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Cost Accounting Standards Board
Attention: Laura Auletta
725 17th Street, NW
Room 9013
Washington, DC 20503

Subject: Comments on the Board's Staff Discussion Paper on the harmonization of Cost Accounting Standards 412 and 413 with the Pension Protection Act of 2006 (Reference case CAS-2007-02S)

We appreciate the opportunity the Cost Accounting Standards Board has given us to provide these comments. We recognize the magnitude of the effort required by the CASB to satisfy harmonization of CAS 412 and 413 with the Pension Protection Act, and we commend the CASB on taking this important early step to request comments from interested parties in order to develop an understanding of the practical considerations of applying CAS 412 and 413 in the business environment. The content of this Staff Discussion Paper demonstrates the willingness of the CASB to explore various perspectives of the multifaceted framework within which this harmonization effort will take place.

In formulating our comments to this Staff Discussion Paper, we considered the most recent Statement of Objectives set forth by the Cost Accounting Standards Board. We believe these concepts are fundamental in the CASB fulfilling its obligations in this harmonization effort. The CASB states its primary objective "*is to promulgate, amend, and revise Cost Accounting Standards designed to achieve (1) an increased degree of uniformity in cost accounting practices among Government contractors in like circumstances, and (2) consistency in costs accounting practices in like circumstances by individual Government contractors over periods of time.*" We understand this to mean that all contractors subject to CAS coverage have sufficient uniformity to achieve the comparability between contractors desired by the Government and that each contractor subject to CAS coverage has sufficient consistency over cost accounting periods to achieve the comparability desired by the Government. These objectives are in accordance with the authority of the CASB as set forth by Public Law 100-679 and described in CAS 9901.302(b). We believe these objectives to be key in answering the question of applicability of the harmonized CAS 412 and 413.

The CASB Statement of Objectives goes on to state that "*In accomplishing this primary objective, the Board takes into account (1) the advantages, disadvantages, and improvements anticipated in the pricing and administration of, and settlement of disputes concerning contracts, (2) the probable costs of implementation, including inflationary effects, if any, compared to the probable benefits of such Standards, and (3) the alternatives available.*" We understand this to mean that the CASB will actively consider different cost accounting methods as options, taking into account the effect of each on pricing, as well as costs and efforts related to practical application of the Standard. These are requirements of the CASB as set forth by Public Law 100-679. We believe that the CASB will continue to require the support of interested parties in effectively evaluating alternatives during the harmonization efforts, and we look forward to providing support to the CASB as they request it during this process.

One final concept from the CASB Statement of Objectives that we considered is that of fairness and equity. As stated by the CASB, "*The Board considers a Cost Accounting Standard to be fair when in the Board's best judgment* (sic) *it provides equitable allocation of costs to contracts and shows neither bias nor prejudice to either party to affected contracts...The concept of equity will be considered by the Board when a Standard is written and/or amended.*" We understand this to mean that the Standards set forth should not be so biased to the Government or the contractor as to put to the other party in peril. We believe the relationship between the Government and the contractor is one of mutual interdependence, that each is critical to the other. Fairness and equity of the Standards balances the needs of each contracting party to the benefit of them both. We believe this concept underlies the reason for the harmonization requirement by Congress for the CASB to revise CAS 412 and 413. While commercial companies have the flexibility to choose to adjust their prices to mitigate the impact of increased cash contributions to pension plans mandated by PPA, Government contractors cannot adjust their prices because the measurement of pension costs for their contracts is set by CAS.

Our comments to this Staff Discussion Paper generally propose that contractors use the same underlying methods and assumptions for developing the PPA minimum contribution and the components of the CAS annual cost. Whatever rate curve the contractor uses to develop the PPA's funding target will also be used to develop the CAS liability. This will be true even if the contractor must use the PPA's "at-risk" assumptions. The CAS liability and normal cost (also called service cost) would be determined using the same method and assumptions and will be equal to the liability amounts used in the PPA calculations.

