

Case 68-193 - Recommended Changes to ASPR 15-205.23, Organization Costs. The Committee approved a draft letter transmitting the revised 15-205.23 and 15-205.47 language to Industry for comment. The staff was requested to finalize the letter for the Chairman's signature.

CASE SUSPENDED  
(6 November 1968)

Case 68-193 - Recommended Changes to ASPR 15-205.23, Organization Costs. Copies of the Chairman's letter to Industry of 14 November 1968, transmitting the revised language in 15-205.23 and 15-205.47, with respect to mergers and acquisitions as a part of organization and reorganization costs for comment, were distributed to the members for information.

(15 November 1968)

Case 68-193 - Recommended Changes to ASPR 15-205.23, Organization Costs Copies of the comments received from Industry and other Government Agencies on the proposed changes to ASPR 15-205.23 "Organization Costs" and 15-205.47 "Economic Planning Costs" were distributed to the members. The Committee determined that the comments should be referred to the Section XV, Part 2 Subcommittee for consideration, recommendations, and identification of any major Industry comments which are not adopted, together with the Subcommittee's rationale for rejection. (Copies of the comments were provided the Subcommittee Chairman for distribution to the Subcommittee Members.)

Members of the Section XV, Part 2 Subcommittee are:

Army	- James H. Fleck, AMC
Navy	- Paul J. Webb, NAVMAT
Air Force	- John F. Snight, AFSPP-BB
DSA	- Lauren Lampert, DCAS
DCAA	- Bertold Bodenheimer, Chairman

The Subcommittee was requested to present a report for consideration by 24 March.

(19 February 1969)

3. Case 68-193 - Recommended Changes to ASPR 15-205.23, Organization Costs. The Committee undertook consideration of a report from the Section XV, Part 2 Subcommittee, dated 24 March 1969, presenting recommended changes to 15-205.23 and in 15-205.47, after review of the comments received from Industry and other Government Agencies on the proposed ASPR changes, making the costs related to mergers and acquisitions specifically unallowable. During consideration of the Subcommittee report, the Subcommittee Chairman advised the members that as a result of the subject case the Subcommittee is going to undertake a review of the 15-205.6 paragraph and consider whether there is a need for a general caveat with respect to the treatment to be accorded in-house labor costs of unallowable functions. The Committee concurred in the Subcommittee's report and approved the language as follows:

"15-205.23 Organization Costs (CWAS-NA). Expenditures in connection with (i) planning or executing the organization or reorganization in the corporate structure of a business, including mergers and acquisitions, or (ii) raising capital, are unallowable. Such expenditures include but are not limited to incorporation fees and costs of attorneys, accountants, brokers, promoters and organizers, management consultants and investment counsellors, whether or not employees of the contractor."

"15-205.47 Economic Planning Costs.

(a) (CWAS) This category includes costs of generalized long-range management planning which is concerned with the future overall development of the contractors' business and which may take into account the eventual possibility of economic dislocations or fundamental alterations in those markets in which the contractor currently does business. Economic planning costs do not include organization or reorganization costs covered by 15-205.23."

By these changes, the Committee intended to clarify the fact that in-house costs for reorganization, including acquisitions and mergers, are unallowable.

The foregoing was APPROVED FOR PRINTING in the next ASPR Revision (Revision No. 4), not in a Defense Procurement Circular.

With respect to the general problem of implementing changes to the cost principles, it was pointed out to the Members that the current procedure of specifying a mandatory effective date with optional use by the Military Departments prior to that date created untold problems in determining when the cost principles would specify a mandatory effective date as of a time certain. This action will preclude the use of cost principles on an optional basis prior to the mandatory date for use of the principles by all elements of Defense.

Lastly, the Committee considered the letter from CODSIA which requested an opportunity to meet with representatives of the Committee prior to final action on the proposed change with respect to Organization Costs (15-205.23). The Committee noted that comments of CODSIA had been thoroughly considered and observed that no benefits would be derived by further meeting with their representatives to consider the same points. Accordingly, it was concluded that there was no necessity to meet with representatives of CODSIA on this matter. The Chairman will advise CODSIA of the Committee's conclusion.

CASE CLOSED  
(9 May 1969)

The foregoing was APPROVED FOR PRINTING in the next ASPR Revision (Revision No. 4), not in a Defense Procurement Circular.

In approving the above changes to the cost principles, it was pointed out to the Members that the current procedure of specifying a mandatory effective date with optional use by the Military Departments prior to that date created untold problems in determining when the cost principles actually were placed into effect. To overcome this difficulty, the Committee agreed that henceforth changes to the contract cost principles would specify a mandatory effective date as of a time certain. This action will preclude the use of cost principles on an optional basis prior to the mandatory date for use of the principles by all elements of Defense.

Lastly, the Committee considered the letter from CODSIA which requested an opportunity to meet with representatives of the Committee prior to final action on the proposed change with respect to Organization Costs (15-205.23). The Committee noted that comments of CODSIA had been thoroughly considered and observed that no benefits would be derived by further meeting with their representatives to consider the same points. Accordingly, it was concluded that there was no necessity to meet with representatives of CODSIA on this matter. The Chairman will advise CODSIA of the Committee's conclusion.

