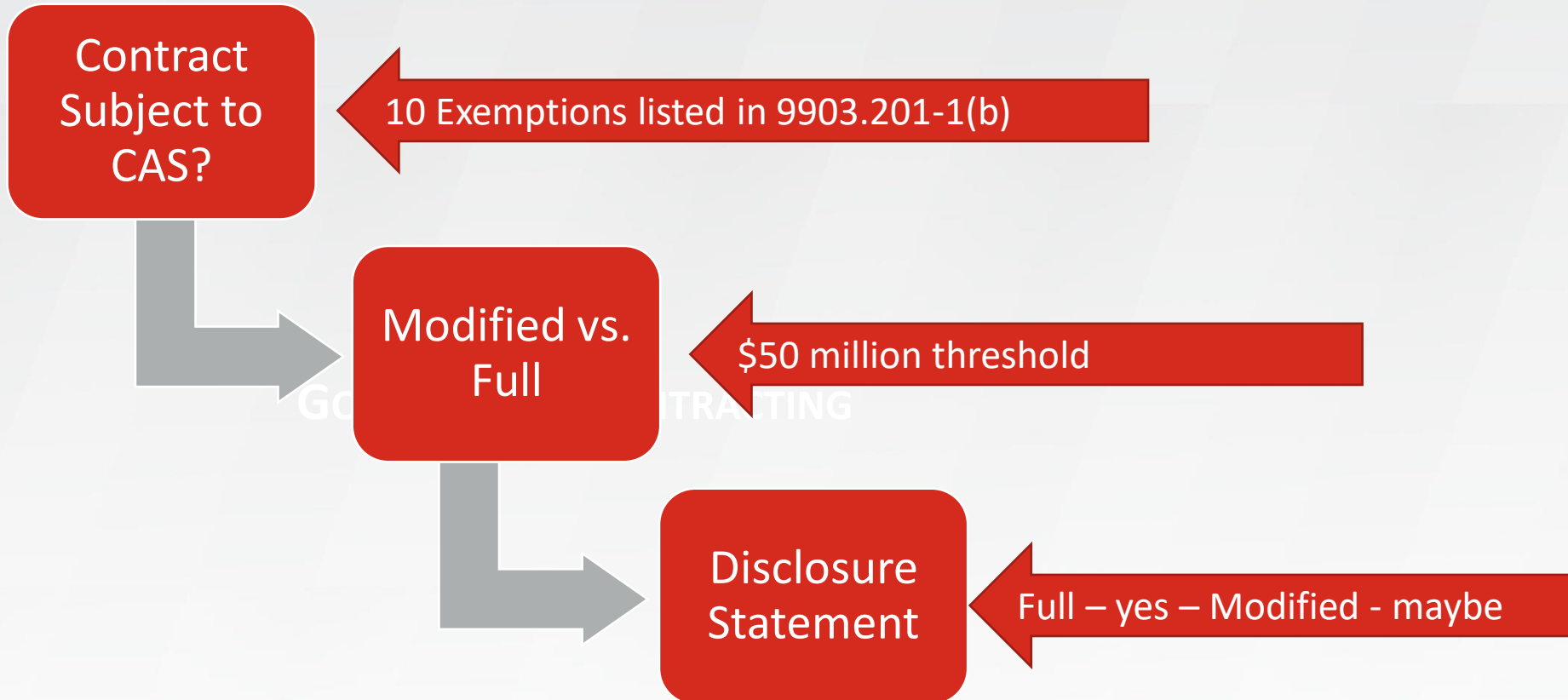
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# CAS in a minute!

- Contracts are subject to CAS – not contractors!