Similarly, we propose that the asset value of the two sets of regulations will be determined in the same manner and will be equal before adjusting for the prepaid expense for CAS or the credit balances for PPA. Although the total asset value before adjustments will be equal, the CAS actuarial value of assets will exclude pension prepayment credits (which do not equal the credit balances for PPA). The PPA calculation excludes credit balances only under certain circumstances and for

certain purposes. Because the assets after adjustments for prepayment credits or credit balances will differ between the two regulations, the shortfalls (currently referred to in CAS 412 as the unfunded actuarial liability) will not be the same.

The CAS pension cost would include the normal cost (corresponds to the PPA's Target Normal Cost) and amortizations of the prior 7 years' shortfalls (corresponds to the amortization schedules described in the PPA). However, the actual amounts of the amortizations would be different between CAS and the PPA.

While PPA requires the CASB to harmonize CAS 412 and 413 with the minimum required contribution for PPA, and we do believe revision to CAS is necessary to satisfy this requirement by Congress, some divergence in these calculations of pension amounts may be necessary to address issues unique to Government contracting, such as the mitigation of volatility which may otherwise prove burdensome to the appropriations process for funding. There are several options we have identified in our response to address this issue, such as using longer amortization periods for CAS than PPA allows. Thus, our comments regard "harmonization" as maximizing the number of common elements in the actuarial calculations for PPA and for CAS. By using generally the same methods and assumptions, the two regulations will essentially be harmonized. In addition, contractors will not be paying duplicate costs for actuaries to calculate two completely different pension amounts. Actuaries' knowledge for complying with CAS will not be an entirely different set of rules to learn with little professional market value outside of a few Government contractors.

The following responses to the questions posed in the Staff Discussion Paper represent an attempt to make CAS more compatible with the pension concepts described within the PPA and are consistent with the approach we suggest above. The responses and recommendations also reflect our attempt to minimize the amount of volatility that a move toward a market-based approach will inevitably create. Although predictability is not an underlying tent of the cost accounting standards, the ability to predict costs and plan budgets is a desirable outcome for both the Government and its contractors.

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 contractors" as defined in Section 106?

We believe the revisions should apply to all contractors with full CAS coverage. Restricting the applicability of the revisions to eligible contractors is contrary to the objectives of the CASB to achieve uniformity between contractors and consistency over cost accounting periods of the same contractor. The Government will lose comparability between larger and smaller contractors subject to different versions of CAS. There will be contractors who will pass in and out of eligible status from year to year or during a single year based on their business results. For example, The Boeing Company is a large defense contractor at risk for oscillating in

eligibility status. One of the criteria for eligibility is that a contractor's primary source of revenue is from business performed under Federal contracts. Though "primary" is not defined in Section 106, given that The Boeing Company is an almost equal split of commercial and Government business, we may be greater than 50% in commercial business one year and then shift the following year to being greater than 50% in Government business. It would be wholly impractical for a contractor to pass in and out of applicability of the revised CAS regulation.

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?

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We believe the intent of Congress in passing the PPA was to secure the cumulative benefits earned for an employee by making sure the company has enough assets in a pension trust to fully fund those benefits, where assets and liabilities are measured using an approximate market, rather than smoothed, basis. This approach when applied annually as required by PPA effectively significantly reduces the potential exposure to PBGC.

By comparison, we do not agree that the existing CAS 412 and 413 substantially meet the intents of PPA. The CAS concepts of segment closing, plan termination, and curtailment of benefits do not relate to the solvency of the company or the pension plan. In these situations, there is an expectation that the company remains an on-going concern despite a change in the pension plan. While CAS 413 provides for a measurement of the assets and liabilities of the pension, the resulting difference "*represents an adjustment of previously-determined pension costs*" [CAS 413-50(c)(12)]. This adjustment amount has no affect on the solvency of the pension plan itself, because it does not obligate or compel the contractor to either contribute to or withdraw assets from the pension trust. Without affecting the actual assets in the pension trust, the CAS provisions have no affect on the solvency of the pension plan itself. This calculation in these circumstances simply allows the Government to "true up" the amount of pension cost which has been charged to Government contracts, no more no less.

