DEPARTMENT OF DEFENSE

GENERAL SERVICES ADMINISTRATION

NATIONAL AERONAUTICS AND SPACE ADMINISTRATION

48 CFR Part 31

[FAC 2005–10; FAR Case 2004–014; Item VI; Docket 2006–0020, Sequence 7]

RIN 9000–AK19

Federal Acquisition Regulation; FAR Case 2004–014, Buy-Back of Assets

AGENCIES: Department of Defense (DoD), General Services Administration (GSA), and National Aeronautics and Space Administration (NASA).

ACTION: Final rule.

SUMMARY: The Civilian Agency Acquisition Council and the Defense Acquisition Regulations Council (Councils) have agreed on a final rule amending the Federal Acquisition Regulation (FAR) by revising the contract cost principle regarding depreciation costs. The final rule adds language which addresses the allowability of depreciation costs of reacquired assets involved in a sale and leaseback arrangement.

DATES: *Effective Date:* July 28, 2006.

FOR FURTHER INFORMATION CONTACT: For clarification of content, contact Mr. Jeremy Olson, at (202) 501–4755. Please cite FAC 2005–10, FAR case 2004–014. For information pertaining to status or publication schedules, contact the FAR Secretariat at (202) 501–3221.

SUPPLEMENTARY INFORMATION:

A. Background

In response to public comments related to proposed language at FAR 31.205–16 regarding the recognition of gains and losses associated with a sale and leaseback arrangement (submitted under FAR case 2002–008 by the FAR Part 31 Ad Hoc Committee), the Committee revised FAR 31.205–16 to state that the disposition date is the date of the sale and leaseback arrangement. FAR case 2002–008 addressed three cost principles. A new case, FAR case 2004–005, was later split-off and only addressed sale and leaseback arrangements.

During the deliberations of FAR case 2002–008, DCAA brought to the Committee's attention a concern regarding the cost treatment when a contractor subsequently re-acquires title to an asset under a sale and leaseback arrangement. The Committee recognized this concern, not just for sale and leaseback arrangements, but also for assets that are purchased, depreciated, sold, and subsequently repurchased. As such, the issue involves a myriad of situations where a contractor depreciates an asset or charges cost of ownership in lieu of lease costs, disposes of that asset, and then reacquires the asset.

For example, in a sale and leaseback arrangement, a contractor may purchase an asset in 2001. The contractor then enters into a sale and leaseback arrangement in 2004, with a ten year lease. At the end of 2014, the contractor reacquires the asset. The question is if and how much the contractor can charge for depreciation costs or usage charge related to that asset.

In addition, consider a purchase of an asset in 2003 (without a sale leaseback arrangement). The contractor depreciates the asset for 15 years, and then in 2018 sells the asset. In 2020, the contractor reacquires the asset. Again the question is if and how much the contractor can charge for depreciation costs or usage charges related to the asset.

The Committee recognized this issue required research and deliberation. The Committee therefore recommended that the DAR Council establish a new case to address this buyback issue. The DAR Council concurred with the recommendation, established the subject case (FAR case 2004–014), and assigned the case to the FAR Acquisition Finance Team.

On August 31, 2004, the FAR Acquisition Finance Team issued its report on the subject case. The report noted that there are situations when a contractor can and will reacquire an asset after relinquishing title, in either a sale and leaseback arrangement or simply a typical sale and subsequent repurchase. After extensive discussion within the Team and respective members' Agencies, the Team concluded that the only area that currently requires coverage is a sale and leaseback arrangement.

The report noted that a contractor should not benefit or be penalized for entering into a sale and leaseback arrangement, *i.e.*, the Government should reimburse the contractor the same amount for the subject asset as if the contractor had retained title throughout the service life of the asset. Therefore, the Team recommended revised language for the determination of allowable depreciation expense that includes consideration of—

- The depreciation expense taken prior to the sale and leaseback arrangement;
- Any gain or loss recognized in accordance with FAR 31.205–16(b); and
- Any depreciation expense included in the calculation of the normal cost of ownership for the limitations at FAR 31.205–36(b)(2) and 31.205–11(h)(1).

