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

RE: CAS-2007-02S

Prudential Retirement is pleased to have this opportunity to provide comments regarding the Staff Discussion Paper – Harmonization of Cost Accounting Standards 412 and 413 with the Pension Protection Act of 2006. Prudential Retirement provides complete and customized retirement solutions for companies, including delivering actuarial consulting services.

Question 1. Should the Board apply any revisions to all cost-based contracts and other Federal awards that are subject to full CAS coverage, or only to ``eligible government contractors'' as defined in Section 106?

The Board should apply any revisions to all contractors, not only to ``eligible government contractors''. Applying different requirements to contractors based on size would be unnecessarily complex.

Question 2. Does the current CAS 412 and 413 substantially meet the Congressional intent of the PPA to protect retirement security, to strengthen funding and ensure PBGC solvency?

No. As required under Section 106(d) of the Pension Protection Act (PPA), the CAS 412 and 413 requirements should be revised to harmonize reimbursable pension costs with the minimum required contributions.

Question 3. Should CAS harmonization be focused only on the relationship of the PPA minimum required contribution and the contract cost determined in accordance with CAS 412 and 413?

Yes. The harmonization should focus on the relationship of the minimum required contribution and the CAS cost since this is the intent of Section 106(d) of the PPA.

(a) Do the measurement and assignment provisions of the current CAS 412 and 413 result in a contractor incurring a penalty under ERISA in order to receive full reimbursement of CAS computed pension costs under Government contracts?

Contractors would not incur a "penalty under ERISA". However, contractors could incur cash flow problems since the PPA minimum required contribution could significantly differ from the current CAS cost.

(b) To what extent, if any, should the Board revise CAS 412 and 413 to harmonize with the contribution range defined by the minimum required contribution and the tax-deductible maximum contribution?

The current requirement that the CAS cost must neither be less than zero nor exceed the sum of the maximum tax-deductible contribution plus prepayment credit should be retained. Note that the PPA has significantly increased the maximum tax-deductible contribution, so the CAS cost would rarely be affected by the upper limitation.

(c) To what extent, if any, should ERISA credit balances (carryover and prefunding balances) be considered in revising CAS 412 and 413?

ERISA credit balances should not be considered in revising CAS 412 and 413. ERISA credit balances reflect the cumulative funding in excess of the minimum required contribution. They do not reflect the historical difference between the minimum required contribution and the CAS cost.

CAS prepayment credits and their general application under CAS 412 and 413 should be retained.

(d) To what extent, if any, should revisions to CAS be based on the measurement and assignment methods of the PPA?

The CAS revisions should reflect the general measurement and assignment methods of the PPA. This is necessary in order to harmonize the CAS cost with the PPA minimum required contribution.

(i) To what extent, if any, should the Board revise the CAS based on rules established to implement tax policy?

The primary focus of the revisions should not be to implement tax policy.

(ii) To what extent, if any, should the Board consider concerns with the solvency of either the pension plan, or the PBGC?

The solvency of the pension plan or the PBGC should not be the primary concern of the Board. Rather, the Board's primary focus should be harmonizing the CAS cost with the PPA minimum required contribution.

Question 4. (a) Accounting Basis. For Government contract costing purposes, should the Board (i) Retain the current ``going concern'' basis for the measurement and assignment of the contract cost for the period, or (ii) revise CAS 412 and 413 to measure and assign the period cost on the liquidation or settlement cost basis of accounting?

The Board should retain the current "going concern" basis for measuring and assigning costs based on the PPA funding rules. This basis should be consistent with the methods outlined by the PPA provisions, including the use of the unit credit funding method for liability measurement and a 7-year amortization of unfunded liability.

Note that we believe the PPA funding rules are, in fact, "going concern" rules.

(b) Actuarial Assumptions. For contract cost measurement, should the Board (i) Continue to utilize the current CAS requirements which incorporate the contractor's long-term best estimates of anticipated experience under the plan, or (ii) revise the CAS to include the PPA minimum required contribution criteria, which include interest rates based on current corporate bond yields, no recognition of future period salary growth, and use of a mortality table determined by the Secretary of the Treasury?

The CAS should be revised to include the PPA minimum required contribution criteria, as this is consistent with the harmonization objectives.

(c) Specific Assumptions. Please comment on the following specific assumptions:
(i) Interest Rate: (1) For measuring the pension obligation, what basis for setting interest rate assumptions would best achieve uniformity and/or the matching of costs to benefits earned over the working career of plan participants? (2) To what extent, if any, should the interest rate assumption reflect the contractor's investment policy and the investment mix of the pension fund?

The interest rate basis for CAS cost calculations should be similar to the basis used for PPA purposes.

(ii) Salary Increases: For measuring the pension obligation, should the CAS exclude, permit or require recognition of future period salary increases?

Consistent with the PPA, CAS should only recognize salary increases when measuring the target normal cost for the current measurement year.

(iii) Mortality: For measuring the pension obligation, should the CAS exclude, permit, or require use of a (1) Standardized mortality table, (2) company-specific mortality table, or (3) mortality table that reflects plan-specific or segment-specific experience?

CAS should follow the PPA requirements for selecting a mortality assumption.