The recent default of several large pension plans to the PBGC demonstrates a fundamental weakness of the long-term, smoothed approach to measuring pensions. Liabilities and assets may behave much as we expect them to over a very long time, but if a company is not robust, the company and its pension plans may not survive a severe economic downturn, making what the results might have been over many decades a moot point. The smoothed approach of the existing CAS does not provide adequate protection against such a downturn, and as a result, tends to understate the overall, long term economic cost of the plans. The fact is that economic downturns, especially severe ones, tend to have adverse economic repercussions that are disproportionately larger than the corresponding economic good times. In the last five years, several agencies, and the PBGC in particular, have expressed similar views on many occasions.

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?

Certainly any revisions to CAS need to satisfy Section 106 of the PPA which explicitly mandates harmonization with the minimum required contribution. However, harmonization may best be addressed by revising CAS so that the PPA and CAS measure assets and liabilities using the same underlying methods and assumptions. If the CAS cost is measured using the same definitions of liabilities, normal cost, and assets that appear in the PPA, then a strong argument could be made that harmonization has been achieved. Once the "harmonized" basis is established using the same underlying methods and assumptions, the CAS can add elements appropriate to determining CAS pension cost, rather than the determination of a minimum cash contribution.

We do not recommend that CAS cost be equal to the PPA minimum required contribution, as this would almost certainly increase volatility and make it difficult to ensure costs are properly assigned to cost accounting periods. It would also make it difficult to ensure equity between the contractors and the Government unless there were extensive transition provisions that would be likely to result in very large short-term costs to the Government. This equity issue arises from contractors who have large prepayment credits in their pension plans. The credits represent funds contributed by the contractor to the pension plan trust that have not been reimbursed by the Government. The PPA calculation does not acknowledge the concept of prepayment credits. All assets are used when developing the PPA minimum contribution amount. Thus, contractors with prepayment credits would be unable to recover those funds without some extensive transition provisions. We recommend continuing in CAS the concept of prepayment credits to avoid this transition concern.

Question 3(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?

There is no direct penalty. When the contractor makes contributions that exceed the CAS cost, the prepayment credit provision in CAS provides a mechanism for eventual recovery of amounts funded into the pension plan. Conversely, the current CAS provisions for assignable cost deficits and assignable cost limitations provide for equitable cost recovery when CAS cost exceeds the amount of funding permitted under ERISA.

However, it is possible, and even likely, that most contractors with substantial prepayment credits are unlikely to receive full reimbursement through current CAS pension cost calculations in a timely manner. It may be years, and possibly

decades, before the accumulated CAS cost will allow for recovery of the prepayment credits. This deferral of cost recovery is likely to be exacerbated by PPA which is expected to increase the amount of pension contributions required by contractors. This disparity between the funding requirements and the timing of the cost recovery is largely a matter of the divergence in perspectives, with PPA taking a pessimistic, short-term approach and CAS taking a more optimistic, long-term approach.

Question 3(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 range between the minimum required contribution and the tax deductible contributions will be substantial for most contractors in the foreseeable future, so linking CAS cost to the such a range would create large inconsistencies among contractors and tremendous volatility from year to year. We believe this result is contrary to the stated objectives of the Board.

We recommend that the harmonization focus on using the same underlying methods and assumptions to develop CAS cost as used to develop the minimum required contribution. Beyond this recommendation, we believe the Board should retain the concepts of assignable cost deficits and prepayment credits as exist currently in CAS when they consider the additional elements for determining CAS cost from the harmonized basis.

Question 3(c). To what extent, if any, should ERISA credit balances (carryover and prefunding balances) be considered in revising CAS 412 and 413?

Based on our recommended method outlined, the credit balances are not part of how the CAS cost would be determined.