CASE CLOSED  
(9 May 1969)

Case 68-193 - Recommended Changes to ASPR 15-205.23, Organization Costs. Copies of the Chairman's letter to CODSIA, dated 26 May 1969, advising the Association of the Committee's action in approving the material developed under the subject case for printing, were distributed to the members.

(28 May 1969)

The minutes of 9 May 1969 were revised as follows:

Page 6, Item 3, Case 68-193 - Recommended Changes to ASPR 15-205.23, Organization Costs (9 May 1969):- the minute item was revised to read:

"3. Case 68-193 - Recommended Changes to ASPR 15-205.23, Organization Costs. The Committee undertook consideration of a report from the Section XV, Part 2 Subcommittee, dated 24 March 1969, presenting recommended modifications in the language of 15-205.23 and in 15-205.47, after review of the comments received from Industry and other Government Agencies on the proposed ASPR changes, clarifying the part that costs related to mergers and acquisitions are specifically unallowable. During consideration of the Subcommittee report, the Subcommittee Chairman advised the members that as a result of the subject case the Subcommittee is going to undertake a review of the 15-205.6 paragraph and consider whether there is a need for a general caveat with respect to the treatment to be accorded in-house labor costs of unallowable functions. The Committee concurred in the Subcommittee's report and approved the language as follows:

"15-205.23 Organization Costs (CWAS-NA). Expenditures in connection with (i) planning or executing the organization or reorganization in the corporate structure of a business, including mergers and acquisitions, or (ii) raising capital, are unallowable. Such expenditures include but are not limited to incorporation fees and costs of attorneys, accountants, brokers, promoters and organizers, management consultants and investment counsellors, whether or not employees of the contractor."

"15-205.47 Economic Planning Costs.

(a) (CWAS) This category includes costs of generalized long-range management planning which is concerned with the future overall development of the contractors' business and which may take into account the eventual possibility of economic dislocations or fundamental alterations in those markets in which the contractor currently does business. Economic planning costs do not include organization or reorganization costs covered by 15-205.23."

Case 68-193 - Recommended Changes to ASPR 15-205.23, Organization Costs.

Copies of a memorandum from the Air Force, dated 1 August 1968, with respect to interpretation of ASPR 15-205.23 and 15-205.31(d), were distributed to the members. The memorandum recommended that action be taken to resolve any ambiguity which may exist in the cost principles in the subject areas. The Committee was also provided copies of a memorandum from the Director, DCAA, dated 24 July 1968, addressing this identical problem. The Committee determined that the two memoranda should be referred to the Section XV, Part 2 Subcommittee for consideration and recommendations. Members of the Subcommittee are:

Army	- James H. Fleck, AMC
Navy	- Paul J. Webb, NAVMAT
Air Force	- John F. Snight, AFSPP-BB
DSA	- Lauren D. Lampert, DCAS-AFF
DCAA	- Bertold Bodenheimer, Chairman

The Subcommittee was requested to present a report for consideration by 7 October.

(7 August 1968)

2. Case 68-193 - Recommended Changes to ASPR 15-205.23, Organization Costs. The Committee considered a report from the Section XV, Part 2 Subcommittee, dated 30 September 1968, presenting a proposed clarification to 15-205.23 and 15-205.47 to highlight that the cost of mergers and acquisitions are unallowable. Following extended discussion, these paragraphs were revised, on a consensus basis, as follows:

"15-205.23 Organization Costs (CWAS-NA) Expenditures in connection with (i) planning or executing the organization or reorganization in the corporate structure of a business, including mergers and acquisitions, or (ii) raising capital, are unallowable. Such expenditures include but are not limited to incorporation fees and costs of attorneys, accountants, brokers, promoters and organizers, management consultants and investment counsellors, whether or not employees of the contractor."  
\* \* \* \* \*

"15-205.47 Economic Planning Costs.

(a) (CWAS) This category includes costs of generalized long-range management planning which is concerned with the future over-all development of the contractor's business and which may take into account the eventual possibility of economic dislocations or fundamental alterations in those markets in which the contractor currently does business. Economic planning costs do not include organization or reorganization costs covered by 15-205.23."

The Army Member, while not objecting to the foregoing changes, expressed concern over the fact that some mergers or acquisitions may be beneficial to the Government, and hence should be considered as allowable items of cost. It was the consensus of the Committee that such situations could not be measured.

It was suggested that 15-205.23 also specify that proxy solicitations and related costs incident to mergers and acquisitions are unallowable. The Committee, however, concluded that the revised language of 15-205.23, when read in conjunction with 15-205.24, makes it clear that **abnormal proxy solicitation costs such as costs incurred by management in resisting acquisitions by another corporation, are unallowable.**

The foregoing language was approved for forwarding to Industry for comment. The Chairman of the Section XV, Part 2 Subcommittee volunteered to draft a letter transmitting the foregoing to Industry.

The Committee also considered and noted a memorandum from the Director, Procurement Analysis and Planning, dated 11 October 1968, commenting on the Subcommittee report, in light of the recent Secretary of Defense's actions toward contributing to the resolution of the pressing social problem as advanced in his speech before NSIA.