# Layout of CAS the Series

- Pilot Episode – 90-minute webinar to kick off the series
- Individual 90-minute episodes:
  - Episode 1 – CAS Clauses, Exemptions and Full/Modified CAS
  - Episode 2 – Cost Accounting Practice Changes & Administration
  - Episode 3 – CAS 401, 402, 405 & 406
  - Episode 4 – Compensation – CAS 408, 412, 413 & 415
  - Episode 5 – Direct and Indirect Costs – CAS 418
  - Episode 6 – Home office allocations – CAS 403

# Layout of CAS the Series

- Episode 7 – G&A and B&P/ IR&D – CAS 410 & 420
- **Episode 8 – COM and Standard Costs – CAS 407, 414 & 417**
- Episode 9 – Assets & Material – CAS 404, 409 & 411
- Episode 10 – Insurance and CAS 419 – CAS 416 and the mystery of CAS 419
- Episode 11 – Disclosure Statements
- Episode 12 – CAS Administration – Roles of DCMA & DCAA



# The Cost Accounting Standards

- BASIC Standards
  - CAS 401: Consistency
  - CAS 402: Direct v. Indirect Costs
  - CAS 405: Unallowable Costs
  - CAS 406: Cost Accounting Period
- The Cost Allocation Standards
  - **CAS 407: Standard Costs**
  - **CAS 414: Cost of Money**
  - CAS 410: General & Administrative
  - CAS 403: Home Office expenses
  - CAS 418: Direct & Indirect
  - CAS 420: B&P and IR&D
- Asset Accounting Standards
  - CAS 404: Capitalization
  - CAS 409: Depreciation
  - **CAS 417: Self Constructed Assets**
- Compensation Standards
  - CAS 408: Compensated Assets
  - CAS 412 & 413: Pensions
  - CAS 415: Deferred Compensation
- Other Standards
  - CAS 411: Material Costs
  - CAS 416: Insurance Costs

# The Format of the Standards

- Purpose (.20)
- Definitions (.30)
- Fundamental Requirement (.40)
- Techniques for Application (.50)
- Illustrations (.60)
- Interpretation (.61)
- Exemption (.62)
- Effective Date (.63)

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# CAS 407

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# Polling Question #2

If your company is a manufacturer, do you use standard costs for either direct labor or direct material?

1. Yes, for direct labor
2. Yes, for direct material
3. Yes, for both
4. No
5. N/A



# History

- CAS 407
  - Published on April 1, 1974
  - Took effect on October 1, 1974
- CASB determined that many defense contractors used standard cost systems, but there were no well-defined practices concerning the use of standard costs for contract costing purposes

# CAS 407 – Standard Costs for Direct Material and Direct Labor

- Provides criteria:
  - For using standard costs for estimating, accumulating, and reporting costs of direct material and direct labor
  - relating to the establishment of standards, accumulation of standard costs, and accumulation and disposition of variances from standard costs.
- Does not cover the use of pre-established measures solely for estimating.

# CAS 407 - Definitions

- **Labor cost at standard** means a pre-established measure of the labor element of cost, computed by multiplying labor-rate standard by labor-time standard.
  - **Labor-rate standard** means a pre-established measure, expressed in monetary terms, of the price of labor.
  - **Labor-time standard** means a pre-established measure, expressed in temporal terms, of the quantity of labor.
- **Material cost at standard** means a pre-established measure of the material element of cost, computed by multiplying material-price standard by material-quantity standard.
  - **Material-price standard** means a pre-established measure, expressed in monetary terms, of the price of material.
  - **Material-quantity standard** means a pre-established measure, expressed in physical terms, of the quantity of material
- **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 cost** means any cost computed with the use of pre-established measures.
- **Variance** means the difference between a pre-established measure and an actual measure.