Question 3(d). To what extent, if any, should revisions to CAS be based on the measurement and assignment methods of the PPA?

As outlined previously, we recommend using the same underlying methods and assumptions for developing the PPA minimum contribution and the components of the CAS annual cost. Whatever rate curve the contractor uses to develop the PPA's funding target will also be used to develop the CAS liability. This will be true even if the contractor must use the PPA's "at-risk" assumptions. The CAS liability and normal cost (also called service cost) would be determined using the same method and assumptions and will be equal to the liability amounts used in the PPA calculations.

Similarly, the asset value of the two sets of regulations will be determined in the same manner and will be equal before adjusting for the prepaid expense for CAS or

the crediting balances for PPA. Although the total asset value before adjustments will be equal, the CAS actuarial value of assets will exclude pension prepayment credits (which do not equal the credit balances for PPA). The PPA calculation excludes credit balances only under certain circumstances and for certain purposes. Because the assets after adjustments for prepayment credits or credit balances will differ between the two regulations, the shortfalls (currently referred to in CAS 412 as the unfunded actuarial liability) will not be the same.

The CAS pension cost would include the normal cost (corresponds to the PPA's Target Normal Cost) and amortizations of the prior 7 years' shortfalls (corresponds to the amortization schedules described in the PPA). However, the actual amounts of the amortizations would be different between CAS and the PPA.

Again, we believe that if the CAS cost is measured using the same definitions of liabilities, normal cost, and assets that appear in the PPA, then a strong argument could be made that harmonization has been achieved. Once the "harmonized" basis is established using the same underlying methods and assumptions, the CAS can add elements appropriate to determining CAS pension cost, rather than the determination of a minimum cash contribution.

We do not recommend that CAS cost be equal to the PPA minimum required contribution because we believe this would not maintain the Board's stated objectives. Unless extensive transition rules were implemented, the results would not be equitable to many contractors, and if such equitable transition rules were implemented, the likely large short-term costs for the Government would be an undesirable result.

Question 3(d)(i). To what extent, if any, should the Board revise the CAS based on rules established to implement tax policy?

We understand this question to address circumstances in which current CAS cost falls outside the range of minimum required and maximum tax-deductible amounts. We believe the current CAS provisions for assignable cost deficits, assignable cost limitations, and prepayment credits are equitable mechanisms for such circumstances. However, we caution the Board that with the implementation of PPA, such circumstances will be exacerbated and the existing mechanisms alone would be inadequate to meet the objectives of the CASB.

If, however, this question is asking if the Board should revise CAS to be consistent with tax policy, we refer to Section 106 of the PPA which explicitly mandates harmonization of CAS 412 and 413 with the minimum required contribution under PPA, not tax policy.

Question 3(d)(ii). To what extent, if any, should the Board consider concerns with the solvency of either the pension plan, or the PBGC?

We do not believe that the Board should consider the solvency of the pension plan, as that is the responsibility of ERISA.

Question 4(a). For Government contracting 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?

We have observed that in the last 20 years the going concern basis of accounting has evolved into more of a market-based snapshot at a point in time, which contains elements of a liquidation or settlement measurement. Liabilities under our proposed method generally require a market based set of assumptions rather than resembling settlement based ones. For example, the liabilities include cumulative earned amounts to date without the effect of future earnings or future service of participants. This market-based perspective is shared broadly by regulations across accounting disciplines worldwide, including the PPA, U.S. Financial Accounting Standards Board, international Accounting Standards Board, British accounting standards, and Canadian accounting standards. Given this breadth of consensus, we regard the market-based perspective as having been established as the general rule of measure for pension costs.

It is important to note that despite the use of market-based measurement, the pension plans are considered going concerns, absent a significant event otherwise, and therefore do not incur the substantial transaction costs and special plan provisions that inevitably accompany a true liquidation or settlement.