A proposed rule was published in the **Federal Register** at 70 FR 34080, June 13, 2005. In response to the proposed rule, comments were received from two commenters. These commenters oppose the proposed rule, asserting that the rule penalizes contractors, ignores GAAP and CAS, ignores the requirement to pay a contractor a reasonable cost, and imposes an administrative burden. In addition, one commenter asserts that the rule would cause a situation where a given asset's value and allowable depreciation will differ depending on the relationships of the parties from whom the asset is acquired. The Councils disagree with each of the commenters assertions. As such, the final rule is identical to the proposed rule published on June 13, 2005.

Public Comments

1. Contractor is penalized under proposed rule.

Comment: The commenters assert that the proposed rule is not consistent with the Government position that a contractor should not benefit or be penalized for entering into a sale and leaseback arrangement. The commenters further assert that the recent changes to FAR 31.205–11, 31.205–16, and 31.205–36 have constructed parameters that penalize a contractor for having owned its facilities at any time during contract performance. The commenters state that these rules ensure the Government never pays more than the initial capitalized cost of an asset regardless of changes in ownership, changes in invested capital or changes in market rate.

Councils' Response: When a contractor purchases an asset and holds that asset for the entire period of contact performance, the Government pays no more than the initial capitalized cost of an asset. This has been the longstanding policy of the Government. The Councils believe this same policy should apply when a contractor re-acquires an asset for which there was a sale and leaseback arrangement, *i.e.*, the Government should pay no more than the initial capitalized cost of the asset. The Councils believe the proposed rule accomplishes this objective.

2. GAAP and CAS 404.

Comment: The commenters assert that limiting allowable depreciation costs to that which would have resulted if the contractor had retained title throughout the service life of the asset ignores

fundamental Cost Accounting Standard (CAS) 404 requirements and Generally Accepted Accounting Principles (GAAP) for an asset to be capitalized at its purchase price, even if that purchase is the reacquisition of a previously owned asset.

Councils' Response: CAS provides criteria for measuring, assigning, and allocating costs for CAS-covered contracts. However, FAR part 31 provides the criteria for allowability of those costs. Under the proposed and final rules, the costs are measured, assigned, and allocated in accordance with CAS for contracts that are subject to CAS 404. The proposed and final rules provide for a limitation on the allowability of those measured, assigned, and allocated costs. Thus, the proposed rule does not conflict with CAS.

In regards to GAAP, there are a number of cost principles, as well as some cost accounting standards, that deviate from GAAP. This deviation occurs for a variety of reasons. In many cases, the deviation is necessary because GAAP is focused on reporting to investors, while FAR focuses on cost reimbursement for Government contracts.

In the subject case, the Councils believe that neither CAS nor GAAP provide adequate coverage when a contractor re-acquires an asset that was part of a sale and leaseback arrangement. The Councils believe this final rule is necessary to provide for consistent reimbursement treatment for capital assets, *i.e.,* the Government pays no more than the initial capitalized cost of the asset.

3. Contractor should be reimbursed a reasonable cost.

Comment: The commenters assert that the proposed rule ignores the basic principle that a contractor should be reimbursed for reasonable cost incurred in the course of business.

Councils' Response: The Councils do not believe the contractor is reimbursed an unreasonable cost under the proposed rule. The Councils believe the longstanding policy of reimbursement based on the initial capitalized cost is reasonable. The Councils further believe it is unreasonable to reimburse a contractor for additional costs merely because it sold an asset and then chose to re-acquire it shortly afterwards.

4. Administrative burden.

Comment: The commenters state that the administrative time required to document and track the ownership trail of the asset will become needlessly complex and excessively burdensome.

Councils' Response: In drafting the proposed rule, the Councils considered the administrative burden of tracking these assets for long periods of time. The application of this provision is limited to instances where the asset generated either depreciation expense or cost of money during the most recent accounting period prior to the date of reacquisition. The Councils do not believe it is an administrative burden to obtain the necessary records in such cases, since the sale and leaseback arrangement would have expired no earlier than the accounting period prior to when the asset is re-acquired. The Councils note that the application period for re-acquired assets is also consistent with CAS 404–50(d)(1), which provides the capitalization criteria for the acquisition of assets resulting from a business combination.

5. Asset value and allowable depreciation differ based on relationships of the parties.

Comment: One commenter asserts that the rule would cause a situation where a given asset's value and allowable depreciation will differ depending on the relationships of the parties from whom the asset is acquired. The commenter states that when a contractor that owns the building and then re-acquires the asset is compared to a contractor that is conducting business under an operating lease, the contractor that leases the building is reimbursed significantly more costs than the contractor that owned the building. The commenter asserts that the contractor that owned the building is forced to absorb millions of dollars of costs deemed unallowable for Government costing purposes.