CASE SUSPENDED  
(30 October 1968)



OFFICE OF THE ASSISTANT SECRETARY OF DEFENSE  
WASHINGTON, D.C. 20301

INSTALLATIONS AND LOGISTICS

14 November 1968

The attached proposed revisions to ASPR 15-205.23 and 15-205.47 are submitted for your review and comment.

Recently we have noted a decided increase in contractors' costs of contemplated or accomplished mergers and acquisitions of other companies. Most often these costs include expenses for attorneys, accountants, management consultants and the like. Costs of both contractor employees and outside services are involved. In some cases, at least a portion of such costs have not been claimed for reimbursement. In other cases, all or a portion of such costs have been disapproved. Guidance is required to assure consistent accounting for these costs.

Mergers and acquisitions have generally been considered to be in the nature of organizations or reorganizations, the costs of which are presently unallowable under ASPR 15-205.23. The attached revisions accordingly identify mergers and acquisitions as a part of organization and reorganization costs. To assure equitable treatment among contractors with in-house capabilities for these activities and those without such capabilities, the attached revision also clarifies that both the cost of employees and outside services are part of organization and reorganization expenses.

We would appreciate receiving your comments (25 copies if convenient) within the next 60 days.

Sincerely,

A handwritten signature in cursive script, appearing to read "E. C. Chapman".

E. C. CHAPMAN  
Captain, SC, USN  
Chairman, ASPR Committee

Enclosure

30 October 1968

"15-205.23 Organization Costs (CWAS-NA) Expenditures in connection with (i) planning or executing the organization or reorganization in the corporate structure of a business, including mergers and acquisitions, or (ii) raising capital, are unallowable. Such expenditures include but are not limited to incorporation fees and costs of attorneys, accountants, brokers, promoters and organizers, management consultants and investment counsellors, whether or not employees of the contractor."

\* \* \* \* \*

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(a) (CWAS) This category includes costs of generalized long-range management planning which is concerned with the future over-all development of the contractor's business and which may take into account the eventual possibility of economic dislocations or fundamental alterations in those markets in which the contractor currently does business. Economic planning costs do not include organization or reorganization costs covered by 15-205.23."

68-193

March 24, 1969

MEMORANDUM FOR CHAIRMAN, ASPR COMMITTEE

SUBJECT: Case 68-193, Recommended Changes to 15-205.23,  
Reorganization Costs (Mergers and Acquisitions)

I. PROBLEM

To review Industry and other Government agencies' comments on proposed changes to 15-205.23 and 15-205.47 making costs related to mergers and acquisitions specifically unallowable.

II. RECOMMENDATION

That 15-205.23, Organization Costs, and 15-205.47, Economic Planning costs be revised as approved by the ASPR Committee on October 30, 1968. The revised paragraphs are shown on Tab A attached, for ready reference.

III. DISCUSSION

A. Background. A DCAA memorandum of July 24, 1968, and an Air Force memorandum of August 1, 1968, both recommended revisions to 15-205.23 to clarify allowability of costs related to a contractor's merger with or acquisition of another company. It was also recommended that the principle be clarified in regard to in-house costs. Changes to 15-205.23 and 15-205.47 implementing these recommendations were approved by the ASPR Committee on October 30, 1968, and submitted to Industry and other Government agencies for comment. These comments have now been received and are discussed below.

B. Summary of Industry and Other Government Agency Comments. The Atomic Energy Commission, the General Accounting Office, the General Services Administration, the National Aeronautics and Space Administration, and the Associated General Contractors of America concurred in, or did not oppose, the revision. The Council of Defense and Space Industries Associations (CODSIA) had no objection to the change to 15-205.47, but opposed the change to 15-205.23. CODSIA proposed an alternate revision to 15-205.23 which would generally make costs of mergers and acquisitions specifically allowable. The Financial Executive Institute (FEI) acknowledged that a problem exists and recommended certain alternative solutions. The CODSIA and FEI comments are discussed in detail in C. below.

C. Specific Industry Comments and Recommendations.

1. It would be inequitable for the Government to disallow the costs of mergers and acquisitions while accepting the benefits. The benefits include (i) a broader base for burden application; (ii) increased

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Reorganization Costs (Mergers and Acquisitions)

financial strength of the resulting company; and, (iii) improvement in the technological and manufacturing skills and capabilities of the resulting company. (CODSIA)

Subcommittee Comment: The Government benefits to which CODSIA refers are, in the opinion of the Subcommittee, largely illusory. In most cases, the merged or acquired companies retain their separate identities and overhead structure, so broader bases would not necessarily result. Furthermore, a broader base, of course, also means increased overhead expenses. The end result quite possibly could be a higher, rather than a lower, overhead rate. Similarly, the increased financial strength claimed by CODSIA is doubtful at best. Entirely the opposite may be true. In fact, it is in part the prevalence of so-called debt financing of many mergers and acquisitions that has caused recent Congressional concern about conglomerates. Finally, in the opinion of the Subcommittee the improvement in technological and manufacturing skills claimed by CODSIA is too conjectural to be considered a valid benefit.

