

## COFC Holds the Costs of R&D Effort Expressly Excluded from a Contract Are IR&D Costs and Tangible Capital Asset Costs Are Not Development Costs

The Court of Federal Claims has just issued a decision in *ATK Thiokol, Inc. v. United States*, No. 99-440C (Nov. 30, 2005), holding that the cost of research and development effort excluded from a contract and accounted for as an indirect cost consistently with the contractor's disclosed accounting practices is an independent research and development ("IR&D") cost. The court also found that an "implicitly required" standard is incorrect, contrary to the decision in *United States v. Newport News Shipbuilding, Inc.*, 276 F. Supp. 2d 539 (E.D. Va. 2003) and contrary to the implications in *Mayam v. Martin Marietta Corp.* 894 F. Supp. 218 (D. Md. 1995). The *ATK Thiokol* holding means that contractors are entitled to make reasonable delineations between what are costs of a contract and what are IR&D costs, including delineations that result in IR&D efforts that "parallel" contract efforts.

The court also held that the costs of production tooling and equipment not required in the performance of a contract are properly capitalized and accounted for as the costs of tangible capital assets. The court found that an "implicitly required in the performance of a contract" standard that would have required treating the costs of such assets as direct costs was improper and that "development," as used in Cost Accounting Standard ("CAS") 420 and Federal Acquisition Regulation § 31.205-18, does not include tangible asset costs. This holding permits contractors to continue what has been the longstanding practice that, absent the circumstances set out in CAS 409, the cost of tangible capital assets must be capitalized, depreciated and classified as indirect costs.

We believe that the court's holding also should help resolve the issue relating to bid and proposal ("B&P") costs created by the decision in *TRW, Inc.*, ASBCA Nos. 51171, 51530, 01-1 B.C.A. ¶ 31,390, and *United States ex rel. Bagley v. TRW, Inc.*, 2000 WL 33400196 (C.D. Cal. 2000). The *ATK Thiokol* holding recognizes that effort excluded from a contract may result in indirect costs. Thus, an express exclusion from a joint venture or teaming agreement of proposal activity should permit any proposal costs to remain B&P costs under CAS 420.

We will provide you with a more detailed analysis in the near future.

### Contact Info

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