(d) Period Assignment (Amortization). For contract cost measurement, should the Board (i) Retain the current amortization provisions allowing amortization over 10 to 30 years (15 years for experience gains and losses), (ii) expand the range to 7 to 30 years for all sources including experience gains and losses, (iii) adopt a fixed 7 year period consistent with the PPA minimum required contribution computation, or (iv) adopt some other amortization provision?

As mentioned previously, the Board should adopt a 7-year amortization to be consistent with the PPA.

(e) Asset Valuation. (i) For contract cost measurement, should the Board restrict the corridor of acceptable actuarial asset values to the range specified in the PPA (90% to 110% of the market value)?

The PPA asset corridor should also be used for CAS asset values.

(ii) For contract cost measurement, should the Board adopt the PPA's two year averaging period for asset smoothing?

Yes, the Board should adopt the PPA asset smoothing methodology for CAS purposes.

Question 5. To what extent, if any, should the Board revise the CAS to include special funding rules for ``at risk'' plans?

The Board should revise the CAS rules to incorporate the "at-risk" funding requirements as outlined by PPA. In the spirit of harmonization, plans deemed "at-risk" by PPA should also be considered "at-risk" by CAS.

Question 6. (a) To what extent, if any, should the measurement and assignment provisions of CAS 412 and 413 be revised to address contractor cash flow issues?

The most direct way to mitigate contractor cash flow issues is to mirror most of the PPA requirements when revising CAS 412 and 413. This harmonization of PPA and CAS provisions is detailed throughout our response.

(b) To what extent, if any, do the current prepayment provisions mitigate contractor cash flow concerns?

The current prepayment provisions do not effectively mitigate contractor cash flow concerns since large prepayment credits can accumulate for many years in the future.

(c) To what extent, if any, should the prepayment credit provision be revised to address the issue of potential negative cash flow?

The prepayment credit provisions do not need to be revised, except to reflect the actual return on plan assets as described in our response to question 9(a).

Question 7. (a)(i) To what extent, if any, would adoption of some or all of the PPA provisions impact the volatility of cost projections?

Adopting the PPA provisions, in general, would increase year by year volatility in assigned CAS cost. There are two primary reasons for the increase in volatility:

1) **Investment (gains)/losses are likely to be smoothed over a shorter period of time (24 month maximum)**
2) **Discount Rates will vary year by year (with limited smoothing)**

Therefore, the actual assigned CAS cost in any year is more likely to be different than the forecasted cost.

(ii) Are there ways to mitigate this impact? Please explain.

These "actual vs. forecasted" cost differences could be tracked and possibly applied to future costs. If the differences were largely offsetting from one year to the next, no adjustments may need to be made. However, if the differences compounded for a few years, some mechanism for applying the difference (positive or negative) could kick in.

(b) To what extent, if any, should the CAS assignable cost limitation be revised as part of the efforts to harmonize the CAS with the PPA?

Assuming the CAS rules incorporate the PPA funding target and target normal cost, then no changes should need to be made to the assignable cost limitation.

(c) To what extent, if any, should the CAS be revised to address negative pension costs in the context of cost volatility?

The concept of negative pension costs should be avoided. Note that the PPA does not allow for negative costs.

Question 8. (a) To what extent, if any, would adoption of some or all of the PPA provisions affect the measurement of a segment closing adjustment in accordance with CAS 413.50(c)(12)?

The segment closing adjustment should be determined using the PPA funding target, using the PPA assumptions and methods. This would help to harmonize the CAS requirements with the PPA. If there is a pension plan termination, the segment closing adjustment should reflect the amount necessary to settle the obligation (the cost of purchasing annuities or providing lump sums).

(b) To what extent, if any, should the CAS 413 criteria for a curtailment of benefits be modified to address the PPA mandatory cessation of benefit accruals for an ``at risk'' plan?

The PPA mandatory cessation of benefit accruals for "at risk" should not result in a curtailment since this mandatory cessation is typically temporary.

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?

Actual return on plan assets should be used, as this is consistent with PPA.

(b) Contributions Made After End of Plan Year. Should the interest adjustment for contributions made after the end of the plan year be computed as if the deposit was made on the last day of the plan year or on the actual deposit as now required by the PPA?

Consistent with PPA, the actual deposit date should be used for interest adjustment.

(c) Collectively Bargained Benefits. (i) To what extent, if any, should the CAS be revised to address the PPA provision that allows the recognition of established patterns of collectively bargained benefits?

Again, this PPA provision should be applied to the CAS rules.

(ii) Are there criteria that should be considered in determining what constitutes an established pattern of such changes?

The CAS rules should apply the same criteria as the PPA provisions.

Question 10. The Board would be very interested in obtaining the results of any studies or surveys that examine the pension cost determined in accordance with the CAS and the PPA minimum required contributions and maximum tax-deductible contribution.

We agree that further studies and models are necessary once the Board determines what changes will be considered.

Question 11. In light of the changes to the PPA, should the Board consider including specific requirements in CAS 412 and 413 regarding the records required to support the contractor's proposed and/or claimed pension cost?

In our opinion, the harmonization of CAS 412 and 413 does not call for revisions to current audit requirements for proposed/claimed pension cost.

Prudential Retirement appreciates this opportunity to comment on the Staff Discussion Paper. We would be pleased to discuss any questions that you may have regarding our comments.

Sincerely,

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