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Office of Federal Procurement Policy
ATTN: Laura Auletta
725 17th Street, NW., Room 9013
Washington, DC 20503

REF: Office of Federal Procurement Policy, Cost Accounting Standards Board, Case CAS–2007–02S

Dear Ms. Auletta:

We reviewed the Staff Discussion Paper on the harmonization of Cost Accounting Standards (CAS) 412 and 413 with the Pension Protection Act of 2006 (PPA). We are providing input with respect to Question 9 (a) Prepayment Credits: *Should prepayment credits be adjusted based on the CAS valuation rate or the PPA requirement to use the pension fund's actual ''return on plan assets'' for the period?*

Contractors should adjust prepayment credits based on the pension fund's actual "return on plan assets." Otherwise, inequities can occur. The following is an example of how inequities can occur using the CAS valuation rate when a contractor uses segment accounting in tracking its pension costs.

In this example, the government segment has a large surplus that is not projected to come out of full funding status in the near future. The commercial segment is under-funded. The contractor does not distinguish prepayment credits from other assets when calculating gains or losses and allocating them to segments. All plan assets earn the same rate of return. CAS requires prepayment credits to be adjusted for interest at the valuation rate; therefore, the difference between the valuation rate and the actual rate of return generates a gain or loss attributable to the prepayment credits. The contractor allocates the pension plan gains or losses attributable to the prepayment credits based on segment to total asset values, net of prepayment credits. This method allows all segments to receive gains or losses attributable to the prepayment credits. While this benefits the Government when gains occur, Government segments will share in the losses as well. The Government should not share in this risk because it has no ownership interest in the prepayment credit assets.

The CAS valuation rate is based on the actuarial best estimate of the rate of return. Actuarial gains and losses are not foreseeable and result from the element of risk inherent in the investment market. It is not prudent for the government to assume risk associated with assets that it does not own. The gains and losses attributable to prepayment credits should not influence the pension asset balances of any segment. Therefore, we recommend using the actual "return on plan assets."

In addition, the CAS Board should address the subject of the management fees attributable to the prepayment credits. Currently, the fees can be allocated to a segment that has no ownership interest in the credits. The gains, losses, and investment fees attributable to the prepayment credits should remain tied to the prepayment credits until they are required for funding of a specific segment.

Thank you for the opportunity to comment on the proposed rule. If you have any questions, please contact Ms. Mary McBarron at (216) 706-0074, or by e-mail at Mary.McBarron@dodig.mil.

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