

**9904.405-50 Techniques for application.**

(a) The detail and depth of records required as backup support for proposals, billings, or claims shall be that which is adequate to establish and maintain visibility of identified unallowable costs (including directly associated costs), their accounting status in terms of their allocability to contract cost objectives, and the cost accounting treatment which has been accorded such costs. Adherence to this cost accounting principle does not require that allocation of unallowable costs to final cost objectives be made in the detailed cost accounting records. It does require that unallowable costs be given appropriate consideration in any cost accounting determinations governing the content of allocation bases used for distributing indirect costs to cost objectives. Unallowable costs involved in the determination of rates used for standard costs, or for the indirect-cost bidding or billing, need be identified only at the time rates are proposed, established, revised or adjusted.

(b)(1) The visibility requirement of paragraph (a) of this subsection, may be satisfied by any form of cost identification which is adequate for purposes of contract cost determination and verification. The Standard does not require such cost identification for purposes which are not relevant to the determination of Government contract cost. Thus, to provide visibility for incurred costs, acceptable alternative practices would include:

(i) The segregation of unallowable costs in separate accounts maintained for this purpose in the regular books of account,

(ii) The development and maintenance of separate accounting records or workpapers, or

(iii) The use of any less formal cost accounting techniques which establishes and maintains adequate cost identification to permit audit verification of the accounting recognition given unallowable costs.

(2) Contractors may satisfy the visibility requirements for estimated costs either:

(i) By designation and description (in backup data, workpapers, etc.) of the amounts and types of any unallowable

costs which have specifically been identified and recognized in making the estimates, or

(ii) By description of any other estimating technique employed to provide appropriate recognition of any unallowable costs pertinent to the estimates.

(c) Specific identification of unallowable cost is not required in circumstances where, based upon considerations of materiality, the Government and the contractor reach agreement on an alternate method that satisfies the purpose of the Standard.

**9904.405-60 Illustrations.**

(a) An auditor recommends disallowance of certain direct labor and direct materials costs, for which a billing has been submitted under a contract, on the basis that these particular costs were not required for performance and were not authorized by the contract. The contracting officer issues a written decision which supports the auditor's position that the questioned costs are unallowable. Following receipt of the contracting officer's decision, the contractor must clearly identify the disallowed direct labor and direct material costs in his accounting records and reports covering any subsequent submission which includes such costs. Also, if the contractor's base for allocation of any indirect cost pool relevant to the subject contract consists of direct labor, direct material, total prime cost, total cost input, etc., he must include the disallowed direct labor and material costs in his allocation base for such pool. Had the contracting officer's decision been against the auditor, the contractor would not, of course, have been required to account separately for the costs questioned by the auditor.

(b) A contractor incurs, and separately identifies, as a part of his manufacturing overhead, certain costs which are expressly unallowable under the existing and currently effective regulations. If manufacturing overhead is regularly a part of the contractor's base for allocation of general and administrative (G&A) or other indirect expenses, the contractor must allocate the G&A or other indirect expenses to