8th July 2010

The Cost Accounting Standards Board

Office of Federal Procurement Policy

725 17th St. NW – Room 9013

Washington, D.C. 20503

Attn: Mr. Raymond J. M. Wong

Subject: CAS Pension Harmonization NPRM

Reference: Cost Accounting Standards: Harmonization of Cost Accounting Standards 412 and 413 With the Pension Protection Act of 2006; Proposed Rule; Published in the *Federal Register* 10th May 2010

My name is Bill Romenius and I appreciate the opportunity to provide comments to the Cost Accounting Standards Board ("CASB") Notice of Proposed Rulemaking ("NPRM") on the Pension Harmonization that was published in the *Federal Register* on the 10th of May 2010. Please be advised that the following comments are provided as a private citizen and do not represent the position of my employer. I offer my views from the perspective of my many years of working CAS issues on an almost daily basis; be it with Industry or with the US Government, including my time on the CASB from 1999 thru 2000.

The CASB in its prefatory comments and responses to comments from the Advanced Notice of Proposed Rulemaking (ANPRM) stressed the benefits of the utilization of long term/going concern assumptions in computing pension costs for government contracting purposes. The CASB emphasized the need to put into place a methodology that would allow for an accurate and predictable pension costs for pricing purposes.

The CASB identified in the NPRM its five Harmonization Goals as:

- Minimal Changes to CAS 412 and CAS 413
- No direct adoption of Employee Retirement Income Security Act (ERISA)
- Preserve matching of costs with causal beneficial activities over the long term
- Mitigate volatility and enhance predictability
- Make "user friendly" changes - avoid complexity to the degree possible

The thrust of the NPRM is the introduction of a series of prediction triggers at CAS 412.50(b)(7) ("(b)(7)"). The NPRM (b)(7) approach is just unworkable at the field level. These triggers cause so many twists and turns in each year of pricing there is little if any chance that the (b)(7) provisions will result in predictable and accurate pension costs.

The following analysis highlights each of the individual predictions, including the (b)(7) tests, that the contracting parties in the field are required to perform to be compliant with the NPRM provisions. This analysis demonstrates the extremely low likelihood that the NPRM will result in the accurate and predictable pricing of pension costs.

Prediction #1 - CAS requires the calculation of pension expense by taking the sum of the normal cost, the amortization of the unfunded liability, and the amortization of the gains/losses ("Current CAS").

Prediction #2 - (b)(7) requires the comparison of the Current CAS to the ERISA Minimum Funding ("EMF") level and determining if the EMF is greater than the Current CAS. Prediction #2 is the first time, where we are comparing the EMF short term/pension termination assumptions, which by their very nature are more volatile than the Current CAS's long term/going concern assumptions.

Prediction #3 - If the EMF is greater than the Current CAS – (Prediction #2), then we are required to predict whether the sum of the Normal Cost ("NC") and Actuarial Liability ("AL") is greater than the sum of the Minimum Normal Cost ("MNC") and Minimum Actuarial Liability (MAL"). We continue this comparison of long term/going concern assumptions with short term/settlement assumptions.

Prediction #4 – If the sum of the MAL + MNC is the greater of the two then we are required to predict a second pension cost as the CAS pension expense is recomputed using the MNC and MAL as the new AL and NC, ("Revised CAS). This is a crossover from the CASB current long term/going concern assumptions to the EMF and short term/settlement assumptions.

Prediction #5 - The contracting parties are required to predict which of the Current CAS or Revised CAS is greater, with the greater of the two becoming the CAS (b)(7) pension expense.

Predictions #6, #7, & #8 – Contracting Parties are required to determine if the CAS (b)(7) pension expense is going to be subject to any of the three caps set-in place since 1995 at CAS 412.50(c)(2) ("(c)(2)").

The NPRM is requiring contracting parties to make eight predictions before one year's CAS pension expense can be assigned and allocated. For multi-year pricing the contracting parties must make between twenty-four to forty predictions to develop the three-to-five years forward pricing of pension expense.

With the introduction of (b)(7) we are doubling the predictions required in CAS 412 from four to eight. Please note that each of these predictions requires complex calculations based upon current period short-term assumptions, and also forecasts from three-to-five years out as to what these short term "spot type" rates will be.

In short, we are asking the contracting parties in the field to predict if the EMF is going to be greater than the already difficult to predict Current CAS; and then is the sum of the MAL + MNC greater than the AL + NC. If the MAL and MNC sum is greater, then we are required to compute and predict the Revised CAS pension expense, and predict whether it will be less or greater than the Current CAS. Finally, the contracting parties must then continue to determine if any of the three (c)(2) tests are applicable. This is just for one year of a multi-year forward pricing proposal. The contracting parties are then asked to go through the same process again for each of the years covered in the forward pricing proposal.