Team Response: The subject rule does not establish a new policy of providing differing reimbursement based on whether the contractor leases or owns the asset (this is already an established policy). Under FAR part 31, a contractor that enters into an operating lease is reimbursed based on actual rental payments made. On the other hand, a contractor that purchases an asset is reimbursed based on the actual costs of ownership, which includes depreciation. As a result, the amount a contractor is reimbursed differs depending on whether the contractor leases or owns the asset. Under the subject rule, the reimbursement for purchased assets continues to be based on cost of ownership, i.e., the basis for reimbursement is the initial capitalized cost of the asset.

This is not a significant regulatory action and, therefore, was not subject to review under Section 6(b) of Executive Order 12866, Regulatory Planning and Review, dated September 30, 1993. This rule is not a major rule under 5 U.S.C. 804.

B. Regulatory Flexibility Act

The Department of Defense, the General Services Administration, and the National Aeronautics and Space Administration certify that this final rule will not have a significant economic impact on a substantial number of small entities within the meaning of the Regulatory Flexibility Act, 5 U.S.C. 601, *et seq.*, because most contracts awarded to small entities use simplified acquisition procedures or are awarded on a competitive, fixed-price basis, and do not require application of the cost principles and procedures discussed in this rule. For Fiscal Year 2003, only 2.4% of all contract actions were cost contracts awarded to small business.

C. Paperwork Reduction Act

The Paperwork Reduction Act does not apply because the proposed changes to the FAR do not impose information collection requirements that require the approval of the Office of Management and Budget under 44 U.S.C. 3501, *et seq.*

List of Subjects in 48 CFR Part 31

Government procurement.

Dated: June 20, 2006.

Linda Nelson,

Deputy Director, Contract Policy Division.

■ Therefore, DoD, GSA, and NASA amend 48 CFR part 31 as set forth below:

PART 31–CONTRACT COST PRINCIPLES AND PROCEDURES

■ 1. The authority citation for 48 CFR part 31 continues to read as follows:

Authority: 40 U.S.C. 121(c); 10 U.S.C. chapter 137; and 42 U.S.C. 2473(c).

■ 2. Amend section 31.205–11 by revising paragraph (g); removing paragraph (h); and redesignating paragraph (i) as (h). The revised text reads as follows:

31.205–11 Depreciation.

* * * * *

(g) Whether or not the contract is otherwise subject to CAS the following apply:

(1) The requirements of 31.205–52 shall be observed.

(2) In the event of a write-down from carrying value to fair value as a result of impairments caused by events or changes in circumstances, allowable depreciation of the impaired assets is limited to the amounts that would have been allowed had the assets not been

written down (see 31.205–16(g)). However, this does not preclude a change in depreciation resulting from other causes such as permissible changes in estimates of service life, consumption of services, or residual value.

(3)(i) In the event the contractor reacquires property involved in a sale and leaseback arrangement, allowable depreciation of reacquired property shall be based on the net book value of the asset as of the date the contractor originally became a lessee of the property in the sale and leaseback arrangement—

(A) Adjusted for any allowable gain or loss determined in accordance with 31.205–16(b); and

(B) Less any amount of depreciation expense included in the calculation of the amount that would have been allowed had the contractor retained title under 31.205–11(h)(1) and 31.205–36(b)(2).

(ii) As used in this paragraph (g)(3), reacquired property is property that generated either any depreciation expense or any cost of money considered in the calculation of the limitations under 31.205–11(h)(1) and 31.205–36(b)(2) during the most recent accounting period prior to the date of reacquisition.

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31.205–16 [Amended]

■ 3. Amend section 31.205–16 by—

■ a. Removing from the introductory text of paragraph (b) ''31.205–11(i)(1)'' and adding ''31.205–11(h)(1)'' in its place; and

■ b. Removing from paragraph (c) ''31.205–11(i)'' and adding ''31.205–11(h)'' in its place.

