

each final cost objective is substantially the same as it would have been if separately allocated under this provision.

(3) Insurance administration expenses which are material in relation to total insurance costs shall be allocated on the same basis as the related premium costs or self-insurance charge.

(c) *Records.* The contractor shall maintain such records as may be necessary to substantiate the amounts of premiums, refunds, dividends, losses, and self-insurance charges, paid or accrued, and the measurement and allocation of insurance costs. Memorandum records may be used to reflect any material differences between insurance costs as determined in accordance with this standard and as includable in financial statements prepared in accordance with generally accepted accounting principles.

[57 FR 14153, Apr. 17, 1992; 57 FR 34168, Aug. 3, 1992]

9904.416-60 Illustrations.

(a) Contractor A pays a company-wide property and casualty insurance premium for the policy term July 1, 1980, to July 1, 1983, and includes the entire amount as cost in its cost accounting period which ended December 31, 1980. This is a violation of 9904.416-50(a)(1)(i) in that only one-sixth of the policy term fell within the cost accounting period which ended December 31, 1980, and therefore only one-sixth of the premium should have been included in cost in that cost accounting period.

(b) Contractor B has a retrospectively rated worker's compensation insurance program. The policy term corresponds with the contractor's cost accounting period. Premium refunds are normally received and applied in the following cost accounting period. The contractor's practice is to include the entire gross premium in insurance cost in the cost accounting period in which it is paid and to credit the refund against insurance cost in the cost accounting period in which it is received. This practice conforms with 9904.416-50(a)(1)(i). The contractor could also, under the provisions of 9904.416-50(a)(1)(vi), have followed a consistent practice of estimating such refunds in

advance and including the estimated net premium in insurance cost.

(c) Contractor C establishes a self-insured program of life insurance for active and retired persons. The contractor pays death benefits directly to the beneficiaries of deceased employees and includes such payments in insurance costs at the time of payment. This practice complies with 9904.416-50(a)(2)(iii) which requires that only the actual losses be recognized unless a trustee reserve or fund is established in accordance with 9904.416-50(a)(1)(v).

(d) Instead of paying death benefits directly, contractor D purchases annual group term life insurance on active and retired persons and charges the premiums to insurance costs (with proper recognition for refunds and dividends). Contractor D's retired persons wish to be protected against possible discontinuance of the program. Contractor D, therefore, establishes a trustee fund. As each employee retires, contractor D deposits in the fund an amount which is equal to the premium on a paid-up policy for that employee, and he advises the trustee that the fund is to be used to continue to pay premiums on retired persons in the event the program is discontinued. The contractor also continues to purchase group term insurance on both active employees and retired persons and charges both the premiums and the deposits to insurance costs. This practice does not comply with 9904.416-50(a)(1)(iv)(D) which requires that if payments to accomplish the stated objectives of the reserve or funds are made from a source other than the reserve or fund, the payments into the fund shall be reduced accordingly.

NOTE: In this instance the contractor could comply with the standard by paying from the fund that portion of the group term premium which represented the retired persons or by reducing the deposits to the fund by an equivalent amount in accordance with 9904.416-50(a)(1)(iv)(D). This practice would also comply with the requirement of 9904.416-50(a)(1)(v)(C) that the amount added to the fund not be greater than an amount which would be required to fairly allocate the cost over the working lives of the active employees in the plan.

(e) Contractor E wishes to provide assurance of his life insurance program continuance to both active and retired

employees. He establishes a trustee fund in accordance with 9904.416-50(a)(1) (iv) and (v) and thereafter pays into the fund each year for each active employee an actuarially determined amount which will accumulate to the equivalent of the premium on a paid-up life insurance policy at retirement. He charges the annual payments to insurance costs. Benefits are paid directly from the fund (or the fund is used to pay the annual premiums on group term life insurance for all employees). This practice also complies with the requirement of 9904.416-50(a)(1)(v)(C) that the amount added to the fund not be greater than an amount which would be required to fairly allocate the cost over the working lives of the active employees in the plan.

(f) Contractor F has a fire insurance policy which provides that the first \$50,000 of any fire loss will be borne by the contractor. Because the risk of loss is dispersed among many physical units of property and the average potential loss per unit is relatively low, the actual losses in any period may be expected not to differ significantly from the projected average loss. Therefore, the contractor intends to let the actual losses represent the projected average loss for this exposure to risk. Property with an actual cash value of \$80,000 is destroyed in a fire. The contractor charges the \$50,000 of the loss not covered by the policy to insurance costs for contract costing purposes. The practice complies with the requirement of 9904.416-50(a)(2). However, had the contractor's plan been to make a self-insurance charge for such losses, then any difference between the self-insurance charge and actual losses in that cost accounting period would not have been allocable as an insurance cost.

(g) Contractor G is preparing to enter into a Government contract to produce explosive devices. The contractor is unable to purchase adequate insurance protection and must act as a self-insurer. There is a significant possibility of a major loss, against which the Government will not undertake to indemnify the contractor. The contractor, therefore, intends to make a self-insurance charge for this exposure to risk.

The contractor may, in accordance with 9904.416-50(a)(2)(i), use data obtained from other contractors or any other reasonable method of estimating the projected average loss in order to determine the self-insurance charge.

(h) Contractor H purchases liability insurance for all of its motor vehicles in a single, company-wide policy which contains a \$50,000 deductible provision. However, the company's management policy provides that when a loss is incurred in a segment, only the first \$5,000 of the loss will be charged to the segment; the balance of the loss will be absorbed at the home-office level and reallocated among all segments. Because the risk of loss is dispersed among many physical units and the maximum potential loss per occurrence is limited, the actual losses in any cost accounting period may be expected not to differ significantly from the projected average loss. Therefore, the contractor intends to let the actual losses represent the projected average loss for this exposure to risk. An analysis of the loss experience shows that many past losses exceeded \$5,000. Contractor H's practice of allocating the loss in excess of \$5,000 to the home office is a violation of 9904.416-50(b)(1). The limit of \$5,000 cannot realistically be considered a measure of a "catastrophic" loss when losses frequently exceed this amount, and the use of a limit this low would obscure segment loss experience.

9904.416-61 Interpretation. [Reserved]

9904.416-62 Exemption.

None for this Standard.

9904.416-63 Effective date.

This Standard is effective as of April 17, 1992. Contractors with prior CAS-covered contracts with full coverage shall continue this Standard's applicability upon receipt of a contract to which this Standard is applicable. For contractors with no previous contracts subject to this Standard, this Standard shall be applied beginning with the contractor's next full fiscal year beginning after the receipt of a contract to which this Standard is applicable.