Imagine how fortunate the contracting parties would be if they were able to predict accurately which of the (b)(7) and (c)(2) triggers were applicable in any one year, never mind also trying to predict the current period pension cost associated with the correct prediction of the triggers and doing so over multiple years.

The more likely scenario is that contracting parties are unable to forecast accurately and, for example, incorrectly use the Revised CAS in pricing instead of the Current CAS or vice-versa or capping the CAS (b)(7) with one of the (c)(2) limitations, etc., and doing so for several years in the multi-year pricing forecast. This is hardly creating a non-volatile pricing environment.

This (b)(7) approach creates the opportunity for unpleasant pension surprises when actuals hit the books and/or there are significant changes in forecasts due to an inaccurate prediction. Making several inaccurate predictions can exacerbate the situation with a cascading impact on forecasted pension expenses. This is not the correct way to produce predictable and stable pension costs.

Furthermore, except perhaps for objective #2 of the aforementioned Harmonization objectives, one could make a very strong case that the NPRM was not on target with any of its Harmonization Objectives and its desire to base the CAS on long term/going concern assumptions. Determining the applicability of the (b)(7) triggers and their impact that could then require another CAS calculation, does not: meet the minimal change objective, preserve matching costs with cost objectives on a causal/beneficial relationship, mitigate volatility, or find itself to be user friendly.

It is suggested that we step-back and review the actual requirements of Section 106(d) of the Pension Protection of 2006 ("PPA") to determine if there is a simpler approach to address PPA harmonization.

> COST ACCOUNTING STANDARDS PENSION HARMONIZATION RULE.—The Cost Accounting Standards Board shall review and revise sections 412 and 413 of the Cost Accounting Standards (48 CFR 9904.412 and 9904.413) to harmonize the minimum required contribution under the Employee Retirement Income Security Act of 1974 of eligible government contractor plans **and** government reimbursable pension plan costs not later than January 1, 2010. Any final rule adopted by the Cost Accounting Standards Board shall be deemed the Cost Accounting Standards Pension Harmonization Rule. **[Emphasis Added]**

Please note the difference between the above requirement and the title of the NPRM as published in the Federal Register, i.e., : Cost Accounting Standards: Harmonization of Cost Accounting Standards 412 and 413 **With** the Pension Protection Act of 2006; Proposed Rule **[Emphasis Added]**

The CASB is required to harmonize the EMF **and** government reimbursable pension plan costs, not harmonize CAS **with** the PPA.

It appears that the use of "with" instead of "and" has led the CASB to incorporate the EMF into the basic CAS structure, principally at CAS 412.50 and the plethora of illustrations at 412.60. However, integration of the EMF into the CAS is not required to meet the CASB's PPA Section 106(d) obligation "(106(d) obligation)". The CASB could be perfectly fine in meeting its 106(d) obligation by focusing its harmonization effort on the impact of the initial adoption of the PPA.

Once a contractor has calculated the "catch-up" impact, the current CAS provisions would govern the treatment of any subsequent variance between forecasted and actual asset and liability performance. Turning the words around a little, subsequent plan performance results (after the impact of the initial adoption is identified) should not be treated differently than that which the CAS currently provides.

By adopting this position, the CASB could view the initial adoption of the PPA as a special event and afford it the same type of treatment that it did for the costs accounting treatment of external restructuring costs at 406.61.

Specifically, the CASB in an Interpretation at 412.61 could require contractors to identify the impact of the initial adoption and funding of the PPA, remove it from all other calculations, amortize it (with a time value of money factor as part of the amortization) over a fixed period of years within a 10-to-20 year corridor, and include the annual amortization in the Current CAS number until the amortization has been completed.

By adopting such an approach, the CASB can eliminate the entire complex and difficult (b)(7) prediction trigger tests, and have much more stable, predictable, accurate, and reimbursable pension plan costs. It also will have a much more transparent process in place to demonstrate the precise steps taken to meet the 106(d) obligation, as well as, the impact.

Contracting parties understand how to go about assessing the impact of a specific `change and then creating an amortization schedule. It is doubtful that anyone understands completely the "in's and out's" of (b)(7) to the extent required to produce a reliable estimate of pension costs for multiple years.

Accordingly, it is recommended that the CASB consider that adoption of PPA Section 106 (d) can be accomplished by adding Interpretation 412.61. This Interpretation calls for the impact of the initial adoption and related funding of the PPA to be segregated and amortized over an agreed to period of time within a 10-to-20 year corridor. For pricing purposes the parties may agree to begin such amortization up to two years after the effective date of this interpretation. The current CAS would continue to govern over all other aspects of measuring, assigning, and allocating reimbursable pension plan costs.

I would be pleased to discuss the NPRM issues with the CASB.

Sincerely:

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