2. Determination of the cost of employees related to mergers and acquisitions is virtually impossible since corporate accountants, attorneys and other executives do not normally identify the time spent in discharging their multiple management responsibilities. (CODSIA)

Subcommittee Comment: The Subcommittee recognizes that identification of employees' time may cause a problem. However, there is ample precedent for requiring identification of employee costs related to unallowable functions. A similar problem prevails in connection with organization and reorganization costs (15-205.23); raising capital (15-205.17 and 15-205.23); advertising (15-205.1 and 15-205.33); patents (15-205.26); and other costs. Ideally, a contractor's accounting procedure provides for identification of in-house costs related to unallowable functions. In the absence of such identification, however, auditors have in the past made reasonable estimates and can continue to do so.

3. The terms "organization" and "reorganization" are ambiguous in their general usage, but usually involve three types of costs: (i) fees or taxes related to incorporation, stock issues, stock registration, SEC



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registration statements, and the like; (ii) legal fees, audit fees and stockholders' meetings related to mergers and acquisitions; and, (iii) internal planning aimed at internal reorganization. Under recommended alternative language, the first two categories of cost would be allowable if costs benefit the Government, while the third category would be specifically allowable. (FEI)

Subcommittee Comment: In the opinion of the Subcommittee, the FEI recommendation avoids the issue involved in this case. The issue is the allowability of merger and acquisition costs, within definition of organization and reorganization. The Subcommittee continues to be of the view, as stated in its report of September 30, 1968, that the definition of organization and reorganization encompasses mergers and acquisitions. In the opinion of the Subcommittee, the conclusion is inescapable that the end result of a merger or acquisition is substantially the same as that of an organization or reorganization, i.e., a new or different entity emerges. Under the circumstances, there appears to be no valid reason why the costs should not be treated identically. In addition, the Subcommittee does not subscribe to the theory that the allowability of organization and reorganization costs, including merger and acquisition costs, should depend on benefit, as FEI suggests. As noted in paragraph 2. above, the benefits to the Government are normally too remote to form a valid basis for the allowability of the costs.

#### IV. MISCELLANEOUS MATTERS

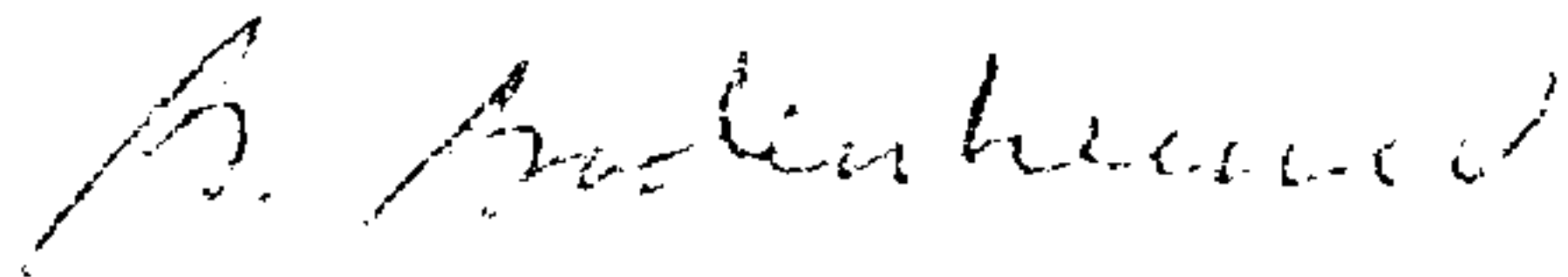
A. Meeting with Industry. CODSIA requests a meeting with representatives of the ASPR Committee if their recommendations are not adopted. FEI indicates a willingness to discuss the proposed changes. While the Subcommittee does not oppose such a meeting, it is considered doubtful whether significant additional information would result.

B. Effective Date. The Subcommittee understands that in the past there has been some confusion as to the effective date of any revised cost principle, particularly when it is first published in a DPC. Accordingly,

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Reorganization Costs (Mergers and Acquisitions)

the Subcommittee recommends that upon publication of any revision as a result of this and other cases, the DPC or Notes and Filing Instructions specify the precise effective date of the revised principle.



B. BODENHEIMER  
Chairman, Part 2,  
Section XV Subcommittee

Attachment  
Tab A

Part 2, Section XV Subcommittee

DoD Representatives

Mr. J. Fleck - Army  
Mr. R. Lynch - Navy  
Major J. Gilliland - USAF  
Mr. L. D. Lampert - DCAS

Other Agency Representatives

Mr. J. McGee - GSA  
Mr. L. Ohnstad - AEC  
Mr. M. Asch - NASA

OASD(C) Consultant

Mr. O. Sollom

TAB A  
Case No. 68-193  
March 24, 1969

REVISED ASPR 15-205.23 and 15-205.47  
AS APPROVED AND SUBMITTED TO INDUSTRY

15-205.23 Organization Costs (CWAS-NA) Expenditures in connection with (i) planning or executing the organization or reorganization in the corporate structure of a business, including mergers and acquisitions, or (ii) raising capital, are unallowable. Such expenditures include but are not limited to incorporation fees and costs of attorneys, accountants, brokers, promoters and organizers, management consultants and investment counsellors, whether or not employees of the contractor.

15-205.47 Economic Planning Costs.

