

presenting unallowable costs provided—

(i) The statistical sampling results in an unbiased sample that accurately represents the sampling universe; and

(ii) The statistical sampling permits audit verification.

(d) If a directly associated cost is included in a cost pool that is allocated over a base that includes the unallowable cost with which it is associated, the directly associated cost shall remain in the cost pool. Since the unallowable costs will attract their allocable share of costs from the cost pool, no further action is required to assure disallowance of the directly associated costs. In all other cases, the directly associated costs, if material in amount, must be purged from the cost pool as unallowable costs.

(e)(1) In determining the materiality of a directly associated cost, consideration should be given to the significance of—

(i) The actual dollar amount;

(ii) The cumulative effect of all directly associated costs in a cost pool; and

(iii) The ultimate effect on the cost of Government contracts.

(2) Salary expenses of employees who participate in activities that generate unallowable costs shall be treated as directly associated costs to the extent of the time spent on the proscribed activity, provided the costs are material

in accordance with paragraph (f)(1) of this subsection (except when such salary expenses are, themselves, unallowable). The time spent in proscribed activities should be compared to total time spent on company activities to determine if the costs are material. Time spent by employees outside the normal working hours should not be considered except when it is evident that an employee engages so frequently in company activities during periods outside normal working hours as to indicate that such activities are a part of the employee's regular duties.

(3) When a selected item of cost under 31.205 provides that directly associated costs be unallowable, such directly associated costs are unallowable only if determined to be material in amount in accordance with the criteria provided in paragraphs (f)(1) and (f)(2) of this subsection, except in those situations where allowance of any of the directly associated costs involved would be considered to be contrary to public policy.

3. Amend section 31.204 in the first sentence of paragraph (a) by removing "shall be allowed" and adding "are allowable" in its place; revising paragraph (b); and redesignating paragraph (c) as paragraph (d) and adding a new paragraph (c) to read as follows:

**31.204 Application of principles and procedures.**

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(b)(1) For the following subcontract types, costs incurred as reimbursements or payments to a subcontractor are allowable to the extent the reimbursements or payments are for costs incurred by the subcontractor that are consistent with part 31:

(i) Cost-reimbursement.

(ii) Fixed-price incentive.

(iii) Price redeterminable (*i.e.*, fixed-price contracts with prospective price redetermination and fixed-ceiling-price contracts with retroactive price redetermination).

(2) The requirements of paragraph (b)(1) of this section apply to any tier above the first firm-fixed-price subcontract or fixed-price subcontract with economic price adjustment provisions.

(c) Costs incurred as payments under firm-fixed-price subcontracts or fixed-price subcontracts with economic price adjustment provisions or modifications thereto, for which subcontract cost analysis was performed, are allowable if the price was negotiated in accordance with 31.102.

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[FR Doc. 03-12892 Filed 5-21-03; 8:45 am]

BILLING CODE 6820-EP-P