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DEPARTMENT OF DEFENSE

GENERAL SERVICES ADMINISTRATION

NATIONAL AERONAUTICS AND SPACE ADMINISTRATION

48 CFR Parts 8, 33, and 52

[FAC 2005–10; Item VII; Docket 2006–0021]

Federal Acquisition Regulation; Technical Amendments

AGENCIES: Department of Defense (DoD), General Services Administration (GSA), and National Aeronautics and Space Administration (NASA).

ACTION: Final rule.

SUMMARY: This document amends the Federal Acquisition Regulation (FAR) to make editorial changes.

DATES: Effective Date: June 28, 2006.

FOR FURTHER INFORMATION CONTACT The FAR Secretariat, Room 4035, GS Building, Washington, DC, 20405, (202) 501–4755, for information pertaining to status or publication schedules. Please cite FAC 2005–10, Technical Amendments.

SUPPLEMENTARY INFORMATION:

List of Subjects in 48 CFR Parts 8, 33, and 52

Government procurement.

Dated: June 20, 2006.

Ralph De Stefano,

Director, Contract Policy Division.

■ Therefore, DoD, GSA, and NASA amend 48 CFR parts 8, 33, and 52 as set forth below:

■ 1. The authority citation for 48 CFR parts 8, 33, and 52 continues to read as follows:

Authority: 40 U.S.C. 121(c); 10 U.S.C. chapter 137; and 42 U.S.C. 2473(c).

PART 8—REQUIRED SOURCES OF SUPPLIES AND SERVICES

■ 2. Revise section 8.714(a)(1) and (2) to read as follows:

8.714 Communications with the central nonprofit agencies and the Committee.

(a) * * *

(1) National Industries for the Blind, 1310 Braddock Place, Alexandria, VA 22314–1691, (703) 310–0500; and

(2) NISH, 8401 Old Courthouse Road, Vienna, VA 22182, (571) 226–4660.

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PART 33—PROTESTS, DISPUTES, AND APPEALS

33.102 [Amended]

■ 3. Amend section 33.102 by removing from the end of paragraph (b)(1) the word ''and''; and by removing the period from the end of paragraph (b)(2) and adding ''; and'' in its place.

PART 52—SOLICITATION PROVISIONS AND CONTRACT CLAUSES

■ 4. Amend section 52.208–9 by revising the date of the clause and paragraphs (c)(1) and (2) to read as follows:

52.208–9 Contractor Use of Mandatory Sources of Supply or Services.

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CONTRACTOR USE OF MANDATORY SOURCES OF SUPPLY OR SERVICES (JUN 2006)

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(c) * * *

(1) National Industries for the Blind, 1310 Braddock Place, Alexandria, VA 22314–1691, (703) 310–0500; and

(2) NISH, 8401 Old Courthouse Road, Vienna, VA 22182, (571) 226–4660.

(End of clause)

■ 5. Amend section 52.212–3 by revising the date of the clause; and removing from the heading of paragraph (h) ''Executive Order 12549'' and adding ''Executive Order 12689'' in its place. The revised text reads as follows:

52.212–3 Offeror Representations and Certifications—Commercial Items.

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OFFEROR REPRESENTATIONS AND CERTIFICATIONS—COMMERCIAL ITEMS (JUN 2006)

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■ 6. Amend section 52.225–11 by revising the date of the clause; and removing from paragraph (b)(2) the comma after ''or'' in the first line. The revised text reads as follows:

52.225–11 Buy American Act—Construction Materials under Trade Agreements.

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BUY AMERICAN ACT—CONSTRUCTION MATERIALS UNDER TRADE AGREEMENTS (JUN 2006)

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[FR Doc. 06–5705 Filed 6–27–06; 8:45 am]

BILLING CODE 6820–EP–S

DEPARTMENT OF DEFENSE

GENERAL SERVICES ADMINISTRATION

NATIONAL AERONAUTICS AND SPACE ADMINISTRATION

48 CFR Chapter 1

Docket FAR—2006—0023

Federal Acquisition Regulation; Federal Acquisition Circular 2005–10; Small Entity Compliance Guide

AGENCIES: Department of Defense (DoD), General Services Administration (GSA), and National Aeronautics and Space Administration (NASA).

ACTION: Small Entity Compliance Guide.

SUMMARY: This document is issued under the joint authority of the Secretary of Defense, the Administrator of General Services and the Administrator of the National Aeronautics and Space Administration. This *Small Entity Compliance Guide* has been prepared in accordance with Section 212 of the Small Business