(a) (CWAS) This category includes costs of generalized long-range management planning which is concerned with the future over-all development of the contractor's business and which may take into account the eventual possibility of economic dislocations or fundamental alterations in those markets in which the contractor currently does business. Economic planning costs do not include organization or reorganization costs covered by 15-205.23.

September 30, 1968

MEMORANDUM FOR THE CHAIRMAN, ASPR COMMITTEE

SUBJECT: Case 68-193, Recommended Changes to 15-205.23, Organization Costs

I. PROBLEM

To consider and make recommendation on DCAA and Air Force memoranda of July 24, 1968, and August 1, 1968, respectively, recommending changes to 15-205.23 making the costs of mergers and acquisitions unallowable.

II. RECOMMENDATIONS

A. That 15-205.23 be clarified to make costs of mergers and acquisitions unallowable in accordance with Tab A attached.

B. That 15-205.47(a) be clarified to specifically exclude from allowable costs of economic planning the costs of organization and reorganization, in accord with Tab A attached.

III. DISCUSSION

A. As noted in the DCAA memorandum, contractors are engaging in intensified activity in the areas of planning and accomplishing reorganizations for the purposes of diversification. While not all of the costs of such activities are necessarily claimed, those costs that are claimed can nevertheless be substantial. One major contractor is known to have incurred in one year \$1,777,000 for identifiable costs of activities related to a merger with another corporation. This amount represents only the costs of outside services and does not include the costs of the contractor's own employees engaged in such activities. The contractor included \$669,000 of this amount in overhead allocated to Government contracts. Claimed amounts included such items as management consulting fees, legal fees, fees to investment counselors and the like. Substantial costs for such activities, both in-house and for outside services, are expected to continue.

B. The Air Force memorandum expresses the opinion that the cost of "organization and reorganization" now unallowable under 15-205.23 include the costs of mergers and acquisitions. The Air Force believes that it was the intent of 15-205.23 to make non-recurring costs of organization unallowable and concludes that the cost of mergers and acquisitions, being non-recurring are therefore unallowable. The history of 15-205.23 seems to support this conclusion. Early versions of the existing cost principles combine what was ultimately published as 15-205.23 and 15-205.24. The latter paragraph specifically allows "recurring expenses" such as stock certificates transfer charges and stockholder meetings. The separation of organization costs in 15-205.23 from recurring expenses in 15-205.24 is believed to have been made to clearly set out the non-recurring costs as unallowable.

C. Accounting texts also seem to support the inclusion of merger and acquisition activities with those of organization and reorganization. For example, "A Dictionary for Accountants (3rd Edition), by Eric L. Kohler,

SUBJECT: Case 68-193, Recommended Changes to 15-205.23, Organization Costs

defines "organization cost" as "Any costs incurred in establishing a corporation or other form of organization; as, incorporation, legal and accounting fees, promotional costs incident to the sale of securities, security-qualification expense, and printing of stock certificates."

"Reorganization" is defined in part as "A major change in the financial structure of a corporation or a group of associated corporations resulting in alterations in the rights and interests of security holders; a re-capitalization, merger, or consolidation." (Emphasis added)

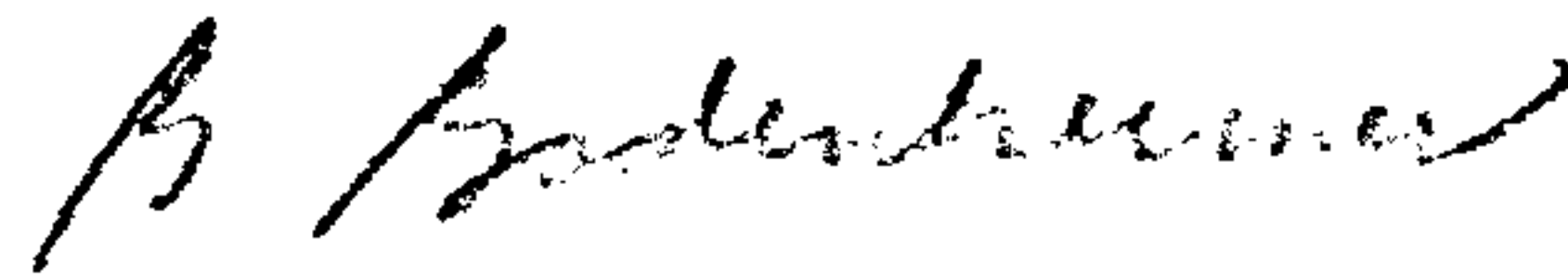
D. The Subcommittee believes that the unallowability of merger and acquisition costs is entirely consistent with the "basic consideration" in 15-201. According to 15-201.4, a cost is allocable if it is (i) incurred specifically for the contract; (ii) benefits both the contract and other work; or (iii) is necessary to the overall operation of the business, although a direct relationship to any particular cost objective cannot be shown. In the opinion of the Subcommittee, merger and acquisition costs would rarely, if ever, meet any of these tests of allocability. Such costs clearly would not be incurred for the contract; and benefit to existing work or necessity for the operation of the existing business would be highly remote. Mergers and acquisition costs are incurred for the purpose of expanding or diversifying an existing business but cannot be said to relate to the work of the existing corporation. In fact, in many cases, a merger or acquisition may be to the detriment of the Government by the elimination of independent sources of supply.

