

Cost Accounting Standards Exemption for Overseas Contracts Eliminated - Effective October 11

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On August 10, 2011, the Cost Accounting Standards Board of the Office of Federal Procurement Policy eliminated the existing exemption from Cost Accounting Standards (CAS) coverage for contracts executed and performed entirely outside the United States, its territories and possessions. As a result, contractors performing work outside the United States on U.S. government contracts are now subject to complex and possibly costly CAS compliance requirements from which they were previously exempt.

This change, which becomes effective on October 11, 2011, has important implications for both U.S. and non-U.S. companies doing business with the federal government:

- Agencies such as DOD have noted that most of the activity with the overseas exemption has taken place at the subcontractor level; as a result, both prime and subcontractors on U.S. government contracts should be aware of the effect of this change on foreign subcontractors performing work outside the United States on U.S. government contracts.
- U.S. and non-U.S. companies with U.S. government prime contracts should verify that relevant clauses such as FAR 52.230-4 (Disclosure and Consistency of Cost Accounting Practices for Contracts Awarded to Foreign Concerns) are flowed down to subcontractors performing work outside the United States. Prime contractors should also take additional steps to protect themselves from liability for the potential CAS violations of foreign subcontractors, such as requiring subcontractor indemnification for the effects of such violations.
- More generally, because CAS coverage applies to contracts and not to contractors, companies with U.S. government contracts and subcontracts (regardless of place of performance) should carefully review existing contracts as well as solicitations under consideration for the inclusion of FAR 52.230-1 (Cost Accounting Standards Notices and Certification), which is included in all solicitations for proposed contracts potentially subject to CAS.
- Companies with CAS-covered contracts may be required to comply with various CAS provisions, including CAS 401 (which relates to consistency in cost estimation and reporting) and CAS 402 (which relates to consistency in allocating costs). Though the CAS Board has described CAS 401 and 402 as “minimal requirements,” they are in fact quite complex, and companies with CAS-covered contracts should plan to examine and possibly revise their

accounting practices in order to satisfy these and other CAS requirements.

- Companies with CAS-covered contracts should be aware of the breadth of CAS applicability. Certain CAS provisions apply to individual CAS-covered contracts of \$7.5 million or more (“modified” CAS coverage), while additional provisions apply to individual CAS-covered contracts of \$50 million or more or to multiple smaller CAS-covered contracts totaling \$50 million (“full” CAS coverage).
- Contractors and subcontractors should also be aware of the implications of CAS violations. Penalties for CAS violations can include correction of the noncompliance, submission of a description of accounting practice changes necessary for compliance, and adjustment of the contract price or cost allowance.
- Despite the elimination of this exemption from CAS, additional CAS exemptions remain. Both U.S. and non-U.S. prime contractors and subcontractors should review applicable regulations to determine whether other CAS exemptions may apply.

In issuing this final rule, the CAS Board responds to the National Defense Authorization Act for Fiscal Year 2009, which required the CAS Board to review whether the existing CAS exemption for overseas contracts would benefit the government. The CAS Board determined that the statutory basis for the exemption no longer exists, found no accounting basis for the overseas exemption, and foresaw that the application of CAS to overseas contracts would not create hardships for agencies, contractors or subcontractors.

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