# CAS 407 – Fundamental Requirement

- To use standard costs for estimating, accumulating, and reporting costs of direct material and direct labor – all of the following criteria must be met:
  - Standard costs are entered into the books of account
  - Standard costs and related variances are appropriately accounted for at the level of the production unit
  - 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 – Techniques for Application - General

- Requires a written statement of practices with respect to standards.
- Written practices must address:
  - Bases and criteria (such as engineering studies, experience, or other supporting data) used in setting and revising standards;
  - the period during which standards are to remain effective;
  - the level (such as ideal or realistic) at which material-quantity standards and labor-time standards are set; and
  - conditions (such as those expected to prevail at the beginning of a period) which material-price standards and labor-rate standards are designed to reflect.
- Where only either the material/labor price or material/labor quantity is set at standard, with the other component stated at actual, the result of the multiplication shall be treated as material cost at standard.

# CAS 407 – Techniques for Application – Labor Standards

- A labor-rate standard may be set to cover a category of direct labor if the functions performed within that category are not materially disparate and the employees involved are interchangeable with respect to the functions performed
- A labor-rate standard may be set to cover a group of direct labor workers who perform disparate functions only under either one of the following conditions:
  - Where the group of workers all work in a single production unit yielding homogeneous outputs
  - Where the group of workers, in the performance of their respective functions, forms an integral team
- Labor-cost variances must 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.
- A separate labor-cost variance shall be accumulated for each production unit.

# CAS 407 – Techniques for Application – Material Standards

- Material-price standards may be used and their related variances may be recognized either:
  - at the time purchases of material are entered into the books of account, or
  - at the time material cost is allocated to production units
- Variances must be accumulated separately by homogeneous groupings of material, however, insignificant variances may be included in appropriate indirect cost pools
- Material-price variances recognized at the time material cost is allocated to production units may be combined with material-quantity variances into one material-cost variance account

# CAS 407 – Illustration #1

- Contractor A's written practice is to set material-price standards for an item on the basis of average purchase prices expected to prevail during the calendar year.
- For that item whose usage from month to month is stable, a purchase contract is generally signed on May 1 of each year for a 1-year commitment. The current purchase contract calls for a purchase price of \$3 per pound; an increase of 5 percent, or 15¢ per pound, has been announced by the vendor when the new purchase contract comes into effect next May. Contractor A sets the material-price standard for this item at \$3.10 per pound for the year ( $[\$3.00 \times 4 + \$3.15 \times 8] \div 12$ ).
- Since Contractor A sets the material-price standard in accordance with his written practice, he complies with CAS 407

# CAS 407 – Illustration #2

- Contractor B accumulates, in one account, labor cost at standard for a department in which several categories of direct labor of disparate functions, in different combinations, are used in the manufacture of various dissimilar outputs of the department.
- Contractor B's dept. is not a production unit as defined in CAS 407
- B could accumulate the standard costs and variances separately:
  - For each of the several categories of direct labor, or
  - For each of several subdepartments, with homogenous output for each of the subdepartments

# CAS 407 – Illustration #3

- Contractor D uses materials where prices are expected to fluctuate, recognizes material-price variances at the time purchases of material are entered into the books of account.
- D maintains one purchase-price variance account for the whole plant.
- Purchased items are requisitioned by various production units in the plant.
- Since prices of material are expected to fluctuate at different rates, this plant-wide grouping does not constitute a homogeneous grouping of material.
- Of course, D's practice does not comply with CAS 407.
- D could maintain several purchased-items inventory accounts, each representing a homogeneous grouping of material, and maintain a material-price variance account for each of these homogeneous groupings of material to comply with CAS 407.

# CAS 414

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# History

- CAS 414 - Cost of Money as an Element of the Cost of Facilities Capital
  - Published on June 2, 1976
  - Took effect on October 1, 1976
  - Preceded by 3 issues papers – June '74, April '75 and December '75
- CASB recognized that the economic cost of facilities is “real and relevant for contract costing purposes”
- Prior to CAS 414, contractors were compensated for this economic benefit through an undifferentiated fee



# Polling Question #3

Does your company estimate cost of money?

- Yes
- No
- Not sure
- N/a



## CAS 414, Cost of Money as an Element of the Cost of Facilities Capital

- Established criteria for the measurement and allocation of the cost of capital committed to facilities as an element of contract cost.