E. The Subcommittee recognizes that there may be rare occasions when a merger or acquisition may be to the advantage of the Government, or may even be encouraged by the Government. Such may be the case when a contractor merges with or acquires an important supplier. Another example would be where the contractor merges with or acquires another important contractor who is experiencing financial or technical difficulties. The Subcommittee, however, believes that if merger and acquisition costs of these rare exceptions are to be allowed, this can be accomplished by means of an ASPR deviation.

F. Both the Air Force and DCAA memos note that the existing 15-205.23 appears to address itself primarily to purchased services, such as outside consultants, and does not specifically address the cost of the contractor's own staff. The DCAA memorandum indicates that such in-house costs could be substantial. In this connection, the Subcommittee agrees with the Air Force opinion that "there does not appear to be any sound justification for ruling that, on one hand, a fee paid a merger consultant should be unallowable and, on the other hand, the salary paid a staff attorney working on the merger is allowable." Accordingly, 15-205.23 on Tab A provides that the costs of both the contractor's own employees and outside services pertaining to organizations and reorganizations are to be unallowable.

SUBJECT: Case 68-193, Recommended Changes to 15-205.23, Organization Costs

G. The Subcommittee believes that in the absence of a clear statement to the contrary, some conflict may arise between allowable economic planning costs under 15-205.47 and unallowable merger and acquisition costs under 15-205.23. Accordingly, 15-205.47 has been revised pursuant to Tab A to specifically exclude organization and reorganization costs from allowable costs of economic planning. In the opinion of the Subcommittee, it was not the intent of 15-205.47 to allow the costs of mergers and acquisition. This paragraph was put into ASPR "so that conversion planning would be specifically cited as an allowable cost," according to a memorandum of August 14, 1963, from the Assistant Secretary of Defense (International Security Affairs) to the Assistant Secretary of Defense (I&L/Procurement). The memorandum went on to state that "it is not intended that allowable costs should go beyond generalized planning." "Economic planning" as used in this cost principle refers to contractor's planning to adjust from defense work to other work in the event of the adoption of Government policy relating to arms control and disarmament. Mergers and acquisition normally would not accomplish the desired objectives of economic planning because they would provide additional capacity and labor but would not necessarily provide nondefense work for the existing contractor.



B. BODENHEIMER

Chairman

Part 2, Section XV Subcommittee

Encl

Part 2, Section XV Subcommittee

DoD Representatives

Mr. J. Fleck - Army  
Mr. R. Lynch - Navy  
Mr. J. F. Snight - USAF  
Mr. W. E. Lahr - DCAS

Other Agency Representatives

Mr. J. McGee - GSA  
Mr. L. Ohnstad - AEC

RECOMMENDED CHANGES TO ASPR, SECTION XV

15-205.23 Organization Costs. (CWAS-NA) Expenditures, ~~such as incorporation fees, attorneys' fees, brokers' fees, fees to promoters and organizers,~~ in connection with (i) [planning or executing the organization or reorganization of a business, [including mergers and acquisitions,] or (ii) raising capital, are unallowable. [Such expenditures include but are not limited to incorporation fees and costs of attorneys, accountants, brokers, promoters and organizers, management consultants and investment counsellors, whether or not employees of the contractor.]

15-205.47 Economic Planning Costs.

(a) (CWAS) This category includes costs of generalized long-range management planning which is concerned with the future over-all development of the contractor's business and which may take into account the eventual possibility of economic dislocations or fundamental alterations in those markets in which the contractor currently does business. [Economic planning costs do not include organization or reorganization costs covered by 15-205.23.]

\* PROPOSED LETTER TO INDUSTRY ON CHANGES TO ASPR 15-205.23 and 15-205.47  
CONCERNING MERGERS AND ACQUISITIONS (ASPR CASE 68-193)

The attached proposed revisions to ASPR 15-205.23 and 15-205.47 are submitted for your review and comment.

Recently we have noted a decided increase in contractors' costs of contemplated or accomplished mergers and acquisitions of other companies. Most often these costs include expenses for attorneys, accountants, management consultants and the like. Costs of both contractor employees and outside services are involved. In some cases, at least a portion of such costs have not been claimed for reimbursement. In other cases, all or a portion of such costs have been disapproved. Guidance is required to assure consistent accounting for these costs.

Mergers and acquisitions have generally been considered to be in the nature of organizations or reorganizations, the cost of which are presently unallowable under ASPR 15-205.23. The attached revisions accordingly identify mergers and acquisitions as a part of organization and reorganization costs. To assure equitable treatment among contractors with in-house capabilities for these activities and those without such capabilities, the attached revision also clarifies that both the cost of employees and outside services are part of organization and reorganization expenses.

We would appreciate receiving your comments (25 copies if convenient) within the next 60 days.