Using the existing definition of going concern, where assets are smoothed considerably and assumptions reflect a very long-term view that is likely to be overly optimistic in today's environment, we cannot recommend the Board retain such a view. We recommend the Board consider a basis between the two extremes of the ongoing concern and the liquidation (or settlement), such as a market-based basis which will allow the achievement of harmonization as mandated while allowing the Board flexibility to mitigate volatility.

Question 4(b). For contract 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?

Based on our approach, we recommend using (ii) the PPA minimum required contribution assumptions.

Question 4(c)(i)(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?

Using the rate curve specified by the PPA would achieve consistency among contractors and be in accordance with prevailing economic thought. It would also provide the best basis for matching costs to the benefits earned.

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Question 4(c)(i)(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?

We recommend using the rate curve approach specified by PPA, which would achieve consistency among contractors and be in accordance with our proposed method to achieve harmonization.

The generally accepted approach to investments for pension trusts is to minimize risk to the assets, and such investments tend to yield lower earnings, though possibly not as low as those prescribed by the PPA bond rates. This approach is going to be reinforced by PPA to mitigate the volatility of potential funding requirements. Thus, differences in investment policies and investment mixes between contractors are likely to be diminished and returns on assets are likely to be lower than in previous years as a result.

Question 4(c)(ii). For measuring the pension obligation, should the CAS exclude, permit, or require recognition of future period salary increases?

Permissive recognition of salary increases would undermine consistency among contractors and be contrary to the stated objectives of the Board, so we would not recommend such an approach.

One could argue that to include salary increases in calculation of the obligation would improve the matching of costs to contracts incurred. Since the actual pension payments made after an employee's retirement are generally based on earnings during only the last few years of employment, it is the future salary levels for an employee that determine the pension payouts more so than the current salary level, unless the employee is already within the last few years of employment. Including salary increases would likely increase CAS costs, which could encourage contractors to fund more than the PPA minimum because they would be able to recover the additional funding amounts. However, mandatory recognition of salary increases for determining CAS cost would move away from harmonization with PPA.

We recommend the exclusion of future salary increases as required by PPA. This is consistent with our proposal to create a harmonized basis of the underlying methods and assumptions for CAS with PPA.

Question 4(c)(iii). For measuring the pension obligation, should 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?

We recommend that CAS require the use of same mortality table that the contractor uses for PPA. We recognize that PPA does permit companies to use a company-specific table, but that such a table must then be used for all plans sponsored by the company. We believe that differences between contractors are likely to be minimal from the use of company-specific tables, so the use of such tables would generally be in accordance with the Board's objectives and with our proposal to create a harmonized basis with PPA.

It is unlikely that a contractor would have enough exposure to produce a credible plan-specific or segment-specific mortality table, and if it did, it seems unlikely that much accuracy would be lost by precluding the use of such tables in any case. Such an approach for determining CAS cost would also be a move away from harmonization with PPA.

Question 4(d). 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?

Based on our proposal, we believe that option (iii), the fixed 7 year amortization period, should be the starting point for the Board during its harmonization efforts.

However, we believe that a longer amortization period than PPA permits is an option that the Board should consider for mitigating volatility for CAS cost. If the CAS cost is measured using the same definitions of liabilities, normal cost, and assets that appear in the PPA, then a strong argument could be made that harmonization has been achieved. A difference in amortization periods applied after the "harmonized" basis may address volatility concerns for CAS costs without preventing achievement of harmonization.

Question 4(e)(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?

Based on our proposal, we recommend that contractor's pension asset values (before adjusting for the PPA credit balances or the CAS prepayment credits) be

equal under the PPA and CAS calculations. Therefore, we recommend that the Board adopt the 90% to 110% corridor range specified in the PPA for contractors who elect to smooth assets. We believe that to satisfy the mandate for harmonization, CAS measurements of assets and liabilities should use the same underlying methods and assumptions. We believe that having the same asset values for CAS and PPA is evidence of harmonization. While adoption of this narrower corridor is more likely to result in more frequent adjustments of assets to market that require amortization, we believe that a longer amortization period than PPA permits is an option that the Board should consider for mitigating any undesirable effects for CAS cost.