# CAS 414 - Definitions

- **Business Unit** means any segment of an organization, or an entire business organization which is not divided into segments.
- **Cost of capital committed to facilities** means an imputed cost determined by applying a cost of money rate to facilities capital.
- **Facilities capital** means the net book value of tangible capital assets and of those intangible capital assets that are subject to amortization.
- **Intangible capital asset** means an asset that has no physical substance, has 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 benefits it yields.
- **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 of possession beyond the current accounting period for the services it yields.










# CAS 414 – Fundamental Requirement

- Provides the criteria to measure and allocate cost of facilities capital.
- The allocated amount shall be used as a base to which a cost of money rate is applied.
- The cost of money rate shall be based on rates determined by the Secretary of the Treasury, pursuant to Public Law 92-41 (SecTreas)
- The cost of capital committed to facilities shall be separately computed for each contract using facilities capital cost of money factors computed for each cost accounting period

# CAS 414 – Techniques for Application

- The investment base used in computing the cost of money for facilities capital shall be computed from accounting data used for contract cost purposes.
- CASB-CMF is the form used to make the computation – Detailed in Appendix A
- The cost of money rate for any cost accounting period shall be the arithmetic mean of the Sec Treas interest rates
- Where cost of money is determined on a prospective basis, the cost of money rate shall be based on the most recent available Sec Treas rate
- A facilities capital cost of money factor shall be determined for each indirect cost pool to which a significant amount of facilities capital has been allocated and which is used to allocate indirect costs to final cost objectives.

# CoM Interest Rates

<i><b>Date Period</b></i>	<i><b>Interest Rate</b></i>	<i><b>Federal Register</b></i>
<i><b>Jul-23 through Dec-23</b></i>	4.875%	 <a href="#">Volume 88, Number 156 /8/15/2023 / Page 55501</a>
<i><b>Jan-23 through Jun-23</b></i>	4.625%	 <a href="#">Volume 88, Number 21 /2/1/2023 / Page 6812</a>
<i><b>Jul-22 through Dec-22</b></i>	4.000%	 <a href="#">Volume 87, Number 146 /8/1/2022 / Page 47034</a>
<i><b>Jan-22 through Jun-22</b></i>	1.625%	 <a href="#">Volume 87, Number 8 /1/12/2022 / Page 1839</a>
<i><b>Jul-21 through Dec-21</b></i>	1.125%	 <a href="#">Volume 86, Number 138, 07/22/2021, page 38813</a>
<i><b>Jan-21 through Jun-21</b></i>	0.875%	 <a href="#">Volume 86, Number 17, 01/28/2021, page 7457</a>
<i><b>Jul-20 through Dec-20</b></i>	1.125%	 <a href="#">Volume 85, Number 133, 07/10/20, page 41671</a>
<i><b>Jan-20 through Jun-20</b></i>	2.125%	 <a href="#">Volume 84, Number 249, 12/30/2019, page 72139</a>
<i><b>Jul-19 through Dec-19</b></i>	2.625%	 <a href="#">Volume 84, Number 208, 10/28/2019, page 57809</a>
<i><b>Jan-19 through Jun-19</b></i>	3.625%	

# Averaging Interest Rates

Rates

Jul-23 to Dec-23	4.875%
Jan-23 to June-23	4.625%
Jul-22 to Dec-22	4.000%

For FYE 9/30/2023

3 months	4.875%	1.219%
6 months	4.625%	2.313%
3 months	4.000%	<u>1.000%</u>
<b>Weighted Average Rate</b>		<b>4.531%</b>

For FYE 12/31/2023

6 months	4.875%	2.438%
6 months	4.625%	<u>2.313%</u>
<b>Weighted Average Rate</b>		<b>4.750%</b>