Sincerely,

E. C. CHAPMAN  
Captain SC, USN  
Chairman, ASPR Committee



68-193



OFFICE OF THE ASSISTANT SECRETARY OF DEFENSE  
WASHINGTON, D.C. 20301

11 OCT 1968

INSTALLATIONS AND LOGISTICS

MEMORANDUM FOR THE CHAIRMAN, ASPR COMMITTEE

SUBJECT: ASPR Case 68-193, Recommended Changes to  
15-205.23 Organization Costs

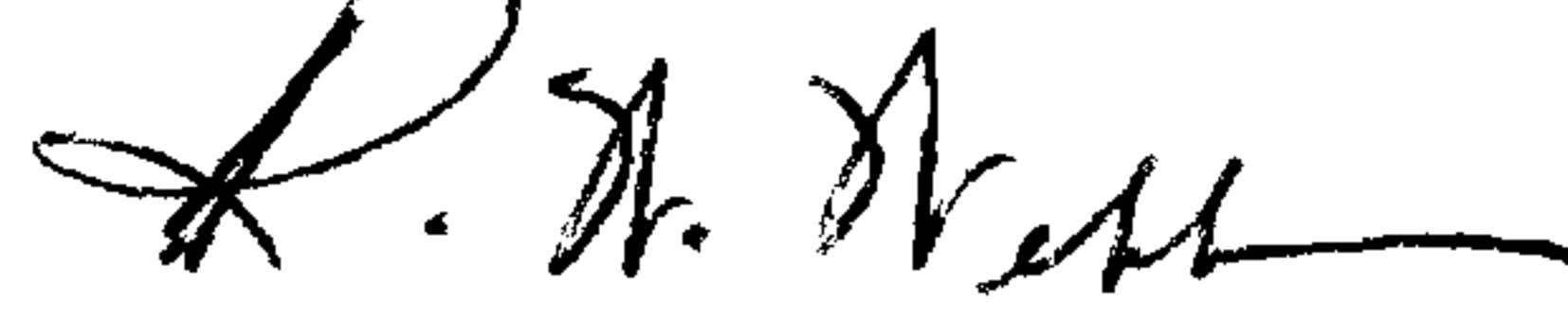
We suggest to the Committee that it may want to consider, before adopting the Subcommittee's recommendations in this case, the recent Sec Def actions towards contributing to the resolution of the pressing social problem as advanced in his speech before NSIA.

Normally, we would not volunteer comments on a Subcommittee's recommendations and would, if asked, support the Subcommittee's interpretation of what was intended by ASPR 15-205.23. However, the Military Departments and the ASDs have been requested to consider various new and imaginative ways to assist in alleviating some of our most pressing domestic problems. Quite naturally, we will need considerable "voluntary" action and support of any program by the defense industry.

The adoption of the Subcommittee recommendations might be considered as an irritant to industry, and stimulate a reaction out of proportion to the actual effect of the cost principle revision. We respectfully suggest that consideration be given to whether ASPR 15-205.23 in its present form could not be used in any current problem to effect a disallowance of merger or acquisition costs.

As food for thought, we would visualize it possible to incur "organization costs" incident to the establishment of new-generation manufacturing units by merger, acquisition or other means to provide training and job opportunities in ghetto areas. Under such circumstances, it would be ironical if DOD refused to share in such costs.

These views are submitted for your consideration.

A handwritten signature in black ink, appearing to read "R. W. Webb". The signature is written in a cursive style with a large, looping initial "R" that extends upwards and to the left.

R. W. WEBB  
Director,  
Procurement Analysis  
and Planning

DEPARTMENT OF THE AIR FORCE  
WASHINGTON

OFFICE OF THE GENERAL COUNSEL

1 August 1968

ASPR Case 68-193

MEMORANDUM FOR THE CHAIRMAN, THE ASPR COMMITTEE

SUBJECT: Interpretation of ASPR 15-205.23 and 15-205.31(d)

Recently the issue has arisen as to whether merger and acquisition expenses are allowable under current ASPR cost principles. The most relevant provision appears to be Section 15205.23 which states specifically that "expenditures, such as incorporation fees, attorneys' fees, accountant's fees, brokers' fees, fees to promoters and organizers, in connection with (i) organization or reorganization of a business, or (ii) raising capital, are unallowable." There are essentially two problems in determining whether merger and acquisition expenses are within the purview of that provision. In the first place, "organization or reorganization" technically may not be identical with merger or acquisition. In addition the list of examples contained in the provision suggest that it is limited to costs incurred for obtaining third party professional and consultant services. Accordingly, some ambiguity exists whether the above provision disallows in-house costs incurred for merger and acquisition purposes. Neither the GAO nor the ASBCA have addressed these specific issues.

While for certain purposes, "organization or reorganization" may be distinct from a merger or acquisition, it is my opinion that the phrase "organization or reorganization" was intended to cover nonrecurring transactions that significantly affect the corporate structure and, accordingly, include mergers and acquisitions. The ASPR does recognize that certain corporate expenses involved in stock transactions may be allowable. For example, Section 15-205.24 specifically states that "such recurring expenses as registry and transfer charges resulting from changes in ownership of securities issued by the contractor . . ." are allowable. However, the word "recurring" should be emphasized, for it is this

phrase that seemingly would preclude consideration of acquisition and merger expenses. Moreover, this provision is limited to the costs incurred in the actual transfer of stock and, consequently, does not encompass the major costs of a merger or acquisition.