Question 4(e)(ii). For contract measurement, should the Board adopt the PPA's two year averaging period for asset smoothing?

Based on our proposal, we believe that for contractors who elected to use a smoothed rate curve for their PPA calculations, the two year averaging period for asset smoothing used by PPA should be the starting point for the Board during its harmonization efforts.

However, we believe that a longer amortization period than PPA permits is an option that the Board should consider for mitigating volatility for CAS cost. If the CAS cost is measured using the same definitions of liabilities, normal cost, and assets that appear in the PPA, then a strong argument could be made that harmonization has been achieved. A difference in amortization periods applied after the "harmonized" basis may address volatility concerns for CAS costs without preventing achievement of harmonization.

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

ERISA has the responsibility for setting up requirements for funding pension plans to protect their solvency, so we do not believe the Board needs to include any revisions for funding rules of "at risk" plans other than to clarify that when "at-risk" assumptions and methods apply under the PPA calculation, those same "at-risk" assumptions and methods must also be used for the CAS calculation.

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?

Given the Board's stated objective of fairness and equity defined as showing neither bias nor prejudice to either party to affected contracts, we believe revision of how CAS measures pensions is necessary. We believe that the intent of Congress in mandating harmonization was to safeguard the financial security of existing pension plans, in accordance with the intent of PPA as a whole. By mandating that the Board revise CAS, Congress seems to be addressing the

inequity for Government contractors as a result of the enactment of the PPA. Unlike commercial entities, which have the flexibility to adjust their prices to recover additional funding requirements due to PPA, Government contractors must comply with CAS and do not have such flexibility. Conceivably, not harmonizing CAS with PPA could place a Government contractor with a currently underfunded pension plan in such a cash deficit in complying with PPA that the contractor may have to choose to terminate the pension plan to survive rather than wait years into the future to recover the funds through contracts. Since Congress intended to protect pension benefits by enacting the PPA, the requirement to harmonize CAS appears to be a natural extension of that intent. Harmonization of CAS with PPA mitigates a cash flow inequity that may otherwise discourage Government contractors from retaining their pension plans. Given the Board's objective for fairness and equity, along with Congress' mandate for harmonization, we believe CAS 412 and 413 should be revised to use the same underlying methods and assumptions as PPA with added elements as appropriate to address concerns about volatility and the like while allowing Government contractors a more timely cost recovery of their pension contributions.

Question 6(b). To what extent, if any, do the current prepayment provisions mitigate contractor cash flow concerns?

While the current prepayment provisions in CAS do allow a contractor to ultimately recover their pension contributions made in excess of CAS assignable costs, this recovery may be years, possibly decades, into the future. Such an extended deferral of cost recovery is likely to be exacerbated by PPA, which is expected to require increased contributions that will probably become prepayment credits. Cost recovery so far into the future for a contractor must almost be disregarded as cash flow to run operations for program performance today. We believe the measurement of CAS pension cost should be revised as we have outlined to provide for equitable timely cost recovery for contractors.

Question 6(c). To what extent, if any, should the prepayment credit provision be revised to address the issue of potential negative cash flow?

We do believe the mechanism provided by CAS prepayment credits is important. The concept provides for equity between the Government and contractor. The Government is protected from a contractor overfunding their pension plan and immediately recovering the excess amounts through contracts, and the contractor generally has a timely cost recovery with a vehicle for full cost recovery of the contributions.

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?

There are several provisions of PPA that, if adopted, may introduce volatility.

The use of a short (two year) rolling average as the bond interest rate used for discounting the future pension liability to today's dollars will expose the liability calculation to the volatility of the securities market. This is a change from existing CAS and the single stable discount rate generally used today. Considering the magnitude of the liabilities involved, even small market fluctuations would likely translate into large dollar impacts.