# CAS 414 – Form CAS-CMF

Form CASB-CMF		APPENDIX A FACILITIES CAPITAL COST OF MONEY FACTORS COMPUTATION						
CONTRACTOR:			ADDRESS:					
BUSINESS UNIT:								
COST ACCOUNTING PERIOD:		1. APPLICABLE COST OF MONEY RATE _____%	2. ACCUMULATION & DIRECT DISTRI- BUTION OF N.B.V.	3. ALLOCATION OF UNDISTRIBUTED	4. TOTAL NET BOOK VALUE	5. COST OF MONEY FOR THE COST ACCOUNTING PERIOD	6. ALLOCATION BASE FOR THE PERIOD	7. FACILITIES CAPITAL COST OF MONEY FACTORS
BUSINESS UNIT FACILITIES CAPITAL	RECORDED			BASIS OF ALLOCATION	COLUMNS 2 + 3	COLUMNS 1 x 4	IN UNIT(S) OF MEASURE	COLUMNS 5 + 6
	LEASED PROPERTY							
	CORPORATE OR GROUP							
	TOTAL							
	UNDISTRIBUTED							
	DISTRIBUTED							
OVERHEAD POOLS								
G & A EXPENSE POOLS								
TOTAL							//////////	//////////





# A working example of Form CASB-CMF

Form CASB-CMF							
APPENDIX A FACILITIES CAPITAL COST OF MONEY FACTORS COMPUTATION							
CONTRACTOR:		ABC Corp.		ADDRESS:			
BUSINESS UNIT:		A Division					
COST ACCOUNTING PERIOD:	1. APPLICABLE COST OF MONEY RATE	2. ACCUMULATION & DIRECT DISTRIBUTION OF N.B.V.	3. ALLOCATION OF UNDISTRIBUTED	4. TOTAL NET BOOK VALUE	5. COST OF MONEY FOR THE COST ACCOUNTING PERIOD	6. ALLOCATION BASE FOR THE PERIOD	7. FACILITIES CAPITAL COST OF MONEY FACTORS
YE 12/31/75	8.00%						
BUSINESS UNIT FACILITIES CAPITAL	RECORDED	\$ 8,270,000	BASIS OF ALLOCATION	COLUMNS 2 + 3	COLUMNS 1 X 4	IN UNIT(S) OF MEASURE	COLUMNS 5 ÷ 6
	LEASED PROPERTY	-					
	CORPORATE OR GROUP	450,000					
	TOTAL	\$ 8,720,000					
	UNDISTRIBUTED	\$ 3,450,000	↓				
	DISTRIBUTED	\$ 5,270,000					
OVERHEAD POOLS	Engineering	\$ 320,000	\$ 756,000	\$ 1,076,000	\$ 86,080	\$ 2,000,000	0.04304
	Manufacturing	4,500,000	2,250,000	6,750,000	540,000	3,000,000	0.18000
	Technical Computer	-	444,000	444,000	35,520	2,280	15.57895
		-	-	-	-	-	-
		-	-	-	-	-	-
		-	-	-	-	-	-
		-	-	-	-	-	-
G&A EXPENSE POOLS	G&A Expense	\$ 450,000	\$ -	\$ 450,000	\$ 36,000	\$ 36,700,000	0.00098
		-	-	-	-	-	-
		-	-	-	-	-	-
TOTAL		\$ 5,270,000	\$ 3,450,000	\$ 8,720,000	\$ 697,600		

# Fun Facts about CAS 414

- Regulations needed to be updated to incorporate cost of money computed through CAS 414 – read with FAR 31.205-10
- *Raytheon Co.* – Land for expansion is included
- *Gould Defense Systems, Inc.* – Goodwill can be included (However FAR 31.205-49 makes Goodwill amortization an unallowable cost)
- *Engineering Inc.* – Even if COM is waived in a proposal, it is still included in the cost of ownership for the purpose of determining allowable rental cost

# CAS 417

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# History

- CAS 417 - Cost of Money as an Element of the Cost of Capital Assets Under Construction
  - Published July 21, 1980
  - Took effect on December 15, 1980
- The last Standard promulgated by the original CASB
- A logical outgrowth of CAS 414
- OFPP was firmly opposed to CAS 417

# CAS 417 – CoM as an Element of the Cost of Capital Assets Under Construction

- Established criteria for the measurement of the cost of money attributable to capital assets under construction, fabrication, or development as an element of the cost of those assets.