In view of the numerous examples contained in the provision, the argument that Section 15-205.23 is limited to expenses incurred for obtaining outside services seems appealing. Nevertheless, the operative language of the provision remains as "expenditures in connection with organization or reorganization of a business or raising capital are allowable." There does not appear to be any sound justification for ruling that, on one hand, a fee paid a merger consultant should be unallowable and, on the other hand, the salary paid a staff attorney working on the merger is allowable. The language of the provision does not demand this seemingly inconsistent conclusion.

Notwithstanding the above arguments, I think it would be worthwhile for the ASPR Committee to revise this section in order to resolve any ambiguity that may exist. One improvement might be to modify the section to read as follows:

"Expenditures, such as incorporation fees, fees to promoters and organizers, costs of professional services whether or not performed by employees of the contractor, in connection with (a) organization or reorganization of a business including mergers and acquisitions, or (b) raising capital, are unallowable."

*Martin D. Schneiderman*

MARTIN D. SCHNEIDERMAN  
Air Force Legal Member



DEFENSE CONTRACT AUDIT AGENCY

CAMERON STATION  
ALEXANDRIA, VIRGINIA 22314

68-193

IN REPLY REFER TO  
CA-APC

JUL 24 1968

MEMORANDUM FOR CHAIRMAN, ASPR COMMITTEE

SUBJECT: Recommended Changes to ASPR 15-205.23 Organization Costs

Inquiries from field auditors have shown intensified activity by major defense contractors in the areas of planning and accomplishing reorganizations for purposes of diversification. These contractors' reorganization costs involve the use of both in-house capabilities and outside consultants in analyzing potential merger or acquisition candidates and in accomplishing any subsequent reorganization. While the in-house effort is not readily identifiable in all cases, the recognizable costs of (i) departments where contractors have centralized the activity and, (ii) fees charged by outside consultants for their assistance, involve substantial expenditures.

We have found that while contractors do not generally claim the formal costs of accomplishing a reorganization, they do not, as a rule, identify the in-house costs incurred for this purpose and frequently include consultant fees related to merger investigations in their reimbursable overhead submissions. Although it is recognized that every element of cost and every situation that might arise in a given case are not included in ASPR 15-205, the significance of the merger and acquisition costs currently being incurred warrants, in our opinion, elaboration of ASPR 15-205.23. Accordingly, it is recommended that the ASPR provision pertaining to reorganizations be revised to include references to in-house and merger or acquisition planning effort as set forth in the enclosure. The enclosed proposed change would more explicitly define certain costs which contractors have been reluctant to correctly identify in their records as long as they felt that doubt existed with respect to their allowability.

It is understood that the USAF is also concerned with the above described problem and is in the process of recommending ASPR clarification. If such recommendation has already been made, it is hoped that this memorandum will provide additional support.

Related studies are being conducted by this Agency that may result in subsequent recommendations for specifically referring to both in-house and purchased services in other cost principles. Conceivably, such studies may indicate a need for some overall guidance applicable to this matter, rather than repeated references in each

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SUBJECT: Recommended Changes to ASPR 15-205.23 Organization Costs

applicable cost principle. However, these studies are mentioned for future planning purposes only and it is not recommended that clarification of ASPR 15-205.23, as explained above, be delayed pending their completion.

If this Agency can be of further assistance in this matter, please advise.

A handwritten signature in black ink, appearing to read "W. B. Petty", with a horizontal line extending to the right from the end of the signature.

WILLIAM B. PETTY  
Director

Encl

15-205.23 ORGANIZATION COSTS (CWAS-NA)

Costs incurred (by a contractor's own staff or through purchase from outside sources) related to planning acquisitions or mergers or investigating potential candidates for such action are unallowable. In addition, ~~expenditures~~ Expenditures, such as incorporation fees, attorneys' fees, accountants' fees, brokers' fees, fees to promoters and organizers, in connection with (i) organization or reorganization of a business, or (ii) raising capital, are unallowable.

Enclosure

15-205. \_\_\_\_\_ Disarmament Conversion Planning Costs

(a) This category of costs includes all planning efforts for adjusting from defense work to other work in the event of the adoption of Government policy relating to arms control and disarmament. Included in this category of costs are: (i) generalized economic planning, and (ii) research and development designed to lead to new products for sale to the general public.

(b) Generalized economic disarmament planning costs are allowable as an indirect cost appropriately allocated to all of the contractor's work. The costs of research and development designed to lead to new products for sale to the general public should be allocated to such new products and are hence not allowable.



68-193

26 MAY 1969

Council of Defense and Space  
Industry Associations (CODSIA)  
1730 K Street, N. W.  
Washington, D. C. 20006

Gentlemen:

The ASPR Committee recently approved for printing a change to ASPR 15-205.23, Organization Costs, defining organizations and reorganizations as including mergers and acquisitions. It also approved a change to ASPR 15-205.47, Economic Planning Costs, specifying that these costs do not include organization or reorganization costs. In making these changes, the comments and recommendations in your letter of February 10, 1969, were carefully considered. In this connection, we appreciate your offer to meet with representatives of the ASPR Committee on this subject, but believe that under the circumstances such a meeting is not required.

Sincerely,

SIGNED

E. C. CHAPMAN  
Captain, EC, USN  
Chairman, ASPR Committee