The narrower corridor (90% to 110%), as compared with the current corridor (80% to 120%), allows for less tolerance of asset valuations outside the market acceptable measure before adjustment to market are necessary. This means that the frequency of asset adjustments to market value are likely to increase. In addition, the short (two year) smoothing period for these adjustments does not alleviate volatility in comparison with the smoothing methods permitted under current CAS rules.

The shortened amortization period (7 years) of any unfunded liability for PPA will also reduce the smoothing previously seen in current CAS which permits contractors to use a period of 10 to 30 years. The amortization of the unfunded liability for PPA does not distinguish between pension plan changes, method changes, assumption changes, or straight forward underfunding of the cumulative liability. Notably, the permissible range for amortization of all of these sources of difference for current CAS is the same, a period of 10 to 30 years.

Despite these exposures to volatility, we believe that adoption of the underlying methods and assumptions used by PPA in the revised CAS is necessary to satisfy the harmonization requirement, and we believe there are options for the Board to mitigate these sources of volatility subsequent to the harmonized basis in CAS cost development.

Question 7(a)(ii). Are there ways to mitigate this impact? Please explain.

Prior to PPA, pensions for ERISA and CAS were not equal amounts, but were generally regarded as acceptably aligned, perhaps even harmonized. A notable difference in the pension calculations for ERISA prior to PPA and for CAS is the length of amortization periods used, especially for experience gains and losses. ERISA amortized actuarial gains and losses over 5 years; CAS, 15 years. Differences in amortization periods are among the least disruptive to the process of the actuarial calculations while providing greater smoothing of volatilities for CAS purposes. We recommend that the Board consider longer amortization periods for the unfunded liabilities and actuarial gains and losses resulting from the PPA calculations as an option to mitigate the volatility introduced in these two areas. We believe that extending the amortization periods would still allow the Board to achieve a harmonized basis in that the CAS cost would be measured using the same definitions of liabilities, normal cost, and assets.

Question 7(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?

We recommend that the assignable cost limitation be retained in CAS. We believe this mechanism will still be effective for underfunded pension plans and fits within the context of our proposal to use the same underlying methods and assumptions for CAS and PPA.

Question 7(c). To what extent, if any, should the CAS be revised to address negative pension costs in the context of cost volatility?

We do not recommend any revision in CAS to allow for negative pension costs. When pension costs for CAS are claimed, those costs must be funded by assets in the trust which cannot be withdrawn. Thus, if negative pension costs were permitted for CAS, essentially contractors would have paid pensions costs twice, once through required contributions into the pension trust and then again to the Government contracts. We do not believe such duplicate funding by contractors would be consistent with the objective of the Board to be fair and equitable.

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

Essentially, the PPA approach to pensions is taking a market-based snapshot each year at a point in time. We believe that the PPA calculation would provide a good starting point for the measurement of a revised segment closing adjustment calculation for CAS, again aligning both PPA and CAS with regard to the underlying methods and assumptions. However, the Board should retain the CAS concepts for the settling up of any underfunding (unfunded liability) or overfunding (less prepayment credits) related to previously determined CAS pension costs, the provisions for segment closings related to transfers of ownership, and the provisions for plan terminations in which the liability is measured by the amount paid to irrevocably settle the benefit obligations.

Question 8(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?

Clearly the existing curtailment provisions in CAS envision the permanent cessation of benefit accruals for a pension plan. However, this is not the intention of the PPA provision for "at risk" plans. In fact, subsequent to adequate funding contributions being made, the benefit accruals are essentially restored as if the cessation had not occurred at all. We believe that should the curtailment provision be retained in CAS during harmonization, the simple addition of language excluding the PPA defined "at risk" plans from being curtailments is all that is

necessary. Should an "at risk" plan fail to achieve adequate funding and be terminated, the existing provisions for plan terminations in CAS would be sufficient to address the circumstances.