# CAS 417 - Definitions

- **Intangible capital asset** means an asset that has no physical substance, has 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 benefits it yields.
- **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 of possession beyond the current accounting period for the services it yields.

# CAS 417 – Fundamental Requirement

- The cost of money applicable to the investment in tangible and intangible capital assets being constructed, fabricated, or developed for a contractor's own use shall be included in the capitalized acquisition cost of such assets

# CAS 417 – Techniques for Application

- The cost of money for an asset shall be calculated as follows:
  - The cost of money rate used shall be based on the Sec Treas rate
  - A representative investment amount is computed for each cost accounting period for each capital asset being constructed, fabricated, or developed
  - Other methods for calculating the cost of money to be capitalized, such as the method used for financial accounting and reporting, may be used, provided the resulting amount does not differ materially from the amount calculated using CAS 417
- If substantially all the activities necessary to get the asset ready for its intended use are discontinued, cost of money shall not be capitalized for the period of discontinuance. However, if such discontinuance arises out of causes beyond the control and without the fault or negligence of the contractor, cessation of cost of money capitalization is not required.



# CAS 417 – Illustration #1

- A contractor decided to build a major addition to this plant using both his own labor and outside subcontractors. It took 13 months to complete the building. The first 10 months of the construction period were in one cost accounting period. At the end of the cost accounting period the total charges, including cost of money computed in accordance with 9904.414, accumulated in the construction-in-progress account for this project amounted to \$750,000. However, most of the construction costs were incurred towards the end of the cost accounting period.
- In developing a method for determining a representative investment amount, appropriate consideration must be given to the rate at which costs have been incurred. Therefore, the contractor averaged the 10 month-end balances and determined that the average investment in the project was \$245,000.
- Two cost of money rates were in effect during the 10-month period; their time-weighted average was determined to be 8.6 percent. Application of the 8.6 percent rate for ten-twelfths of a year to the representative balance of \$245,000 resulted in the determination that \$17,558 should be added to the construction-in-progress account in recognition of the cost of money related to this project in its first cost accounting period

# CAS 417 – Illustration #2

- A contractor built a major addition with identical basic data to the prior illustration except that the costs were incurred at a fairly uniform rate throughout the period.
- Because of the pattern of cost incurrence, the contractor used beginning and ending balances of the cost accounting period to find the representative amounts - \$375,000.
- Application of the average interest rate of 8.6 percent for ten-twelfths of a year resulted in the determination that \$26,875 should be added to the construction-in-progress account in recognition of the cost of money related to this project in its first cost accounting period.

# Positioning for future sessions . . .

*November 30<sup>th</sup> – 2:00 Eastern . . .*

**Episode 10 – Insurance and CAS 419 – CAS 416 & the mystery of  
CAS 419**

GOVERNMENT CONTRACTING

Government Contracting

# Last Chance for Some Questions

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The information set forth in this presentation contains the analysis and conclusions of the author(s) based upon his/her/their research and analysis of industry information and legal authorities. Such analysis and conclusions should not be deemed opinions or conclusions by FORVIS or the author(s) as to any individual situation as situations are fact specific. The reader should perform its own analysis and form its own conclusions regarding any specific situation. Further, the author(s) conclusions may be revised without notice with or without changes in industry information and legal authorities. FORVIS has been registered in the U.S. Patent and Trademark Office, which registration is pending.

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