Question 9(a). Should prepayment credits be adjusted based on the CAS valuation rate or the PPA requirement to use the pension fund's actual "return on assets" for the period?

We recommend that prepayment credits be adjusted based on the pension fund's actual asset returns as required by PPA. This is consistent with our proposal to create a harmonized basis of the underlying methods and assumptions for CAS with PPA.

Question 9(b). 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?

We recommend that interest adjustments be computed based on the actual deposit dates as required by PPA. This is consistent with our proposal to create a harmonized basis for CAS with PPA and would eliminate existing disparities now in the dates used that leave opportunity for errors.

Question 9(c)(i). To what extent, if any, should CAS be revised to address the PPA provision that allows the recognition of established patterns of collectively bargained benefits?

We recommend a permissive approach, rather than a mandatory approach, be taken for recognizing established patterns of collectively bargained benefits for CAS pension cost. The permissive approach is required by PPA. This is consistent with our proposal to create a harmonized basis for CAS with PPA.

Question 9(c)(ii). Are there criteria that should be considered in determining what constitutes an established pattern of such changes?

We recommend using the same criteria as those used by PPA. This is consistent with our proposal to create a harmonized basis of the underlying methods and assumptions for CAS with PPA.

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 believe that it is imperative that the Board understand the ramifications of any proposed standard in evaluating possible solutions to harmonization and appreciate

that the Board is seeking to take this action. The ramifications are likely to be different depending upon the circumstances of individual contractors, so we are hopeful that a number of information sources will be identified to support the Board as we intend to do. Circumstances we encourage the Board to consider include different funding levels (over, under), existing assignable cost deficits, existing prepayment credits, and those with "at risk" plans.

Given the 2008 implementation of PPA, we are in the process of studying the effects of funding requirements on The Boeing Company. We would certainly consider sharing our data as appropriate with Board in the future to support the harmonization efforts. However, we are unclear as to the direction of harmonization efforts at this time, so are concerned about the vast array of possible models this question from the Board may intend. Should the Board be considering our recommended approach and desire our PPA modeling results as a starting point of harmonization, we recommend the Board clarify this question to that end and ask responders to provide information during a subsequent comment period.

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 to support the contractor's proposed and/or claimed pension cost?

Requirements for supporting documentation for costs already exist, so no provision in CAS is necessary. FAR 31.205-2(d) requires contractors to maintain adequate records for costs, and FAR 52.215-2 provides for Government access for auditing these records.

We understand the Board's concern prompting this question may be that the current calculations for ERISA will become obsolete with the implementation of the PPA in 2008, and since CAS will not immediately change, Government contractors will essentially be required to maintain both the new calculations for ERISA under PPA as well as continue portions of the out-of-date ERISA calculations to support the development of CAS pension cost. This awkward period should be minimized by the provisions of Section 106 in PPA deferring implementation for eligible contractors and for all contractors by the timely publication of harmonized CAS requirements. We believe the short period of two years exposure for some contractors in maintaining duplicative records under new and old ERISA is acceptable.

There are other benefits of CAS harmonization, as we envision it, including that contractors would not be incurring duplicative costs for actuaries to partially develop CAS costs under the archaic methods using software designed for an ERISA calculation that no longer exists. Nor will contractors be faced with the future challenge of finding actuaries with knowledge of the former ERISA calculations long after their obsolescence to be able to calculate CAS costs. Furthermore, any software for calculating the current ERISA costs will almost inevitably become unsupported by vendors as their primary market migrates to

software that supports the PPA methods. It would seem undesirable to the Board, for a variety of reasons including record keeping, to base a harmonized CAS calculation upon a former version of the ERISA calculation.

We appreciate this opportunity to provide the CASB information we hope will be helpful in the harmonization of CAS 412 and 413 with PPA. As the Board progresses in its efforts, we look forward to future opportunities to provide additional information that may be useful for the Board's success in this challenging task.

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Sincerely,

Michael D. Lem
Assistant Controller
Cost Accounting & Estimating
The Boeing Company